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update

Knightsbridge Wealth

Dear friends and colleagues,

The Federal Reserve recently announced what may have been the most keenly awaited interest-rate announcement since the economic crisis began. Following upheaval in the markets, investors had gone from expecting a small rise to anticipating a freeze – but accompanied by a warning that rates would still be rising soon. So, when the Fed maintained rates at 0%-0.25%, few were surprised. What did startle markets was the tone of the official statement and press conference that followed.

The timing of future rate rises will depend on "progress – both realised and expected – toward the objectives of maximum employment and 2% inflation". But Fed chief, Janet Yellen, also noted that the rising US dollar had already tightened US financial market conditions. The Fed also said it would pay attention to "the outlook abroad", a reference to the collapse of the Chinese stock-market over the summer, and a drop in commodity prices.

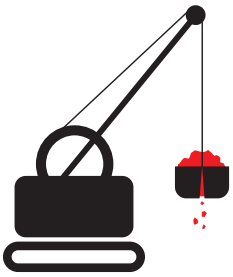
If the aim was to calm markets, it was soon disappointed. Both US and European equity markets fell by around 2%, and have continued to struggle. Investment banks – which were expected to benefit from a rising interest- rate cycle, boosting their profit margins – were particularly hard hit.

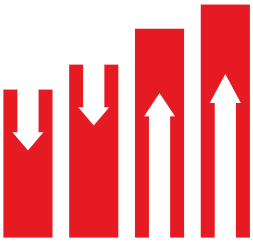
The end of the year will be important for global markets and for those preparing their investment strategy. Some predict oil at $25 a barrel, and that could lead to some major corporate bankruptcies among the big firms, whose forecasts of their own performance assumed an oil price of $100. Chinese equities will remain volatile. China is an emerging market - not a developed one. It isn't collapsing. It is just slowing down – as it should, given that it needs to rebalance its economy from one focused on investment and superfast growth, to one focused on making people's lives better. China exposure remains appropriate for many of our clients' portfolios.

The severe stock market falls in the summer seem unlikely to lead to a bear market yet. The economic recovery looks strong enough to cope with a slight increase in interest rates and, if there is a downturn, central banks still have a wide range of measures they can employ.

There are still plenty of problems with the world economy. Our international clients benefit from the security of dealing with an exclusive and distinctive wealth management company, based in a well-regulated centre. No matter what your unique financial requirements are, the team at Knightsbridge Wealth looks forward to working with you.

Market Report





Precious Metals
Keep holding gold
Gold usually performs well when markets are nervous and last month was no exception. Despite rising 7% in the summer it has since given back some of those gains and is still down by around 4% so far in 2015. Silver, which is more volatile than gold, also rallied initially, but gave back all of its gains to hit a new low for the year of just over $14/per oz.

Investors should continue to hold part of their portfolio in gold as protection against a crisis in stocks and bonds, as well as a hedge against the eventual return of inflation.

Equities
Value may be emerging
The summer was very difficult for stock-markets around the world. The S&P 500, which had previously been comparatively immune to jitters elsewhere, plunged by more than 10% between 17 August and 25 August. While US stocks still look expensive, pockets of value are beginning to emerge elsewhere.

The MSCI Asia ex Japan index, which is down by more than 13% so far this year, trades on a price/book ratio of 1.2, well below its long-term average of 1.7. European stocks also look attractive remains attractive.

Bonds
Don't reach for yield
"Safe haven" bonds performed relatively well over the summer. US ten- year Treasury bond yields dropped as low as 2% whilst the UK then year gilts fell to 1.75%. With the threat of interest rate hikes, who would really want to lock their money away for 10 years for 1.75% per year?

Meanwhile, riskier bonds fell heavily. Bond investors should focus on safety and avoid being tempted to take on more risk in pursuit of higher yields.

Cash
Rates aren't going up yet
Until the latest bout of market turmoil, the US Federal Reserve looked almost certain to raise interest rates in Septmber. Instead, statements by Fed board members suggest that at least some of them believe that a rate rise should be pushed back until the end of the year.

In the UK, Mark Carney, the governor of the Bank of England, suggested that rates are still set to begin rising in the first quarter of next year, while one monetary policy committee (MPC) member voted for an immediate rise in August's meeting. But it's clear that many of the MPC are concerned about acting too quickly, so further delays are likely when the new year rolls around.

Property
Construction cooling off
UK commercial property construction seems to be cooling slightly, suggesting that the sector is unlikely to see a glut of new space in the near future, which should help to support both rents and capital values.

Meanwhile, the US residential property market continues to strengthen, helped by record low mortgage rates. Prices were up by 6.9% year-on-year, according to the CoreLogic House Prices index.

Oil
A false hope
Brent crude, the industry benchmark, dropped below $43 per barrel towards the end of the summer, before rallying 25% in just three trading sessions. Traders were encouraged by signs that suggested that US shale producers are cutting back on production faster than expected, together with speculation that oil cartel Opec was considering reducing output.

Industrial metals
Time for tin to shine
Prices of industrial metals such as copper, aluminium, lead, tin, nickel and zinc fell together over the summer, amid fears of weaker demand in China. The near-term outlook looks weak, with tin being the main exception. Indonesia, the world's top exporter of tin, has introduced new regulations on the production of the metal, which are already holding up exports.

Feature: Eastern Europe

Emerging markets have proven to be even more cyclical than those in wealthier countries. The marketing of high-growth economies, best encapsulated by one of the most hollow marketing gimmicks ever – the promotion of the "Brics" markets of Brazil, Russia, India, China and South Africa – has also resulted in disastrous losses. And there might be more to come. Even Asia's "Tiger" economies – South Korea, Taiwan, Hong Kong and Singapore have sputtered and their stock-market performance has been even worse.

This should not be surprising. Rising markets and asset prices follow a well-known pattern. The more they rise, the more investors and commentators are entranced. Yet there has been one group of nations that, with occasional hiccups, has been growing while producing reasonable market returns. That is Eastern Europe.

During the 1990s, most of these countries underwent a largely successful transformation, moving away from their focus on their Russian. Basics such as a working telephone system, shops that stocked food, and street lighting outside of capital cities soon became normal. The gap between this "New Europe" and Russia became a chasm. The income gap, already meaningful, has steadily expanded. The human rights gap, be it a functioning legal system and property rights, a less oppressive police force and state security system, or generally free elections, became wider still. Thus, as each year passes, this new-found independence and desire to choose becomes increasingly entrenched.

Poland is the best example, with a population of 39 million. The comparison with the fashionable Asian economies is note worthy. During the 1990s, Poland's growth rate was marginally behind Thailand, a country long-considered one of the most promising in Asia, with 68 million people. Since the turn of the century, Poland's growth rate has been higher than Thailand's. Slovakia has beaten Singapore over the last decade, while over the last five years much, even much-criticised Romania has beaten Taiwan. During the last 20 years, GDP growth in the Czech Republic has easily exceeded Hong Kong.

The headline numbers mask more important trends. For all this growth, income per head is lower in Poland, the Czech Republic and Hungary han in all four of the Tigers. While Polish and East European wages remain slightly higher than China's, so much has the gap narrowed that the outsourcing to China and Asia, which dominated manufacturing until 2010 after Asia and has reversed. The comparative attractiveness of "legally friendly", low-cost eastern Europe has become ever clearer.

At the national level too, the finances of most eastern European countries are in considerably better shape, not only than mainstream EU countries but other international rivals too. Government debt in the Baltic countries, as well as Poland, Romania, Bulgaria, the Czech Republic and Slovakia, it is less than 50% of GDP – averaging around 25%. With the exceptions of Norway and Sweden, all other EU countries have a debt-to-GDP ratio in excess of 60%.

What stands out in eastern Europe is its technical expertise.

Before the Second World War, the Czech Republic was respected as the most advanced specialist engineering country in the world. This skill persists, which is why global companies such as Volkswagen and Fiat have relocated plants both there and to other eastern European countries. The once-derided Skoda has become one of the sleekest, relatively cheap and most-awarded mid-market car brands in the world. Romania has the largest number of IT professionals in Europe.

In medicine, Eastern European expertise is well regarded. Last year, the UK's Health service encouraged the imprisonment in Marbella of the parents of five-year-old Ashya King, who was severely ill. They had removed him from a Southampton hospital against the wishes of his doctors to seek treatment in Prague for his brain cancer. They were released only after a High Court judge in London granted permission for the trip. Today, Ashya shows no sign of the tumour.

The real test for Eastern Europe was the 2008 crisis. During the previous six years most of their stock-markets had risen at least fourfold. But, unlike developed European countries, they did not ask for aid when crisis hit but slashed salaries for government employees and cut spending – preparing to rebuild when stability returned.

There are still risks in Eastern Europe. The biggest is that Russia seeks to recreate the perceived glories of the failed USSR. However, despite military incursions into Ukraine and Georgia, cyber-attacks on Estonia, or bribes to pro-Russian politicians across the region, the Nato/EU border grows stronger.

Russia's only real lever – energy – is not as powerful as it was. Poland and Lithuania have just built new liquefied natural gas (LNG) terminals – so their once-total dependency on Russian gas or electricity generation has ended; they can switch to other sources at a moment's notice. Slovakia is building two nuclear power stations, which within three years will provide energy independence.

Eastern Europe represents less than 5% of world stock-market capitalisation, with most financial advisers oblivious to the region – and yet it is one of the best growth/value plays in the world. Its nations are truly hidden dragons and ones that we are anxious to ensure our clients benefit from.

London property : Through the roof

As house prices rise globally, they have soared in Britain. In the past 20 years, they have increased more than any other country in the G7. Right Move recently reported that, at today's level of appreciation, the average London property will be £1m in 2020.

Chancellor George Osborne's new tax rules will almost certainly make residential property in the UK less attractive to investors. The UK housing market is often referred to as a bubble, and affordability is certainly not improving, with average wages lagging house-price growth. However, if you take a step back from the UK-wide averages, then there's a very clear divide between London and everywhere else.

If you look at Nationwide's price data, even in nominal terms, house prices in many areas are still lower than they were at the peak of the last bubble. In Northern Ireland, average house prices are still more than 40% down on the peak. Prices in Scotland, Wales and the north of England are 5%-8% lower than in mid-2007. In the Midlands, prices are flat. In the South West, prices are up about 5%, while in East Anglia they are 7% higher.

London prices are roughly 40% higher than at the 2007 peak, with a 20% rise in the "outer metropolitan" area (the bits that are within commuting distance of London) and a 13% rise in the rest of the South East.

And according to an analysis of Land Registry data by The Guardian, London is by far the least-affordable area, with the average property price now 12 times the regional average income – compared to 4.4 times in 1995.

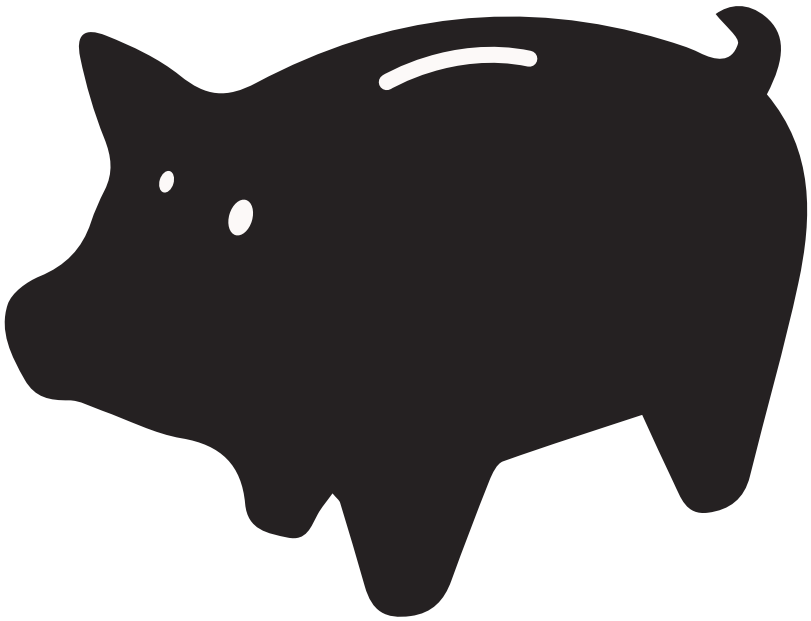
Record low interest rates have also been a boon for a generation of private landlords, but the party's coming to an end.

Buy-to-let has been an investment phenomenon. At the turn of the millennium, few people had even heard of it and even fewer had ever contemplated becoming private landlords themselves. By 2007, a full one in five mortgages were being given to buy-to-let investors and, according to the Bank of England, 15% of all mortgage debt outstanding is to buy-to-let landlords.

There is evidence that buy-to-let landlords have been able to take great advantage of rising immigration, the decline in social housing provision, and the obligations on local governments both to house the needy and pay a market rent to the landlords who own that housing.

For those without family support, it's increasingly difficult for many to buy. The average renter now spends 41% of their income on housing, according to The Money Charity. That's before all other living and working costs, and it's a good deal higher than the 34% that Nationwide building society reckons the average homeowner spends on their mortgage costs.

As a result, it's taking young people up to a decade of work to save enough on their own. During the 1990s, the average age of a first-time buyer was 27. But now, most first-time buyers are well into their 30s – specifically 37.



Buy-to-let investors have enjoyed great competitive advantages over first-time buyers in a low-rate environment. So whether rates rise early next year, as many are predicting, or somewhat later than that, there is only one way that rates can move from here - and that's up. That will be painful for buy-to-letters when it happens. The economics of buy-to-let are very sensitive to low rates. In 2005, there was a visible slowdown in buy-to-let activity – it fell about 25% below trend – following a one-year, 1% rise in base rates that took place the year before. So, in the long run, the solution to the UK's distorted housing market will be the re-normalisation of rates.

Up until now, investors have also enjoyed an overwhelming advantage in the form of preferential tax treatment. Firms (including buy-to-lets) are taxed on profits – revenues less costs. One such cost is debt interest payments. Homeowners with mortgages have to pay interest out of their post-tax income but not buy-to-let investors. They can offset their interest costs against rental income, and thus easily end up paying no tax at all. The difference for home owners is that they aren't subject to capital gains tax (CGT) on any profits when they sell.

Chancellor George Osborne's decision to phase out buy-to-let tax relief at the higher income-tax rate on interest payments by 2020, as well as restricting the "wear and tear" allowance to costs, should go some way to re-levelling the playing field.

All this will dampen growth potential for UK property, particularly in London over the next year. Clients wishing to have UK property exposure are well advised to take comprehensive advice. Knightsbridge Wealth works with a number of established property-finders, and tax lawyers, to ensure our clients' individual requirements are met.

Interest rate freeze remains. For how long?

It us now seven years since the US Federal Reserve pegged short term interest rates at 0%.

Unlike many central banks, the Fed is empowered to pursue two specific mandates: stable prices, and maximum employment. The data on jobs look clear: the US unemployment rate stands at just 5.1%, half its level during the height of the financial crisis. And inflation is practically non-existant, even though the Fed is sitting on $4.5trn of Bonds, pumped into the market to support the economy.

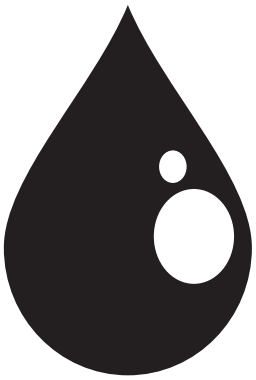
Given that the experiment of quantitative easing (QE) was always focussed on triggering inflation, the near total lack of it might be seen as something of a failure.

The recent decision by Janet Yellen, Head of the Federal Reserve, to maintain rates at these emergency low levels, cited both China's economic problems and the rise in the US Dollar as a reason to delay a rate hike.

Most Fed meetings don't matter, but this one did. As the McKinsey consultancy noted earlier this year, after a financial crisis triggered by the bursting of a vast debt bubble, there is now more debt than ever before: $57trn more, raising global debt-to-GDP ratios by some 17%.

Nudging rates higher by a quarter percentage point would certainly have made life more interesting for bond traders, most of whom have never seen a bear market in their careers. But it would also have sent a powerful signal.

Paul Ashworth of Capital Economics said that Fed officials are "fooling themselves into thinking that, if they only just wait a little longer, all the uncertainty will clear up and they can raise interest rates with no danger of making a mistake. The real world doesn't work like that... there is always considerable uncertainty." Ashworth still expects a December increase, but it is possible that the Fed will wait until early 2016. The longer the delay, higher interest rates will eventually go.



How long will oil prices stay low?

The slide in oil prices since last year was sparked partly by a decision by Saudi Arabia to flood the market. They hoped this would crush its shale-producing rivals in North America and help it hang onto market share. This is slowly changing the global balance of economic power. Unsurprisingly, with the price of Brent crude now below $50 a barrel, compared to $100 just 18 months ago, exporters have been hit hard by the slump.

Saudi Arabia – which produces oil at dirt-cheap prices but needs a high price per barrel to sustain current public spending – has been forced to raise money on global bond markets for the first time in eight years. Other Middle Eastern economies have been hit just as hard, while Russia (one of the largest oil producers in the world) is now in recession and could stay there for quite some time if oil prices drops much further.

Shortly before the slump, state-owned Gazprom tied itself into a £256bn 30-year oil-supply deal with China, which offers it no protection against a low oil price. Even at current prices, says the FT, the project is unprofitable. And Norway, which owns the world's biggest sovereign wealth fund, built on oil profits, is having to dip into its savings as it faces a slump that is likely to cost the country more jobs than the 2008 recession.

None of this bodes well for political stability in the world's more volatile regions. However, there have been plenty of winners too. Large importers of oil – including China, India and Japan – have benefited from falling costs, which in turn boost consumer spending. The US has reduced its dependency on imported oil and is even starting to loosen its long-held ban on exporting oil, as a recent deal to swap supplies with Mexico demonstrates. On the other hand, there's no doubt that the plunge has hit the fracking industry hard, with companies slashing spending.

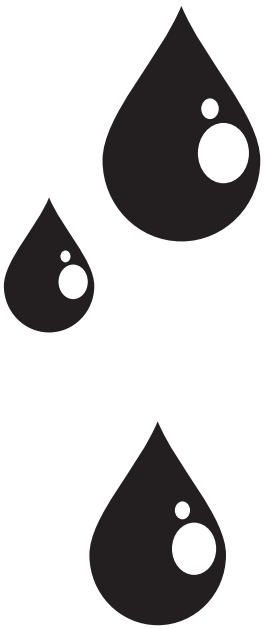
Between the spring of 2011 and the summer of 2014, prices were unusually steady, mostly trading within about ten dollars of the $110 mark, a level that came to be seen as the new normal. But, in the year since then, the price of Brent collapsed to below $50 in January, and perked up a bit in the spring to above $65 – before resuming its downward trend and hitting a six-year low of $43 in August.

Oil is a commodity and its price is sensitive to shifts in supply and demand. Right now there is a glut in the supply of oil, while demand has slowed. US domestic production has doubled in the past six years (thanks largely to the shale boom), pushing out imports.

That means oil from (for example) Saudi Arabia, Nigeria and Algeria, formerly sold to the US, is now competing for other markets, such as Asia, driving prices down. Meanwhile, global demand has been hit by weak activity – especially in Europe and some developing countries – but also by the increased efficiency of many vehicles, and a shift away from oil to other fuels and renewables.

The consensus view is that prices will stay low for years – not months. According to an Opec memo leaked to The Wall Street Journal earlier this year, the oil-producing nations' club believes the price will not return to $100 for at least a decade. Indeed, in its most optimistic scenario, oil will be trading at around $76 in 2025. Today's low price means many new exploration and drilling projects are being postponed or mothballed.

Opec has traditionally cut supply to prop up the oil price. But this time around its dominant player, Saudi Arabia, has taken a strategic decision to fight for market share. Its refusal to cut suppy means price falls to make life difficult for rivals – in particular, more expensive US fracking. They might yet change tack, under pressure from other Opec members (and in the interests of political self- preservation), but there's no sign of that so far.



Knightsbridge Wealth's senior team and support staff have over 250 years experience in the world's largest Banks

Alexander Wade

Alexander is one of the most experienced London advisers in the international market, specialising in this field over the last 17 years at HSBC, consistently recognised as one of its most accomplished advisers. He has over 21 years' experience in financial services. He is particularly interested in the Middle East market and understands the specific issues which are relevant there.

Stuart Poonawala

Stuart has worked in financial services since 1998. In 2003, he helped to found HSBC's specialist London arm advising international clients which quickly became one of the bank's most successful UK divisions. In 2009, he launched Kubera Wealth, our sister company, focussing on providing quality advice to the UK market.

Graeme Cowie

Graeme is responsible for building our professional connections with international lawyers and accountants, as well as co-ordinating our relationship with key fund managers at a number of international Private Banks and Discretionary Fund Managers. He has spent over 20 years in financial services and investment management, most recently spending more than six years at UBS where he led the Strategic Partnership team.

Adam Young
is the team's Financial Planner. He previously spent 25 years at Dragonfly Planning and Trust Services, the last three years as Managing Director.

Chris Salacinski
is Customer Relationship Manager and brings to us a high level of technical experience. He is particularly interested in pension planning and is responsible for writing many of our technical articles.

Kelly Kular
is Personal Assistant to the Partners. She previously worked with HSBC for 27 years, latterly as Personal Assistant to the Regional Director for Central London Region.

Kirti Paw
is our Client Relationship Manager. She has joined us from HSBC where she spent 33 years, followed by a brief time with Santander.

Shana Patel
is our Client Relationship Manager. Before joining us, she worked at HSBC Bank for 26 years, most recently as a Senior Wealth Manager dealing with high net worth clients.

Kellie Lewis
is our Client Relationship Manager. Before joining us she for HSBC for 26 years and has extensive banking and wealth management experience. She spent eight years as a Premier Relationship Manager, looking after a portfolio of High Net Worth Clients.

David Barnard
spent 35 years at HSBC before leaving in 2011. He is our Office Manager, and works closely with our compliance support and partner companies to ensure our rigorous standards of advice are maintained.

Contact us

If you require further information about our services or would like to discuss your financial situation with us, then please call us on the number below, or send us an email about how and when we can contact you.

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