MOUNT INVEST

OUTLOOK 2018

January 2018

Partner of AWAP

INTRODUCTION

MOUNT INVEST

DO YOU REMEMBER « METROPOLIS »?

The workers revolt led by an android. The rise of dissident machines allied to working people rebellions that led to discord and chaos. A fracture of the working and ruling classes.

The visionary Fritz Lanz adapted in 1927 the novel of Thea von Harbou. Year 2026: underground workers of a fabulous Metropolis ensure happiness to the rich who live in the hanging gardens of the city. An android leads the workers to revolt of the masses. A deflationary world driven by globalization, ageing population and new technologies are among the troubles the world is facing.

Global manufacturing numbers on the rise again. Disparities still present but an overall improvement persists. This year has been positive for global equities. Till now, everything looks ok. The economic expansion has room to go, but expect the trend with a late cycle style. Political changes combined with shifts in monetary policies and disruptive technologies are risks for the appearance of sharp downturns and corrections. Those factors will require a combination of more agile investments and portfolios strategies.

The digital world will change the face of the next 10 years. A complete reshuffle of activities will gather strength but will also add to disparities like the Metropolis silent movie era and its dehumanization engendered by technology. After the lost control of the robots followed by their destruction by the workers, the reconstruction of the city.

WRONG TIMING

The 2017 portfolio hedges where not effective and have cost too much returns on portfolios. We acknowledge the fact and work to have a more systematic approach on theme segments in order to provide with a comprehensive investment approach. Flexible and evolutive strategies with your investment specialist.

https://www.youtube.com/watch?v=yB3S_ivukkg

		2017 Accurate view	2018 FORECASTS				
1	USD	✔			●		
2	GBP	✔			●		
3	EUR	✔✔✔				●	
4	JPY	✔✔			●		
5	EM Currencies	✔✔✔				●	
6	US Equities	✖✖		●			
7	EU Equities	✖✖				●	
8	UK Equities	✖✖		●			
9	EM Equities	✖✖✖				●	
#	Japan Equities	✖✖✖			●		
#	US Gov Bonds	✔✔✔		●			
#	EU Gov Bonds	✔✔		●			
#	Corp Bonds	✔			●		
#	Corp EM. Markets	✔✔			●		
#	Corp High Yield	✔		●			
#	Metal Commodities	✔✔			●		
#	Agriculture Commo	✔			●		
#	Precious Metals	✔✔✔				●	
#	Oil	✔✔			●		
#	Volatility	✖✖✖					●

PARALLEL

The socio-economic context of this mega movie production helped the filmmaker to have a mega budget but because of the synchronous sound in the cinema that became the new fashion that same year, the movie became quickly obsolete. The movie becomes today perhaps more actual than ever.

MOUNT INVEST

LIQUIDITY & SIMILAR

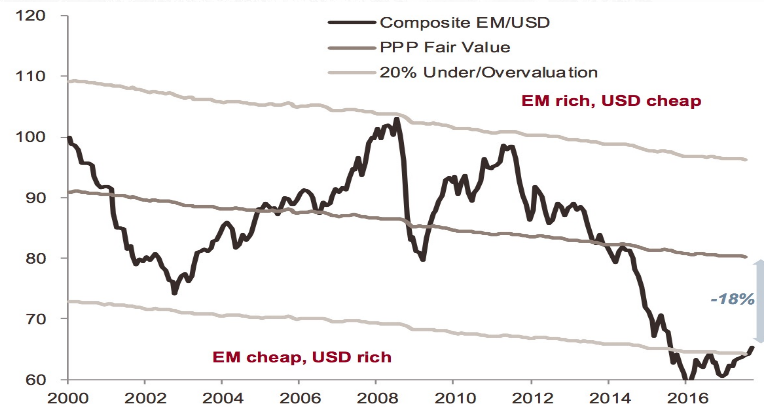
The Central bankers need to normalize monetary policy with great cautiousness. The persistent problem: weak inflation. Watch the USD as it could rally more than forecast estimates due to a tighter FED on rates. The ECB will scale back bond purchases and monitor inflation to adjust its future path of monetary normalization. No rate hikes till 2019 expected. The monetary policy uncertainty will add volatility to currencies in 2018. We expect the EUR and the USD to strengthen slightly (note that the former should loose its rally contest). The GBP will suffer the BREXIT but will gather pace later on. Watch the refuge currencies that could indicate a return of volatility. We believe some Emerging Markets currencies could gain some strength but with certain limits and risks.

Tepid inflation = troubles among the FED officials. Before, a temporary problem, now a troubling factor with roots well beyond a simplistic transitory problem. This could turn bad if a stronger dollar emerges. Wages pressure to alleviate such. The Quantitative Tightening will probably cause troubles to markets that have lived since the crisis on an expansionary phase (laggard considering the huge amount of balance-sheet utilization). Expect the USD to rally if inflation picks-up (to a smaller extend if FED holds). Otherwise, we see a peaked in the currency.

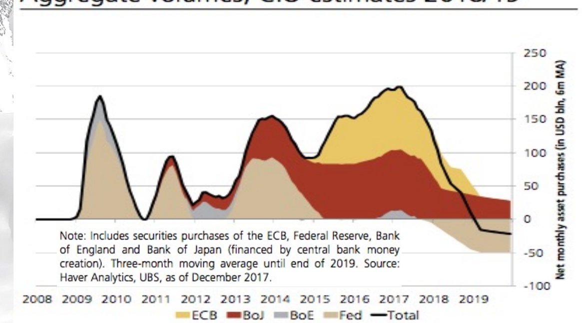
The European Central Bank (ECB) should slowly adjust its Quantitative Easing towards the end of the year. Tapering will be monitored as a pick-up in economic growth does not justify anymore a status-quo on additional stimulus. Any rate hike will come probably in the second half of 2019. We believe the EUR should strengthen some more towards the 1.25 level.
The Pound is set for a weaker trend till the BREXIT materializes. Watch for any sharp downside to start building exposure again.

The CHF should weaken but any market troubles could see investors run for the currency. A stable JPY unless used a refuge currency like the CHF.

A special note on Mexican Peso. With an implied volatility of 11.25%, it is among the highest of the 16 major currencies looked with Bloomberg. We believe the currency has room for improvement but the NAFTA negotiations and more importantly the presidential election in July will be key. Our view: if the leftist AMLO (López Obrador) wins the race, the Peso will devaluate above the 21 mark. Otherwise, expect the currency to stay within the range of 18-20 during 2018. Complete forecast on the appendix.



Aggregate volumes, CIO estimates 2018/19



EMERGING FOREX

Opportunities within a global basket of fallen angel EM currencies.

MOUNT INVEST

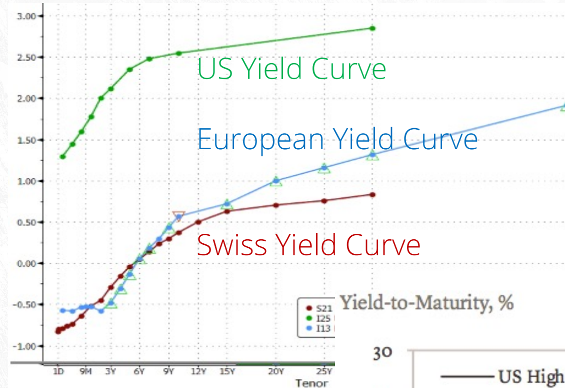
FIXED INCOME & SIMILAR

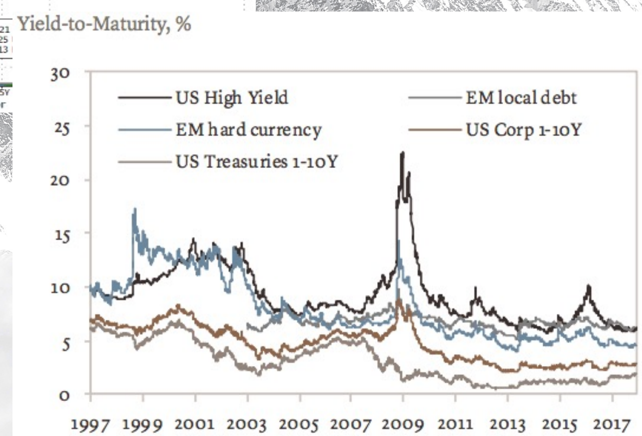
Bond yields to rise in 2018 as global monetary normalization is growing. The global subdued inflation will remain. The FED just raised rates but the long part of the curve still reflects some worries even after the normalizing policy seen since 2015. The US flattening curve is a concern. Is the FED is behind the curve? We think so. Beware of any curve inversion… The risk-reward for holding High Yield bonds has decreased and spreads are tight. The credit rally will cool down in 2018. Defaults to remain low but watch segments with spikes and credit contraction. Globally, reduce the portfolios duration and increase the quality. We continue with the convertible segment that should gather strength. Some Emerging Market Bonds still attractive but selection within countries are important.

Some major central banks have been normalizing monetary policies with tapering and rate hikes even if inflation remains muted and well below their targets. A flattening of the US Treasury yield curves worries us. The FED just raised another quarter point on interest rates. Even with a slightly better economic outlook, it still plans to normalize interest rates at a gradual pace. We believe at least 3 more rate hikes will come in 2018. The laggard inflation (the core gauge increased only 0.1% in October. It currently stands at 1.7% well below the FED target of min. 2%) will be closely monitored to see if a more hawkish tone can be set. Still, we believe a faster tightening should have been implemented as this elusive inflation is perhaps below what the numbers are showing. Quantitative Tightening is not enough. The FED will have to press harder on the brakes…

In Europe, rate normalization will come later in 2019. Prior to such, monetary tapering will occur and will be relative to inflation & geopolitical disruptions. Position portfolios for higher yields and add floaters. BREXIT uncertainties will wait on rates that should stay low in the UK.
In the US, watch carefully any yield curve inversion (it could well indicate the end of the market upside). We maintain the barbell strategy.

In Emerging Markets, rate normalization should also gather some strength. Attention to China that will probably tighten its monetary policy causing yields to rise and investors to buy more domestic bonds than US foreign ones… We favor Asian High Yield Bonds.
Keep exposure to convertibles as expected positive factors should gather strength to the segment.





INFLATION: A MUST

The inflation is a tax on the holding of money, for the benefit of the money issuer. No wonder why the Central Banks are expecting or wishing its return.

EQUITIES & SIMILAR

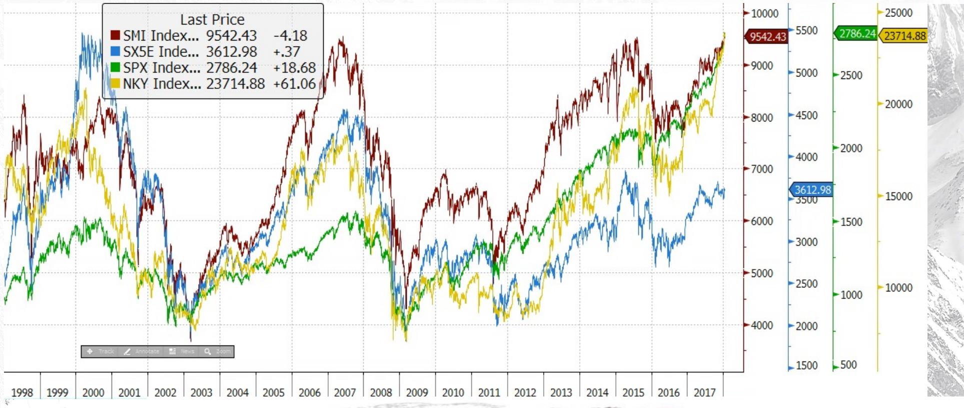
Risk-on stance but with less room for positive upside surprises. Today's market rally is fueled by momentum and liquidity. Perhaps we are underestimating the potential of the current expansion but some factors have been troubling. We are close to an euphoria but not there yet and some headwinds are ahead. We believe the Emerging Markets (EM) could get a boost looking at the earlier stage of their expansion in comparison with developed markets. Watch the elections in many of those EM countries. Increasing corporate profitability will be key. The Europeans finally posting globalized growth and markets have some catch-up to do to revert to previous sound levels. We like themes we called FIT (Future Investment Themes) and will focus our risk exposure towards those.

The US Tax reform has been approved but comes in a late-cycle context. It is less ambitious than the initial project but should anyway add some points to the GDP. It is worth to mention that many companies will be favored by the tax decrease but are still facing leveraged balance sheets. But the rally could run for some time in this environment. So far so good... Many investors will catch the train and do a run to risk emphasis that if not correctly assessed, will be devastating in their portfolios.
A troubling data: the S&P 500 dividend yield is lower than the one of the 2 years note!

The European countries are showing a better globalized growth. The corporate earnings are on the rise and if we can avoid the programmed "Europe Implosion" (EI), growth would add to positive performance. Globally, a 15% discount vs the US market levels have to be catched up.

We favor Emerging Markets as higher earnings yield suggests that they are likely to outperform the developed-markets. We like particularly Mexico, Russia and China. Attention to the latter as it holds some keys to the global growth trend (and particularly in case of any correction spread among Emerging's). Firmer commodities prices could help to add also some boost to their expansion.

A special focus on what we called the FIT (Future Investment Themes). A segment approach that will define trackers, stocks, bonds, structures, etc. with a bias towards themes of future: artificial intelligence, cybersecurity, sustainable, alternative energies, automation, digitalization, aging population, etc.



Biggest New Generating Countries

OUR STATUS

Vigilant and favor recession-proof securities as well as Future Investment Themes (FIT segments).

ALTERNATIVE INV. & SIMILAR

Are you holder of cryptocurrencies? If not: wait. If yes, you are potentially a big winner if you can get out on time... 2018 will not see a robust market trend like before. Volatility: dangerous lows should not persist this year. It should trend higher but any spike should not be considered like the first sign to the end of the stocks bull market. Rather look for spikes combined with other warning signs like earnings flattening or more restrictive financial conditions for any tendency clue. Oil good performance should abate a bit and the prices will follow the demand side rather than the offer one. Metals are out of fashion but can see a significant return of interest as they proved to be a good buffer of potential risks. Real Estate still present in our allocation. A Base metal to consider: Zink.

Central banks should criminalize cryptocurrencies in the next few months/years if Governments cannot regulate them. Moreover, the anti-money laundering model should apply to those new "crypto instruments". To decrease volatility and speculation, increase confidence and use, regulation is urgently needed. We do not invest in cryptocurrencies but look at the technology behind them, the blockchain, a very disruptive element but with the possibility to create new business models like peer-to-peer community exchanges.

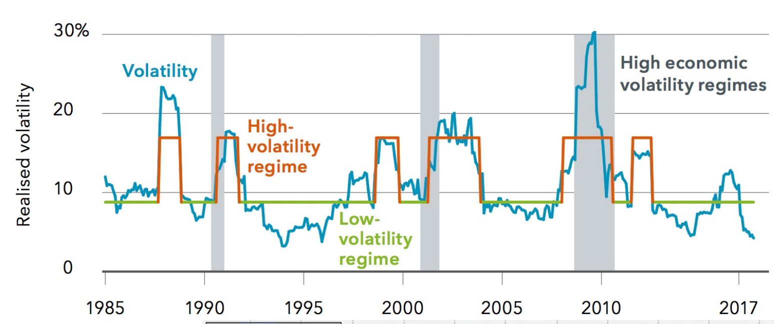
The VIX Index hit an historical low. It's level today is lower than each average of any year before market peaks and corrections. We should see price fluctuations again, with volatility spikes like the ones seen during 2015.

The Oil curve backwardation (downward sloping, or inverted curve) may attract demand and current prices should be sustained or even increase slightly as the offer side should be limited thanks to the OPEC restrain production (among others).

Precious metals like Gold were out of favor. Recent gains may by sustained and additional positive sentiments could be seen if fundamentals hits back the investors mind when thinking of geopolitical instability among other effects. Indications of a resurgence of the precious metal rally ...

As you know, the Hedge Funds segment is not part of our investment universe. Nonetheless we advise investors to take caution on any of them, particularly if liquidity restrictions are part of the deal. When investors wants to sell the funds in any bear market or corrections, negative headwinds are usually seen.

Realised monthly US equity volatility, 1985–2017



BLOCKCHAIN

A fundamental and decentralized database that includes a list of transactions. A block creation uses cryptography and encryption.

A WORLD IN TRANSITION

Globally, markets have been relatively immune to geopolitical risks and this is quite unusual. We do not believe the next crisis will come through in early 2018 but prepare yourself for a long period of lower returns. Fundamentals lag technicals.

The credit impulse (the flow of new credit issued by the private sector in % of GDP) contraction to monitor as it can show the premises of an economic slowdown. As mentioned in the last report, we believe the peak of the US cycle is behind us even if the US tax reforms can add some GDP points to the equation.

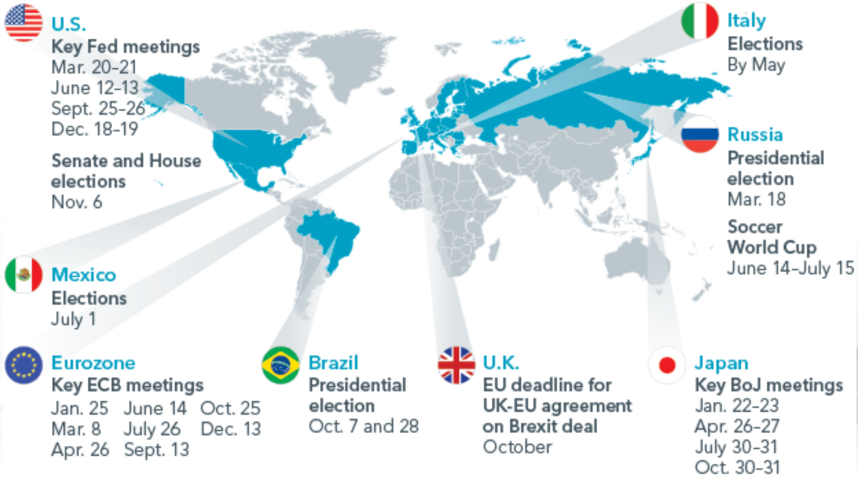
More significant labor-market disruption as Artificial Intelligence and innovative technologies proliferates. Note that this could be positive for the economic growth as the increase of capital investment in the segments should take over the consumption growth lead.

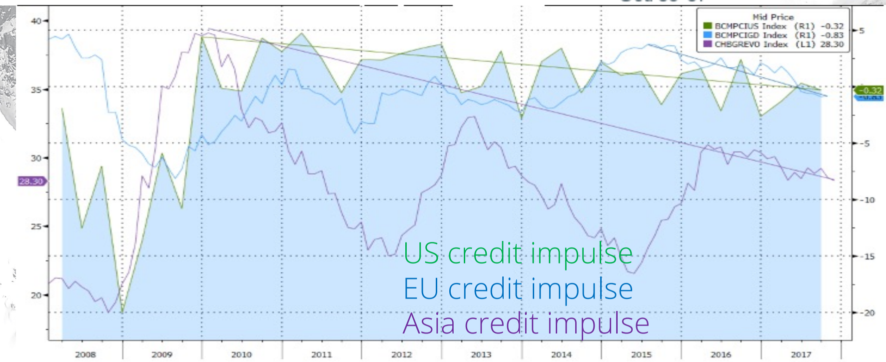
A parallel with the Metropolis movie: the megalopolis where the ruling families live, in idleness, luxury and entertainment, while the workers make the city work. The revolution will come from the people upset by the current economic discrepancies combined with digital technologies that will disrupt the traditional work and economy.

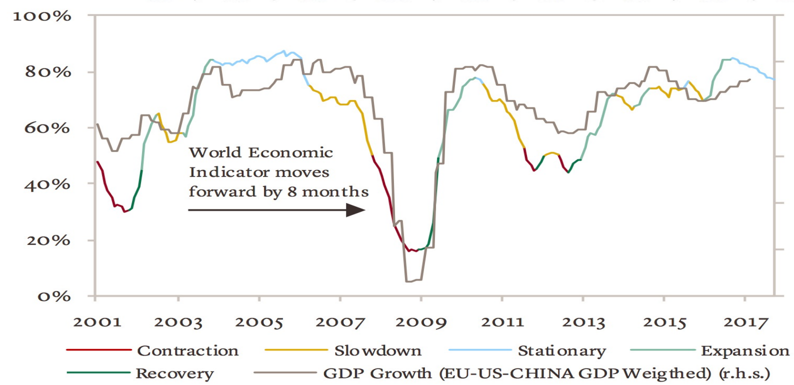
In contrast to the Lang film staging, we do not believe the technology is only negative by its effects. The 4th industrial revolution theme we spoke in our "Markets & Comments 2Q17" will gather importance and become an added value for productivity and improving performances.

Attention as the slingshot rumbles!

"Commute" with the markets and make adjustments if needed. A flexible Asset Management will be key in 2018. Our new approach will help to position the portfolios for any market trend as it gather interest on themes that will be key for the short, medium and long term.







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Sources: UBS,BlackRock, Lombard Odier, USGS/BMI, Bloomberg, World Wide Web, etc.

APPENDIX

ASSET CLASSES & ALLOCATIONS – 1Q 2018

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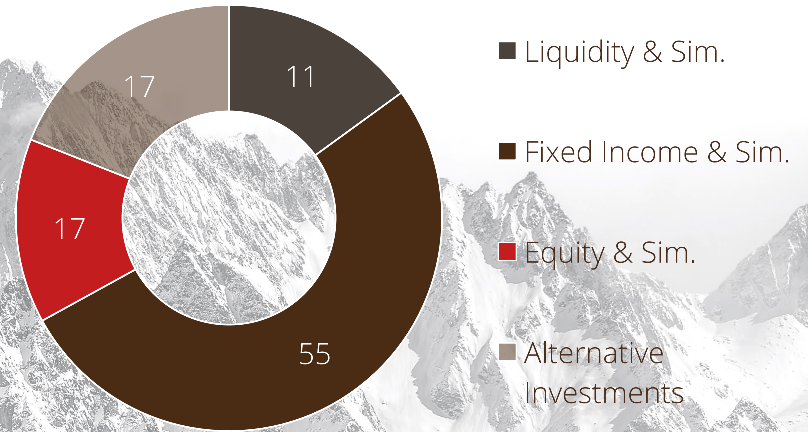
"Special USD Balanced" Asset Allocation*

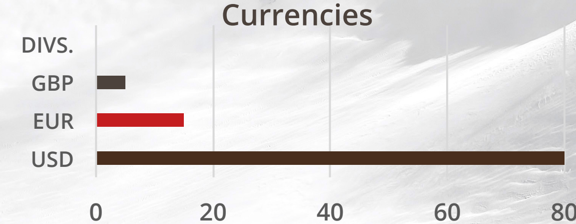


% ALLOCATIONS

ASSET CLASSES		CURRENCIES	
Liquidity & Sim.	11	USD	80
Fixed Inc. & Sim.	55	EUR	15
Equity & Sim.	17	GBP	5
Alternative Inv.	17	DIVS.	0
	100		100

*Example of a "Special Balanced" portfolio USD based. Not recommended for all investors.
** % opportunistic allocations included in each category (for details, contact your advisor)

Currencies



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