Edwards Wealth Management AG
Switzerland

MORA wealth management

Investment Policy

September 2018

Our market view in a nutshell – September 2018

- **Divergence** in **economic performance, monetary policies** and **earnings** growth have translated into a very **uneven financial market performance** this year between the US and the rest of the world. Moreover, the apparent resolution of the Fed to continue along its **monetary policy normalization** path is causing some **stress in the system**, manifesting itself in those areas that tend to be more affected, like emerging markets

- In our opinion, the sharp corrections in the **Argentinean Peso** and the **Turkish Lira** are not necessarily a harbinger of an emerging markets crisis, but just the result of these countries being singularly badly prepared to cope with **a higher dollar and increasing interest rates**. However, **contagion cannot be ruled out** if a market herd mentality prevails over discerning by fundamentals

- The **probability of recession** in developed economies looks **low by a number of leading indicators** like corporate spreads, consumer and business confidence, and financial market conditions. However, there is an increasing risk that the **Fed could make a policy mistake** as there is ample uncertainty about inflation and the neutral interest rate

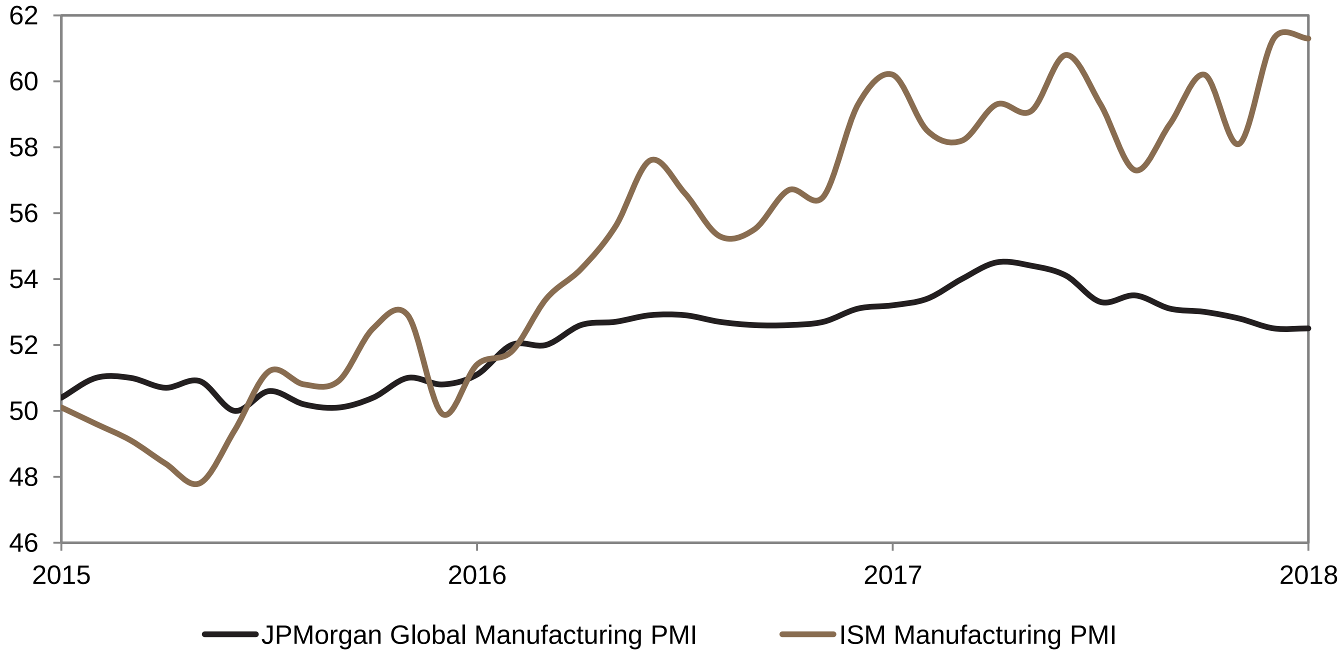
- Amongst the risks, a **slowdown in the Chinese economy** remains our largest source of concern, as a “hard landing” could prove devastating for the global economy and financial markets. The likelihood of such scenario materializing is increasing as a result of the **twin risks posed by the prospects of a Trade War and potential contagion from EM**

EWM Investment Policy

Asset Class		View	Rationale
Fixed Income	US Treasuries	+	Treasuries offer protection from a slowdown in growth – although this less likely with the fiscal stimulus in the US – whilst TIPS offer protection against rising inflation as a consequence of reflationary policies
	US Credit	+	Corporate debt and High Yield currently offer the best combination of risk and return. We prefer medium maturities as the yield curve has flattened considerably and there is little term premium to compensate for taking interest rate risk
	European Sovereign	–	High quality debt in Euros presents a very unattractive combination of risk and return as current yields offer very little cushion to weather potential interest rates increases
	European Credit	+	In European credit we only see value in subordinated debt, asset-backed securities and short-duration high yield
	Emerging Markets	–	We avoid Emerging Markets until there is more clarity on the new US administration trade policy, and the effects of a stronger dollar and higher financing costs for Emerging Markets are calibrated by the market
Equities	US	–	Equity valuations in the US remain very high, mostly supported by low long-term interest rates, but also due to a reacceleration in profit growth consequence of the tax reform and the deregulation agenda. We retain an exposure to the US market via quality growth companies
	Europe	+	From a relative valuation perspective, we like European stocks as they trade at lower multiples, and we expect profits to pick up as economic activity accelerates
	Japan	+	Japanese stocks are the cheapest in developed markets, but have suffered recently due to sluggish growth, and concerns about global trade
	Emerging Markets	+	Emerging markets have corrected sharply since the beginning of the year affected by a strong dollar and trade concerns. We deem the correction suffered has been excessive, and continue favoring India and Frontier Markets within EM
	Sectors & Themes	+	Amongst others, we favor Biotechnology and listed Real Estate
Alternative Investments	Commodities	+	Multi-manager/ multi-strategy hedge funds that offer daily liquidity offer a much needed source of diversification
	Multi-Strategy Hedge Funds	=	Our diversified commodities and gold allocations, further help us to increase diversification and to protect the portfolios against a scenario of rising inflation
	Private Equity	=	Investing in late-stage private equity provides access to the asset class with liquidity provision up to a certain degree

+ Overweight – Underweight = Neutral

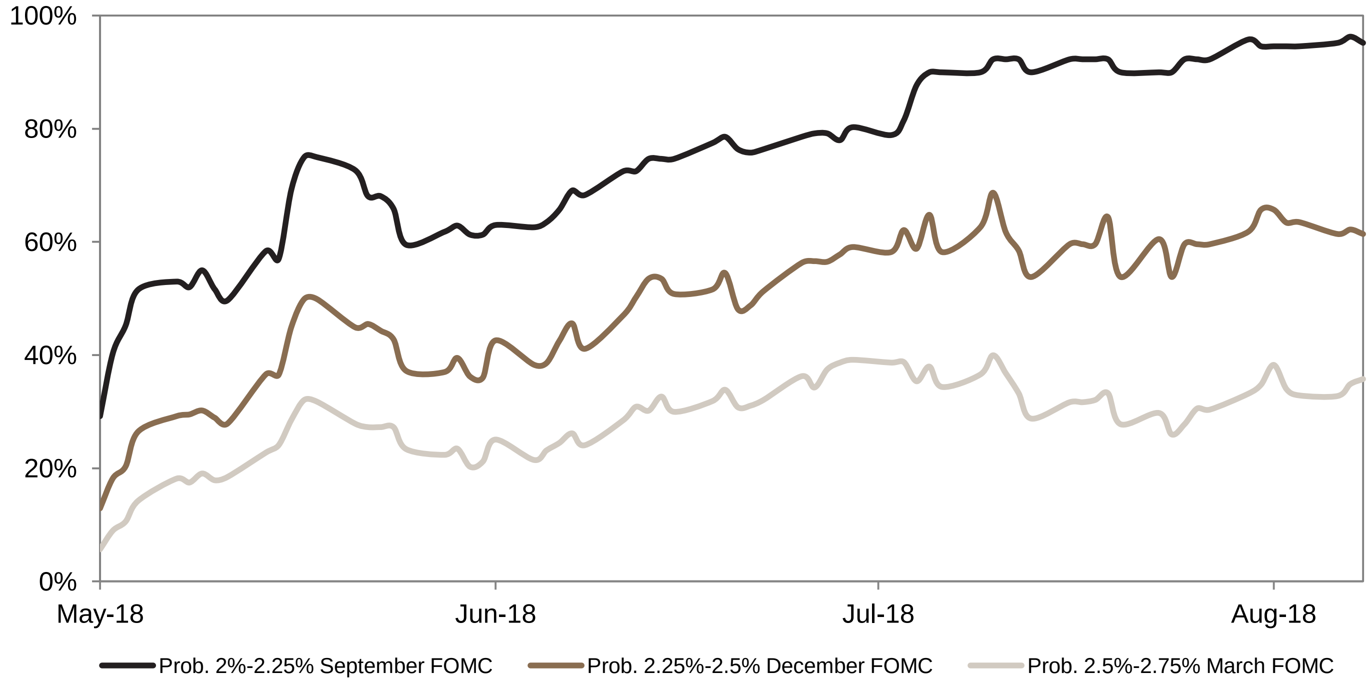
Economic divergence continues



- The **divergence in economic growth** between the US and the rest of the world **keeps on widening**, as US growth continues surprising on the upside, whilst Europe, Japan and emerging markets have slowed down
- **Leading indicators**, like the PMI, keep on pointing in this direction

Source: Bloomberg

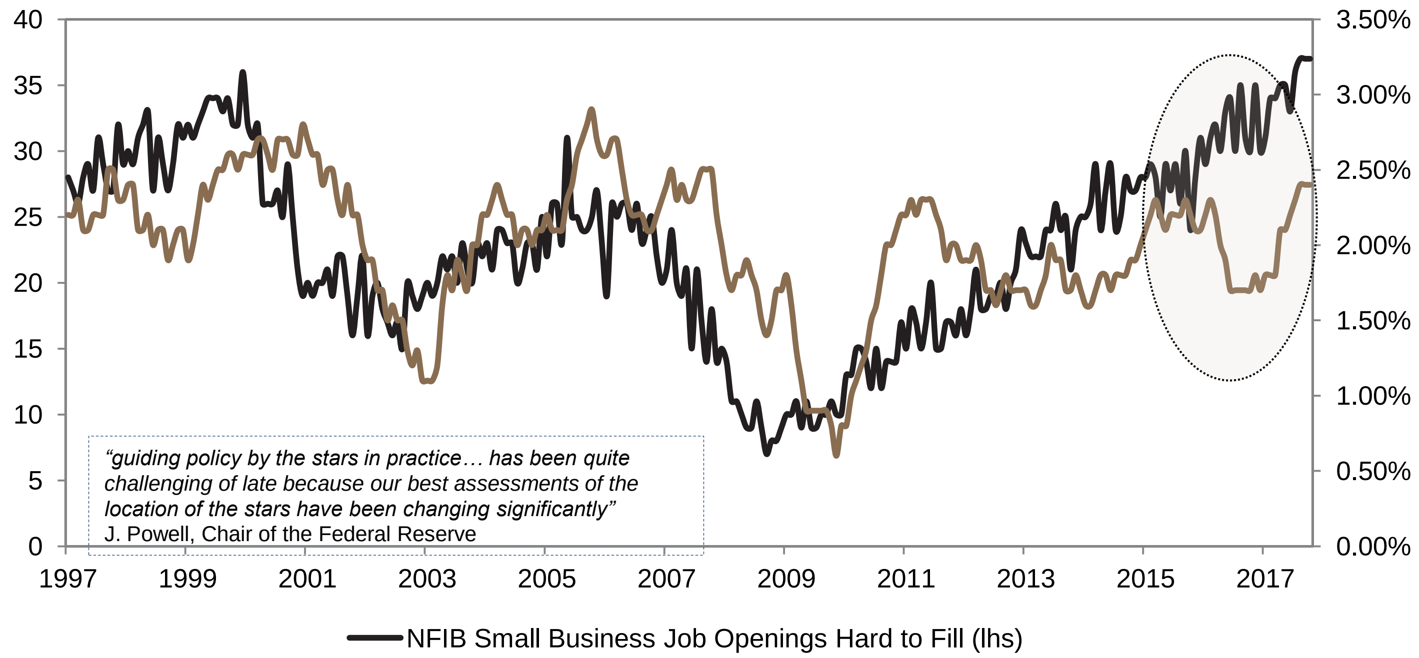
And unprecedented monetary divergence



- **Unprecedented monetary policy diverge** worsens, with the Fed progressing in its normalization path, whilst Europe, Japan, and (again) China, continuing with an ultra-accommodative monetary policy
- Looking at market **implied probabilities**, the Fed is expected to **tighten 2-3 times by March 2019**

Source: Bloomberg

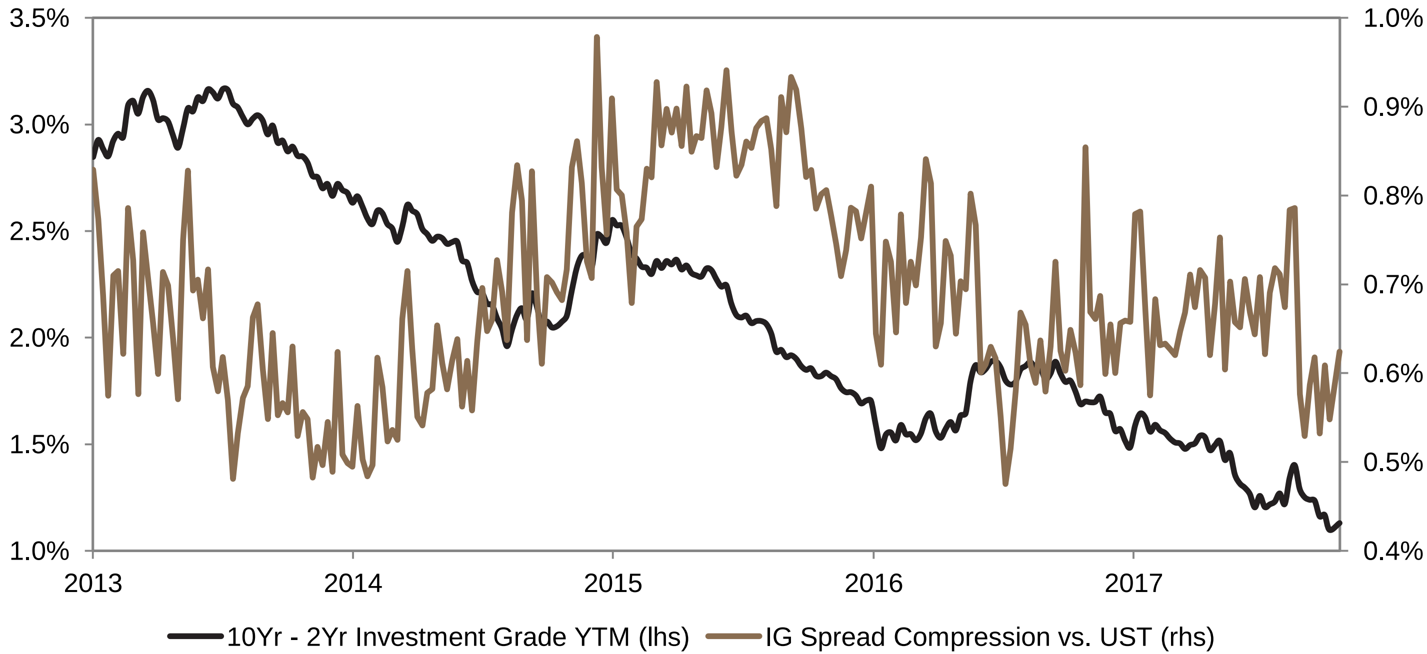
Deflation risk is over, but will inflation pick up?



- Inflation has normalized − particularly in the US − and **deflation is no longer a threat**, which provides support for the Fed, and other central banks, **normalizing interest rates**
- However, there are **few signs pointing to an acceleration of inflation**, despite the US economy running at close to its full potential. This increases the **risk of making a policy mistake** by tightening too aggressively

Source: Bloomberg

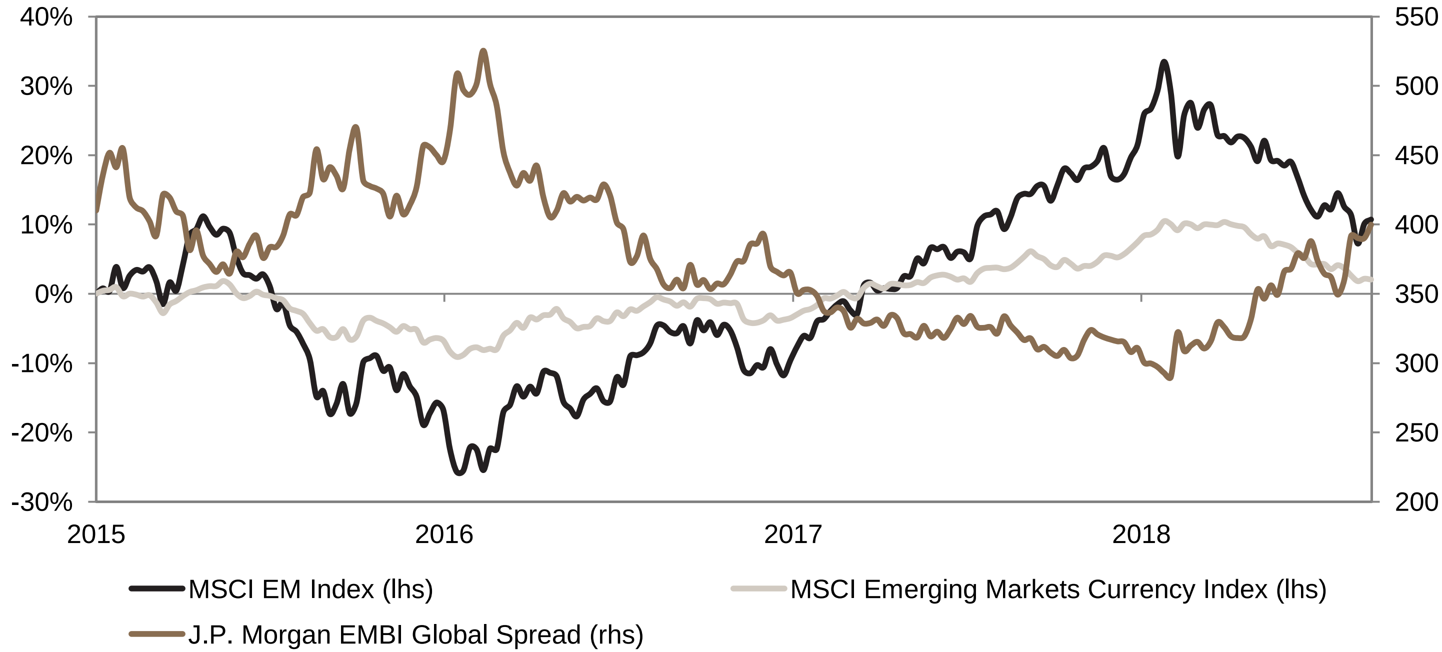
Market verdict is still unclear



- The **flattening of the yield curve** in the US can be interpreted as if the market were signaling an **increased probability of recession**, or as a reflection of very **low neutral interest rates** as a result of structural changes in the economy driven by globalization, technology and demographics
- **Corporate spreads** a rather pointing to the second factor, but in any case **the Fed needs necessarily to incorporate this clue into their decision making**

Source: Bloomberg

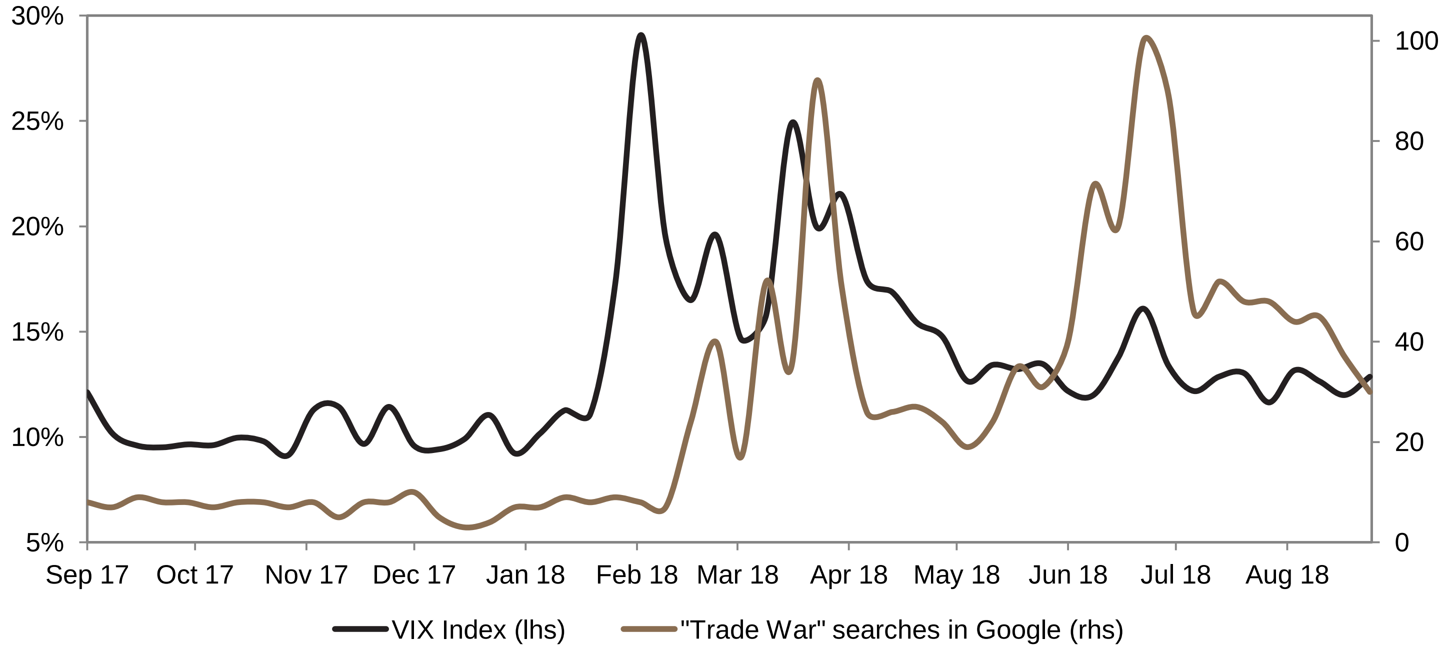
Emerging Markets under stress



- **Rising interest rates**, slowing global growth and a **stronger dollar** are impacting emerging markets currencies, bonds and equities alike
- Countries like **Turkey** or **Argentina** that in a weaker position (current account deficits, dollar financing, poor governance, etc.) are suffering the most. However, it is **too early to speak about a generalized emerging markets crisis**

Source: Bloomberg

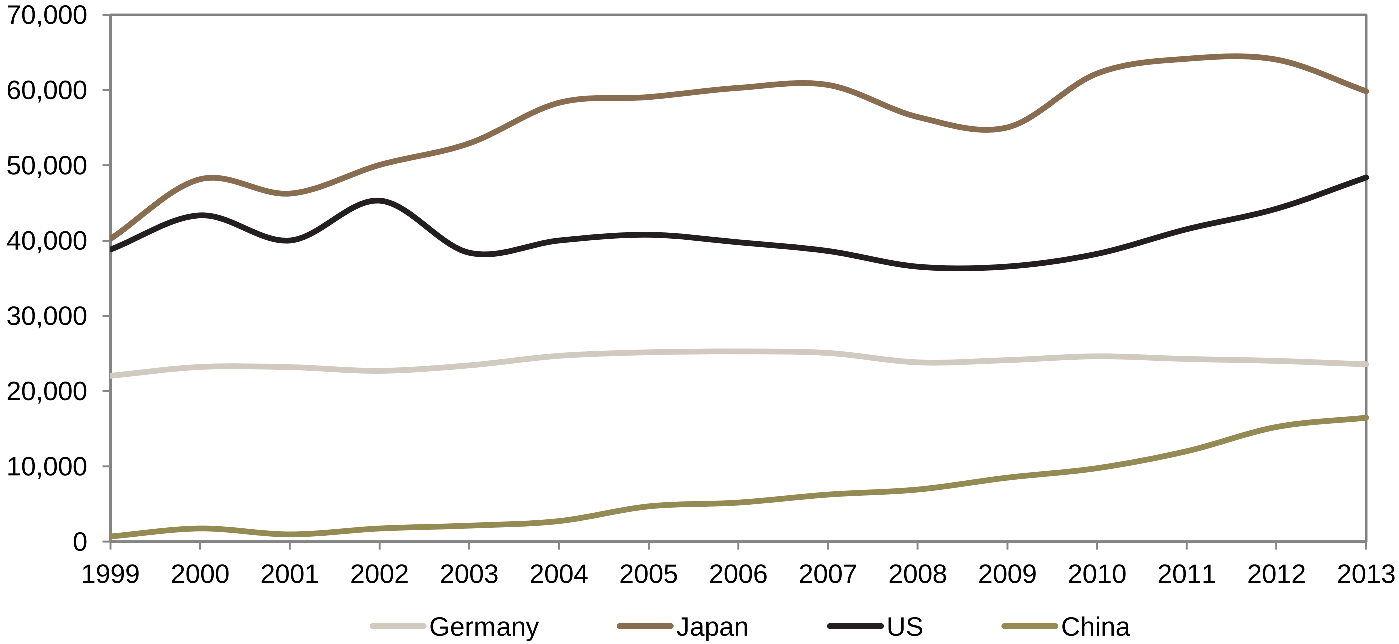
Trade war rhetoric discounted by markets



- **Trade war** rhetoric has been to a large extent **discounted by markets**, as it is becoming increasingly clear that it will be a **long-lasting dispute** that will not have an immediate resolution
- However, the **twin risks** of Trade War and EM contagion make us to be even more observant on China, as a repeat of the 2015-16 concerns about a **“hard landing”** of the Chinese economy would be heavily felt in financial markets

Source: Bloomberg and Google Trends

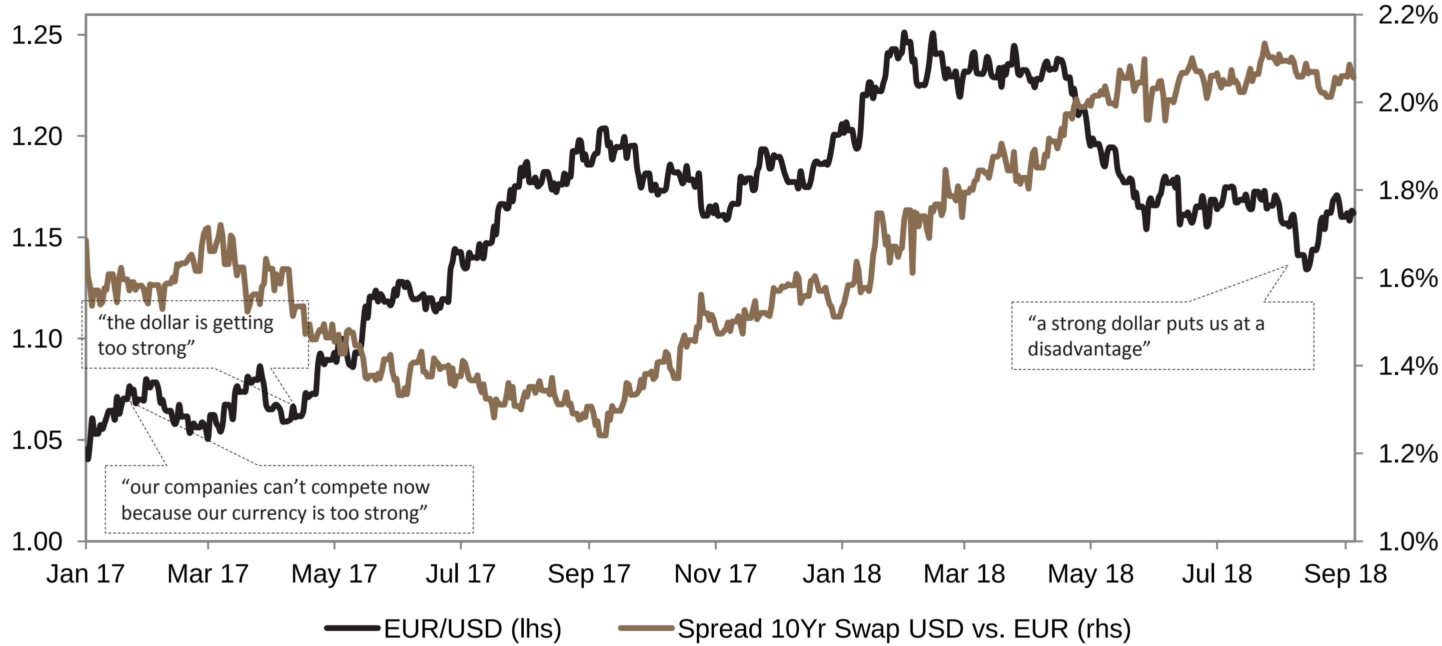
Economic war to be uncertain and long-lasting



- Beyond the short-term motivations to achieve **better terms of trade** with those trading partners with whom the US has a trading deficit, lies a concern of the country **loosing its hegemonic role**
- Although it is very likely that the Chinese economy will overtake that of the US within the next decades, **maintaining the US technological advantage is a strategic imperative** for the US administration

Source: Bloomberg

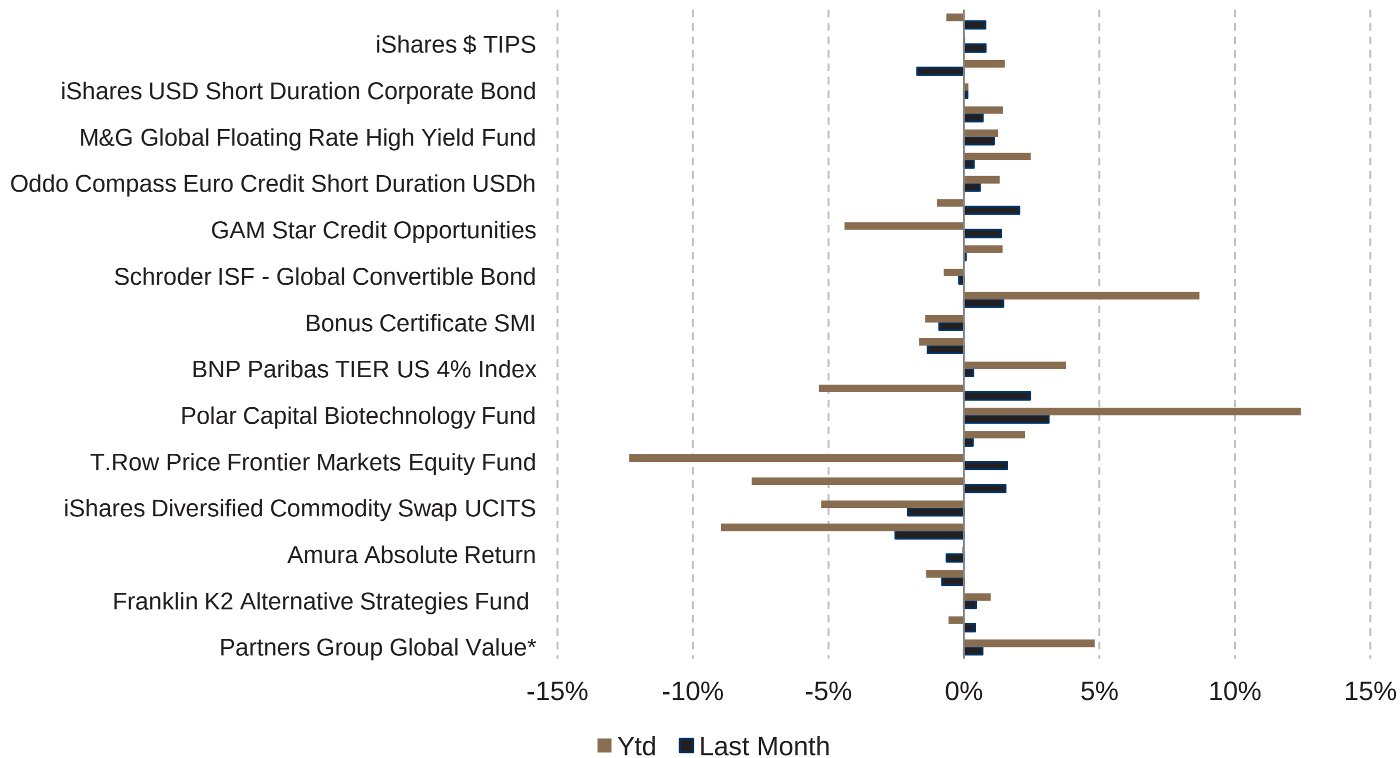
USD fundamentals will prevail over Twitter



- **Trump's tweets can do little** to weaken the dollar if **fundamentals are heavily underpinning the currency**
- **Interest rate differentials** and **growth differentials** are massively in favor of the dollar, whilst **inflation** is relatively similar and the **PPP level** is not that far form the current cross

Source: Bloomberg

Model portfolio evolution



Source: Bloomberg as of September 1, 2018
* Fund publishes monthly NAV with a 1 month of delay

Investment scenarios

	Scenario 1 Recession by political/policy accident	Scenario 2 Goldilocks	Scenario 3 New regime
Drivers	• Global economic slowdown caused by political accidents or policy errors (Trade war with China, EU breakup, a too aggressive Fed, etc.) • Deflationary scenario due to a combination of low growth and structural factors, although the rise of protectionism would be inflationary • The Fed will have to reverse curse, which would be complicated if inflation is rising	• The fiscal stimulus in the US provides a short-term impulse to the global economy, but not enough to attain a higher growth trajectory • Inflation, particularly in the US will pick-up, but remains subdued globally due to structural factors (demographics, low aggregated demand, deleveraging) • The Fed will continue its normalization path	• Growth concerns dissipate, with economic activity accelerating in US, Europe and Japan • Inflation in the US increases, as a consequence of president Trump's fiscal stimulus, and pulls other developed economies off deflation • The Fed will have to step up the pace of rate increases and/or reduce balance sheet
Market impact	• Correction in credit due to a rise in defaults and a widening of corporate spreads • Correction in equities due to lower projected earnings, though low rates will offer support • Sovereign and IG credit to profit due to flight to quality and the continuation of an ultra-loose monetary policy globally • USD neutral to weak as flight to quality is counterbalanced by low interest rates • Commodities will fall	• Equities appreciate moderately, with Europe and Japan catching up with the US • Credit spreads remain stable as the credit cycle is further elongated • Sovereigns suffer as monetary policy is progressively normalized • USD appreciate moderately due to higher interest rate differentials • Commodity prices will rise in the short-term, normalizing once the impulse vanishes	• Impact on equities will depend on how much real economic growth is sustained, and how accommodative the Fed remains • Sovereign and IG bonds will face steep losses due to higher rates, particularly if long-term inflation expectations rise • Corporate credit will correct moderately if inflation comes together with higher growth • The USD will appreciate, particularly against those currencies facing deflation • Commodities will gain from higher inflation
Probability	40% (+5%)	30% (-5%)	30%

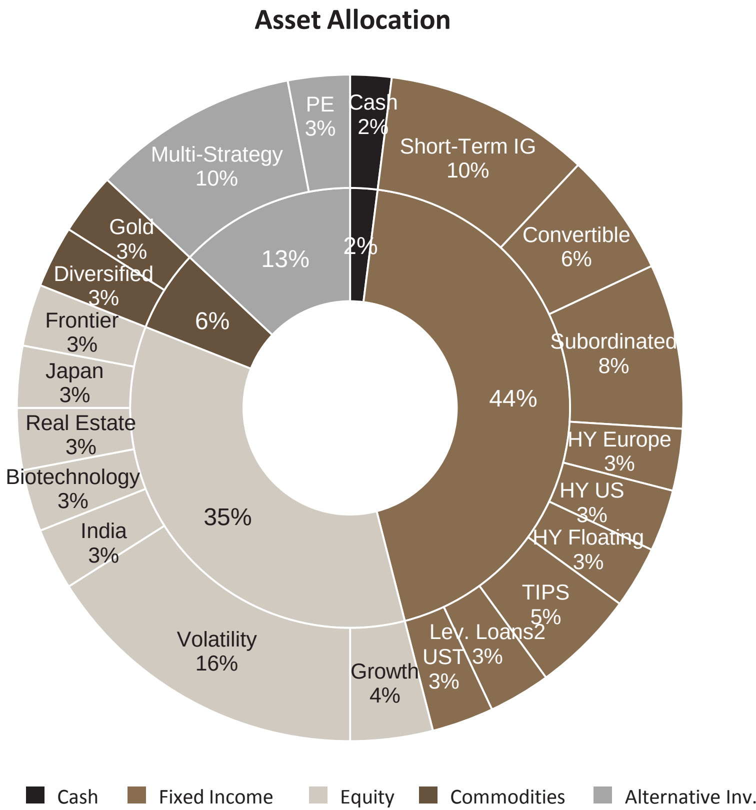
Short-term catalyzers

Fiscal stimulus in the US, improvement in macro-data globally, lower geopolitical tensions

Other risks

Trade wars, Spread of populist political parties, China slowdown, Terrorism

EWM Model Portfolio Balanced USD

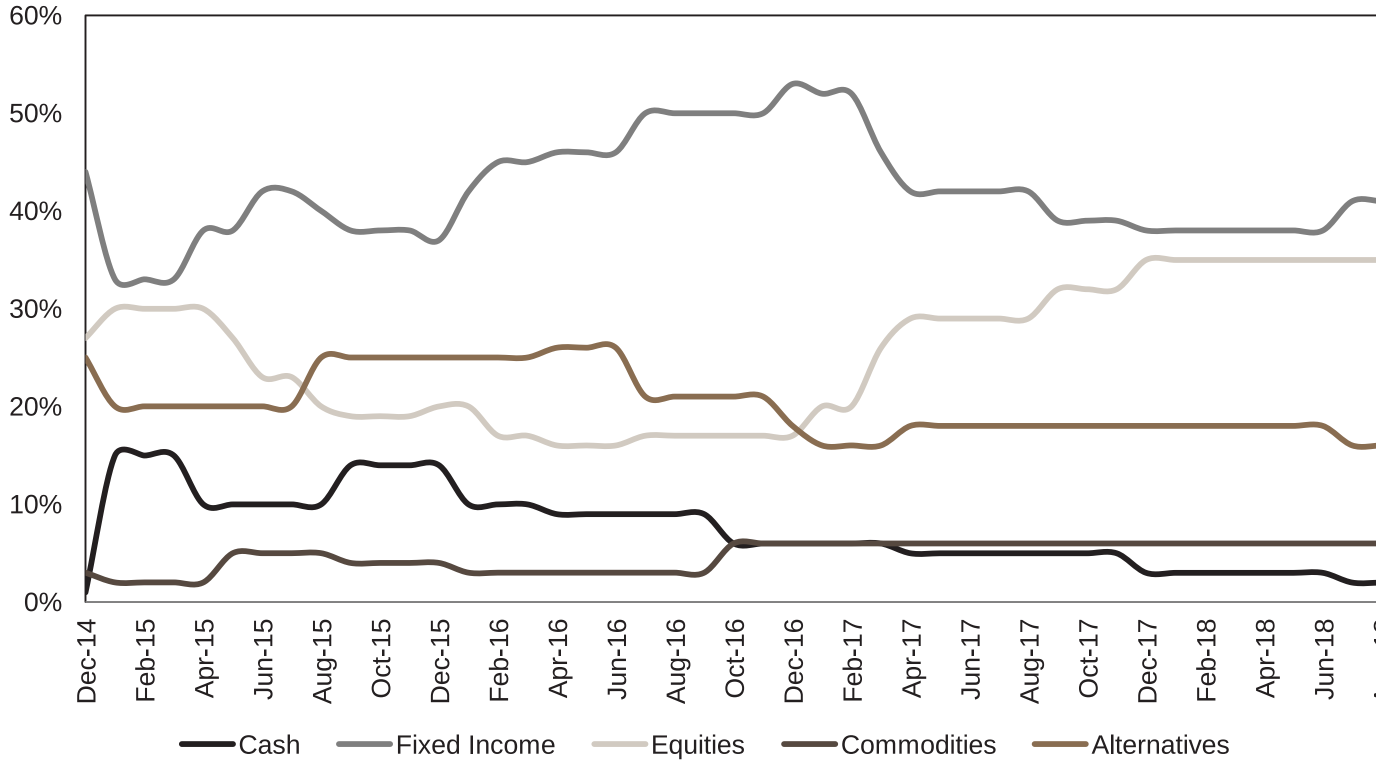


EWM Investment Profiles

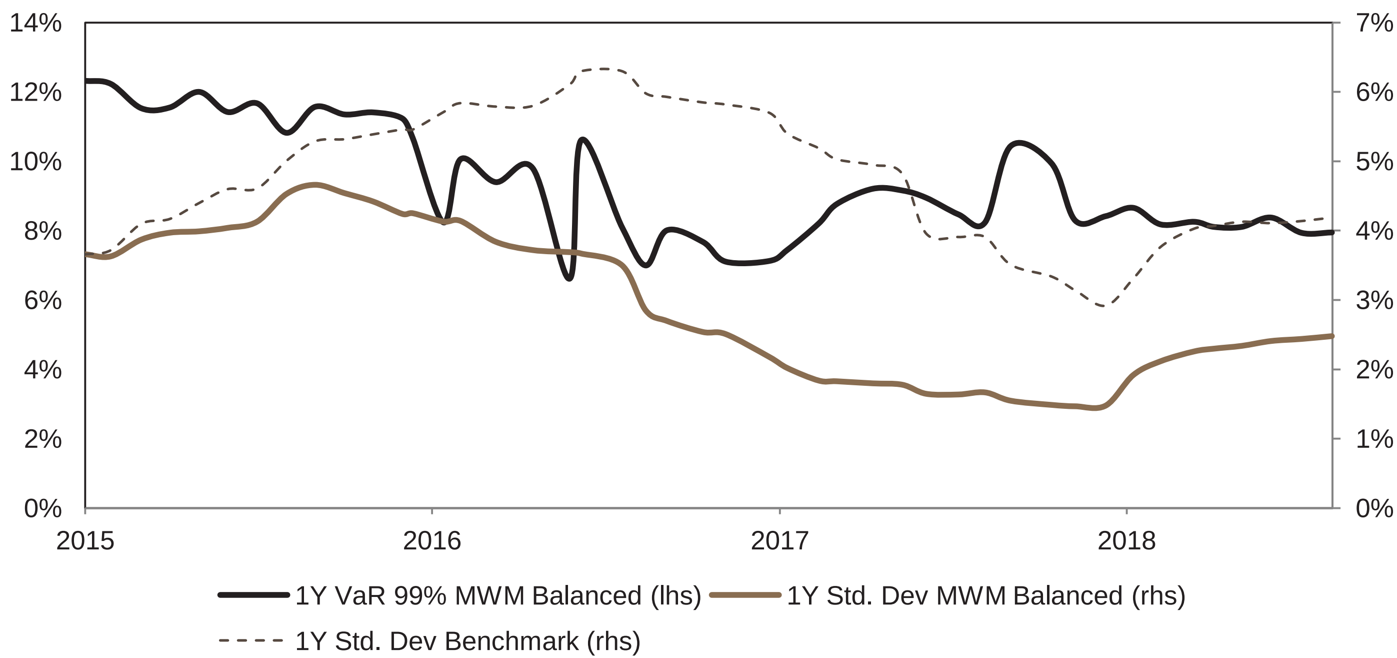
	Conservative	Balanced	Growth
Cash	5% 3%	5% 2%	5% 1%
Fixed Income	64% 62%	43% 44%	22% 26%
Equities	24% 23%	38% 35%	52% 49%
Commodities	2% 4%	4% 6%	6% 8%
Alternative Investments	5% 8%	10% 13%	15% 16%

Strategic Asset Allocation

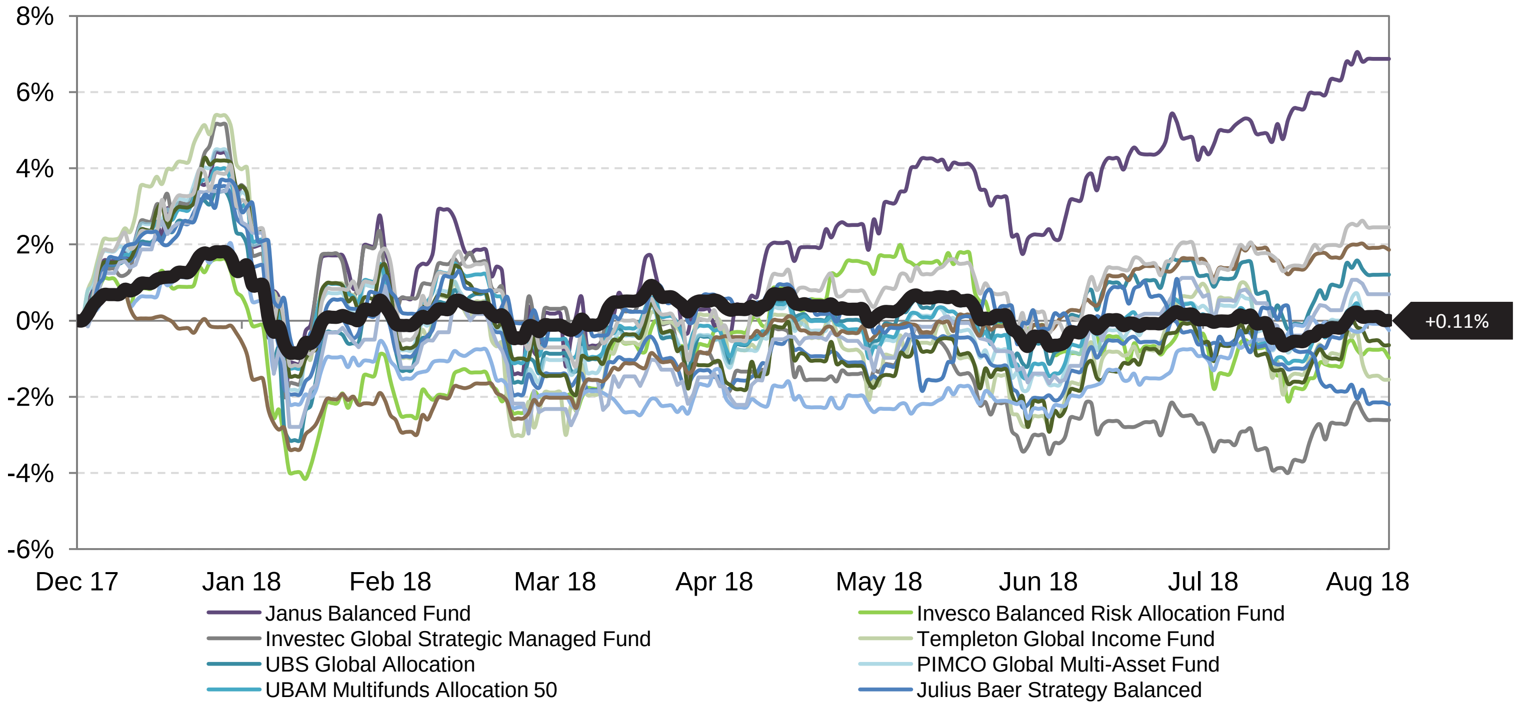
EWM Model Portfolio – Asset Allocation evolution



EWM Model Portfolio – VaR evolution



EWM Model Portfolio – Peer comparison

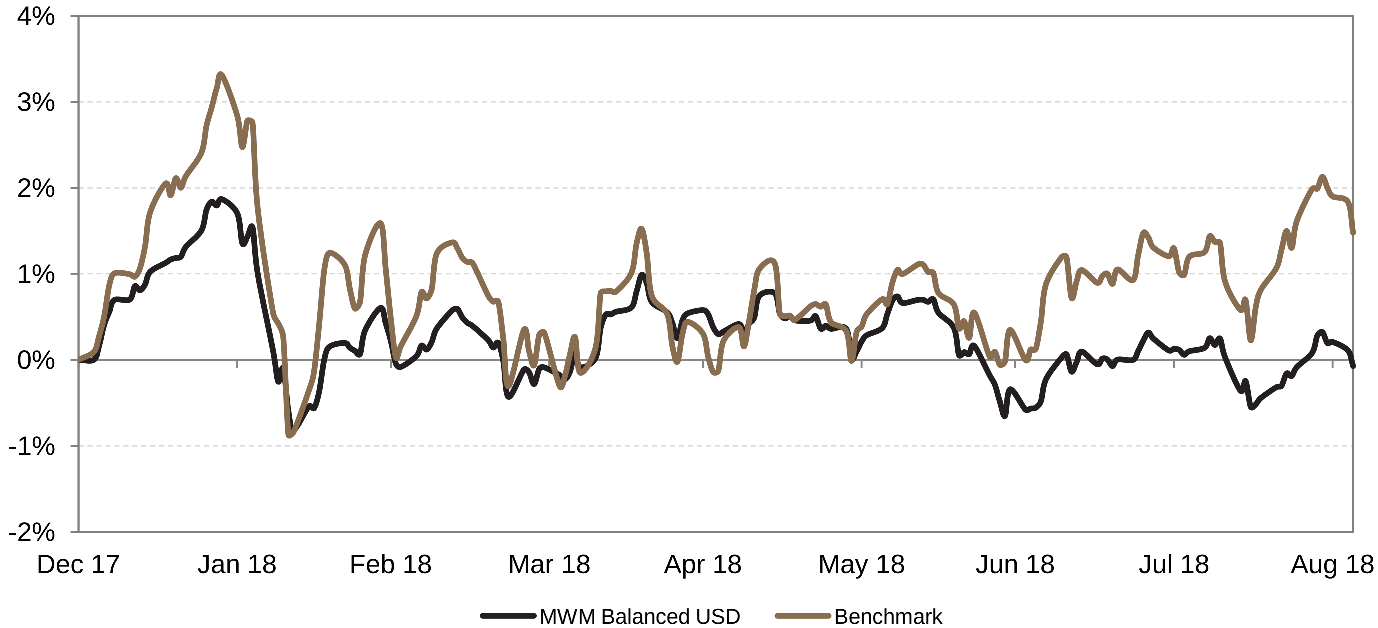


- **Total Return** (Ytd[1]): **7th out of 15**
- **Standard Deviation** (1 year[1]): **1st out of 15**
- **Downside Risk** (1 year[1]): **1st out of 15**
- **Sharp Ratio** (1 year[1]): **8th out of 15**

[1] As of September 4, 2018

Source: Bloomberg

EWM Model Portfolio – Ytd performance

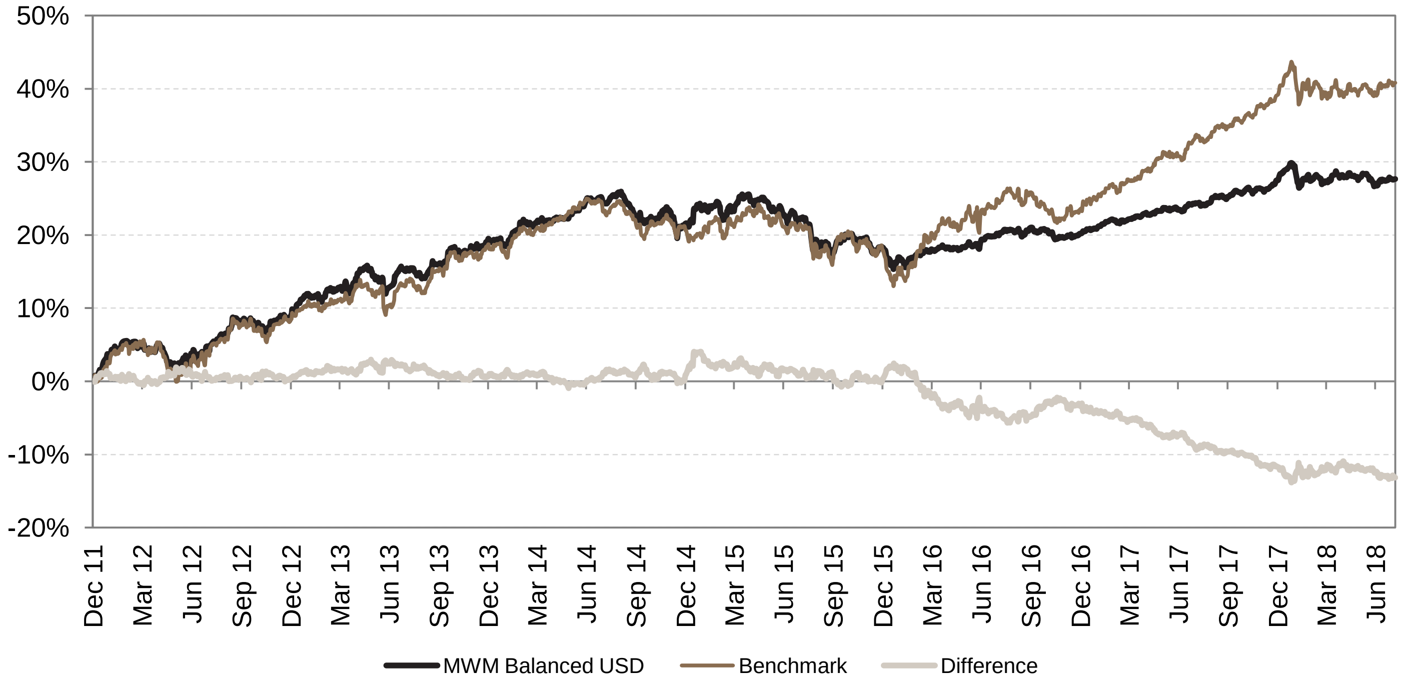


- **Total Return** (Ytd[1]): **0.11%** vs. **1.84%** Benchmark[2]
- **Standard Deviation** (Ytd[1]): **2.81%** vs. **4.84%** Benchmark[2]
- **Downside Risk** (Ytd[1]): **2.23%** vs. **3.76%** Benchmark[2]
- **Sharpe Ratio** (Ytd[1]): **-0.57** vs. **0.22** Benchmark[2]

[1] As of September 4, 2018

[2] Benchmark = 5% Fed Funds + 43% JPM Global Aggregate Bond Index + 38% MSCI World + 4% S&P GSCI + 10% HFRI FoHF

EWM Model Portfolio – Historical performance (1)

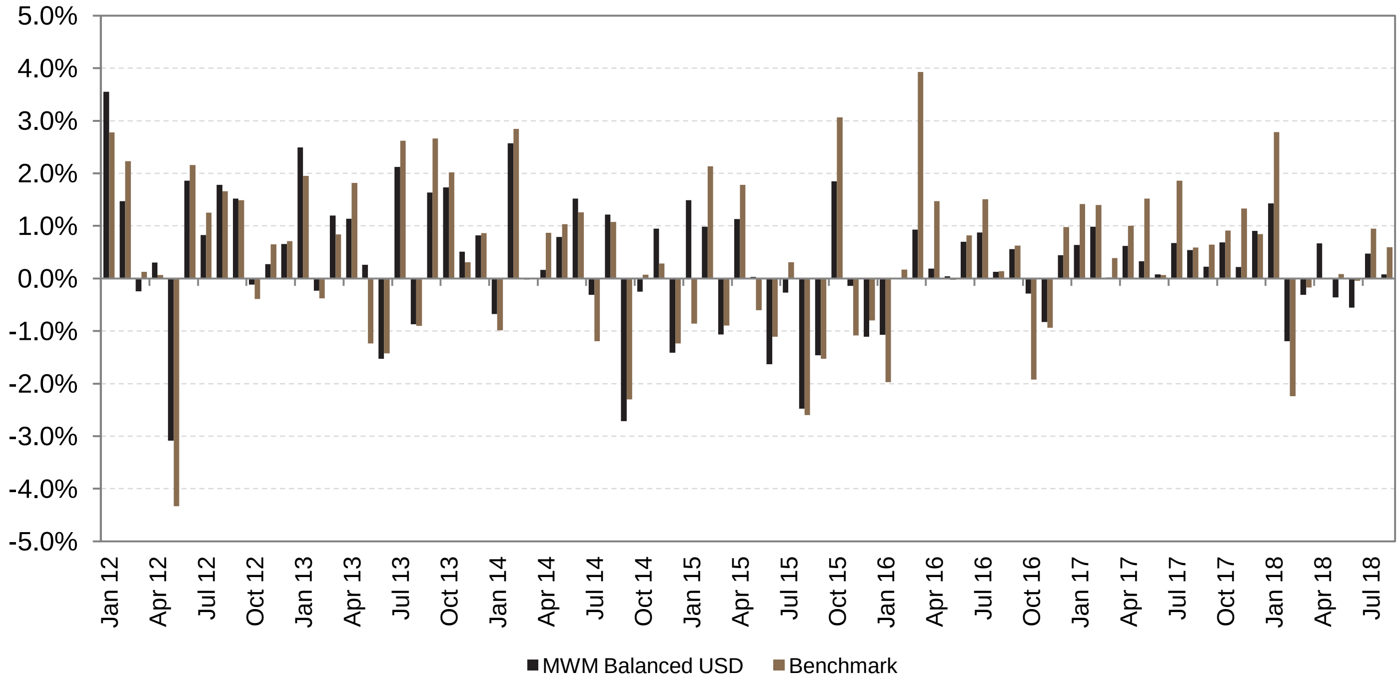


- **Total Return** (1 year[1]): **2.02%** vs. **5.61%** Benchmark[2]
- **Total Return** (3 year[1]): **7.36%** vs. **20.44%** Benchmark[2]
- **Total Return** (Since Jan 12[1]): **27.38%** vs. **41.12%** Benchmark[2]

[1] As of September 4, 2018

[2] Benchmark = 5% Fed Funds + 43% JPM Global Aggregate Bond Index + 38% MSCI World + 4% S&P GSCI + 10% HFRI FoHF

EWM Model Portfolio – Historical performance (2)



- **Standard Deviation** (1 year[1]): **2.48%** vs. **4.19%** Benchmark[2]
- **Downside Risk** (1 year[1]): **1.95%** vs. **3.27%** Benchmark[2]
- **Sharpe Ratio** (1 year[1]): **0.18** vs. **0.98** Benchmark[2]
- **Var 95% - 1day** (1 year[1]): **-0.24%** vs. **-0.46%** Benchmark[2]

[1] As of September 4, 2018

[2] Benchmark = 5% Fed Funds + 43% JPM Global Aggregate Bond Index + 38% MSCI World + 4% S&P GSCI + 10% HFRI FoHF

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