TAM INTERNATIONAL INVESTMENT NOTE

MH17. Realpolitik in action

The real trouble with liars is that there is never any guarantee against their occasionally telling the truth.
- Kingsley Amis

The weekend's 24-hour coverage of the downing of the Malaysian Airlines flight MH17 has revealed little about what the West intends to do about it. Whilst Putin has been placed in the dock by the media, it seems that, contrary to what David Cameron is pushing for, it's business as usual in Moscow. This is unsurprising since Russia was already weathering the limited sanctions being imposed upon it and has seemingly escaped the EU's notice of further punishment for annexing Crimea. That's a done deal and a distant memory. Also, there is no change in eastern Ukraine where pro-Russian separatists hold the balance of power on the ground.

Meanwhile, President Obama seems unable to force the EU to take a tougher stance against Russia in the form of meaningful actions of any kind. As a result, we are seeing mounting frustration in the public media, notably in the Netherlands who lost at least 192 nationals in the tragedy, asking why there is no response to such an outrage. As these events play out within the geopolitical scene, stock market reaction has been limited. This may well be because the prospect of substantive punishment being doled out to Russia is itself limited because the consequences for the EU economy would be dire. Proper sector wide sanctions from the EU, as opposed to those targeting individuals, could backfire quickly and tip the EU back into recession. So long as there are no new sanctions, the EU economy has a chance to get up off the floor. As this hangs in the balance, so too do European stock markets. Next to nothing came from the EU foreign ministers meeting in Brussels yesterday and FTSE has barely moved since Thursday. For the moment, it appears that markets are expecting little escalation in economic sanctions despite George Osborne calling for tougher measures and warning that the UK should be prepared to take an economic hit as a price worthpaying. Over the coming weeks, whatever the Dutch, UK, Polish and Italians say, it is Angela Merkel who will gauge the level of response because the German economy has the most to lose from cutting Russia adrift economically. For as long as Merkel tows a moderate line, it is unlikely that there will be any serious insubordination from other EU states – a new EU order demonstrated clearly over the appointment of Jean Claude Junker earlier this month.

As of this morning, equity markets are up in Asia, Europe and the UK following a +0.57% gain for the US S&P500 and a new intraday record high of 1,986.24 driven by benign US inflation data, which takes pressure off the Federal Reserve to raise interest rates, and more positive 2nd quarter corporate earnings figures. About a third of US companies have now reported and three quarters of them have delivered results that are better than expected. Even the Russian stock market rose, breaking a 6 day losing streak. The FTSE100 has, yet again, moved above 6,800 and we are still positive on the prospects equities over the next 12 months. The UK 10-year Gilt yield has fallen further to 2.56% and is mildly concerning. The low US inflation data is partly to blame but another factor may be that geopolitical worries are easing, they have not exactly taken a back seat. There is a long way to go and, of course, we must carefully watch events in Egypt, Syria, Iraq and the consequences of the coup in Thailand. All of which makes the year to date performance of equities all the more remarkable.

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