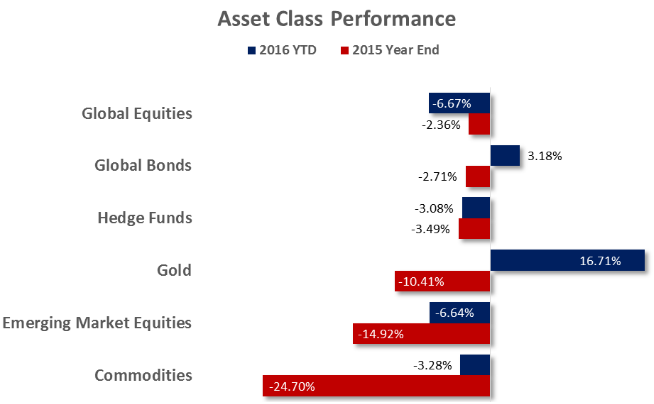
Quarterly Investment Outlook

2nd Quarter 2016 March 2016

ameliora
WEALTH-MANAGEMENT

Asset Class Developments

A central theme last year was how financial assets would be affected by diverging central bank policies. The discussion focused on what distorting effects a US rate hike would have and what benefits further accommodative measures from ECB and BOJ would have. The result was a synchronized fall in asset prices. The properties of asset class diversification yielded few benefits as by the end of 2015 global equities and bonds, commodities, and alternative investments were all down. However, year-end performance measures are only two data points in time – start of the year and end of the year. Since the start of 2016, some assets have substantially reversed last year's trends and erased losses recorded at year end. Measured slightly differently, like on a 12 month basis, the result of asset class diversification certainly holds merit.



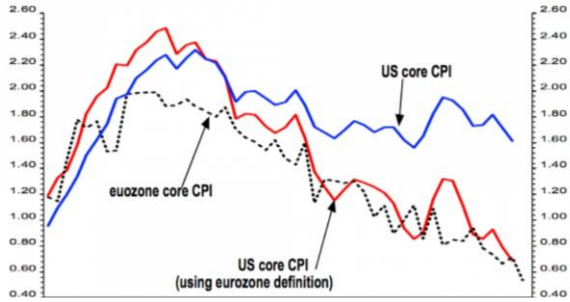
Fixed Income

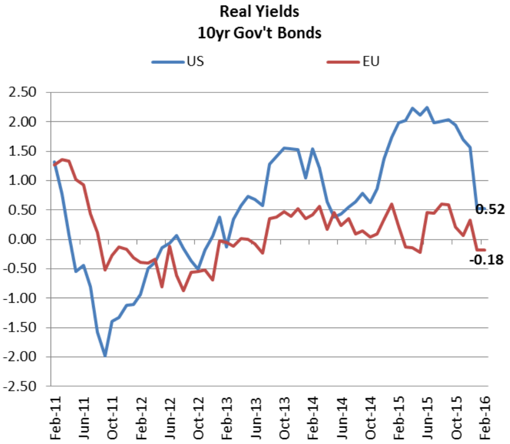
We reduce allocations to sovereign and investment grade bonds

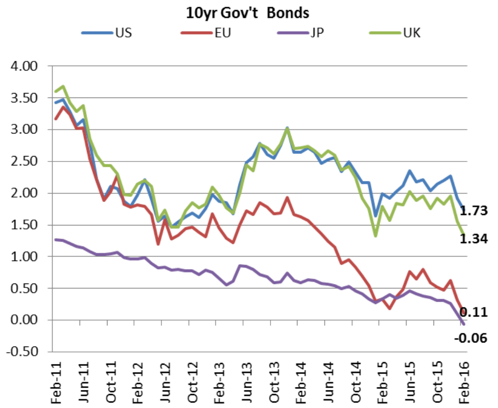
Now that central banks have the unemployment situation under control, or at least they claim so, the next effort is bringing inflation to their preferred level. This task has undoubtedly been more difficult as monetary policies still remain accommodative - even with the Fed's rate hike in December last year - in an effort to move inflation higher. As with employment statistics, both headline and core inflation figures are obfuscated by the components underlying the two inflation measures. On the surface of it, inflation in the United States is ticking higher whereas inflation in the Euro Zone is ticking lower. But the comparison basis is somewhat flawed as the calculation methods between the two differ. Measured on a comparable basis inflation developments in the two regions appear to move in tandem – which show lower inflation.

Conceptually, if inflation were either rising or expected to rise bond yields would also rise as it erodes the nominal value of principal. Additional compensation through higher coupon rates would be expected. Nominal yield spreads, especially between the US and the EU, are wide and one could deduce that inflation expectations between the two regions are causing the interest rate differentials to stay wide. However, measuring the spread with real yields shows a much tighter spread level and one in which US real rates are falling – much in a similar pattern to EU real yields. As US core inflation is presumably increasing, longer term US bond yields are falling, which seems counterintuitive.

Even with diverging monetary policies – tightening vs. loosening – bond yields are heading lower. The amount of highly rated sovereign bonds yielding zero or less is increasing and issues of investment grade bonds trading above par is escalating. We find it prudent to lessen the amount of bonds in our asset allocations.







Sources: Société Générale Bloomberg, Ameliora Wealth Management

Equities

We increase allocations to select sectors

Heading into 2016 financial media were quick to point out that stock markets were in a bear market. Thankful for having a new headline to broadcast, journalists and pundits served up a multitude of predictions of what kind of problems such price falls would have on global equities. Yet, large price falls often open up opportunities to acquire assets at a more reasonable prices which tends to pay off over relative modest holding periods. In fact, over the last 45 years, periods of downward price pressure have set the stage for some reasonably decent medium term equity market returns.

There is some fundamental anchoring to the weakness in global equities in our opinion. Companies' profits declined during the last fiscal year. Interestingly, profits margins of companies in developing nations actually rose. During 2015 overall earnings growth trended meaningfully lower and the analyst community was quick to extrapolate even further weakness for the year ahead. Such bearishness tends to indiscriminately cause wide equity market sell-offs. However, part of this earnings malaise stemmed from just a few sectors and is not necessarily representative of the overall market. The main culprits were energy and materials, two highly cyclical industries facing excess capacity issues and severely depressed commodity prices. Offsetting some of the overall profit decline were sectors like discretionary consumer goods and telecommunication services which recorded high doubled digit earnings growth.

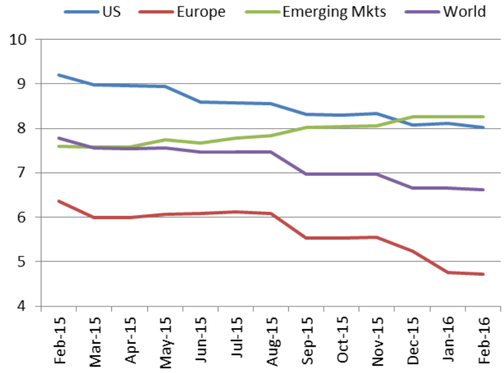
We have opinioned earlier that evaluating various sectors relative to their respective business climate and the equity market overall is a viable approach of capturing opportunities within the broader equity markets. In any economic cycle companies in different sectors tend to exhibit dissimilar dynamics between each other. This was evident throughout 2015 and we expect to see similar developments for the year ahead.

MSCI World Index Bear Markets: 1970-2016

		Performance After Stocks Fall 20%		
Dates	**Drawdown**	**One Year**	**Three Years**	**Five Years**
1970	-19%	36%	72%	57%
1973-74	-40%	8%	18%	54%
1982	-17%	48%	98%	346%
1987	-20%	28%	24%	42%
1990	-24%	25%	51%	87%
1998	-13%	34%	13%	5%
2000-2002	-45%	-4%	6%	39%
2007-2009	-54%	-17%	-2%	26%
2011	-26%	22%	67%	68%
2015-2016	-20%	??	??	??
Averages	-28%	20%	39%	81%

Source: Returns 2.0

Profitability
Net Profit Margin %



Sector	Price/Earnings	10yr Avg P/E	Relative Disc./Prem.
Financials	12.51x	15.69x	-20%
Health Care	21.28x	19.47x	9%
Technology	18.94x	23.64x	-20%
Consumer Discretionary	17.71x	22.77x	-22%
Industrials	17.96x	17.81x	1%
Consumer Staples	23.99x	18.44x	30%
Energy	59.07x	17.11x	245%
Materials	32.59x	29.42x	11%
Telecom Services	19.81x	20.47x	-3%
Utilities	24.00x	19.32x	24%
World	**18.79x**	**21.31x**	**-12%**

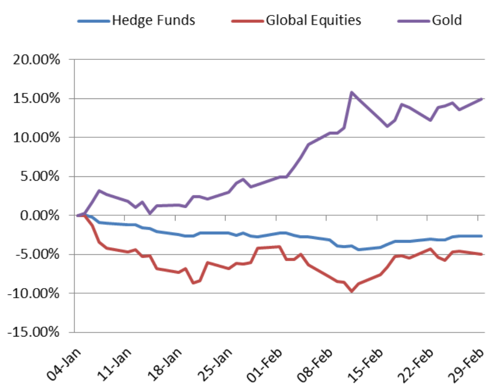
Alternative Investments

We reduce allocations to gold

Our stance on risk diversification remains the same. The lower sensitivity, or beta, of for example hedge funds, dampens price volatility during periods of stress in the equity and credit markets. As such, hedge fund's focus on creating asymmetric pay-off profiles and lower security and asset correlations proves valuable in high volatility environments. The asset allocation benefits from exposure to such vehicles.

Gold's uncorrelated properties manifested itself aggressively over a very short time frame leading into 2016. As global equity and credit markets tumbled at the onset of the New Year, gold showed an almost flawless inverse relationship to risky assets. The rapid upward move let us to readjust the asset back down to its original weight in our asset allocation.

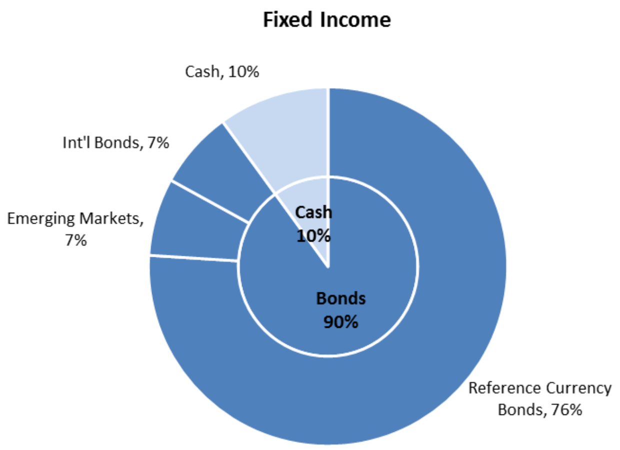
Price Performance YTD

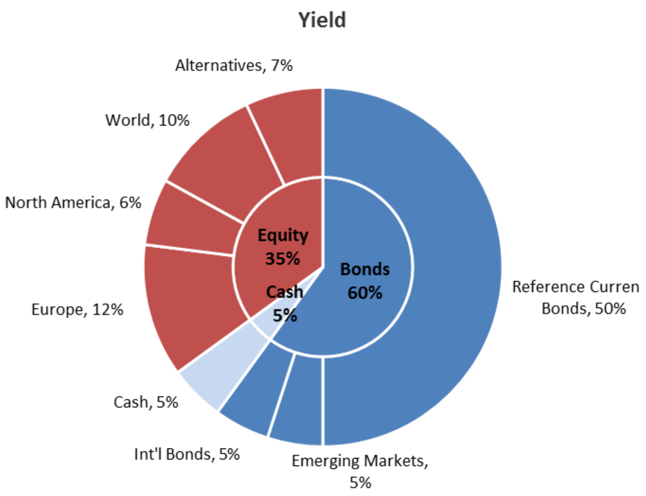


Sources: Dash of Insight, Bloomberg, LLP, Ameliora Wealth Management

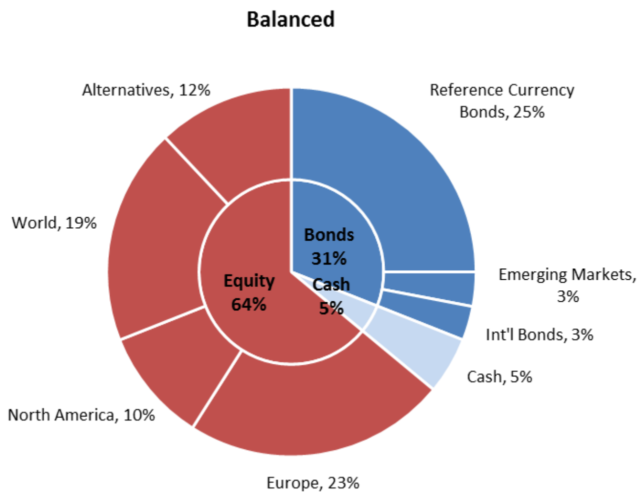
Asset Allocations

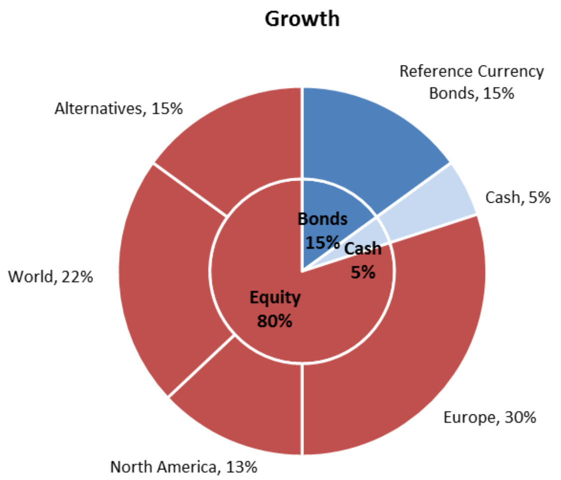
Income Strategies



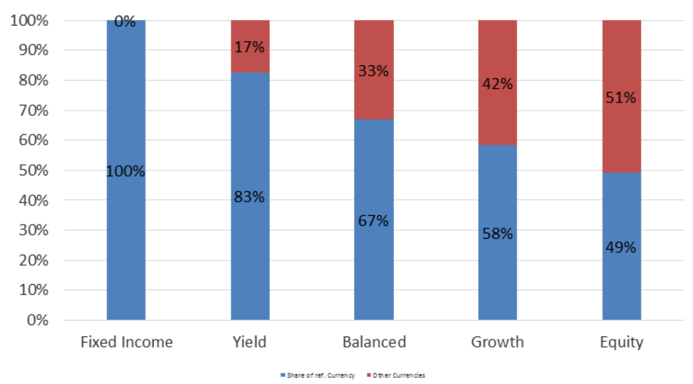


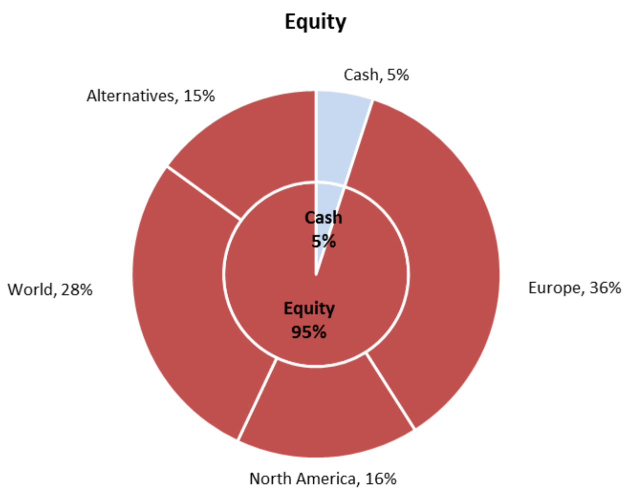
Growth Strategies





Currency Exposure





Source: Ameliora Wealth Management as of 15th March, 2016
Note: Tactical asset allocations are subject to change without notice. The asset allocations represents Ameliora's investment strategy in USD

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