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Below is the latest Market Comment from Ian Williams: (01/12/2014)

The big story over the last month is the collapse of the Oil price following a failure by OPEC to agree any production cuts in the face of sharply rising US Shale production which has caused a glut in the global Oil market to the tune of 1.5 Millions of barrels a day. What are the global implications?

1. The Oil price fall is unambiguously great news for the global economy apart from Oil producers such as Russia & Saudi & the Oil Companies themselves. The fall in Brent crude from \$105 to \$65 a barrel will add at least 1%, possibly more, to global growth IF Oil stabilizes around this level. The biggest beneficiaries will be countries that import most or all of their Oil such as China & Japan. Any doubts about Chinese growth slipping below 7% can now be dismissed.
2. New shale production in the US will fall off a cliff in about 12 months' time. Shale wells are not like conventional wells in that they produce about 70% of the wells capacity in the 1st 12months of their life. As the average cost is around \$75 a barrel they won't get new finance to drill for new production if the price stays around the current level. It also means that the US Shale Industry is now the global swing producer because if Oil prices go back up above the Shale cost the Shale Oil will be back on the market.
3. Most of this year's Shale production will still be profitable as the bulk of the shale oil output was hedged (pre-sold) at much higher prices as a pre-requisite for obtaining funding. This also means that the market will not be as glutted as the daily figures suggest going forward as this Oil has already been sold. Scare stories about Junk Bond defaults are probably also over exaggerated as a result of the hedged selling that has taken place.
4. The big winners will be: Airlines, Cruise ship & Train operators, Chemical Companies, Metal Miners (Diesel costs make up 35% on average of their costs) & Consumers - especially in countries such as the US where Gasoline is not taxed - every consumer in the US has effectively just been given a lot more money to spend. The effect in the UK will be much less pronounced

due to the high petrol taxes imposed by the UK government. As far as US Inc is concerned the benefit to US consumers has to be offset by damage to US Oil companies. For Asian countries it is just win win all round.

5. The fall in the Oil price will allow the ECB to start "proper" QE as it could easily bring the headline rate of Inflation close to or even below zero in many EU countries. It could also delay any rise in rates in the UK or USA.

It is quite important to differentiate between a lower Oil price caused by excess supply (like this one) and a lower Oil price caused by a collapse in demand. The second example could be a sign of Global recessionary / deflationary pressures and might be a cause for concern.

The 1st example is nothing of the sort and is actually reflationary in its effect on global consumer demand. As stated it also allows Central Banks to be even more accommodative if they are targeting an annual CPI target. **Lower Oil prices are disinflationary on CPI and reflationary on demand whilst a higher Oil price is inflationary on CPI and deflationary on demand i.e.** the higher Oil price acts a tax hike on consumers whilst a lower one acts a tax cut.

This should therefore be very bullish for Global Equities (excluding Oil shares) but especially bullish for Equities in countries that are large Oil importers (China & Japan etc). It is mildly supportive of Bonds although many are so overpriced already that any further upside looks limited. With regard to other commodities there is no reason at all that weak oil should mean weak Gold, Copper or Wheat etc especially as the fall in the Oil price has little to do with reduced demand and everything to do with greatly increased supply.

Much of the recent volatility in the other commodity prices is more likely due to Commodity Hedge Funds being liquidated and closed down (no bad thing) rather than any ongoing bear market fundamentals. Also, with Toyota (after 20 years research and development) now introducing a mass production Hydrogen Fuel cell car with a range of 400 miles , a 3 minute refuel & no carbon emissions the ultra-long term market for Oil as the primary source of transport could be in permanent decline.

Warm regards,
Ian Williams, Charteris CEO and the team.

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