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FORUM FINANCE GROUP

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MONTHLY NEWSLETTER

December 2016

KEY ECONOMIC DATA PUBLISHED IN NOVEMBER

- China's October exports dropped by 7.3%, more than expected; imports dropped by 1.4%, slightly below expectations for -1%.
- China's Manufacturing PMI was higher in November at 51.7 (market expectations of 51).
- Economic sentiment in the Euro-Zone improved in November (ZEW survey at 15.8 compared to 12.3 in October). The PMI Composite number at 54.1 was ahead of market expectations of 53.3.
- In Germany, economic sentiment (ZEW survey) weakened in November (58.8 vs. 59.5 in October). The IFO Business Climate indicator was stable at 110.4.
- US consumer confidence rose in November to a level of 107.1, well above market forecasts of 101.1.
- US durable goods orders ex-Transportation rose by 1% in October compared to a 0.2% forecast.
- US payrolls in the private sector increased by 156K in November (forecast of 175K), with October numbers being revised downwards from 142K to 135K.

THE SIGNIFICANT REPRICING OF GLOBAL BOND YIELD CURVES

$ 1.7 trillion

THE AMOUNT WIPED OFF THE VALUE OF THE BLOOMBERG BARCLAYS GLOBAL AGGREGATE INDEX IN NOVEMBER

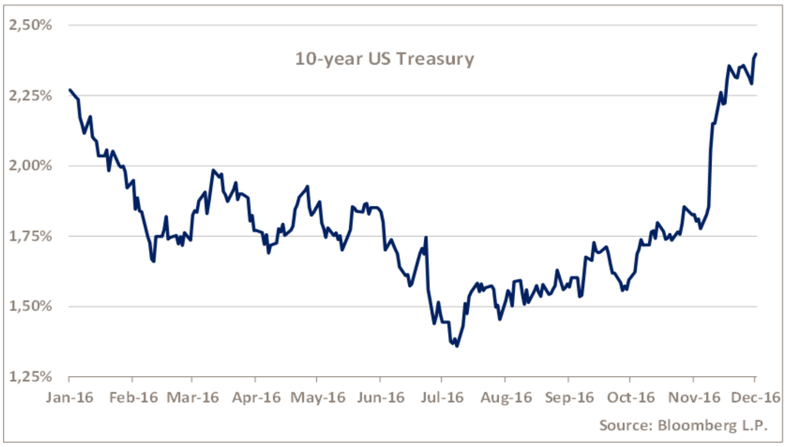
INVESTMENT PERSPECTIVE

November was an eventful month for financial markets following the election of Donald Trump as the next US president. Following an initial shock and a strong bid for safe haven assets as soon as the results were first announced, the ensuing reaction of the markets turned out to be as unexpected as Trump's victory itself. Equity markets quickly recovered, while bond yields started to rise on the back of higher inflation expectations and the prospect of a fiscal stimulus focused on infrastructure spending. The dollar appreciated against all currencies and emerging markets' assets were under pressure. Gold sold off due to the headwinds represented by a stronger dollar and rising bond yields, while the price of oil rallied at the end of the month on the back of an OPEC agreement to cut production.

The most significant of all the market moves that took place during the past month was the repricing across global yield curves. Emerging market bonds were hit particularly hard (down to - 8% in USD terms) and US Treasuries had their worst month since December 2009, with 10-year yields climbing by 55bps to 2.38%. Within the equity asset class, Japanese and US equities outperformed significantly whereas emerging market equities were impacted by heavy outflows. The severe sectorial rotation within US equity markets was also noticeable as financials, industrials and energy were strongly bid to the detriment of consumer staples, utilities and technology.

Finally, the European Central Bank will be next meeting on December 8 and markets are waiting for the bank to provide details related to a likely extension of its quantitative-easing program beyond the provisional end date of March 2017. Markets are now also fully expecting the Federal Reserve to hike its interest rates after its December meeting the following week.

THE SPIKE OF US TREASURIES' YIELDS



The chart above illustrates the accelerating trend of higher Treasury yields during November. This move gained momentum following Donald Trump's victory due to anticipations of a more expansionary fiscal policy, deep tax cuts, a wider budget deficit and higher inflationary expectations. Investors pulled significant amounts from the fixed-income asset class which were primarily reallocated into US equities.

INVESTMENT STRATEGY

As was already the case during the previous month, the overall low duration of our bonds' exposure contributed to limit the impact of much higher bond yields. A large number of investors reduced further their allocation towards G-7 government bonds, a market segment we have largely been avoiding for some time due to its unattractive risk/return profile. Looking ahead, we still prefer credit to sovereign debt as a more expansionary fiscal policy should boost growth prospects and ultimately translate into better earnings. In a context of rising yields, loans should also fare well due to their floating rate coupons.

Despite the recent correction of emerging market equities, we have decided to maintain our positions on the basis of reasonable valuations, a bottoming of earnings and a lot of uncertainty about potential protectionism from the new US administration. Japan is another region which we favour, especially due to improvements at the corporate level, a discount of valuations compared to other developed markets and improving returns on equity.

The initial conclusions that we can draw from the new policy announcements of Donald Trump is that the latter should underpin risk assets due to improving growth forecasts and also lead to a widening of central banks' policy divergence.

PORTFOLIO ACTIVITY/NEWS

During November we carried out several transactions related to the hedging of equity exposures. During the first week, we took the decision to reduce further the portfolios' exposure to risk assets by partially hedging our allocation towards US equities on top of the existing protection on European ones. As was the case with the UK referendum, we were facing a binary event whose outcome was not predictable but which was largely expected to rattle financial markets significantly.

This hedge was tactical in nature and was removed the day after the US elections as equity markets gradually erased initial losses following Donald Trump's conciliatory victory speech. We also lifted the protection on European equities the same day to bring back our equity allocation to a slightly overweight level.

As a reminder, we had also decided to sell our remaining dollar exposure for some portfolios denominated in other currencies. The dollar had had a strong run from its August lows and we opted to lock in profits considering the highly volatile environment around election time.

DONALD TRUMP'S UNEXPECTED ELECTION VICTORY TRIGGERS ASSET REALLOCATIONS

	End 2015	October 2016	November 2016	MTD	2016
Equities					
S&P 500	2043.9	2126.2	2198.8	+3.4%	+7.6%
Euro Stoxx 50	3267.5	3055.3	3051.6	-0.1%	-6.6%
MSCI EM	794.1	905.1	862.8	-4.7%	+8.7%
Yields					
UST 10-year	2.27%	1.83%	2.38%	+55bps	+11 bps
Bund 10-year	0.63%	0.16%	0.27%	+11 bps	-36 bps
BBB EU	1.75%	1.02%	1.31%	+29 bps	-44 bps
Currencies					
EUR/USD	1.086	1.098	1.059	-3.6%	-2.5%
USD/CHF	1.002	0.989	1.017	+2.8%	+1.5%
EUR/CHF	1.088	1.086	1.078	-0.7%	-0.9%
GBP/USD	1.474	1.224	1.251	+2.2%	-15.1%
Commodities					
CRB Index	176.1	186.3	189.3	+1.6%	+7.5%
Oil (WTI)	USD 37.0	USD 46.9	USD 49.4	+5.3%	+33.5%
Gold	USD 1061	USD 1276	USD 1173	-8.1%	+10.6%