01 September 2017

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INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Strengthening economic backdrop despite geopolitical tensions

KEY MESSAGES:

U.S. stocks rose after data underscored the resilience of the American and Chinese economies and concern over North Korea shifted to the background.

Payroll report revealed 156k jobs added in August. Unemployment rose to 4.4% and wages climbed 0.1% month on month. U.S. Q2 GDP was revised upward to 3%.

USD was little changed after trading near its lowest level in more than 2 years. GBP closed at $1.30. The S&P 500 Index rose 1.4% this week and closed at 2,478.

US 10-year treasuries yielded 2.14%. WTI Crude traded at $47.1 a barrel.

Gold rose 2.3% to $1,320.7 an ounce.

Market developments during the week

The week started with renewed geopolitical tensions after reports that North Korean fired a missile over Japan. President Trump said that all options are under consideration in response to the latest provocation. The United Nations stated that it strongly condemns the action, but did not seek to escalate sanctions against the Pyongyang regime. The initial market reaction to the test was a sharp rush into haven assets, which saw the yen and gold rallying, while the yield on 10-year U.S. Treasuries dropped below 2.1% for the first time since November. We took advantage to deploy capital into attractive US and European risk assets and within days, while Asian markets were initially jolted by the news, investors largely shrugged off the North Korea risk. So far this year the Kospi is up 17%, while the won has strengthened 7.2%, making it the best performer after the Thai baht among Asia's emerging currencies.

Later in the week US stocks recorded gains and the dollar strengthened after data bolstered optimism that the American economy is on a firm footing. The August employment report may have been almost predictably disappointing, though it wasn't weak enough to call into question the underlying strength of the U.S. labor market. The data marked the seventh straight August that the government's initial take on payrolls fell short of the median estimate of economists, with 156,000 jobs added compared to a projection of 180,000 in a Bloomberg survey. Yet the bigger picture shows a still-healthy labor market in a mature expansion. One bright spot in the report was a surge in manufacturing and construction employment. The jobless rate rose to 4.4% and wages climbed less than forecast at 0.1% month on month, up 2.5% year on year, in a break from otherwise solid progress in the labor market. The report may represent the cleanest reading on the labor market for several months, as Hurricane Harvey's fallout in the Houston region begins to affect the data in coming weeks. While the storm may depress payrolls at first, jobs will probably get a subsequent boost as construction and utility workers help rebuild housing and infrastructure. We remain bullish on the US economy but concerned about the risk of a stronger £ -v- $.

Other data releases were more encouraging for the economy. The University of Michigan's consumer sentiment survey showed Americans in the first eight months of this year have been more upbeat than at any comparable period since 2000. Households are growing increasingly optimistic about employment and the economic outlook, a positive sign for spending.

U.S. manufacturing expanded in August at fastest pace since 2011, driven by employment gains, figures from the Institute for Supply Management showed Friday. Factory index climbed to 58.8 from 56.3 in July. Steady increases in consumer spending and business investment are delivering sustained gains in manufacturing, which bodes well for third-quarter economic growth.

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U.S. second-quarter growth was revised upward to 3% annualized rate from previous quarter; revised from the initial estimate of 2.6%. The revision shows the fastest pace in two years backed by stronger household spending and a bigger gain in business investment, putting the economy on a stronger track, the Commerce Department data showed Wednesday. The revision puts to bed concerns about the pace of GDP growth from earlier in the year, when many observers took note of the disparity between "hard" and "soft" data in the US economy. Substantial positive revisions to Q2 US GDP indicated stronger momentum going into the third quarter than previously thought, with Hurricane Harvey expected to shave 0.1-0.4 ppts. off growth in Q3.

Hurricane Harvey was the strongest storm to hit the U.S. since 2004 when it struck near Rockport as a Category 4 hurricane. After drenching Texas, Tropical Storm Harvey regained strength over the waters of the Gulf of Mexico and crashed ashore again Wednesday in southwest Louisiana. The U.S. has lost 10% of its fuel-making capacity as refineries in the region are shut. Resultantly, Gasoline surged to the highest in two years and crude oil fell with discount between WTI Crude and its international benchmark Brent widening to the biggest spread in two years. We think oil is approaching a point where it will be attractive to add as an asset class exposure. Gold broke through $1,300 an ounce as investors weighed the damage from the Tropical Storm. Our Safety First portfolios benefitted from this over the past weeks.

The White House responded to the situation with promises to put the full resources of the federal government behind the recovery efforts. Republican House leaders plan to vote next week on President Donald Trump's expected request for $5.95 billion in initial disaster relief funding for Hurricane Harvey victims, but they don't plan to include a U.S. debt-limit increase in the legislation putting them at odds with President Trump, who's considering asking Congress to combine an increase in federal borrowing authority with the aid package.

The move is intended to lower the risk of an unprecedented default as soon as the end of the month. Treasury Secretary Steven Mnuchin has repeatedly said that it's critical that Congress raise the debt ceiling by Sept. 29. Even market angst is growing as Congress has only a limited number of working days remaining to raise the debt ceiling. The spread between one- and three-month Treasury bills has shrunk to around 8 basis points from as high as 24 basis points in May as investors have started demanding higher rates on one-month paper relative to three-month securities in order to compensate for default risk. If the debt-limit increase isn't included in the initial disaster funding, Congress might not act until the U.S. is on the verge of a default. The next chance to include increased borrowing authority in a broader measure would be when Congress considers a stopgap spending bill to keep the government open. We remain negative on the $ -v- £ and are positioned accordingly having hedged our USD $ risk in our client portfolios.

There was also an update on Nafta talks as the second round of talks to update the agreement got underway in Mexico on Friday. Negotiators from the U.S., Canada and Mexico are expected to focus on topics including e-commerce and investment. Discussions take place under a cloud of President Donald Trump's threat to withdraw from the pact as he called Nafta the worst trade deal in history that resulted in the decimation of U.S. manufacturing and the outsourcing of jobs to Mexico. The three countries are expected to hold the third round of talks in Canada later in September.

Currencies

The Bloomberg Dollar Spot Index was little changed after trading near its lowest level in more than two years. Decline was spurred by comments from Treasury Secretary Steven Mnuchin that a weaker currency yields trading benefits and a weak inflation report.

The euro closed at levels similar to last week at $1.19 after reports that the European Central Bank may not be ready to finalize its decision on next year's bond-purchase plan until before the current program expires in December. The euro has advanced more than 14% against the dollar this year on speculation that the European Central Bank will outline its intent to scale back its extraordinary package of

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quantitative-easing measures in the autumn. Demand is expected to continue as we inch closer to next week's monetary-policy review by the ECB.

The Canadian dollar was the best performer among major currencies Thursday amid better-than-expected economic growth, gains in gold and crude oil and a shift forward in expectations for the next Bank of Canada rate increase. The loonie climbed more than 1 % versus its American counterpart and advanced against all of its G-10 peers. Traders focused on stronger-than-expected Canada second-quarter economic growth and priced in a greater chance that the nation's central bank will hike rates at its meeting next week.

GBP closed at $1.30. It was 0.78 % higher over the week.

Yen gained 0.64 % to close at 110.1 per USD.

Equities

U.S. stocks rose as reports showing a gain in consumer sentiment and an increase in manufacturing offset a mediocre August employment report. The S&P 500 Index rose 1.4% this week and closed at 2,478. U.S. tech stocks are also back at record highs, helping the S&P 500 Index in this weekly gain.

The Stocks Europe 600 Index gained a third day, with media companies among the winners.

The U.K.'s FTSE 100 Index rose 0.5% during the week to close at 7,438.

Bonds

The yield on 10-year Treasuries fell three basis points to 2.14%, while the two-year notes yielded 1.34%.

UK 10-year Gilts yielded 1.06%, 0.95% higher over the week.

Germany's 10-year yield remained at last week levels at 0.38%.

Japan's benchmark bond yield fell below zero percent for the first time since November.

Commodities

West Texas Intermediate crude fell 1% this week and closed at $47.1 a barrel.

Gold rose 2.3% to $1,320.7 an ounce.

The LME Index of six industrial metals soared to the highest in almost three years, with copper leading the charge. Gasoline prices fell up to 2% to $1.743 a gallon. The average U.S. price for regular gasoline at the pump rose 7 cents Thursday to $2.519 a gallon, the steepest single-day increase since April 5, 2007, according to data from AAA, the largest U.S. motoring group. Harvey, which made landfall twice along the U.S. Gulf Coast, bringing torrential rains and floods, shut pipelines and took 4.15 million barrels a day, or 22%, of U.S. refining capacity offline, data compiled by Bloomberg showed. Retail gasoline prices have risen by 17 cents a gallon since Aug. 25, the day Harvey first made landfall, and the motor fuel is likely to extend its rally, according to an AAA forecast.

Other major economies:

Euro area

Last weekend, investors were keen to watch ECB President Mario Draghi's speech at Jackson Hole, expecting some indications relating to rollback of monetary stimulus. At his speech, Draghi appeared to temper expectations about any winding down of purchases, saying a significant degree of monetary accommodation is still warranted.

The appreciating euro is becoming a growing concern for the local companies. The common currency has climbed some 13% versus the dollar since the start of the year, causing a tightening of monetary conditions. While ECB President Mario Draghi chose not to mention the euro's appreciation in his Jackson Hole speech on Friday, European central bank officials expressed concern about the currency's strength in the minutes from their last meeting on July 20.

On economic front, consumer prices in the euro area rose 1.5% in August, the highest reading in four months and slightly more than economists' expectations. The acceleration, which is almost exclusively due to energy prices, follows stronger than expected inflation readings for Germany, France and Spain. Spanish Consumer

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Price Index inflation fell slightly short of expectations, while Germany's Consumer Price Index edged up 0.1% in August, as expected. The French Consumer Price Index, in the meantime, rose 0.5% in August, after a sharp 0.3% decline in July. Euro-area core inflation, which strips out volatile elements such as food and fuel, held at a tepid 1.2%.

Euro area economic confidence touched a decade high. An index of industry and consumer sentiment increased to 111.9 in August from a revised 111.3 in July, the European Commission in Brussels said on Wednesday. The unemployment data showed a rate of 9.1%. However, this hasn't yet translated into significantly faster inflation and rising wages, despite the central bank's negative deposit rate and its $2.7 trillion bond-buying program.

Unemployment in Germany fell by a seasonally adjusted 5,000 to 2.532 million with the jobless rate remaining at 5.7%, the lowest since reunification. Chancellor Angela Merkel's record of falling unemployment, stable growth and a balanced budget has helped her maintain a double-digit lead over Social Democratic challenger Martin Schulz as she bids for a fourth term in Sept. 24 election. We are not expecting any surprises.

The Governing Council is set to start deliberations about the future path of quantitative easing when it meets on Sept. 7. With a booming economy showing few signs of being matched by a sustained pickup in inflation and a surging euro threatening to further damp price pressures, policy makers probably won't rush an exit.

Canada

Hurricane Harvey is impacting Canada via higher gasoline prices and lower crude oil prices. However, strong gross domestic product growth data totally overshadowed falls in crude oil prices to give the Canadian dollar a major boost. Monthly Canadian GDP data showed the economy growing at a rapid 4.5% annualized rate, underlining the likelihood of a near term rate hike from the Bank of Canada. Strong consumption growth was the primary driver of the rapid increase in GDP. Other releases indicated Canada's Current Account deficit was smaller than expected in the first quarter.

China

China's manufacturing PMI rose to 51.7 in August, ahead of expectations, as industrial output defied a broader slowdown in the economy. The rebound suggests the resilience of the economy at times where policy makers are increasingly attempting to curb financial risks. The challenge ahead for policy makers is to balance preserving the pace of growth with slowing the pace of credit expansion as economists are warning that debt-fueled growth before the Communist Party congress is unsustainable. One thing that may give the country's leadership some cause for optimism is the possibility that the yuan, at its highest level in more than a year, is slowly but surely becoming more attractive as an international alternative to the dollar. We are not so sure. We see more downside than upside in the yuan.

India

Markets speculation of a rate cut by the central bank boosted and a rally was seen in the Indian sovereign bonds as data showing an unexpected slowdown in GDP. Q2 GDP figures came in at 5.7%. The yield on government notes due May 2027 fell four basis points on Friday to 6.49%, set for its biggest drop since July 10. It climbed six basis points in August, as a steeper-than-expected rebound in inflation reduced bets of more easing by the Reserve Bank of India following a rate cut on Aug. 2. The rupee fell 0.1% to 63.97 per dollar in Mumbai.

UK

Sterling climbed versus all of its Group-of-10 peers after the IHS Markit's factory Purchasing Managers Index rose to 56.9 from 55.3 in July. This marks the strongest pace of expansion in manufacturing in four months, lifted by both export orders and domestic demand.

Other data releases include a surprise contraction for the Nationwide House Price Index, which fell 0.1% after last month's 0.2% increase. This brought year on year house price growth down to 2.1%, down from 2.9% in July. Existing pressure on household finances got a mention as a possible driver of the fall in prices, as did wider economic conditions.

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Money and Credit data from the Bank of England was released without incident, showing Mortgage Approvals creeping up slightly, while lending to private non-financial businesses put in a second strong month of expansion.

On the Brexit front, another round of talks failed to yield a breakthrough, as the EU and the British government remain at loggerheads over the U.K's financial obligations, the enforcement of citizens' rights and even the sequencing of talks. The pound fell to a one-week low after Brexit negotiations between the U.K. and the European Union ended in acrimony.

It was also clear from the press conference delivered by Michael Barnier and David Davis that no substantive progress had been made on the key issues with Michel Barnier stating that the third round of talks were far from seeing sufficient progress.

European Commission President Jean-Claude Juncker said at a press conference that none of the U.K. position papers published ahead of the latest round of talks on Britain's exit from the EU are satisfactory.

Sterling's losses contributed to the currency's biggest monthly decline since October. However, implied volatility in sterling is the among the lowest in the Group-of-10 countries over the next three months.

This despite the failure of the third round of separation talks with the European Union this week, a possible threat to Prime Minister Theresa May's leadership at the Conservative Party Conference next month and an October EU summit, where leaders will decide if sufficient progress has been made to proceed to the next phase of negotiations.

Slowly but surely the daily intrigue of the Brexit negotiations is being overlooked by financial markets and the focus is starting to return to economic fundamentals and relative value. We remain of the view that on that basis £ seems attractive and have positioned the portfolios accordingly.

Jason Granite
Chief Investment Officer
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Frenkel Topping Investment Management's ("FTIM's") Safety First performance

	2016 Performance	2016 Volatility	2017 Performance	2017 Volatility	Volatility since inception *04.01.16
FTIM Safety First 2	1.53%	1.42%	1.88%	3.48%	2.40%
FTIM Safety First 3	3.26%	1.91%	2.27%	3.61%	2.66%
FTIM Safety First 4	4.38%	2.93%	2.78%	4.10%	3.38%
FTIM Safety First 5	5.63%	3.23%	3.53%	4.54%	3.73%
FTIM Safety First 6	10.10%	5.04%	4.89%	5.20%	5.03%

Date: 05 September 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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