22 September 2017

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INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

North Korea tensions ratchet up

KEY MESSAGES:

North Korea threat resurfaces. Fed stood pat on the interest rate and continues to forecast a hike by year end. It announced a plan to commence shrinking its balance sheet in October. Amid a war of words between US and North Korea, USD fell the most in two weeks. Yen rallied the most in two weeks. Oil recorded its third monthly gain for 2017. WTI Crude closed at $50.60 a barrel. Gold closed at $1,296.7 an ounce.

The S&P 500 Index remained at the 2,500 level. European stocks were led higher by Germany's DAX, after economic data bolstered investor sentiment. Germany goes to the polls on Sunday, with Chancellor Angela Merkel expected to secure a fourth term.

Market developments during the week

The focus on monetary policy dominated market attention this week, but later shifted towards geopolitics, as fears about North Korea surface yet again. The USD pared all the post-Federal Markets Open Committee meeting gains, as a risk-off tone permeated markets with the yen and gold advancing. At the same time, treasury yields slipped from this week's highs.

The US imposed new sanctions on North Korea, which is a concern for markets, and Russia threatened to bomb US troops if its own troops were fired upon. Trump and Kim continue their increasingly hostile war of words over North Korea's weapons program, which ultimately led to North Korea indicating it could test a hydrogen bomb in the Pacific Ocean.

Domestically, President Trump is facing a critical deadline for continuing his travel ban. He hinted towards broadening the initial ban, which is set to expire on Sunday, in his response to a terrorist attack in London last week. Even mere renewal of the prohibition on entry into the US by most citizens of those nations would reopen controversy over an action that provoked sharp criticism from prominent corporate leaders, multiple court challenges and internal strife within the White House.

Meanwhile, the GOP continues to struggle for the votes needed to pass a wider package of 'repeal and replace' measures for the Obamacare bill while time is running out for a resolution. Senator John McCain stated he can't support the bill, further dimming prospects for a final push to repeal Obamacare.

The major event earlier in the week was the Fed policy meet. The central bank stood pat on the interest rate and continues to forecast a hike by year end, saying hurricane damage won't derail an otherwise healthy expansion. This caught markets by surprise, as can be reflected in the implied probabilities of an interest rate hike in December, which jumped from near 20% to above 60% in a matter of minutes. In the statement, the Fed set October for the start of their previously announced plan to shrink its $4.5 trillion balance sheet becoming the first central bank in history to reduce its QE program. Officials announced the reduction process will start next month at a pace of $10 billion a month, which will gradually increase to $30 billion a month. This would take over 30 years to finalize the process.

Economic releases this week include US household wealth increased in the second quarter to yet another record, driven by solid gains in financial assets and rising property values, figures from the Federal Reserve in Washington showed Thursday. The increase in household wealth reflects steady growth in house prices. A strong job market and low inflation also are allowing Americans to improve their purchasing power, helping to sustain household spending, the biggest part of the economy.

The report also showed companies had almost $2.3 trillion in liquid assets, giving them the means to boost investment.

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US Housing Starts and Permits for August 2017 reflected homebuilding surprising to the upside in August, even amid negative impact of Hurricane Harvey's during the final days of August. Markets had anticipated a 1174k print, but homebuilders broke ground on 1180k units, from an upwardly revised July figure (+35k). Although the continued effects of Hurricane Harvey, in addition to Hurricane Irma, will lead to a cooling in September's housing starts, this activity will be recouped as the year progresses. With an estimated minimum 20k houses destroyed in the two hurricanes combined, residential investment will receive a boost in the fourth quarter of 2017 and first half of 2018 as rebuilding begins, with additional, but diminishing impacts likely to be felt in the quarters thereafter.

US Existing Home Sales for August 2017 reflected a decline of 1.7% to 5.35 million (annualized), marking the fourth decline in five months. Analysts expected an uptick of 0.2% on the month. This marks another disappointing report, with existing home sales now having contracted for three consecutive months. Although Hurricane Harvey, which disrupted activity in the last week of August, is partly to blame for this month's weakness, low inventory levels nationwide are also a concern.

Currencies

USD fell 0.3%, the most in two weeks amid war of words between US and North Korea leading to probability of North Korea testing a hydrogen bomb in the Pacific Ocean. This also lead a rally in yen which rose the most in two weeks as demand for safe haven assets spurred. Yen saw 1% rise this week, closing at 111.9 per dollar.

The euro advanced 0.8% to $1.2.

The British pound declined 0.7% to $1.35

Equities

The S&P 500 Index remains at the 2,500 level.

European stocks were lead higher by a jump in Germany's DAX after economic data bolstered investor sentiment. Germany's DAX gained 0.6% this week.

Asian stocks closed slightly lower into the weekend following the increase in North Korea tensions. Japan's Topix index fell 0.3% at the close in Tokyo and South Korea's Kospi index slid 0.7%.

Hong Kong's Hang Seng Index lost 0.8% and the Shanghai Composite Index dropped 0.2%.

The MSCI Asia Pacific Index declined 0.2%.

Bonds

The yield on 10-year Treasuries rose five basis points to 2.25%.

Germany's 10-year yield advanced two basis point to 0.45%.

Britain's 10-year yield rose five basis points to 1.36%.

Commodities

Oil recorded its third monthly gain for 2017. WTI Crude for November delivery rose 1.5% this week and closed at $50.60 a barrel. Total volume traded was about 37% below the 100-day average. Brent for November settlement climbed to $56.77 a barrel. The global benchmark crude traded at a premium of $6.17 to WTI.

It has advanced this month on forecasts for rising crude demand and as US Gulf Coast plants recover from Hurricane Harvey, which halted almost a quarter of the nation's refining capacity.

The OPEC concluded a gathering on Friday with no decision on an extension or deepening of supply cuts. Russian Energy Minister Alexander Novak said the cartel and allied producers can wait until at least January to consider prolonging the output limits. Nine months into their agreement, implementation of the pledged 1.8 million barrels a day of production cuts remains high. Still, the group has yet to find an answer to the problem of rising US shale output, which has undermined their efforts. The next key event will be a Nov. 30 meeting of OPEC ministers.

The weekly report from the Energy Information Administration showed that US stockpiles of gasoline hit a 22-month low, suggesting that refiners need to crank up

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their crude processing. US crude stockpiles rose to 472.8 million barrels last week.

Gold advanced 0.2% to $1,293.93 an ounce.

Copper declined 0.2 % to $2.93 a pound, the lowest in more than five weeks amid a deepening rout in industrial metals.

Other major economies:

Euro area

Investor sentiment in the Euro area was boosted by positive numbers, indicating faster growth just before Sunday's German vote. IHS Markit's index of private-sector activity jumped to a four-month high of 56.7 from 55.7 in August. Both services and manufacturing strengthened, with a gauge for the latter reaching a level not seen in more than six years. Markit said the economy showed a burst of activity in September and its surveys point to economic growth of 0.7% over the quarter. That would be the fastest since the start of 2015.

Separate reports on Friday showed improvements in both Germany and France this month, with the PMI for both nations hitting the highest in more than six years. For Germany, IHS Markit said the PMI rose to 57.8 from 55.8 in August, with both services and manufacturing strengthening. As with France, the index is far above the key 50 level that divides expansion from contraction.

The widely followed ZEW survey was released, with the crucial German Economic Sentiment indicator rising sharply to 17, an improvement from last month's level but below the long-term average of 23.8. The eurozone index also rose, although by slightly less than expected. The improvement in business sentiment is notable due to the looming German election, normally a source of uncertainty.

The economy's outlook got another upgrade this month in Bloomberg's latest economic survey. Gross domestic product is now forecast to rise 2.1% this year, up 0.1 percentage point compared with August. That's the eighth positive reassessment in the past year. The European Central Bank also raised its forecasts this month, to 2.2%.

Germany goes to the polls on Sunday, with Chancellor Angela Merkel expected to secure a fourth term, although she may not win an outright majority. Euro's one-week implied volatility is the evidence, which has plummeted about 170 basis points this month.

Canada

Canadian Manufacturing Sales fell 2.6% in July, the sharpest drop in more than a year and significantly faster than expected by most forecasters. A sharp drop in motor vehicles was the primary driver, and sales rose 0.2% once these are excluded. Retail sales rose in July, up 0.4% month-on-month, although slight downward revisions to the June figures broke what would have been a 5-month streak of increased spending. July's gains were entirely due to price increases. The all-items consumer price index for August ticked up to 1.4% on a year-on-year basis in August. On a month-on-month, seasonally adjusted basis, prices rose 0.1%, the first increase since this past May. An uptick in underlying inflation is somewhat encouraging and suggests that inflation may have stabilized in the last couple of months.

Japan

The BOJ left policy unchanged Thursday, as expected. The central bank has kept the 10-year bond yield around its target of zero per cent since introducing its yield-curve control policy last September, while managing to bring down spending below its annual guidance of about 80 trillion yen ($712 billion). The benchmark 10-year bond yield held at 0.03 % after ranging between minus 0.015% and 0.15% in 2017. However, it has failed to spur inflation which remains stuck at 0.5%, just a quarter of the BOJ's 2% target.

China

China has been in the news since start of 2017 for various reforms undertaken by the government to curb its credit situation. This week it was informed that policy makers at the People's Bank of China are drafting a package of reforms that would give foreign investors greater access to the financial services industry. The yuan's 6.1% advance this year has given the country greater freedom to loosen capital controls,

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as deflation risks are now largely off the table. On the domestic front, property prices declined in some of the China's hottest markets last month, indicating that cooling efforts are proving effective. New-home prices, excluding government-subsidized housing, gained in 46 of 70 cities tracked by the government in August, compared with 56 in July, the National Bureau of Statistics said on Monday. That was the smallest number of increases since January. Prices fell in 18 cities from the previous month and were unchanged in six.

Following Moody's footsteps, in a matter of four months, S&P Global Ratings cut China's sovereign credit rating one step to A+ from AA-, citing the risks from soaring debt, and revised its outlook to stable from negative. The downgrade represents ebbing international confidence China can strike a balance between maintaining economic growth and cleaning up its financial sector. China's Finance Ministry responded that S&P ignores the country's sound economic fundamentals and that the government is fully capable of maintaining financial stability if it strengthens supervision and controls credit risk.

While a sovereign-rating cut would generally trigger a boost in yields and an extra layer of difficulty for its companies looking to raise cash offshore. China's bond markets barely reflected it. China's debt landscape, over the longer term, appears to be much more insulated than for other developed and even emerging nations, given the Communist Party's top-down control of the economy and financial markets.

Post China downgrade, S&P also stripped Hong Kong of AAA rating to AA+ indicating the potential spill over risks to the SAR should deleveraging in China prove to be more disruptive than the rating agency currently expects. It's the second time this year Hong Kong's rating has been cut in response to a China downgrade. Moody's Investors Service in May lowered the finance hub's rating and changed the outlook to stable from negative after it cut China for the first time since 1989.

Mexico

Early September results on inflation in Mexico reflected a slowing trend after it reached its fastest pace in 16 years last month. Consumer prices rose 6.53% from a year earlier, compared with 6.74% in the second half of August, the nation's statistics institute said Friday. Core prices rose 4.9% from a year earlier and 0.28% from the previous two weeks, compared with a 0.3% median analyst estimate. Mexico's central bank left its key interest rate unchanged last month at 7% after seven consecutive hikes, saying inflation will slow to its 3% target by the end of next year. The peso has rebounded from a record low in January, easing inflation pressures, on expectations the nation's trade deal with the US can be updated in a constructive way, despite President Donald Trump's threats to end it.

UK

Sterling fell against all of its Group-of-10 peers, as Prime Minister Theresa May let down investors through her much-awaited speech in Florence. Markets were keen to get some signals on her Brexit vision, but the speech turned out to be scant on details. She proposed for the first time to pay to maintain trading links with the European Union for up to two years beyond Brexit, but failed to outline specifics. May said the UK stood willing to cover the cost of EU membership beyond March 2019, in return for a transitional period which mirrored the status quo of tariff-free, regulation-light commerce. The sum could run to about 20 billion euros ($24 billion).

GBP rallied earlier in the week after a report from the ONS revealed UK retail sales rose at the fastest pace in four months in August at 1%, well ahead of the expected 0.2% increase. The figures signal some improvement in consumer demand after faster inflation helped to crimp spending earlier in the year.

Jason Granite
Chief Investment Officer
22 September 2017

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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%	1.30%	3.43%	2.42%
FTIM Safety First 3	3.26%	1.91%	1.76%	3.55%	2.67%
FTIM Safety First 4	4.38%	2.93%	2.30%	4.02%	3.37%
FTIM Safety First 5	5.63%	3.23%	3.02%	4.45%	3.73%
FTIM Safety First 6	10.10%	5.04%	4.37%	5.09%	5.01%

Date: 22 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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