23 January 2017

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INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Sell the rumour, buy the fact

KEY MESSAGES:

The week's major events were Donald Trump's inauguration ceremony, and the World Economic Forum at Davos. USD, GBP remained volatile as Theresa May delivered her long expected address on her Brexit strategy. US futures climbed with the USD and bonds fell as investors awaited the start of Donald Trump's presidency.

Rising consumer prices in the US joined data showing strengthening inflation in the UK and EU, underpinning confidence in global economic growth.

Sell the rumor; buy the fact

The maxim "sell the rumor, buy the fact", has become more relevant in the financial markets than ever before, considering the market sensitivity to political developments. This was much clearer in this week's price action on GBP. Having already sold sterling after the weekend's press reports on the contents of May's speech, the market seemed happy buying the pound on the news that Parliament will get a final vote on the Brexit package.

Even the USD lowered during the week upon comments from President Trump criticizing USD strength. By the end of the week USD rose after Janet Yellen signaled the Federal Reserve stands ready to raise interest rates if the economy strengthens as the central bank anticipates.

Market developments during the week

Last week marked the inauguration day of the 45th President of the United States Donald J Trump. He has taken the reins at a time when the economy is growing steadily with low unemployment. Investors await the details of the policies he will implement in the early days of his mandate. Volatility is expected as evidenced by recent market reactions driven by President Trump tweets, but the direction is clear. US equities should trade higher through 2017, absent any significant global macro shocks.

Ironically, in the run up to the swearing in, US equity funds saw weekly outflows of $2.5 billion, according to a strategy note from Bank of America-Merrill Lynch, citing data from EPFR Global. This week, investors were careful to avoid taking firm positions before the inauguration.

This sell off was arguably irrational, as economic data over the past week has further confirmed the strength of the US economy. The Fed's Beige Book painted a relatively bright picture of the domestic economy. Labor markets were reported to be tight, or tightening while wage pressures were building. Initial jobless claims fell to a 43 year low. Consumer Price Index inflation rose above 2% for the first time in more than two years in December.

The World Economic Forum meeting in Davos was held this week. Though President Trump did not attend it, he dominated the meeting as the question remained how to engage an unpredictable US leader who has pledged to rewrite the tax code, overhaul healthcare, and tear up trade agreements.

Chinese President Xi Jinping urged global business and political elites to reject trade wars and protectionism, in his first public rebuttal of the policies advocated by incoming US leader Donald Trump. In a speech where he did not name Trump, but where his comments were clearly targeted at the president-elect, Xi told the World Economic Forum in Switzerland on Tuesday that failures of governance, not globalization, were fueling anxiety around the globe.

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The corridors of Davos buzzed with concerns that populism around the world must be stopped. Davos, over the decades, has become synonymous with globalization and open markets, but in the background this year is the failure of business and political elites to predict any of the seismic political events that shaped 2016. That has raised questions over whether they are capable of understanding and addressing the anti-establishment forces that have shook the US and Europe over the past year. While International Monetary Fund chief, Christine Lagarde, urged a list of policies from programs to retrain workers to more social spending, others fretted that the turbulence is only just starting.

German carmakers pushed back Donald Trump's threats of import duties on the autos they make in Mexico, pointing to extensive production expansion in the US in recent years. BMW AG sought to defuse potential tensions by stating that its largest factory is in South Carolina and that cars made at a planned, smaller factory in Mexico will be exported globally. Trump said BMW will face a 35% import duty on vehicles it exports to the US from Mexico. Trump's comments were the first aimed at a European carmaker after he issued similar warnings to Ford Motor Co. and Toyota Motor Corp. So far, the threats have prompted conciliatory gestures by the targeted companies. Ford canceled plans for a $1.6 billion factory in the country to instead expand an existing site in Michigan. Toyota, which is set to start producing Corolla cars at a new plant in Mexico starting in 2019, has said it'll take Trump's decisions into account in the future.

Equities & Bonds

US futures climbed with the dollar and bonds falling, as investors await the start of Donald Trump's presidency. Futures on the S&P 500 Index rose 0.2 %. The underlying benchmark is heading for its biggest weekly drop of 2017. Contracts on the Dow Jones Industrial Average were little changed on Friday.

The Stoxx Europe 600 Index traded little changed, as declines from miners offset gains in energy shares.

Asian shares pared weekly losses and fluctuated within narrow ranges as investors await US President-elect Donald Trump's inauguration. The MSCI AC Asia Pacific Index gained 0.1%, paring its first weekly decline in 2017. China's Shanghai Composite index rose the most in more than two weeks as China's gross domestic product accelerated for the first time in two years in the fourth quarter of 2016. Hong Kong's Hang Seng Index and Hang Seng China Enterprises Index had short-lived spikes before holding losses after a report that China cut the reserve ratio requirement for five major banks.

Japan's Topix closed 0.4% higher even as the yen strengthened versus the dollar, after Federal Reserve Chair Janet Yellen said the Fed backs gradual rate rises. India's Sensex dropped the most in 2 weeks, led by lenders and metal makers.

The yield on 10 year Treasuries was little changed after briefly touching 2.5%. Government bonds retreated across the European Union. Yields on Irish 10-year notes climbed 4 basis points to 0.99%. The yields climbed in Europe, playing catch-up with Treasuries, which sold off yesterday after Fed chair Janet Yellen said the American economy is strong enough to warrant higher interest rates, bringing the ECB's quantitative easing into sharper relief as policymakers, led by Draghi, met to discuss the monetary policy.

Currencies

The Bloomberg Dollar Spot Index was up 0.2% as of 7:45 a.m. in New York after falling as much as 0.3%. The gauge is heading toward its first weekly advance since the period ending Dec. 23. The upcoming US fiscal policies looks set to become the key driver of exchange rates.

The pound dropped 0.5% to $1.2285 and the euro retreated 0.2% to $1.0648. Yen strengthened to 114.76/USD.

Emerging market countries offer attractive carry-trade opportunities because they were forced to push up interest rates during the 2015 commodity crash. South Africa's central bank lifted its policy rate four times in the past two years to 7%, where it will likely remain in 2017, according to a Bloomberg survey of economists. Russia's benchmark rate will stay above 8%, the survey shows. Those relatively high rates, together with currency gains against the dollar, garnered carry returns of 32% for the

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ruble and 21% for the rand in 2016. Using the pound as a funding currency, returns in the first two weeks of this year were 4.2% for the ruble and 2.5% for the rand.

The Philippine peso, which weakened 4.6% in the past 12 months, is forecast to be the most resilient to external risks this year, according to a Bloomberg survey of 10 foreign exchange analysts. The Thai baht and Indian rupee together rank second, while China's yuan is last.

Commodities

West Texas Intermediate crude climbed for the second day, gaining 1.5% to $52.13 a barrel and narrowing a weekly loss to 0.5%. Brent futures added 0.3% to $54.35 a barrel.

As per statement by Saudi Arabia's energy minister, the surprising strength of the oil market could lead to OPEC ending the output cuts by the middle of the year. OPEC and Russia may not need to extend the curbs when they expire in June, Khalid Al-Falih said in an interview at the World Economic Forum in Davos, characterizing his view as a "bullish sign."

Meanwhile the OPEC's campaign to prop up oil prices is getting unlikely support from its biggest customer. China's production is forecast to fall by as much as 7% this year, extending a record decline in 2016, according to analysts at CLSA Ltd., Sanford C. Bernstein & Co. and Nomura Holdings Inc. That's about the same size as the output cut agreed by Iraq, the second-biggest producer in the Organization of Petroleum Exporting Countries, which late last year reached a deal to trim supply to support prices. While China consumes more oil than almost any other country, it's also one of the world's biggest producers, with fields stretching from offshore its southern coast to the far north east. The collapse in prices that began in 2014 is taking its toll, and the nation's output suffered a record decline last year. That plays into the hands of OPEC as it seeks to prop up the global oil market, forcing China to depend more heavily on imports. China's output slumped in 2016 as state-owned firms shut wells at mature fields that had become too costly to operate after the crash.

Oil price gains will trigger a "significant" increase in US shale output as OPEC and other producers rein in supply, according to the head of the International Energy Agency.

Earlier this month, WTI gained sharply against Brent for some contracts in future years, amid speculation that a Republican president and a Republican-controlled Congress would agree on a tax proposal. For December 2019, WTI briefly traded at a premium to Brent. The discount for December 2018 WTI broadened $0.07 from Tuesday's close, to $0.97 a barrel. In addition, traders have bet roughly $61 million that the two grades would be at least at parity as early as next June, according to Bloomberg calculations from options trades. The value of these options diminished this week as WTI's price plummeted against Brent, following publication of Trump's remarks. Options contracts for WTI to trade at a $2 premium to Brent have halved in value since last week, while those betting on any kind of premium also declined as Trump described the tax plan as "too complicated" in an interview with the Wall Street Journal this week, casting doubt on the proposal and putting the bets on oil prices at risk. A tax on oil imports would not only raise the price US refiners pay for Brent, it would also trigger an increase in WTI by spurring more demand for the American grade.

Gold moved toward fourth weekly gain closing at 1,202.55 an ounce. The metal has advanced 0.4% this week, touching the highest level since November on Tuesday.

Major economies:

Canada

CAD remained on the defensive against USD, but the pace of its losses slowed by the end of the week. It rose initially on USD weakness seen at the start of the week. The Canadian Survey of Manufacturing showed Manufacturing Sales up 1.5% in November, but this did little to support the loonie after Bank of Canada Governor Stephen Poloz's comments on Wednesday about rate cuts still being a possibility as he kept rates on hold. The Bank's latest Monetary Policy Report also warned about the consequences of any protectionist trade policies of the sort discussed by incoming US President Donald Trump. US Press Secretary Sean Spicer said that Donald

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Trump would act on promises to withdraw from the Trans-Pacific Partnership trade deal and renegotiate NAFTA very shortly after his inauguration. President-elect Donald Trump won't wait for Congress to confirm trade officials to act on his promises to withdraw from the Trans-Pacific Partnership trade deal and give notice he will renegotiate NAFTA, press secretary Sean Spicer said.

Existing home sales rose 2.2% in December rebounding somewhat from a sharp decline in the prior month. Home prices, after adjusting for location and housing type, rose on the month and were up by double digits versus year ago levels across all housing types. Retail sales rose 0.2% in November, with volumes up by a robust 0.7% on the month. Manufacturing sales bounced back by 1.5% in November, reaching the highest level since January. Volumes were up a healthy 1.2%. Headline inflation accelerated to 1.5% in December. The three core inflation measures showed limited price pressures across the economy.

Euroarea

As expected, the ECB kept rates unchanged at its policy meeting, and Mario Draghi called for patience from German savers, who are now seeing higher inflation of 1.7% year on year. Draghi said that the increase in inflation was driven by a relatively transitory increase in energy prices, and that the ECB would continue very accommodative monetary policy until inflation was broad based and sustainable across the Eurozone.

The economic confidence index did hit one year highs in the Eurozone, maintaining the extremely positive momentum of the Eurozone's data. The German Producer Price Index, which rose 0.4% in December.

On the political front, Marine Le Pen is gaining support in France and has taken the lead in a major survey of voters' intentions for the first round of the presidential election. The populist leader of the National Front had between 25% and 26 % support compared with 23% to 25% for Republican candidate Francois Fillon. The French race has been closely watched as another crucial battle between populist and establishment forces. Le Pen has pledged to take France out of the euro if she wins. Under the French electoral system, the two leading candidates face each other in a run-off vote on May 7, presenting a significant hurdle to Le Pen. The poll didn't include data for the second-round vote.

The Dutch elections on March 15 are also gaining importance as the populist surge sweeps Europe and the US Almost all the opinion polls are in agreement: The anti-Islam, anti-European Union Freedom Party led by Geert Wilders is ahead and poised to win the largest number of seats.

China

The flood of domestic currency out of China became more of a trickle last month, signaling that policy makers' efforts to keep cash at home are taking effect. An equivalent of a net $900 million worth of yuan left China via payments in December, State Administration of Foreign Exchange data showed Thursday. That's less than 2% of the record amount in September, and compares with an average of $25.8 billion a month last year.

Also, China's economy accelerated for the first time in two years in the final quarter of 2016, cementing an economic stabilization that's giving leaders a buffer as they transition to neutral policy and prepare for potential trade tensions with Donald Trump. Gross domestic product increased 6.8% in the three months through December from a year earlier, compared with a 6.7% median estimate in a Bloomberg survey. Last year's 6.7 % expansion came at the expense of 15.4% loan growth, while outstanding credit likely rose to about 264% of GDP, fueling concern about financial frailty, Bloomberg Intelligence economists Tom Orlik and Fielding Chen wrote in a report. "China's economy ended 2016 with short-term growth firmly on track, but long-term sustainability veering further off it," they said.

With manufacturing also rebounding and deflation tamed, the central bank is turning to neutral policy to address a debt binge that inflated asset bubbles and may threaten the long-term outlook. Retail sales increased 10.9% from a year earlier in December, the strongest reading in a year and more than the projected 10.7% advance. Industrial production rose 6% in

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December from a year earlier, compared with an estimated 6.1% rise. Fixed-asset investment excluding rural areas expanded 8.1% for the full year.

China will cooperate with the incoming administration of Donald Trump to help promote healthy trade development and economic relations, a government spokesman said. Even, Chinese President Xi Jinping used his speech this week at the World Economic Forum in Davos to warn trade wars have no winners and protectionism should be rejected, his first public rebuttal of policies advocated by Trump, who has threatened to slap tariffs on imports from China. China's government also released plans this week to relax restrictions on foreign investment.

Russia

Russia has been seen as a potential beneficiary of Trump's administration. As the presidency becomes a reality, leading money managers are considering reducing holdings if they don't get evidence that he will take concrete steps to mend frayed relations, including lifting sanctions. A U-turn in US-Russian relation, which deteriorated to a post-Cold War low under Barack Obama, could prove hard to achieve in practice. Many key Republicans in Congress support keeping sanctions in place, particularly after intelligence agencies reported evidence last month that Russia was behind hacking during the November election. Trump himself conceded this month that he'd keep sanctions "for a period of time". Any further signs that the detente is all bluster could trigger a correction in a rally that has sent the ruble to a 17 month high, stocks to a record and Russian bond yields to levels last seen before the nation's invasion of Crimea in 2014.

Egypt

Egypt has created a "well-functioning" currency market which is reflected in the pound's current rate, the International Monetary Fund said, adding that the currency may strengthen after a period of adjustment since last year's float.

Government moves to reform the economy and growing investor confidence are underpinning the gradual return to levels achieved before the 2011 uprising that ousted President Hosni Mubarak, Deputy Finance Ahmed Kouchouk said. Foreign holdings of Egyptian debt rose by as much as $900 million after authorities floated the pound, he said in November. Egypt has been paying yields of about 20 % on domestic T-bonds and T-bills since the central bank raised interest rates on Nov. 3. In addition to dollars, the government may also issue yen- and yuan-denominated bonds as it seeks to reduce costs, the Finance Ministry said last month.

A marketing roadshow for Eurobonds worth as much as $2.5 billion begins in Abu Dhabi and Dubai on Tuesday, and will take in New York, Boston, Los Angeles before wrapping up in London on Jan. 23. Egypt plans to offer 5 year and 10 year maturities, and may consider a 30 year tranche. Egypt sees foreigners buying as much as $10 billion to $11 billion in local Treasury bills and bonds in the coming period, Finance Minister Amr El-Garhy said. Egypt is rated B3 by Moody's Investors Service, its sixth non-investment grade, alongside countries including Ghana and Pakistan.

UK

Reaffirming the current global scenario of markets being more reactive towards political news than the fundamentals, GBP saw the biggest decline in a month to as low as $1.1986 to reports from the Sunday Times about the main substance of Theresa May's speech indicating the prime minister could support a so called "hard Brexit."

"Sell the rumour, buy the fact" was a perfect description of price action on GBP. Having already sold sterling after the weekend's press reports on the contents of May's speech, the market seemed happy buying the pound on the news that Parliament will get a final vote on the Brexit package. The details of May's speech were almost exactly as reported on by media, suggesting that perhaps the Prime Minister had undertaken a deliberate communications strategy to price in the ostensibly sterling negative elements of her speech beforehand.

The blueprint involves quitting the single market, ending large payments to Brussels, clamping down on immigration and repatriating law-making powers. As for future trade, the prime minister wants to customize the EU customs union and

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replace it with a “bold and ambitious” accord in which Britain and the EU enjoy tariff-free trade yet the UK can strike its own commercial agreements with other nations. Her dream deal would take two years to land, would also let London-based banks provide services across the continent with ease, and would grant them and other companies time to adjust to the new order. May said that if she’s unable to get what she wants, she would be willing to remove the UK from the EU with “no deal” at all, even if that means trade duties.

GBP later rebounded and rallied the most since the 1990s after Prime Minister Theresa May promised a parliamentary vote on taking the UK out of the European Union. Investors await Europe’s reply to May’s Brexit plan for UK British businesses gave a mixed response. They welcomed the added insight and commitment to a transition, yet worried the loss of the single market will cost them trade and the threat of a standoff unnerved them. In the short term, companies are simply behaving business as usual. Bankers also praised the phasing in of regulations, but said they will continue to study whether to shift jobs to the EU to maintain access to it. May stroke a more conciliatory tone on the financial services sector at Davos, acknowledging its importance to the economy in an interview with Bloomberg. There was also an upbeat tone from HSBC’s CEO Stuart Gulliver, who, despite confirming that around 20% of the firms revenue generating operations would likely move to France as a direct result of Brexit, stated his belief that the “revenue impact of Brexit will on financial services will be made good in two or three years’ time”.

Headwinds emerging from hard Brexit include employment growth could turn negative, unemployment to pick up, inflation to increase. Even though UK economy could slowdown but a recession, as expected prior to Brexit vote is not on the horizon.

Scotland will vote to become independent within two years due to the hardline position being taken by British Prime Minister Theresa May over Brexit, former Scottish first minister Alex Salmond said on Friday.

On the economic front,

GBP slid during the week after a report showed UK retail sales fell at the fastest pace in almost five years last month, recording a 1.9% drop. Possible explanations include price increases and consumers scaling back purchases after taking advantage of Black Friday discounts the previous month. Mild weather also probably affected clothing sales, down 3.7% on the month, though the weakness in the sector was broad-based, with turnover at food, household goods and department stores all falling. Consumer confidence is weakening and employment growth has stalled while real household disposable incomes are being eroded by higher prices. Consumer-price inflation jumped to 1.6%, according to a report earlier this week, and is forecast to keep climbing through 2017. At the same time retailers themselves are going to see profit margins squeezed by higher import costs due to weaker GBP.

The Unemployment Rate was steady at 4.8%, and over the three months ended November wage growth averaged 2.8%, a slight improvement on the last reading. But there were signs of slowing in the details of the report which showed that the total number of people in work had actually fallen slightly, and that in the month of December alone, wage growth had slowed. The next several months of developments in the labor market will prove crucial, as businesses process the new information recently revealed by the Government about the nature of Brexit.

Jason Granite
Chief Investment Officer
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Contact us
T: 020 3793 7424
T: 0161 886 8000
F: 0161 886 8002
www.frenkel topping.co.uk

Please see FTIM Safety First portfolio performance on the next page

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Frenkel Topping Investment Management's ("FTIM's") Safety First performance

	2016		Since launch (29 Apr – 31 Dec 2016)	
	Performance	**FTIM Volatility***	**Performance**	**FTIM Volatility***
FTIM Safety First 1 is currently a cash product with returns in line with base rate				
FTIM Safety First 2	1.53%	1.42%	1.07%	1.26%
FTIM Safety First 3	3.26%	1.91%	2.33%	1.70%
FTIM Safety First 4	4.38%	2.93%	3.13%	1.98%
FTIM Safety First 5	5.63%	3.23%	3.68%	2.68%
FTIM Safety First 6	10.10%	5.04%	7.53%	4.87%

Date: 31 December 2016
Source: FTIM / FE Analytics
Safety First Portfolio strategies were launched on 29/04/16. From 31.12.16 performance is being reported on a quarterly basis starting 31st March 2017. All figures are on a bid - bid, total return basis and are quoted net of underlying fund charges, our DFM fee of 0.6% including VAT and a platform fee of 0.2%. Advice charges would depend on the charges made by your independent financial adviser. The deduction of these charges would reduce the performance shown.
Actual Past Performance Data is from 29/4/16 only as the models only launched on this date and therefore 5-year performance data is not available and 12-month performance figures are not able to be shown. Pre - launch performance from 4/1/16 – 29/4/16 is Simulated Past Performance.
The figures represent performance of a model portfolio; individual account performance may differ if your account does not follow the model.
Past performance is not a reliable indicator of future performance. Investment values can go down as well as up and may be affected by exchange rate variations.

*Volatility is a measure of the movement in the price of an asset around its average return. The higher the volatility the more risk involved in the investment.