03 November 2017

WEEKLY INVESTMENT UPDATE

Bank of England undertakes a dovish hike

KEY MESSAGES:

Markets were relatively calmer through the week with temporary fluctuations seen on major decisions by Fed, BOJ and BOE, all of which came as per expectations. However, BOE's action was interpreted as a dovish hike sending GBP 1% lower to $1.31.

President Donald Trump confirmed Jerome Powell to be his pick for next Fed chair. Another major milestone was the release of House Republican leaders' version of tax cuts.

USD gained, S&P 500 closed at 2,579. US 10-year Treasuries yielded 2.34%. WTI Crude closed at $54.69 a barrel. Brent closed at $60.90 a barrel. Gold closed at $1,275.8 an ounce.

Market developments during the week

There was no shortage of potential catalysts for investors this week. However, the response was relatively muted as things turned out to be as per expectations. Fed stayed, indicating a hike in December, BOJ kept on hold while the BOE, though pursued a rate hike as per consensus, the dovish tone resulted in GBP selloff, falling 1% to $1.31.

Federal Reserve officials reinforced expectations for a December interest-rate increase by subtly upgrading their assessment of the US economy while staying on hold this month. Pricing in federal funds futures contracts implied an 85% probability of a quarter-point move next month.

However, the Fed Chair pick stole spotlight from the FOMC. President Donald Trump confirmed that Federal Reserve Governor Jerome Powell is his pick to chair the central bank in Feb 2018. The decision was greeted with a shrug by investors who see him as a continuity candidate. On Yellen's watch, the US economy added about 9 million jobs as it recovered from the Great Recession, lowering unemployment to 4.2% from 6.6%, while inflation averaged 1.1%. Powell is set to take the reins when the US economy is rolling along at a pace he'll be under pressure to sustain. Growth is accelerating, inflation is tame and unemployment is the lowest in 16 years. The monetary policy is already set on a tightening course.

On economic front, payrolls data provided a mixed picture of the strength of the labor market, though distortions from the hurricanes in August made it difficult to draw firm conclusions. US employers added 261k jobs, the most workers in a year, rebounding from September's slowdown, as people resumed work after hurricanes Harvey and Irma. The jobless rate fell to the lowest since 2000 at 4.1% while wages stalled. In Europe, monetary officials are scratching their heads over a similar trend.

With payroll gains averaging about 162,000 over the past three months, the jobs report broadly provided more evidence the economy is approaching maximum employment, probably keeping Federal Reserve policy makers on track to raise interest rates in December for the third time this year.

Another measure of economic performance was the US trade deficit that depicted widening in September as gain in imports barely exceeded exports. The gap widened 1.7% to $43.5b (est. $43.2b) from a revised $42.8b in the prior month. Exports climbed 1.1% to $196.8b, highest since December 2014 and led by oil and chemicals. Imports rose 1.2% to $240.3b on industrial supplies, capital equipment and consumer goods. The September figures cap a quarter that saw an improvement in the US trade balance. Trade contributed 0.41 %age point to economic growth in the third quarter, the most since the final three months of 2013. Gross domestic product increased at a 3% annualized rate during the period.

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Contrary to its manufacturing equivalent which retreated in October, the ISM non-manufacturing index held on to recent gains. It rose 0.3 points to 60.1, the highest reading since 2005 after surging an impressive 4.5 points in the month prior. Improvements in business activity and employment sub-indices are indeed very encouraging, but perhaps more significant is the support from the supplier deliveries sub-index which remained unchanged after spiking nearly 8 points last month. Still, the underlying trend remains an encouraging one, with broad underlying strength among the main sub-components reinforcing the notion that the services sector continues to expand at a solid clip. Rebuilding efforts should provide added support to this trend through the end of the year, boding well for another above-trend GDP print in the fourth quarter.

Another significant step in tax overhaul was undertaken this week as House Republican leaders rolled out their version of tax cuts that would cut the US corporate tax rate to 20%, reduce most of the individual tax brackets, and cap the mortgage-interest deduction on new purchases of homes. The measure would phase out the estate tax over five years and impose a tax of as much as 12% on multinational companies' accumulated offshore earnings. A credit given to electric vehicle buyers was scrapped, while the carried interest loophole was preserved.

North Korea tensions may probably be back to focus as President Trump jets off on an Asian trip. The war of words has never ended and this week accusation by North Korea that the US is seeking to ignite a nuclear war, while saying American fighter jets staged a drill in South Korea that replicated a surprise nuclear attack on Kim's regime has kept tensions alive.

Currencies

The Bloomberg Dollar Spot Index gained as the latest jobs report did little to alter views on the timing for higher interest rates.

The euro remained steady at $1.16.

The British pound was also firm at $1.31 after a 1% sell off mid-week upon dovish hike by BOE.

The Japanese yen climbed 0.35% to 114.1 per dollar.

Emerging-market currencies fell on Venezuela debt restructure. President Nicolas Maduro said Venezuela will seek to restructure its global debt blaming US sanctions for making it impossible to find new financing.

Elsewhere, bitcoin extended gains for the fourth consecutive day, hitting $7,000 to establish a fresh record before paring the advance. The digital currency got new impetus this week after CME Group Inc., the world's largest exchange owner, said it plans to introduce bitcoin futures by the end of the year, citing pent-up demand from clients.

Equities

The S&P 500 fell 0.08 % to 2,579 after reaching a record 2,585.95 during the week.

The VIX lost 7% to 9.24.

The S&P/TSX Comp surged 0.2% to 15,991.

The Stoxx Europe 600 Index rose 0.3%.

Spain's IBEX Index fell 1.3%.

FTSE 100 gained 0.5% to 7,544. The inverse relationship between the exporter-heavy FTSE 100 Index and the pound has never been stronger. The 40-day correlation between the two reached its most negative ever on Thursday, after the Bank of England raised rates but said another increase isn't imminent. The relationship, which gave the FTSE 100 a big boost after 2016's Brexit vote-induced currency plunge, has propelled the gauge higher in recent weeks amid sterling weakness.

An index of emerging-market currencies declined the most in a month as the market digests Venezuela's plan to restructure its debt.

Bonds

The yield on 10-year Treasuries fell seven basis points to 2.34%.

Germany's 10-year yield decreased two basis points to 0.36%.

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Britain’s 10-year yield fell eight basis points to 1.27%.

Commodities

West Texas Intermediate crude closed at $54.69 a barrel.

Brent for January settlement closed at $60.90. The global benchmark traded at a premium of $5.99 to January WTI.

Oil extended its fourth straight weekly gain as supply threats abounded on signs that global inventories are shrinking and the OPEC and allied producers may prolong their glut-killing accord beyond its March expiration. In the US, crude stockpiles slid to the lowest level since January 2016 last week, according to an Energy Information Administration report this week. Stockpiles slid by 2.44 million barrels last week, while gasoline supplies edged lower by 4.02 million, according to the Energy Information Administration report.

Gold dipped 0.15% to $1,275.8 an ounce.

A global metals rally saw nickel rise as much as 6% to $13,030 a metric ton.

Copper also rose, with prices climbing 2%.

Other major economies:

Euro area

The main fear of the ECB of inflation turning out to be unsustainable showed signs of becoming reality as it unexpectedly slowed in October despite the bloc’s strengthening economy, underlining why the European Central Bank last week kept its exit from monetary stimulus wide open. Price growth cooled to 1.4% from 1.5% in September. In a further blow to the ECB’s drive to boost inflation, the core rate dropped below 1% for the first time in five months. Even with confidence at its highest in almost 17 years and robust growth helping to create more jobs, a sustained price pickup remains elusive.

The puzzle of low inflation isn’t just a euro-area phenomenon. Federal Reserve Chair Janet Yellen has referred to the mystery of tepid price growth and, even in the UK, where a weaker currency has boosted headline inflation, wage increases remain stubbornly low.

Third-quarter gross domestic product figures for the euro area showed faster-than-forecast 0.6% growth. That’s an 18th quarterly expansion still it was relatively at a slow pace, slowing for the first time in more than a year. On a year-on-year basis, GDP hit 2.5%, the best since early 2011. The French economy grew 0.5% in the third quarter, while Spain’s expanded 0.8%. Another release was the eurozone Manufacturing PMIs, with Italian, Spanish and German figures all positive, but French manufacturing below market expectations. The overall reading for the Eurozone was 58.5.

Political tensions in Spain remained elevated, as eight members of the Catalan government were taken into custody by the orders of the Spanish court of justice for their collaboration in organizing the referendum that later led to the declaration of independence of the Catalan region. Spain issued a European arrest warrant for the Catalan leader Catalan Puidgemont as well, who is currently in Brussels and rumored to be considering an asylum claim. Catalonia is set to see snap election in Dec 21. The established parties in in the region will now have to decide whether to disregard the new elections having been called by a foreign government, or participate in them, which would legitimize the actions of the Spanish government so far, and be seen as an acceptance of the defeat of their recently declared independence.

European Inc earnings growth continues to be a strong foothold for the rally in equities. As of this week, just about 66% of the region’s companies have reported third-quarter results so far, with 55% of Stoxx 600 members beating expectations. Sectors with positive surprises include oil and gas, telecommunications, financials and technology. In contrast, sales have seen a small miss, with 54% of the companies reporting a negative revenue surprise. However, investors should be less concerned by this, given the positive broader sentiment.

Australia

The weakest quarter for Australian retail sales in seven years sent the Aussie lower and bonds climbing. The Aussie dollar dropped as much as 0.5% back below 77 US cents and bond yields extended

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declines as traders pushed back bets on the timing for an interest-rate increase.

Japan

The week started with BOJ policy meet that ended with the Central bank remaining on hold. It trimmed its inflation forecasts, signaling further divergence ahead from its global peers. The yen weakened and Nikkei 225 stock index closed Monday at the highest level in two decades. The economy is facing inflation that is well below its 2% target. It is on track for the longest expansion in 16 years and the labor market is the tightest in a generation.

China

China saw a bond rout this week. The benchmark 10-year yield surging to a three-year high on Monday amid concern policy makers would toughen a drive to reduce borrowing levels in the financial system. On Tuesday, the PBOC applied the balm of liquidity to tingling nerve ends. Its fund injection was enough to cause the biggest single-day decline in overnight interbank rates since February. The Central bank came up with MLF injection offering 404 billion yuan of one-year funds, compared with 207 billion yuan of maturities. That takes total injections this week, through MLFs and reverse-repurchases agreements, to just over 1 trillion yuan. Friday's MLFs were offered at 3.20%, unchanged from the previous operation. Yet yields on the 10-year bond barely slipped 2 basis points from a three-year high and surged 20 basis points in the four days through Monday. Considering that the manufacturing purchasing managers' index came in slightly weaker than expected, the decline in long-term interest costs was too small to signal an end of fear. Chinese equities, taking a cue from the fixed-income market, fell for a second day and saw their biggest weekly drop in almost three months.

Canada

Monthly GDP data showed the economy, which has been posting robust growth figures recently, halted in August, contracting 0.1% after flat growth in July. Declines in manufacturing and resource industries were behind the decline, while services increased slowly. A full 1% contraction in the manufacturing sector was recorded. Though monthly growth data are volatile, but the disappointment was enough to put the loonie firmly on the back foot.

Labor market in October again recorded gains as jobs increased by 35k, stronger wage increases and the biggest-ever two-month surge in full-time employment. The data extends the streak of job gains to 11-months. Hourly wage growth is likely to raise some eyebrows at the Bank of Canada, holding above 2 % for the second consecutive month and even accelerating a touch. With Governor Poloz emphasizing labor market developments as a key indicator of capacity pressures in last week's interest rate announcement, the persistent move back up to over 2.0 % growth in wages will be viewed as confirmation that economic slack has largely diminished.

A separate trade report Friday was more in line with the current trend of weakening data, as exports continued falling and deficits surpassed C$3 billion for a fourth month. Both imports and exports were down 0.3 %. Canada's trade surplus with the US narrowed to $2.2B in September (previously $2.7B), as exports were down 1.2% and imports rose 0.4%. Canada's trade deficit with the rest of the world narrowed to $5.3 billion (previously $5.8B), with exports up 2.4% and imports down by 1.4%. September marks the fourth consecutive month in which export volumes declined. With the Bank of Canada's next move heavily data dependent, the soft export performance does not support a move higher. However, several data reports will be released between now and the Bank's next meeting in December to help the decision making.

UK

The main headline that ruled the UK asset performance this week was the rate hike by Bank of England. The Central bank increased its policy rate for the first time in more than a decade to 0.5% from 0.25%. The move removes the emergency stimulus introduced in the wake of last year's EU referendum while underscoring worries that the economy is fragile as the 2019 split with the EU nears.

Though it was a largely predicted move and sterling was expected to remain unmoved

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as the risk was already priced it. The currency sold off slumping 1 % to around $1.31 on account of the dovish tone from the BOE as the Governor Mark Carney emphasized that the Bank would prefer to undershoot interest rate hikes, and potentially have to deal with the economy starting to overheat, rather than risking choking economic growth. That implies that officials are comfortable with pricing for two more quarter-point increases, roughly one by late next year and another in 2020. The bank kept its bond programs and its forecasts for growth and inflation broadly unchanged and sees price gains at 2.2 % in three years, slightly above its goal. The estimates are based on market projections for the key interest rate reaching 1 % over that period.

The slow-moving Brexit negotiations were spurring concerns which were somewhat calmed this week after EU Brexit Negotiator Michel Barnier stated he was ready to speed up negotiations.

Of the economic releases, major ones were GfK consumer confidence, which remained negative overall at -10 in October from -9 in September, matching consensus, and continued to hover near a three-year low. The Markit Manufacturing Purchasing Managers' Index rose slightly in October, as the surveyed manufacturers reported higher activity and robust order growth. It jumped to 55.6 in October from 53.6 in September, its biggest one-month rise since August 2016.

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%	2.19%	3.43%	2.37%
FTIM Safety First 3	3.26%	1.91%	2.78%	3.55%	2.62%
FTIM Safety First 4	4.38%	2.93%	3.51%	4.02%	3.31%
FTIM Safety First 5	5.63%	3.23%	4.39%	4.45%	3.64%
FTIM Safety First 6	10.10%	5.04%	5.98%	5.09%	4.91%

Date: 06 November 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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