06 March 2017

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INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Investors show confidence in Trump reflation trade

KEY MESSAGES:

Investors were unmoved by Trumps lack of policy detail. Focus shifted towards a rate hike by the Fed in upcoming policy meeting this month.

Global stocks kissed record levels before paring gains by the end of the week. USD weakened over rate hike concerns. GBP declined on poor UK Services figures. US 10-year treasury yield was 2.48% while 2-year treasury yield touched 1.3% briefly. Oil remained at $52 per barrel, as US stockpiles rose. Gold was down 2.3% for the week.

Euro area headline inflation came up at 2% in February. A point of attention was the inflation pick up in Japan, while its sustainability is still questioned. PMIs in euro zone and China rose while those in UK fell.

Market developments during the week

The most awaited President Trump's address to Congress, like earlier instances, turned out to be low on policy detail. He set out his main areas of policy focus but left for later the details of what specific measures he wants to take, how they will be funded, and when they will be implemented.

While U.S. stock futures pared their gains slightly, while Trump was still on his feet, markets were generally unmoved by the rhetoric and showed their confidence in the Trump reflation trade. Since Trump's election, stocks have shown few signs of slowing down. The S&P 500 has advanced 10%, posting 17 record closes in a rally that's added $2.8 trillion in value to the U.S. equity market. Even fundamentals are playing a part in the market's gains. The economy has shown signs of accelerating and corporate earnings are predicted to surge 12% from last year, a turnaround from the profit declines in 2015 and 2016. This asset class still has pockets of value, with current P/E ratio of 21 for the Dow Industrial and 25 for the Nasdaq 100. Developed markets, like that of the UK, represent more attractive relative value, trading on an average P/E ratio of around 13 and yielding 4%.

This clearly shows that markets aren't stretched. Though, in the coming weeks, we see headwinds emerging from political uncertainty in Europe, Brexit negotiations, and the Federal Reserve moving quicker than expected. While we remain alert to the possible triggering of volatility by above events, we retain our confidence in the fundamentals that underlie these equity valuations. Also, global growth figures, a strong jobs market and a build-up of inflationary pressures are generally pointing to better economic conditions in the future, further strengthening our supportive view of equities.

While President Trump's address left markets unmoved, the main market driver was the growing possibility of a Fed rate hike in March, which dominated the USD performance over the week. The increased probability of a March move was spurred by several Fed speakers, the latest being the hitherto dovish Lael Brainard, who suggested conditions may "soon" be propitious for raising rates. Futures traders scrambled to guard against an interest-rate increase by the central bank. A combined record 438,000 contracts traded in April and May Fed Funds as odds for March jumped to 68%. Also, emerging-market borrowers are selling bonds at an unprecedented pace before the Federal Reserve raises interest rates. Weekly inflows into emerging-market bonds funds were running at a rate of more than $1 billion in February, according to EPFR Global. Borrowers are being helped by robust demand from investors seeking respite in the 4.7% average yield offered by emerging-market bonds compared with about 2.4% from 10-year U.S. government notes.

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The February US employment report on March 10 may further guide the Fed in its decision at its March 14-15 meeting.

Currencies

USD weakened for the first time in 6 days in anticipation that the Fed will raise rates this month.

The euro strengthened 0.3% to $1.0541.

GBP slid 0.3% after a measure of the U.K. services sector expanded less than forecast.

Equities

S&P 500 futures were down 0.3%.

The Stoxx Europe 600 index slipped 0.5%, paring its weekly gain to 1% following in the footsteps of U.S. and Asian shares, as traders waited for Janet Yellen to give her verdict on the path for interest rates.

The equity markets were rallying during the week, with the U.S. and U.K. indices setting records on Wednesday. Japanese stocks jumped to the highest level since December 2015. By Friday, stocks pared their strong weekly gains.

Bonds

U.S. government bonds extended losses into a fifth day. Yield on 10-year Treasuries was little changed at 2.48%.

The two-year yield, the coupon most sensitive to Fed actions, touched 1.336% on Thursday, its highest since 2009.

Commodities

Oil gained less than 0.1% to $52.63 per barrel. It has been sliding, as record-high U.S. crude stockpiles were seen jeopardizing OPEC's efforts to drain a global surplus, even though Saudi Arabia's February shipments fell.

Gold slipped 0.5% to $1,228.16 an ounce. It's down 2.3% for the week, after four straight weeks of advances.

Copper was little changed, after Thursday's 1.4% drop. Iron ore fell 2.9%.

Other major economies:

Euro area

Euro-area inflation accelerated to the fastest pace since January 2013. Consumer prices rose 2% in February from a year earlier, according to the European Union's statistics agency in Luxembourg. Rising oil prices are cited as the reason for pushing up inflation across the euro area, including in Germany, Spain and Italy. In a sign of further increases ahead in the euro area, producer-price growth jumped to its highest level in almost five years, rising 3.5% in January on annual basis. Meanwhile, the euro area's core inflation, which strips out volatile elements such as energy, was unchanged for the third consecutive month in February at 0.9%. ECB focuses on core inflation, as Draghi pointed to a new set of criteria arguing that the return to the ECB's inflation goal must be durable, self-sustained and representative of the euro area as whole.

Euro-area unemployment was unchanged at 9.6% in January, as per statistics agency Eurostat. German unemployment continued to decline in February. The number of people out of work fell by a seasonally adjusted 14,000 to 2.59 million, data from the Federal Labor Agency showed on Wednesday.

Euro-area manufacturing accelerated for a sixth month in February, to 55.4, with signs of inflation pressures building in the economy. Companies' economic outlook remains favorable, IHS Markit says. Companies raised output prices at the fastest pace in more than five years as higher commodity prices and a weaker euro drove up costs. Suppliers took longer to fill orders. Manufacturing expanded in all of the region's major economies, with activity strongest in the Netherlands, Austria and Germany. Greek output contracted.

On the political front, independent French presidential candidate, Emmanuel Macron, opened up his biggest lead yet over Republican Francois Fillon and began narrowing the gap with National Front leader Marine Le Pen, helped by endorsements and his rivals' legal troubles. Two polls at the beginning of the week gave Macron the support of 25% of the French electorate going into the first round of the presidential election, two points behind Le Pen. By the end of the week, Francois

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Fillon's woes deepened, as a stream of elected officials from his party disowned his campaign and police searched his Paris home on Thursday.

China

The Chinese growth target for this year has been cut to around 6.5%, down from 6.5% to 7% last year, Premier Li Keqiang announced while addressing the National People's Congress (NPC). Mr Li said he would tackle state "zombie enterprises" producing more coal and steel than the market needed. Though similar pledges in the past have proved hard to fulfil.

This is the unpredictable nature of China's influence on commodities, particularly steel and coal. On the imports front, China remains the largest consumer of a range of commodities from iron ore to soybeans. China has long sought to be the price-maker, rather than a price-taker, for the raw materials it needs. It remains well positioned to curb supply pressures which would then have an evident impact on global prices of commodities. On the exports front, China maintains its strong position which markets perceive as enough to export inflation to the world. For the global economy, it's the pass-through of China's rising costs via exports that matters. Chinese manufacturers long squeezed by increasing wages have been raising their asking prices.

China's producer prices in January have increased the most since 2011, further lifting the outlook for global inflation. Producer price index rose 6.9% in January from a year earlier, more than estimated. The consumer-price index climbed 2.5%, versus a 2.4% rise forecast. Producer prices for mining products surged 31 % year-on-year while those for raw materials climbed 12.9% as per the National Bureau of Statistics.

With such a strong foothold in commodities, particularly in coal, China is now considering reinstating output restrictions that cap the output at an equivalent of 276 days of capacity after the heating season ends in mid-March. China sent coal prices and mining shares on a tear last year after President Xi Jinping's government imposed output restrictions aimed at easing an oversupply and supporting indebted miners. As production slumped, officials scrambled late in the year to boost output ahead of peak winter demand. The possible reinstatement of curbs comes as benchmark coal prices have fallen more than 10% from their recent peak in November. The NDRC wants coal prices in a range of 500 yuan to 570 yuan a ton.

As China is working to maintain foothold in the global marketplace, economic performance has come as a relief. China's manufacturing PMI firmed at 51.6 in February, as producer prices rebounded before the upcoming National People's Congress, which will set the administration's growth target for the year. Steel industry PMI climbed to 51.4. Non-manufacturing PMI stood at 54.2 versus 54.6 in January.

Japan

The Bank of Japan's preferred measure of consumer prices rose for the first time since December 2015, offering some hope that inflation will begin inching toward Governor Haruhiko Kuroda's 2% target this year. Household spending dropped, even as the job market tightened. Consumer prices, excluding fresh food, increased 0.1% in January from a year earlier. Excluding fresh food and energy, prices rose 0.2%. Bank of Japan is counting on oil and a weak yen to help CPI. Yet the sustainability of any price gains in Japan remains unclear, particularly given tepid consumer spending and slow wage growth. More clues on the outlook will come after the BOJ's next policy meeting, which ends on March 16.

Russia

The "Trump Trade" that sent Russian stocks to record high appears to be unwinding. While President Trump comes under increasing pressure from Republican senators to keep sanctions in place, the Russian Government has toned down fawning coverage of the U.S. president by state news outlets. Russia's benchmark Micex Index retreated more than any other stock gauge in the world this month as optimism deflates over prospects for an easing of sanctions under President Donald Trump. In a further sign that investor interest is starting to sour, the world's biggest exchange-traded fund that tracks Russian equities last week logged its largest outflows in 9 months. A lot of the optimism over a possible relaxation of

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sanctions is being priced out. Also a slowdown in the pace of gains in Brent crude after a surge at the end of last year has made stocks of Russian energy exporters among the worst performers this month.

UK

On the Brexit front, the House of Lords voted to amend legislation enabling Theresa May to activate Article 50, adding a clause that requires the government to unilaterally guarantee the right of EU citizens currently in the UK to remain. The Bill will now return to the House of Commons, with the Government's official plan still being to trigger article 50 this month.

Also, the Times reported that Theresa May's team is preparing for Scotland to potentially call for an independence referendum. This risks further GBP declines.

On the economic front, IHS Markit's gauges for manufacturing and the dominant services sector fell in February, with both readings coming in below estimates. While the construction index rose, that wasn't enough to stop the composite Purchasing Managers Index falling to a six-month low of 53.8 from 55.5. GBP/USD fell after its publication and was down 0.3% to $1.2226.

Consumer borrowings softened as U.K. consumer credit remained below average in January. Unsecured lending rose by GBP1.4 billion ($1.7 billion) from December, below the GBP1.6 billion averaged over the previous 6 months, according to Bank of England data.

The figures add to evidence that consumer spending, the engine of the U.K. economy, is losing momentum as living standards come under pressure from rising food and fuel costs. The squeeze on households from faster inflation is the result of the pound's precipitous fall since the Brexit vote. The currency move has had mixed effects for manufacturing, making goods cheaper for overseas buyers while also boosting costs for producers. The factory report also showed that export orders rose for a ninth month in February, and the weakness of the pound helped boost demand from Europe, the U.S. and Asia. Nevertheless, rising input costs are probably outweighing any boost to exports.

UK household confidence weakened this month and Bank of England policy makers expect real incomes to be eroded as the slump in the pound boosts inflation above its 2% target. That's a threat to consumption, one of the main pillars of the economy recent strength.

U.K. house prices gained 0.6% from January, a third month of gains. The research was presented by Nationwide, which doesn't provide a regional breakdown, though other reports suggest the market is weaker in London.

The construction industry showed signs of weakness last month, with a gauge of demand dropping for a second month. Markit said its overall index of construction activity flat lined in January. But homebuilding increased at the slowest pace in six months and commercial building declined. Growth in new orders was the weakest since October. Some respondents to IHS Markit's monthly survey said that rising input costs had an "adverse impact" on decision-making and led to delays in contracts. The "intense" inflation was largely due to imports, reflecting the impact of the pound's decline since the Brexit vote in June.

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

	2016 Performance	2017 Performance	Volatility* 04/01/16
FTIM Safety First 2	1.53%	1.25%	2.07%
FTIM Safety First 3	3.26%	1.61%	2.42%
FTIM Safety First 4	4.38%	2.00%	3.30%
FTIM Safety First 5	5.63%	2.62%	3.60%
FTIM Safety First 6	10.10%	3.63%	5.29%

Date: 06 March 2017
Source: FTIM / FE Analytics

Safety First Portfolio strategies were launched on 29/04/16. 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.