21 July 2017

frenkel topping
INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Dovish tone from the BoJ and ECB

KEY MESSAGES:

In the US, politics were again at the forefront, with reports that US special counsel Robert Mueller is expanding his investigation of President Trump.

The Bloomberg Dollar Index recorded a weekly loss of 0.8 per cent. GBP closed at 1.30 per USD. Despite the unchanged policies and dovish tone from the BoJ and ECB both the yen and euro strengthened.

S&P 500 closed at 2,473. The Stoxx Europe 600 saw the first weekly decline with exporters leading declines due to euro strength.

US 10-year treasuries yielded 2.24 per cent. WTI Crude closed at $47.11 a barrel. Gold closed at $1,251.5 an ounce.

Market developments during the week

Increased hawkishness from the ECB has helped the euro rally from lows last seen near the start of the millennium, with investors expecting tapering to start in the new year and pricing in a 10-basis point rate hike by September 2018. In the US, politics are again at the forefront, with reports that US special counsel Robert Mueller is expanding his investigation of Trump less than a day after the president told the New York Times that any digging into his finances would cross a red line.

President Donald Trump continued attempts to achieve milestones to his campaign promises asking Senate Republicans to stay in Washington until they repeal Obamacare, two days after GOP efforts to enact a new health-care law collapsed after public opposition from four Republicans. Investors now expect President Donald Trump is more likely than ever to end his first year in office without a single major legislative accomplishment as he won't release the broad outlines of his tax overhaul plan until September. The last time Washington did a major tax bill, in 1986, it took more than a year. A $1 trillion infrastructure plan is little more than a talking point now. Congress ignored his budget proposal. Republicans are as divided on these issues as they are on health care. Lawmakers haven't even given Trump money to build his border wall. The worsening political situation for Trump could well turn around this coming week if Trump Jr survives his congressional interrogation and Pence and Mcconnell rally to Trump's support and crack the republican whip on Obamacare.

Away from Politics, it was relatively a light week on the economic docket. US data was robust but not market-moving, with investors looking forward to FOMC and Q2 GDP next week. Major release was US Jobless claims which turned out to be at 9-week low showing a decline of 15k to 233k. Filings fell close to the lowest level since 1973, which shows that employers in the US are hesitant to fire workers as finding qualified applicants becomes increasingly difficult.

Currencies

The Bloomberg Dollar Index recorded a weekly loss of 0.8 per cent. The greenback weakened against most of its G-10 peers as investors assess an investigation into US President Donald Trump that may stall his economic agenda.

The yen closed at 111.3 per dollar, losing 1.06 per cent over the week.

The euro gained 1.6 per cent this week, its second straight five-day advance, closing at 1.16 per USD. The euro strength came on bets the ECB will start tapering its stimulus program. It appears that the euro's rally may have only just begun and could still have further to run with the central bank likely to announce the scaling back of its quantitative easing program in either September or October. At the same time, political risks have largely dissipated. The victory of market-friendly Emmanuel

21 July 2017

frenkel topping

INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Dovish tone from the BoJ and ECB

Macron in France allayed fears after a populist wave swept through the European Union following the Brexit vote and the election of Donald Trump as president of the US Economic growth has also picked up, helping to buoy investor prospects.

GBP closed at 1.30 per USD, losing 0.76 per cent over the week.

Equities

S&P 500 closed at 2,473 gaining 0.57 per cent over the week. Stocks surged Wednesday on earnings strength, with the S&P 500 Index and Nasdaq Composite Index hitting records. Every S&P 500 sector was higher, with energy stocks and materials companies pacing the rise.

According to Bank of America Merrill Lynch’s most recent fund manager survey, allocations to US stocks have reached 20 per cent underweight. The survey was conducted with participants overseeing $586 billion in assets. Investors said the Nasdaq Composite Index was the most crowded trade for the third straight month. Banks overtook tech stocks as the most overweight sector in the survey. That suggests that investors might be trying to lock in profits and find greater value elsewhere. When naming the biggest risks to the markets right now, the three biggest tail risks cited in the survey were a crash in global bond markets, the Federal Reserve or European Central Bank making a policy mistake, and Chinese credit tightening.

The Stoxx Europe 600 saw the first weekly decline in three down 0.8 per cent, with gains in telecom and oil stocks balanced by a drop in automobile companies. Exporters lead declines on euro strength after ECB President Mario Draghi said on Thursday that officials will reassess stimulus in autumn. More volatility is expected coming week as more than half the companies in the Euro Stoxx 50 Index report results, including Daimler AG, Deutsche Bank AG and Banco Santander SA.

The FTSE 100 Index closed at 7,469 gaining 1.23 per cent over the week.

A 24-week pouring of new money into emerging market bond funds, driven by investors fleeing near-zero yields on developed country debt, is losing steam. Net inflows to the asset class fell more than two thirds to $200 million last week, according to research from Bank of America Merrill Lynch citing EPFR Global data. That’s a third consecutive weekly decline and raises the prospect of an imminent end to the longest winning run of flows in four years.

Bonds

The yield on US 10-year Treasuries fell nine basis points to 2.24 per cent.

Benchmark yields in Germany dropped ten basis points to 0.5 per cent, yields in France dipped three basis points.

UK 10-year Gilts closed yielded 1.18 per cent gaining thirteen basis points over the week.

Commodities

Oil headed for a second weekly increase as US crude inventories continued to shrink. US crude inventories slipped 4.73 million barrels last week and nationwide total crude and product inventories tumbled by 10.2 million barrels to 1.32 billion, the lowest level since December, data from the Energy Information Administration showed Wednesday. Meanwhile, US crude production is at the highest level since July 2015. Futures in New York rose nearly 1.2 per cent this week, extending a 5.2 per cent jump in the prior period. While prices in London briefly rose above $50 a barrel on Thursday for the first time in six weeks, skepticism remains about the effectiveness of the OPEC production cuts before meetings in Russia in the coming days. West Texas Intermediate for September delivery was at $47.11 a barrel, up 19 cents. Total volume traded was about 28 per cent below the 100-day average.

Brent for September settlement was up 0.5 per cent to $49.53 a barrel. The contract slipped 40 cents to $49.30 on Thursday. Prices are up 1.3 per cent this week. The global benchmark crude traded at a premium of $2.43 to WTI. Concern is growing that the deal may fray after OPEC member Ecuador said this week that it won’t be able to maintain its pledged cuts. The announcement comes as the deal to cut output among members of the OPEC was already coming under pressure, with compliance falling below 100 per cent in June.

frenkel topping
INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Dovish tone from the BoJ and ECB

However, supply-side stories that normally affect prices aren't having as much impact now. The demand side is also under concern with China's fuel demand weakening as efforts to cut pollution see some of the country's drivers turn to cars fired up by natural gas. The IEA last month cut its estimate for China's 2017 total oil demand growth by 4 per cent to 385,000 barrels a day.

Copper advanced 0.8 per cent to $6,004 a ton, leading a rally in industrial metals.

Gold rose 0.9 per cent to $1,251.5 an ounce and was poised for its first back-to-back weekly advance since June 2 at 1.86 per cent.

Other major economies:

Euro area

One of the major events that markets were keenly observing was the ECB meeting. In his press conference, Draghi read out an assessment of the economic outlook that was very similar to the one he offered in June, when he called for colleagues to allow the central bank's stimulus time to work. He stated policy makers are still waiting for inflation to catch up with the economic recovery putting off discussions on winding back stimulus until after the summer. With less than half a year of quantitative easing left, policy makers have been debating publicly as to when they might start reducing asset purchases. His comments follow what seemed to be a shift in stance three weeks ago, when he said that renewed reflationary forces may provide room for "adjusting the parameters" of current stimulus, while keeping the level of accommodation broadly unchanged. Draghi suggested the message he delivered three weeks ago had been overinterpreted. He said much was made of the word "reflation" and little has changed in the outlook for price growth. Economists predict the first official decision on the future of the policy path will be announced in September, when the Governing Council next meets and publishes new projections. ECB staff are studying various options for how bond-buying might eventually be wound down, according to euro-area officials familiar with the matter. Draghi said committees haven't been asked to assess scenarios.

The International Monetary Fund agreed to a new conditional bailout for Greece worth as much as $1.8 billion, ending two years of speculation on whether it would join in another rescue and giving the seal of approval demanded by many of the country's euro-area creditors. The disbursement of funds is contingent on euro-zone countries providing debt relief to Greece. IMF officials estimate that, even if Greece carries out promised reforms, the nation's debt will reach about 150 per cent of gross domestic product by 2030, and become "explosive" beyond that point. European creditors could bring the debt under control by extending grace periods, lengthening the maturity of the debt or deferring interest payments, the IMF said in a report accompanying the announcement.

Having the IMF co-finance Greece's rescue program was a key demand of many of the country's euro-area creditors, led by Germany, who see the fund's participation as ensuring the credibility of the reforms the country is asked to implement. But upcoming elections in Germany also made it impossible for Berlin to concede to any further debt relief for Greece, pushing instead for all decisions to be taken at the end of the country's bailout in the summer of 2018, and only if needed. While the fund's decision helps both the IMF and Germany stick to their guns, it does mean the issue will likely arise after the German elections in the fall, when the question of whether Greece will receive any loans from the IMF resurfaces.

A much-anticipated Greek return to bond markets this week has been held off partly due to a 325 billion-euro ceiling set by the IMF on the amount of debt the country can hold. The cap is such that the country can't issue any more debt until it repays some of what it owes, meaning it has to wait until at least July 20 when it will pay another 4 billion euros ($4.6 billion) on bonds held by the European Central Bank. Using possible workarounds like debt swaps, that could improve Greece's maturity profile without increasing the overall load, the government is waiting on how markets react to the IMF's debt sustainability analysis before a possible foray as soon as next week. Greek bonds rallied on the news of the deal, with yields on notes across maturities hitting successive multi-year lows. Yields on 2019 notes rose 4 basis points to 3.5 per cent on Wednesday morning in Athens.

21 July 2017

frenkel topping
INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Dovish tone from the BoJ and ECB

China

Economic growth continued at a robust pace in the second quarter, with GDP expanding at a better than expected 6.9 per cent. A rebound in industrial output, which rose 7.6 per cent in June from a year earlier, far exceeded economists' estimates for a 6.5 per cent increase. The onshore yuan traded near the highest level in eight months after the growth figures were released. The expansion highlights the resilience of China’s economy, as activity has remained robust even as policy makers have tried to curb excessive and speculative borrowing, leading to a slowdown in money supply growth.

Domestic stocks tumbled after authorities warned about the build-up of debt across the economy, calling the problem a "gray rhino", a highly probable, high-impact threat that people should see coming, but often don’t. While up to now policy makers have focused on a build-up of liabilities at smaller banks and big private-sector companies, President Xi Jinping has made clear that local government authorities and China’s behemoth state-owned enterprises too must restrain borrowing. Xi’s comments at a top financial-regulatory gathering last weekend were the latest signal of determination to head off any future destructive debt-bubble deflation.

Japan

The Bank of Japan announced it was maintaining its policy position unchanged, while yet again delaying the deadline to hit 2 per cent inflation for a sixth time. The decision means the bank is increasingly out of step with its developed-world peers. By again delaying the timing for hitting its price goal, the BOJ acknowledged the need to continue easing for at least several more years, probably beyond 2020 because of a sales-tax increase scheduled for late 2019. The central bank raised its growth forecasts slightly for this year and next, but noted in its policy statement that the risks to inflation and growth are skewed to the downside. The BOJ is under pressure to explain when, and under what conditions, it might begin an exit. Its asset buying, mainly of Japanese government bonds, has swelled its balance sheet to nearly the same size as Japan’s economy.

Yet in its own region, Asia, the BOJ is far from alone. While the People’s Bank of China is turning to open market-operations and lending tools to curb excessive leverage in parts of the financial system, it’s holding benchmark rates at all-time lows to keep growth humming. Slowing inflation in India has put the prospect of more easing back on the table, and the regions’ smaller central banks are also signaling no rush to raise borrowing costs.

On the economic front, Japan returned to Trade Surplus of 439.9 billion yen ($3.9 billion) in June, with both imports and exports continuing the strong growth they have had all year. Exports rose 9.7 per cent from a year earlier (estimate 9.5 per cent). Imports increased 15.5 per cent (estimate 14.4 per cent).

Australia

The Aussie Dollar slumped after officials say market misread minutes. Minutes of the Reserve Bank of Australia’s July meeting released Tuesday included a discussion of the level of the neutral interest rate, which was estimated at about 3.5 per cent, a long way from the current 1.50 per cent. Traders interpreted the discussion as a signal that rate hikes were on the way and sent the Australian dollar soaring, effectively tightening conditions in the economy.

On the regulatory front, Australia’s big four banks rallied in Sydney trading as new capital requirements turned out to be less onerous than expected and the financial regulator signaled they may not get any higher. The decision to raise capital requirements is the latest element of regulatory efforts to ensure the country’s large lenders can weather any downturn, particularly in the property market. Home loans account for more than 60 per cent of domestic bank lending in Australia and the regulator has grown concerned that existing capital rules don’t reflect this concentration of lending and risk. Property prices in the country’s biggest cities have soared in recent years, stoking fears of a house price bubble.

Saudi Arabia

In Saudi Arabia consumer prices dropped again in June, reflecting the nation’s worst economic slowdown since 2009 as the kingdom struggles to cope with low oil prices. The economy shrank 0.5 per cent

21 July 2017

frenkel topping

INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Dovish tone from the BoJ and ECB

year-on-year in the first quarter amid lower oil output and cutbacks in spending to shore up public finances. However, the reinstatement of public sector benefits and bonuses, and the introduction of value-added taxes in 2018 should support a return of positive inflation.

UK

The second round of Brexit talks wrapped up in Brussels. French Finance Minister Bruno Le Maire used a hearing in the French parliament to take a hard line on what the EU believes the UK owes the bloc in terms of liabilities and obligations. France insisted that the UK pay a Brexit bill of as much as 100 billion euros ($115 billion), underlining the hurdles to substantial progress in negotiations toward a new relationship with the European Union.

Reports by the Guardian indicated that the UK cabinet will accept the free movement of EU citizens for up to four years after Brexit as part of a transitional deal. The news comes after a meeting between the prime minister and British businesses in which companies stepped up pressure on Theresa May to avoid a so-called hard Brexit.

Citizen rights have become the first major stumbling block in negotiations with Brussels as the issue is a red line for both sides. We believe there is worse to come and that the negotiations will be more complicated, volatile and turbulent than many expect.

Price growth in the United Kingdom unexpectedly slowed to 2.6 per cent in June, weakening the case for a Bank of England rate hike in the near future.

The Bank of England makes its' next policy decision on August 3. The pound dropped from a 10-month high to trade at $1.3026 after the data was released. Core inflation dropped to 2.4 per cent from 2.6 per cent in May. Investors lowered the odds of a hike this year to about 40 per cent from 50 per cent after the inflation data, according to short sterling trades.

Britain reported a larger-than-expected budget deficit last month as rising inflation pushed up debt payments. Net borrowing was 6.9 billion pounds ($9 billion), up from 4.8 billion pounds in June 2016. It left the shortfall in the first three months of the fiscal year at 22.8 billion pounds, up 9 per cent on the year. The figures highlight the risks facing the public finances as rising prices and stagnant wage growth take their toll on the economy. Spending was also driven by a surge in payments to the European Union and a 12 per cent increase in government spending on goods and services. The UK economy is creaking but arguably this is being disguised at present. We remain bearish.

The figures may raise fresh questions about whether Chancellor of the Exchequer Philip Hammond can limit borrowing to 58 billion pounds this year, as forecast by his budget watchdog in March. It seems increasingly unlikely.

UK retail data showed a rebound of 0.6 per cent in June, ahead of forecasts, as warming temperatures boosted clothing sales. This followed a 1.1 per cent decline in May. Overall sales rose 2.9 per cent from a year earlier, up from growth of 0.9 per cent in May.

What is increasingly clear to me is that the UK economy is increasingly fragile and risks on the downside outweigh risks to the upside. There are some very troubling signs and we have positioned the Safety First portfolios to protect against these risks.

Jason Granite
Chief Investment Officer
21 July 2017

21 July 2017

frenkel topping

INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Dovish tone from the BoJ and ECB

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

	2016 Performance	2017 Performance	Volatility* 04/01/16
FTIM Safety First 2	1.53%	0.89%	2.40%
FTIM Safety First 3	3.26%	1.26%	2.69%
FTIM Safety First 4	4.38%	1.69%	3.45%
FTIM Safety First 5	5.63%	2.30%	3.81%
FTIM Safety First 6	10.10%	3.46%	5.17%

Date: 21 July 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.