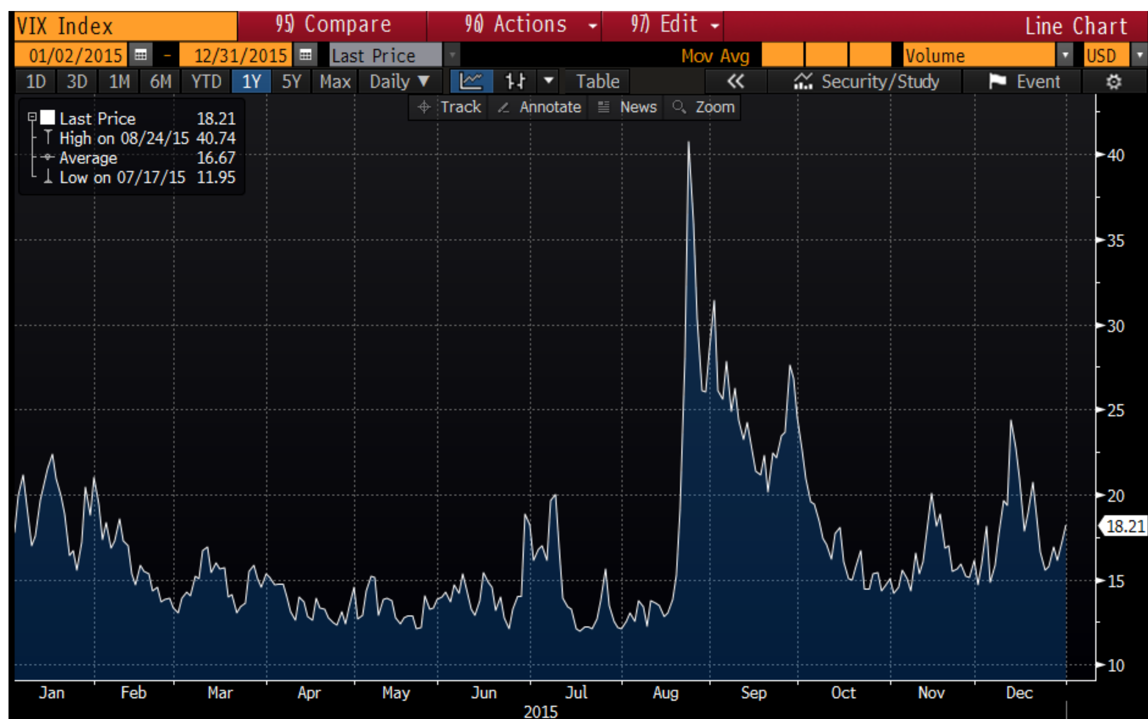
December 31, 2015

Dear Client

We are pleased to enclose your end-of-year portfolio statement, accompanied with a brief commentary on the key events of the year 2015 and the expectations for the upcoming year 2016.

Economic and financial summary of the year 2015

After a brief pause in early 2015, the general climate of uncertainty and volatility observed in previous years returned. The first half of the year was characterized by fairly favorable financial markets and global economies news, but the second half was more complex, due to a series of shocks not easy to forecast.

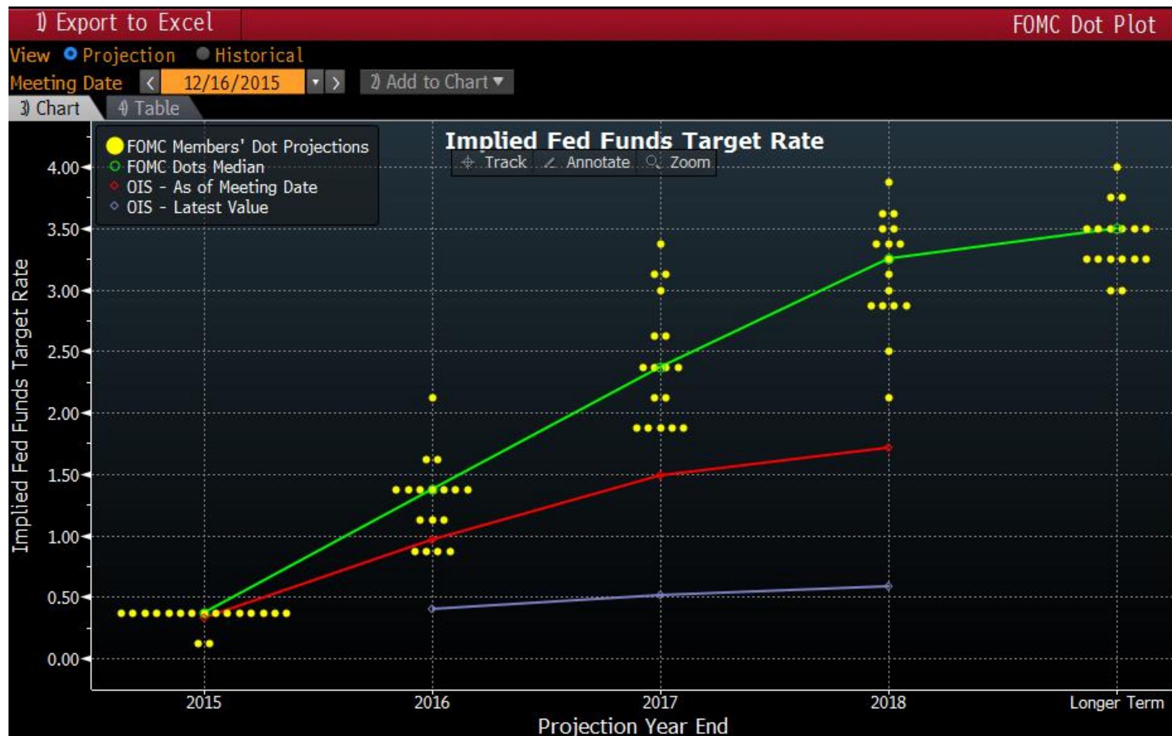


Source: Bloomberg

The year started (again) driven by the domination of central banks. In January, the Swiss Central Bank (SNB) surprised the market and abandoned the implicit EUR/CHF peg. The central bank countered the monetary tightening with a drastic interest rates cut, taking them into negative territory, and by intervening on the forex market.

Soon after that, the European Central Bank (ECB) began its government bond purchase program. The ultra-accommodative policy supported the economy in Europe, especially the peripheral countries (Italy, Spain) that surprised on the upside. The trend in consumer prices remained weak (risk of deflation!), prompting the ECB to extend its purchase program until (at least) 2017 and lower the deposit rate.

Another main topic was the expected reversal of the monetary policy in the US, on the back of solid economic indicators (especially employment). Many expected a first rise in the first half of the year. Although the US economy was weak during the winter months, it strengthened progressively during the year, leading to a first increment of the rate at the end of the year and a solid increase expectation in the upcoming years.



Source: Bloomberg

The second half of the year was marked by a series of adverse events. First, the Greek crisis continued and a solution was only found after tiresome and turbulent negotiations with creditors, enabling a third default in three years and avoiding the exit of the country from the Euro area.

The situation of the global economy worsened in August. Weak economic data and the unexpected devaluation of the Renminbi triggered fears of a potential slowdown of the Chinese economy. The nervousness was exaggerated, but domino effect observed in emerging markets highlighted the risk associated with a potential deceleration of China.

Market outlook for the year 2016

The economic outlook for 2016 continues to be uneven. While a mild acceleration in the global economy is expected due to a supportive policy mix and improving global trade, it is expected that developed economies will continue to fare better than emerging economies (due to subdue commodity prices).

One key feature of the current juncture is the strong services activity against the weakness in manufacturing seen in the US. This is relevant for the inflation outlook, which is then seen staying

low for longer as resources oversupply, from labor to commodities, setting a cap on input costs and inflation.

Global monetary policy is expected to continue very accommodative, and after years of retrenchment, the public sector contribution to growth is expected to be marginally positive.

The year 2016 will be influenced again by the political agenda (Brexit referendum in June and USD presidential election in November), and market volatility can be expected.

The divergence in policy cycles will also increase during the year, in our view. The FED policy normalization will have a number of consequences. The USD shall strengthen further due to rising interest rate differentials, leading the headwinds for the US manufacture and corporate earnings, global commodity prices and the recovery in emerging markets.

Elsewhere, a loose monetary policy is needed. Both Europe and Japan are still in a balance sheet recession: the private sector is reluctant to borrow money and focuses on reducing the existing debt, leading to very low (if not negative) inflation pressure.

Monetary policy coordination will be essential to achieve the expected effectiveness. In the emerging markets, all eyes will continue to be on China.

A look at the main asset classes in 2015

Equity market

The key theme of 2015 was “divergence” of monetary policies, which primarily helped the European and Japanese stock markets. Equities moved higher in the first half of 2015, driven by the energy sector and significant M&A activity.

In June, stock markets came to a halt, triggered by uncertainty about the situation in Greece, and a substantial reversal of the (rather irrational) Chinese stock market.

Equity markets run into difficulties at the end of August, following the devaluation of the Renminbi and fears of higher interest rates in USA. Stocks quickly took off again in autumn, stimulated by the rate cuts implemented in China, ECB statements regarding the launch of a new QE program, and the FED stated intention to follow a gradual interest rate tightening process.

Stock markets closed the year with mixed results, with good performance in Europe and Japan, with marginal gains (including dividends) in US and Switzerland, and with negative returns in emerging markets.

Source: Bloomberg

Due to the still attractive equity risk premium vs. bonds yields, equities remain our preferred asset class for 2016.

Bond market

2015 was a complicated year due to the slowdown in the emerging economies and the weakness of commodity prices. After a strong start of the year for all major fixed-income asset classes, the second half of 2015 featured a sharp decline of bond prices.

The volatility in the markets increased due to the less-than-expected economic data, especially with regards to inflation. This impacted the market's expectation regarding global monetary policy, leading to a further stronger dependency on monetary decisions.

During the first quarter of the year, bonds performed fairly well, leading to a positive performance in Switzerland, Europe, USA, and corporate bonds. The environment became though particularly troubled during the summer, due to doubts about the solvency of an unusually high number of issuers, derived from the collapse of the commodity prices and specific company scandals (e.g. Petrobras, Volkswagen). This lead to significant volatility and a widening of spreads in all credit categories (investment grade, high-yield and emerging markets).

Source: Bloomberg

Looking ahead to 2016, we expect a very gradual upward pressure on yield in the USD, while European markets should continue to be resilient. Bond prices are expected to continue at very high levels, with yield suppressed across all classes.

Foreign exchange markets

2015 was characterized by huge moves of Forex, from the January sharp Swiss Franc appreciation after the removal of the SNB floor against the euro and the progressive strengthening of the USD against most currencies.

Looking forward, currency moves will continue to be driven by the divergence in monetary policy regimes across the main countries. This speaks in favor of the USD, whose appreciation should continue in the next quarters. Against the normalization in US monetary policy, the Euro, Yen and Swiss Franc shall continue to lose ground vs. the USD in the near future.

Emerging currencies will also be subject to weakening pressure against the USD, although the pace of adjustment will probably be more moderate going forward. The unexpected decision by China to allow for more flexibility in the Renminbi last August triggered a broad based flight from emerging markets assets on fears of Chinese hard landing, which have, so far, proved exaggerated.

Source: Bloomberg

The evolution of the Chinese economy and it's monetary measures will be key in the year to come.

Commodities

After the collapse of the commodity prices in 2015, it is too early to call for a structural long position on the commodities space, particularly due to unfavorable supply/demand conditions, which are expected to weigh on the returns across the commodity spectrum for quite a while.

Today, we are witnessing a tangible oversupply response coming from important producers; oil is, notably, more advance into the production cutting process and remains under pressure due to a structural over-capacity (driven mainly from the increment of production capacity in the US).

Despite Chinese efforts to stimulate its economic activity, the demand for industrial metals continues to disappoint, creating a structural over-supply, and increasing the risk of spilt-overs into other markets (e.g. iron industry in Europe and USA).

China, who led the longest metal and commodities bull market, has become dormant as the primary buyer of industrial metals.

Finally, as we view the commodity trade as an early call under a risk-reward perspective, we cautiously await for a supply cycle turnaround that will eventually translate into a more constructive environment.