23 June 2017

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INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Oil slides into bear territory

KEY MESSAGES:

Global equity markets gave mixed signals. U.S. stocks fell the most in a month, retreating from all-time highs, as crude oil slid into bear territory.

Crude dropped below $43, heading for a fifth weekly decline on concern the global supply glut will persist.

USD gained, 10-year Treasuries yielded 2.16%. Havens were in demand with gold closing at $1,257.5 an ounce.

GBP dropped amid Brexit concerns. Britain kicked off exit negotiations with the EU. Theresa May appeared to have softened her stance over Brexit deal, after losing her parliamentary majority.

Market developments during the week

Weakness in energy prices were the theme of the week, with oil in New York and London dropping into a bear market on concerns that expanding supply in the U.S. and Libya will counter output cuts from the OPEC. This led energy stocks and the main indices lower, which were just bolstered by a rebound in tech shares. With little in the way of economic data, Fed speeches took centre stage, as markets continue to expect a September pause and a December interest rate hike. Federal Reserve Bank of New York President, William Dudley put himself on the same side as Fed Chair Janet Yellen, stating that he also expects inflation to rise due to the currently tight labour market in the US. While Harker and Evans put an emphasis on waiting for further proof to hike again. Also in focus were the newly-started negotiations on Britain's split with the European Union. As Brexit talks kicked off, residency rights and clearing of euro-denominated financial instruments were among the first issues making headlines.

The week was low on economic releases from the US, with the only significant economic data release pertaining to housing activity. Existing home sales surprised on the upside posting a 1.1% rise to a 5.62 million annual rate in May as reported earlier this week by the National Association of Realtors. Meanwhile, sales in the smaller and more volatile new home market, also rebounded in May. Also, median sales price surged 16.8%. Record prices for new U.S. homes amid a sales pickup indicate the supply of houses may be tight at the lower end of the market, pinching first-time buyers. Any supply rebound may be a ways off, as new-home construction starts are down in recent months and permits were at a one-year low in May, according to government data.

Among other releases were weekly unemployment claims, which once again recorded low levels last week at just 241,000, while the Conference Board's leading index of forward looking economic indicators rose 0.3% in May.

Like economic releases, there was slightly low activity in Trump administration updates, with the major ones being Senate Republican leaders issuing a long-awaited health-care proposal aimed at winning over both the moderate and conservative wings of their party. However, their draft bill was immediately opposed by a group of four GOP senators, opening way for further negotiations. Their opposition could threaten passage of the bill as the Republicans can only afford to lose two GOP votes amid unanimous Democratic opposition. Senate Republicans' proposal to replace Obamacare would provide an additional $50 billion over four years to stabilize insurance exchanges.

Intensifying the worsening relations with North Korea, President Donald Trump said Tuesday that efforts by China to rein in North Korea have failed, suggesting he's weighing new options to deal with a regime that's vowed to develop nuclear weapons capable of striking the U.S. mainland.

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Currencies

The Bloomberg Dollar Spot Index is up 0.4% for the week, after rallying at the start of the week on Fed rate-hike expectations.

The euro roughly closed at same levels as last week at $1.12 closing an uneventful week overall.

The pound dropped 0.5% over the week to $1.2718.

The yen rose 0.27% to 111.2 per dollar.

Equities

The S&P 500 Index rose 0.82% to 2,435. Health-care shares have surged 3.5% in the week as Senate unveiled overhaul plan, while the energy group is down 2.8% as oil slides into bear territory. Nasdaq's biotech ETF pushed its four-day rally past 9%. The rebound in biotech comes on signs that the Trump administration has softened its stance on drug pricing.

The Stoxx Europe 600 Index slipped 0.2% over the week, extending the longest run of weekly losses in a year as U.K.-listed stocks struggled on the anniversary of Britain's vote to leave the European Union. The FTSE 100 Index saw a 0.5% weekly decline to 7,421.

The MSCI Emerging Markets Index rose 0.4%.

Chinese stocks were little moved by their addition to MSCI Inc.'s benchmark indexes, as investors weighed the symbolic importance of inclusion against the limited impact on short-term inflows. The Shanghai Composite Index swung between gains and losses for much of the trading session on Wednesday, before a late-afternoon rally lifted it to a 0.5% advance.

MSCI also announced including Saudi Arabia on its watch list for potential classification as an emerging market. The country's Tadawul All Share Index leaped 5.5% on Wednesday, the most since August 2015, as traders embraced a trio of key announcements, the other ones being ruler King Salman enacting a palace shakeup and restoration of a raft of benefits for state employees.

Global markets appear to be in a strange sweet spot. Last week, the Federal Reserve, the Bank of Canada and the Bank of England shifted to a more hawkish tilt, relative to market pricing, and, arguably, underlying core price pressures. The result was treasuries, global stocks and risk assets rallied, and market expectations about the path of U.S. interest rates stayed stubbornly dovish, all while subdued inflation and price expectations across advanced economics flatten the yield curve. In other words, falling inflation is spurring further asset reflation, as markets discount the Fed's hawkish rhetoric, while easier financial conditions intensify the positive feedback loop. At the same time, U.S. stock market indexes are continuing to make new highs while the Chicago Board Options Exchange Volatility Index (VIX), which measures option-implied S&P 500 volatility, is near its lowest level since 1993. Even as conditions call for a healthy dose of caution, there is no need to panic longer term as we remain positive on the fundamentals underlying the valuations.

Bonds

The yield on 10-year Treasuries added one basis point to 2.16%. It's virtually unchanged for the week. Mid-week, yield slipped to 2.1511%, near the lowest since November, signaling increasing doubt on the Fed's ability to cut its balance sheet and aggressively push borrowing costs higher. Bond traders are ramping up wagers that the Federal Reserve is done raising interest rates until December which is being reflected in the buying and selling of call spreads on futures contracts.

German 10-year bund yielded three basis points lower compared to last week at 0.25%.

U.K. 10-year gilt yields rose one basis point to 1.03%, led by losses in shorter-dated securities as U.K. money markets push odds of a rate hike by the end of 2017 over sixty per cent.

Commodities

Oil headed for a fifth weekly decline with futures edging up 0.5 % in New York after losing nearly 5% since the start of the week.

West Texas Intermediate for August delivery was at $42.97 a barrel. Total volume traded was about 20% below the 100-day average. Prices have fallen 21%

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from their peak in February; a bear market is defined as at least a 20% drop.

Brent for August settlement was at $45.50 a barrel on the London-based ICE Futures Europe exchange, up 28 cents. The global benchmark crude traded at a premium of $2.53 to WTI.

Concerns dragging the oil towards decline include expanding U.S. crude production, Libya is pumping the most in four years and oil stored in tankers rose to a 2017 high earlier this month. A committee tasked with monitoring compliance to the OPEC-led cuts gave only cursory attention to the possibility of deepening existing curbs.

A report Wednesday from the Energy Information Administration showed U.S. oil production increased to the highest since August 2015. The U.S. oil production rose by 20,000 barrels a day last week to 9.35 million, the EIA reported Wednesday. While crude stockpiles slid by 2.45 million barrels to 509.1 million, a steeper decline than forecast in a Bloomberg survey, inventories remain about 100 million barrels above the five-year average. Also U.S. drillers continued to add rigs increasing the rig count by six to 747 last week. Rigs targeting crude in America climbed for a 22nd straight week, the longest uninterrupted stretch of growth in three decades, according to data from Baker Hughes Inc.

Libya’s oil production has risen to about 900,000 barrels a day after some fields restarted and the country’s biggest deposit, Sharara, increased output. Libya, exempt from the OPEC deal, plans to boost output to the highest since 2013 by the end of July.

Gold gained 0.3% over the week to end at $1,257.5 an ounce as crude’s slump this week stoked concern reflation will remain tepid.

Other major economies:

Euro area

The week was quite low on economic releases from the euro area as well. Few major releases include German Producer Price Index numbers which came out slightly lower than expected at 59.3 after 59.5 last month, as did the German Current Account surplus. Overall, the Eurozone Manufacturing Purchasing Managers data performed very well, reading 57.3 for the month. Services PMIs for both releases were below expectations but in growth territory. The German Producer Price Index showed a 0.2% month on month decrease this morning, slightly lower than the 0.1% decrease which was expected.

The political risks emanating from France further faded as President Emmanuel Macron’s party and its allies won a comfortable majority in the French parliament, securing 350 out of 577 seats in yesterday's second-round vote, cementing a legislative majority that will easily allow him to pass his reform program. French stocks jumped the most since May on the news with the CAC 40 climbing 0.9%. The French benchmark is up 9.2% this year, outperforming the broader European gauge. While the victory wasn't the landslide some polls had predicted, and turnout was a record low for the vote, it does bolster the President's legislative agenda. The new parliament meets for the first time in the coming week, with labor-market reform at the top of the agenda, a task that has eluded French presidents for generations. The government is being watched both domestically and internationally because France’s 3,000-page labor code is blamed for discouraging hiring and keeping French growth below the euro-area average. Unemployment in France is roughly double that of Germany and the U.K., helping Le Pen to attract her party’s biggest ever vote in May’s presidential runoff. Luckily for Macron, he’s inheriting an economy showing signs of a cyclical improvement for the first time in years, with consumer confidence at its highest in a decade.

Regarding the other regions in the euro area, the spread between Italian and German bonds is being watched by the investors as it approaches its lowest point since January. This difference between prices of the two bonds is considered a strong indicator of risk appetite in the market, with the perceived safety of German bonds contrasting with the perceived high-risk status of Italian bonds. The difference in pricing fell as news was released that the Italian parliament will not follow through with its controversial electoral reform law, further reemphasizing that market confidence in Europe continues to increase. Despite this, we should remain cautious that two Northern Italian banks, Veneto Banca and Banco Populare di Vicenza, remain in deep trouble, and thus further market turmoil on the horizon does still remain.

Canada

At the start of the week with the price of oil being trimmed by 16% last month and continue to experience an acceleration of a price decrease in the last three days, being down 4.5%, the CAD usually followed suit on the direction of the oil price movements. However, the loonie defied the fall in crude oil prices, reversing its declines from earlier in the week. A very strong print in monthly Retail Sales data was the primary driver, as sales rose 0.8% in April after strong growth in March. The figures strongly supported comments made earlier in the week by Bank of Canada deputy Governor Carolyn Wilkins, who spoke favorably of the economy's near-term prospects and talked up the possibility of a hawkish shift at the BoC. Inflation eased for a fifth straight month. While soft inflation is likely to keep the Bank of Canada on hold through July, the pick-up in economic momentum offers good grounds for an October rate hike.

China

The week's major highlight relating to China was the announcement by MSCI Inc. of approval of Chinese-listed stocks in its global benchmarks. The $6.8 trillion onshore market is the world's second-largest and accounts for 9% of global stock value, but was rejected for index inclusion three times by MSCI over issues including capital controls and long trading halts. The MSCI decision will add 222 China A-share stocks starting in May 2018.

Meanwhile, investors continue to grapple with a series of regulatory surprises. The latest bombshell came Thursday, when shares slumped on news that the government had stepped up scrutiny of the nation's most active overseas acquirers. Later, stocks swung higher amid speculation of support from state funds.

Other economies

Saudi's Tadawul All Share Index leaped 5.5% on Wednesday, the most since August 2015, as traders embraced a trio of key announcements, the MSCI Inc' announcement of putting the country on watch list for potential classification as an emerging market, ruler King Salman enacting a palace shakeup and restoration of a raft of benefits for state employees. The developments may continue to drive up Saudi equities for investors who anticipate inflows from passive funds, an emboldened economic-reform platform and consumers with more cash to spend. Banks were the biggest winners, although almost every sector of the 172-member index advanced. Trading volume more than doubled its 30-day average. Meanwhile, the retroactive restoration of benefits to state employees is a boon because the government is one of the country's biggest employers and a driver of economic growth. Removal of the bonuses and allowances in September sparked a 3.8% decline in Saudi Arabia's benchmark index.

Qatar dispute with the Saudi alliance continued into the fourth week, with the latest update being Saudi Arabia and its allies presenting Qatar with a list of steep demands to end the crisis. The 13 requirements include shutting the Al-Jazeera TV network, cutting back diplomatic ties with Iran, severing relations with the Muslim Brotherhood and ending Turkey's military presence in Qatar are predicted by diplomats as likely to be refused. Qatar's foreign minister said his country wouldn't bargain away what it sees as its sovereign rights and called on the Saudi alliance to conduct negotiations in a "civilized way," after first lifting the blockade. He said Qataris were united behind their emir, and called Al-Jazeera and foreign policy as internal affairs not open to negotiation.

Argentina sold 100-year bonds barely a year after settling a protracted legal dispute tied to a $95 billion default. With the $2.75 billion sale, the government of South America's second-largest economy joins Mexico, Ireland and the U.K. in issuing debt that matures over a century, which is often particularly attractive to insurers and pension funds seeking to lock in long-term returns. Argentina, for its part, is taking advantage of historically low borrowing costs to finance the budget and pay off debt that's maturing in the next few years. Its debt now yields an average of about 4 %age points more than similar-maturity U.S. Treasuries, less than one-third the

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level of just four years ago. Argentina's issuance comes as global money managers flock to emerging-market funds, pumping in $38.6 billion in 20 straight weeks of inflows.

UK

Nearly a year after the Brexit vote, negotiations began this week in Brussels with confusion remaining on what the U.K. wants from the breakup. The negotiations kicked off with little fuss as the British team agreed to the EU's timetable for talks, which leaves any trade deal discussion until after the terms of exit are agreed. The UK had been petitioning that the terms of a trade deal with the European Union were negotiated at the same time as settling the divorce bill. The EU, conversely, wanted "substantial progress" on the divorce bill before entering trade negotiations. Despite the lead UK negotiator, David Davis, having predicted that this would be the "row of the summer", the EU's logic has appeared to have very quickly won through, eliminating the first of, albeit many, potential hurdles in the negotiations.

Exit talks only kicked off this week, and the U.K. has just until March 2019 to secure a deal with the bloc. Prime Minister Theresa May, whose two-year program was announced in Parliament on Wednesday by Queen Elizabeth II, will have to juggle opposition from all sides as her minority government tries to pass laws to implement the divorce.

Without a majority for her Conservatives in the U.K. Parliament, Theresa May now says she will work to reflect the wide range of views on Europe that exist in Britain, a signal her Brexit policies could soften. By the end of the week, she presented a proposal to EU leaders to safeguard the rights of their citizens, stating that no EU citizens living lawfully in Britain at the point it leaves the bloc in March 2019 would be asked to leave. Those who had lived in Britain for five years would have "settled status" and would be eligible to the same healthcare, pensions, benefits and education rights as British nationals.

On the domestic front, her legislative program has become more complex, as officials admit that lawmakers in Scotland could be given a separate vote on the prime minister's plans for leaving the EU. May said her officials are in talks with their counterparts in Scotland over whether the Edinburgh parliament will be legally required to give its consent to the so-called Repeal Bill, which paves the way for Brexit. The bill will overturn more than 80,000 pieces of EU law that apply across Scotland as well as England, Wales and Northern Ireland, covering everything from trade to workers' rights.

The pound dropped below $1.26 during the week as traders see many risks on the horizon with a cloud of uncertainty remaining over both U.K. leadership and the outlook for Brexit negotiations.

The pound also sank as Bank of England Governor Mark Carney emphasized his dovish stance, saying he's still worried about the impact of Brexit on the local economy. However, the Bank of England's policymakers are increasingly split over the need to raise interest rates for the first time in a decade. A 5-3 vote last week in favour of keeping borrowing costs unchanged was closer than expected, and on Wednesday the BoE's chief economist surprised investors by saying he was close to voting for a rate hike too. Some Monetary Policy Committee members argue that rising inflation requires a hike, especially at a time when they believe the economy is running at close to full capacity. But the majority say slow wage growth and Brexit uncertainties justify keeping rates at a record low.

Exporters also are still enjoying free and direct access to the EU's single market of 500 million consumers. The Bank of England said Wednesday that weaker sterling and strong global growth are supporting manufacturing and overseas sales. A measure of factory orders jumped to the highest in almost 30 years this month as export demand improved. The CBI orders index jumped to 16 in June, from 9 in May. Its export gauge rose to 13, the strongest reading in 22 years. That boost will probably come to an end under May's Brexit vision, and most economists agree there will ultimately be negative economic impacts from potential tariffs, less migration and lower investment.

Looking ahead, the MPC's August meeting is now a potential time for a hike, and incoming data, especially pertaining to inflation and wages, will be crucial over the coming months. Industrial Order

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Expectations Index from the Confederation of British Industry showed order books at their strongest level since 1988, underlining just how positive sterling weakness has been for the manufacturing sector, which represents some 10% of the economy.

Jason Granite
Chief Investment Officer
23 June 2017

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

	2016 Performance	2017 Performance	Volatility* 04/01/16
FTIM Safety First 2	1.53%	0.09%	2.36%
FTIM Safety First 3	3.26%	0.32%	2.65%
FTIM Safety First 4	4.38%	0.66%	3.44%
FTIM Safety First 5	5.63%	1.10%	3.80%
FTIM Safety First 6	10.10%	2.12%	5.21%

Date: 23 June 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.

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