Investment Policy | Q3 2018

English Version

Axion | SWISS Bank

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Macro

Global growth appears sustained and synchronised for now, with signs of a slowdown in Europe. The critical factors seem to emanate from geopolitics, in particular from the protectionist policies brought forward by the Trump administration. In the most recent phase, destabilising elements focused-in on Europe, where the resolution of the debt issue of most exposed countries remains a topic , and, more generally, at an institutional level, the common handling of the relationship with Russia and the application of the relevant sanctions has become a dividing issue. The rise of oil price and of other commodities fuels in the meantime some inflationary pressures.

Equity

It isn't just the liquidity injected by central banks that propels one of the longest rally in history but also corporate profits and, in the USA, the expected benefits from the fiscal reform initiated by president Trump. Valuation are, however, rich and different uncertainties weigh on markets. Nonetheless, there are neither expectable reasons that could cause a drastic sell-off – black swans apart. If anything, passive investing should be replaced by active stock picking. As for geographic areas, Euro weakness favours the recovery of European corporate profits, but for Italy, at least in the short term, political risks prevail. The export oriented Swiss market is attractive owing to a relatively weak currency and its benefits from global growth. Emerging Markets maintain all structural benefits such as demographics and growth, but in the short term, may be penalised by a stronger USD, rising energy cost and higher interest rates.
Selectivity is key, especially in countries where cyclical growth is high, like China and India. Amongst stock specific investment themes, the big "4" tech companies, Facebook, Amazon, Netflix and Google-Alphabet, continue to dominate Wall Street along megatrends in robotics, security, medical and agro/food technologies.

Investment Policy

The euphoria that has characterised the first half of the year, propelling equity indices towards historical highs, has given way to a more cautious stance, in a context of higher volatility. The new scenario is a consequence of the uncertainties surrounding the protectionist tone of US trade policy on one side and the likelihood of higher deficits and debt owing to the possible infrastructure investments on the other side. Concerns about the pace of rising rates, if too fast and beyond a certain level also negatively affect sentiment and could provoke a correction at Wall Street but also weigh on consumer spending and the real estate market.

A further tightening in the labour market culminating in wage pressure could negatively affect corporate earnings. Furthermore, the divisions that trouble the European Union have to be considered, especially after the most recent political developments in Italy and Spain, which condition the choice of the ECB in a delicate moment such as the start of the normalisation of monetary policy. Moreover, the European economic recovery shows some signs of slowing down whilst some, albeit timid, sign of inflation linked to higher energy and commodity prices are emerging. The S&P 500 is up by more than 5% since the beginning of the year whilst the Eurostoxx 50 is, in comparison, mildly negative but potentially more attractive would there not by geopolitical issues. The greenback's attraction is in the yield differential that has climbed beyond 3% on 2-year rates.

Fixed Income

US dollar bonds have become attractive owing to the interest rate differentials, especially for corporate and HY bonds with short duration and FRNs with positive real rates. Pursuing a carry strategy, i.e. financing longs from currencies with lower yields may be interesting, but once 10y rates cross 3%, the risk of an overshoot in rates becomes meaningful. In Europe, Government bonds remain a safe haven despite low or nil yields for many investors, but also this strategy, it seems, will have run its course by the end of the year. The political crisis of late, especially the Italian one, have led to a widening of spreads adding to an already difficult scenario. In the medium-term, holdings in Italy are more of an opportunistic investment apt to exploit its volatility. Emerging market bonds, also in local currency, remain attractive but a cautious and selective approach is warranted, given crisis in Venezuela, Argentina, Turkey, Russia and the Middle East whilst the Korean front is enjoying a relief after the historic meeting between Donald Trump and Kim Jong-Un in Singapore.

Alternative Investments

A prolongued phase of low volatily and low dispersion in evaluations has limited the interest for alternative investments that were not able to generate meaningful performance. Now, as circumstances have changed, it is wise to pair long-only strategies with long-shorts that will benefit from market drawdowns and high volatility. Oil is also interesting with an excess of demand and the spread WTI / Brent spread in favour of the former. In the commodities space agriculture remains depressed and attractive as a hedge for the return of inflation. The bullion price is stable around 1300 USD but it has not lost its "safe heaven" status even if it is temporarily out of favour in the face of rallying equity markets, temporary strenght in the USD and absent inflation.

Outlook

Given these conditions, the expectation is for a fragile and volatile equity market, driven by macro data, corporate events and geopolitical and political agendas. Markets remain supported by a global and synchronised expansion. The Far East remains the most attractive of the regions. In particular, China, which is already a key element to growth, with its new focus on domestic consumption and high quality trade rather than capital expenditures alongside enormous structural investments in Asia, Africa, the Gulf and Middle East as well as Europe, is on a path to global economic leadership.

In fixed income, the emphasis on the quality of the issuer, duration and liquidity is more and more important. ILS securities and FRNs are progressively more attractive although they are not immune to a widening of spreads.

Forex

Interest rate differentias favour the US dollar which is approching the lower limit of the trading range of 1,16-1,26. As for the Swiss Franc, the tension in Europe has strenghtened the currency temporarily to 1,15. Anyhow the old threshold set by the BNS at 1,20 against the Euro can be exceeded with ensuing weakness towards 1,23. Volatility in emerging market currencies is to stay but this could be one of the drivers of performance in the second half of the year.

Asset Allocation Q3 2018

Private & Confidential

Classic Mandate

Axion SWISS Bank's classic mandate allocates at least 65% of assets to the reference currency of the mandate. The investment objectives are Income, Yield, Balanced or Growth. Mandates are available in CHF, EUR & USD.

Multi Currency Mandate

Axion SWISS Bank's multi currency mandate allocates at least 20% of assets to the reference currency of the mandate. A balanced currency diversification is achieved for clients who wish to do so. The investment objectives are Income, Yield, Balanced or Growth. Mandates are available in CHF, EUR & USD.

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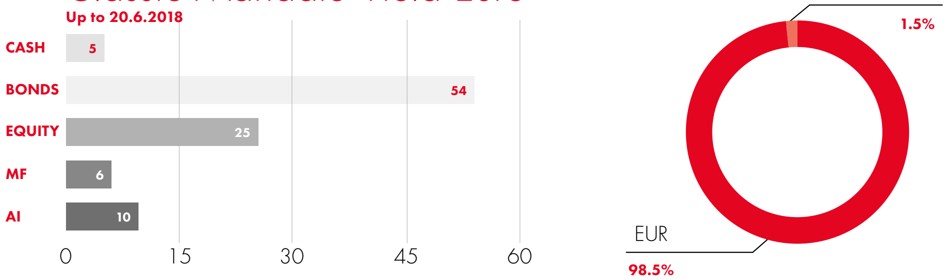
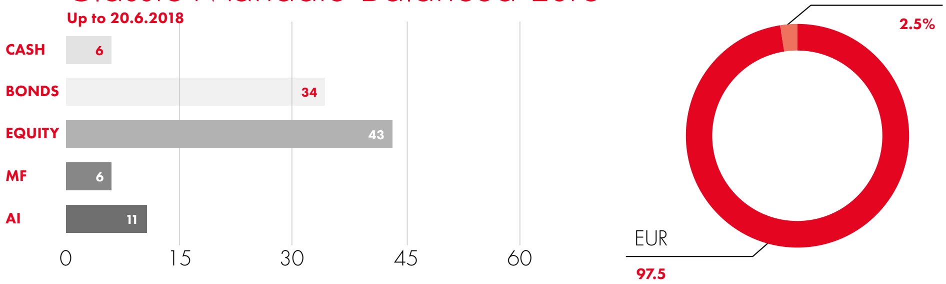
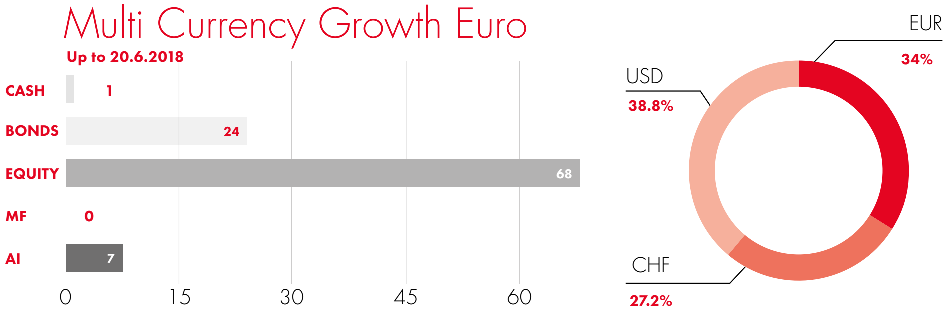
Classic Mandate Yield Euro



Classic Mandate Balanced Euro



Multi Currency Growth Euro



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