



## A logic bypass

All dogs have four legs; my cat has four legs. Therefore, my cat is a dog. This is an example of association fallacy when a conclusion is made about something that is based on some dubious similarity. For the keen eyed observer we see these arguments bandied around all over the place. For the less keen eyed observer, try watching BBC Parliament for a couple of hours. Governments with sound fiscal policies and modest borrowings enjoy low government debt yields. Therefore low interest rates mean that a government has sound fiscal policies and modest borrowings. Really? Or maybe Mr. Osborne, if I may be so bold? The seemingly unstoppable decline in the Gilt yield might be a reflection of the awfulness of other government's debt.

But why, out of all the weeks that the gilt yield has been sinking, would we necessarily choose this one to rant about its causes (no, not rant; carefully consider the arguments). On Thursday of last week, for the first time since the bear market trough in March 2009, the yield on the 10 year Gilt was briefly below that of the 10 year German government bond. If we were to overly simplify what this means, we could say that the UK, albeit briefly, was considered a safer haven than Germany. Germany – that net exporting country with relatively low levels of personal debt, similar levels of net debt to GDP, and a much lower fiscal deficit. You have to squint very hard to make Germany appear riskier than Blighty.

Maybe then the euro is to blame. It seems logical that as the yield of various European sovereign debts rose, in order of lowest quality to highest, eventually we would get to the top. The rapid spread tightening between Großbritannien und Deutschland witnessed last week was set off as investors shunned a bund issue on Wednesday. The common denominator between all the European countries for which this has been the case is in fact the denomination. During the last football World Cup you could, if you were so inclined, buy a t-shirt in Scotland carrying the legend A.B.E – Anyone But England. Perhaps bond investors could resurrect the abbreviation for 'Anywhere But Euroland' because the only thing that marks Germany as somewhere unattractive to invest is the fact it is in the Eurozone.

Moving on, but staying with Europe, the ECB's response to falling money supply is becoming increasingly irksome. It too, it seems, is guilty of association fallacy. We all know inflation when it gets a bit high is a jolly bad thing. It follows therefore, that a good chunk of deflation is a jolly good thing, right? Er no. Here's a little bit of history – the ECB was born out of the old Deutsche Bundesbank. The Bundesbank was founded with the principles learnt by its predecessor, the Reichsbank, which presided over the hugely destructive and very painful hyperinflation of the early 1920s. The ECB hates inflation as much as a St. Paul's protestor hates me. But in its aversion to inflation, is it not risking the greater danger of deflation?

Although at a first glance, deflation doesn't seem so bad, the Japanese lost decade(s) of growth and occasional spurts of deflation ought to provide a reason for its avoidance. Every year savers see the value of their bank deposits rise in real terms as each year goods, services and potentially assets get cheaper. In this case what is the impetus to spend or more importantly invest? Who would want to buy a new house that would be worth less next year? Why would a business wish to expand if, in nominal terms, the price of the goods it sold were falling every year and the value of its investments were in terminal decline? No one wants to see hyperinflation but in its avoidance the new ECB chairman Mario Draghi may want to consider the risk of deflation and follow the example of the Bank of England and the Fed with a little quantitative easing.

Finally, the only animal other than the human being that can contract leprosy is the armadillo. Today, when did England reach their landmark 1,000th goal in football?

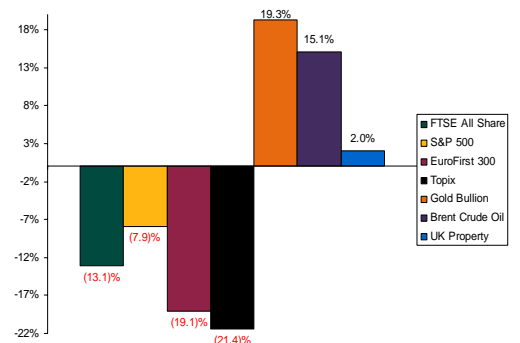
### FTSE 100 Weekly Winners

Admiral	7.4%
Bunzl	1.1%
Weir	0.7%
BSkyB	0.1%
Morrisons Supermarkets	-0.2%
Reckitt Benckiser	-0.3%
Rexam	-0.4%

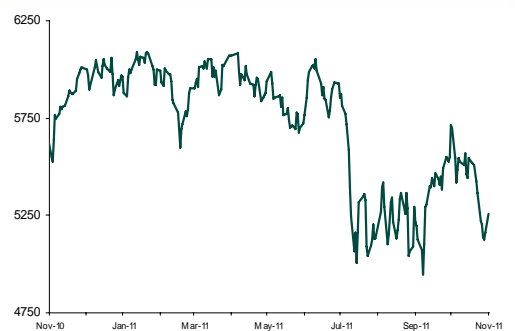
### FTSE 100 Weekly Losers

Essar Energy	-11.9%
Man Group	-11.1%
Hargreaves Lansdown	-10.5%
Royal Bank of Scotland	-8.9%
Cairn Energy	-8.7%
Vedanta	-8.1%
Lloyds Banking Group	-8.0%

### Year To Date Market Performance



### FTSE 100 Index, Past 12 Months



source: Thomson Reuters



## Selected stock comments

**BRBY – Burberry Group – Upgraded to BUY 1145p (TP cut to 1400p)** We believe that Burberry is a strong company in terms of its financial strength and brand name and that it is well placed for future growth. There are market concerns regarding the impact of a fall in global consumer demand across its business, but in our view, it is well placed to manage any potential slowdown and with its emerging market customer base, it is better positioned than most. Our target price is lowered to 1400p to reflect these concerns but following the fall in its share price we now recommend BUY.

**CPG – Compass – BUY 560p (TP 650p)** Compass released full year results in line with expectations and issued a reassuring outlook statement. Volumes are expected to remain 'dull' but that shouldn't prevent it delivering another year of respectable organic growth and improving margins, helped by easing inflation and recovery in Japan. The strong balance sheet is to be deployed buying back £500m of shares - around 5% of the outstanding equity – which can easily be accommodated without stretching the balance sheet ratios or debt ratings.

**United Utilities – ADD 605p (TP up to 650p)** United Utilities reported a 2% fall in underlying EPS in its interim results, but its dividend was increased by 6.7% to 10.67p in line with its policy of increasing dividends at 2% above RPI until March 2015. We expect the rate of inflation to ease back and see United Utilities as well placed in relation to the other two water companies in that it has a higher level of index linked debt, which will therefore be cheaper. We increase our target price to reflect a premium of 7% to the March 2012 regulatory asset base in our valuation. The shares yield 4.9% prospectively at our target price.

**DXNS – Dixons – Downgraded to REDUCE 9.5p (TP lowered to 5p)** Dixons has released its interim results. For a retailer, the second half is more important than the first; however after such a dire first half the company is facing an uphill battle. We consider the company to be a special situation in that it is extremely difficult to value as slight changes in underlying assumptions can lead to a big change in the fair value. Our message remains that Dixons is inappropriate for private investors and fundamentally we do not encourage ownership.

### This Week's Forthcoming Events

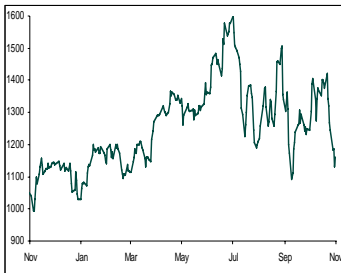
UK	Nov CBI distributive trades
UK	Nov Nationwide house prices (m/m)
UK	Nov CIPS manufacturing PMI
UK	Nov CIPS construction PMI
US	Oct new home sales
US	Nov consumer confidence
US	Nov ISM manufacturing
US	Nov non-farm payrolls
Emu	Nov consumer sentiment
Emu	Nov manufacturing PMI
China	Nov manufacturing PMI

### Last Week's Highlights

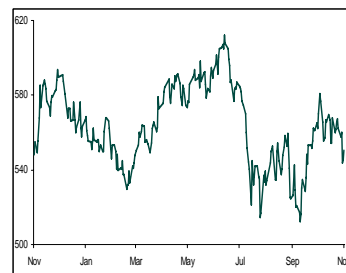
Pennon Group - Downgrade to HOLD  
Johnson Matthey - Upgrade to ADD

Black Friday retail sales up 16% on last year in US

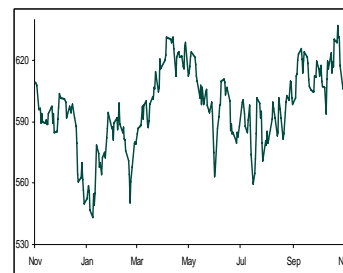
**Burberry**



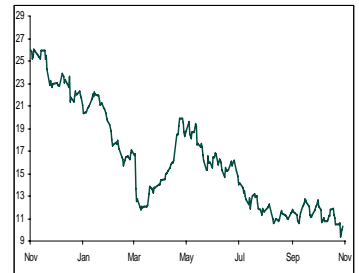
**Compass**



**United Utilities**



**Dixons Retail**



All data sources: Thomson Reuters. All charts share price for previous 12 months. This report has been issued by the Research Department of Williams de Broë Limited (Williams de Broë) on the basis of publicly available information, internally developed opinions and other sources believed to be reliable. All views and recommendations expressed are based entirely on such data. Our material is regarded as non-independent research and a marketing communication which means that it has not been prepared in accordance with legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research. Employees of Williams de Broë are, however, subject to our internal Personal Account Dealing Policy and our Conflicts Management Policy is available at <http://www.wdebroe.com/disclaimer/research/>. Williams de Broë, its employees or a connected company may trade in the investments referred to herein and may also perform investment or other banking services for such companies. Williams de Broë does not have any corporate relationships with any of the companies discussed in this document. However, Evolution Securities Limited (a fellow member of the Evolution Group plc) may provide or may have provided corporate services to issuers of securities mentioned in this material and any reference to their research should not be relied upon as being impartial. This document is not intended as an offer or solicitation for the purchase or sale of any investment or any other action. Past performance is not a guide to future performance. The value of investments and the income from them varies and you may realise less than the sum invested. Higher volatility investments are subject to sudden and large falls in value and could result in a loss equal to the sum invested. Certain investments are not readily realisable and investors may experience difficulty in realising the investment or in obtaining reliable information on the value or associated risks. For securities denominated in a currency other than sterling, changes in exchange rates may have an adverse effect on the value of the investment or on the income thereon. The stated price of any securities mentioned herein is at the end of the business day immediately prior to the publication date on this document unless otherwise stated and is not a representation that any transaction can be effected at that price. No personal recommendation is being made to you; the securities referred to may not be suitable for you and this material should not be relied upon in substitution for the exercise of independent judgement or seeking independent advice. Williams de Broë will not be liable for any direct or indirect damages, including lost profits, arising in any way from the information contained in this material. This material is for the use of intended recipients only and is not directed at you if Williams de Broë is prohibited or restricted by any legislation or regulation in any jurisdiction from making it available to you. This document is being supplied to you solely for your information and may not be re-produced, re-distributed or passed to any other person or published in whole or in part for any purpose. The material in this document is not intended for distribution or use outside of the United Kingdom. Williams de Broë Limited. Registered office: 100 Wood Street, London, EC2V 7AN. Registered in England and Wales under Company Number: 2485266. A wholly owned subsidiary of the Evolution Group plc. Authorised and regulated by the Financial Services Authority. A member of the London Stock Exchange.