Prime Partners
SINCE 1998

MARKET INSIGHT

FEBRUARY 2019

Calm is returning to the markets, but it remains to be seen whether this will last

Has the beginning of a new year brought investors to their senses? This is a legitimate question given the dramatic difference in the way in which markets have performed over the last two months. Rising equity markets, the rally in corporate bonds, higher 10-year US Treasury yields and a more stable US currency are all examples of this change of investor attitude. January was clearly characterised by renewed risk appetite.

It is true that the correction during the last quarter of 2018, especially in December, had many of the hallmarks of a capitulation, against a backdrop of doubts about the future of the global economic cycle. In addition, monetary tightening had continued to pick up steam, with the end of the European Central Bank's quantitative easing programme and the Federal Reserve's decision

> "The excessive falls at the end of 2018 created a window of opportunity, albeit temporary, to buy equities."
>
> **FRANÇOIS SAVARY,** CHIEF INVESTMENT OFFICER, PRIME PARTNERS

to hike its key rates for the eighth time in this cycle.

The question then is whether we are seeing a relief rally, or whether the rise in risky assets, led by equities, is based on tangible elements.

First of all, there has been a change in tone to central bank statements.

The latter are cautious, i.e. more conciliatory regarding the inevitability of a monetary policy normalisation in the immediate future.

For example, M. Draghi is more circumspect about the economic outlook in Europe, threatened by greater risks. Similarly, Jerome Powell is less assertive about the Fed's intentions as regards the reduction of the Fed's balance sheet over the coming months.

These change have reassured investors since they limit the likelihood of seeing monetary policy mistakes push the global economy into recession in the short term.

This is a key point, since investors seemed convinced, just a few weeks ago, that a recession was inevitable. Moreover, recently released PMIs show that even if the economic outlook continues to weaken, it is "wrong" to assert that conditions justify fears of a recession. As a matter of fact, the sharp contraction of credit spreads is the best proof that such fears have abated lately

We have always defended the idea that the global economy is not threatened by a recession in the short term. We are obviously satisfied that investors have found reasons to be persuaded by this argument. However, this does not mean that we should dismiss such a risk out of hand. We are therefore we conitnue to pay special attention to managing the overall portfolio risk.

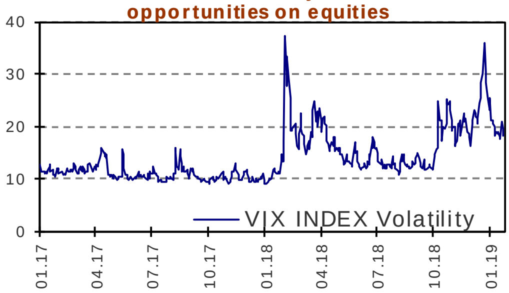
We are in the last phase of the economic and financial cycle and (geo)political risks mean that we cannot afford to be complacent.

In this regard, trade tensions remain a key issue, not only because of their effect on market sentiment, but also because of their immediate impact on economic growth and corporate earnings, with the results announced in recent weeks largely confirming this reality.

As announced, we adjusted our allocation in January by increasing our equity exposure. The excessive falls at the end of 2018 created an opportunity, albeit temporary, to buy such assets.

We have not changed our regional allocation. We favor emerging and, Japanese stocks.

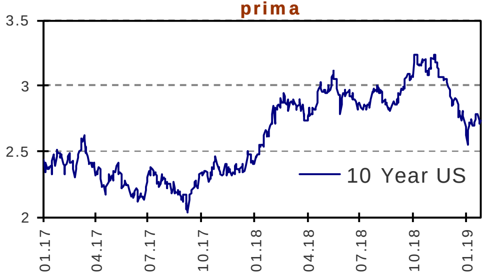
Excessive volatility offered opportunities on equities



However, we have reduced our underexposure to US equities, which suffered badly in December. This choice was based on the fact that we are unlikely to see a stock market rally without the participation of US stocks. Moreover, we have chosen to increase our exposure to the technology sector (widely represented in US indices) in order to reduce the defensive bias of our sector allocation.

We have increased our equity risk through index-based products, but also through conviction-based investing. The latter approach seems particularly appropriate in an end of cycle scenario, which should enable portfolio managers who focus on stock picking to do well.

Lower yields means improved equity risk prima

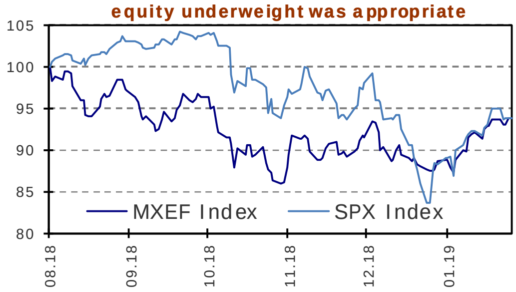


The increase in our equity exposure should be considered within the general context of our overall strategy, which remains focused on risk management. Therefore. we are not departing from our policy which aims to favour equities at the expense of bonds, credit in paticular, and maintain a good weighting of uncorrelated assets.

This leads us on to the question of performance. The strength of markets in recent weeks has enabled our investment strategy to generate very satisfactory returns, especially since all of our portfolio positions have risen, in particular equities.

In this regard, our thematic products have staged a comeback, while the decision to increase our gold exposure at the end of 2018 has proved sound.

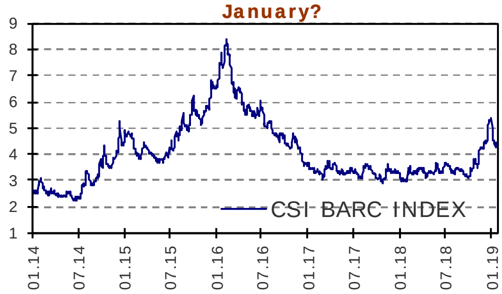
After the fall in December, reduce the US equity underweight was appropriate



In conclusion, market conditions at the beginning of 2019 are far calmer than in the last quarter of 2018. However, we still believe that a new volatility regime has taken hold of the markets on a lasting basis.

We have considered it appropriate to seize opportunities, while not losing sight of the importance of risk management.

End of fears about a credit bubble since January?



With the earnings season now under way, we are adopting a wait-and-see approach in order to get a clearer picture of corporate earnings growth.

There has been a significant development on this front, though, as analysts are no longer sharply revising down their EPS growth expectations. This suggests that we might have seen the worst as regards this key indicator for the performance of markets.

We will continue to take advantage of opportunities as they arise over the coming weeks, while bearing in mind that we cannot unreasonably extrapolate future returns based on the strong performance of our allocations in January.

Geneva, 31 January 2019

Prime Partners SA
Rue des Alpes 15
P.O. Box 1987
1211 Geneva 1

www.prime-partners.com

CONTACTS

François Savary
Chief Investment Officer

Jérome Schupp
Equity Analyst

Julien Serbit
Portfolio Manager

T: 41 22 595 09 97
fsavary@prime-partners.com
jserbit@prime-partners.com