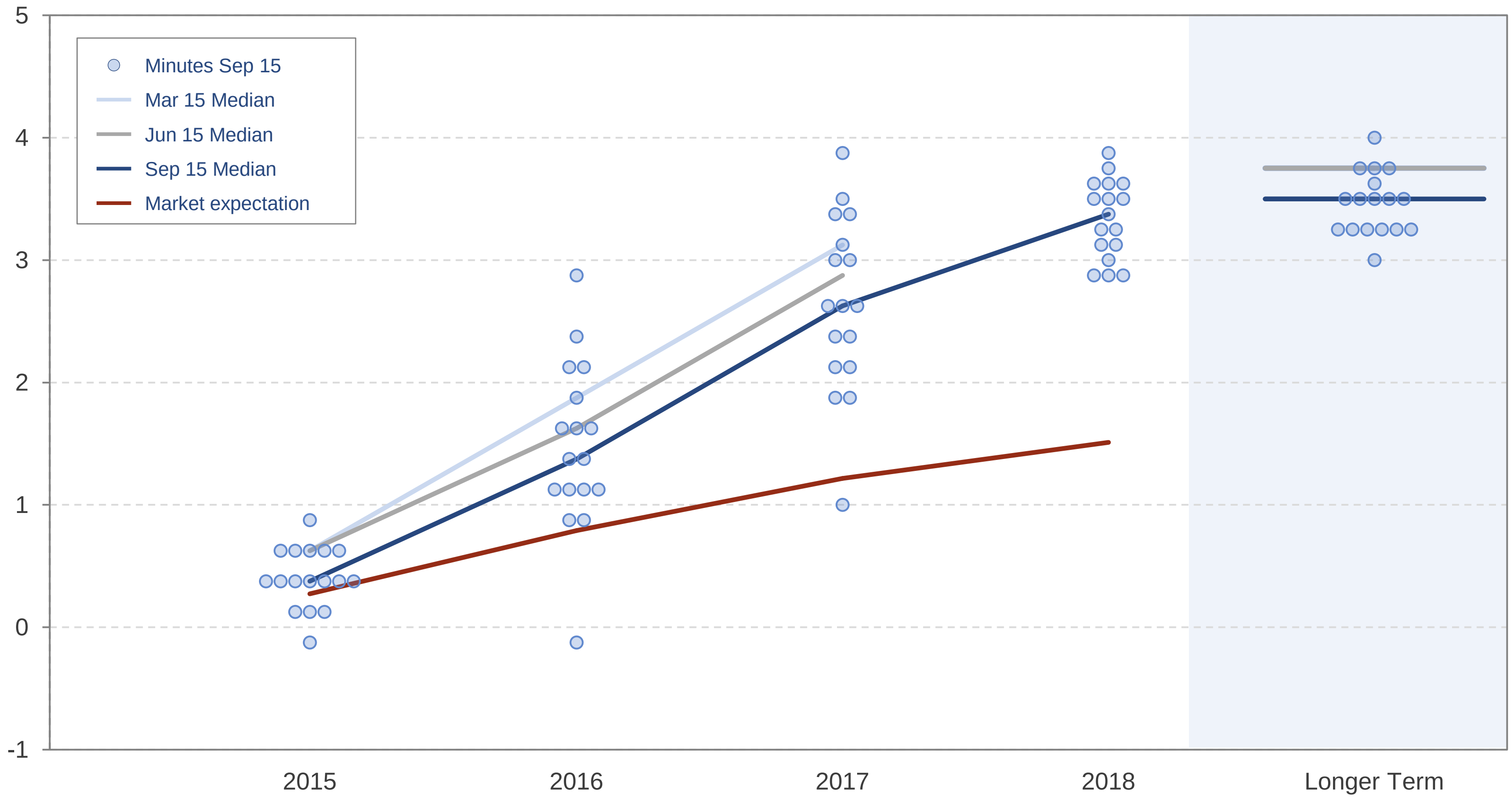
Investment Policy

MORA WEALTH MANAGEMENT

December 2015

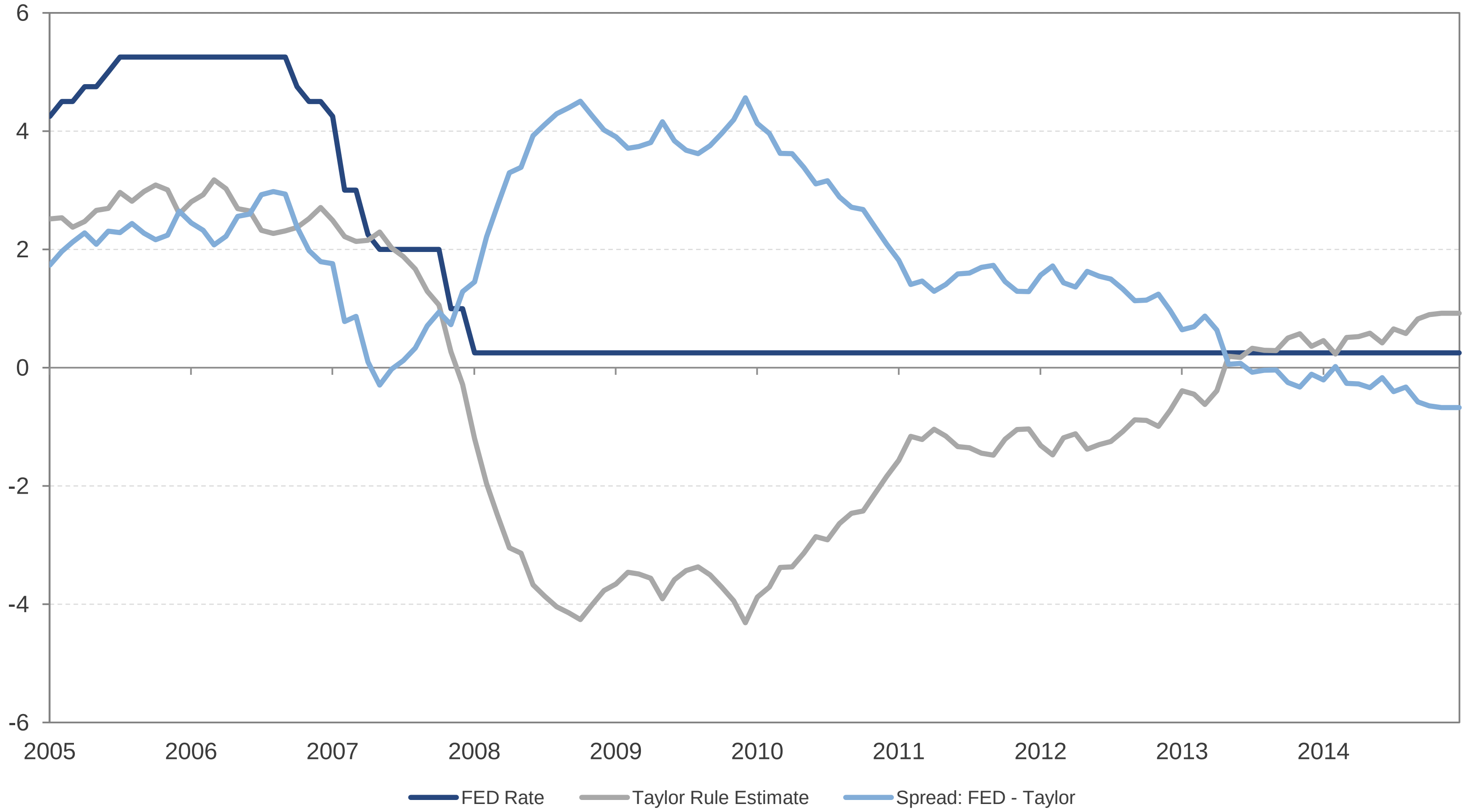
Market vs. Fed



- The market is currently implying a **77% probability** of a Fed lift-off in **December 2015**
- However, there is a **significant divergence** between **market expectations** of future interest rate rises and those of the **FOMC members**, as depicted by the "Fed dots"
- **Closing this gap** will certainly create **market volatility**. If the Fed were to come closer to the market, possibly due to lower economic growth than expected, this could prove troublesome for credit and equity markets whilst good for high quality bonds. The reverse may probably happen if the market had to catch up with the Fed

Source: Bloomberg

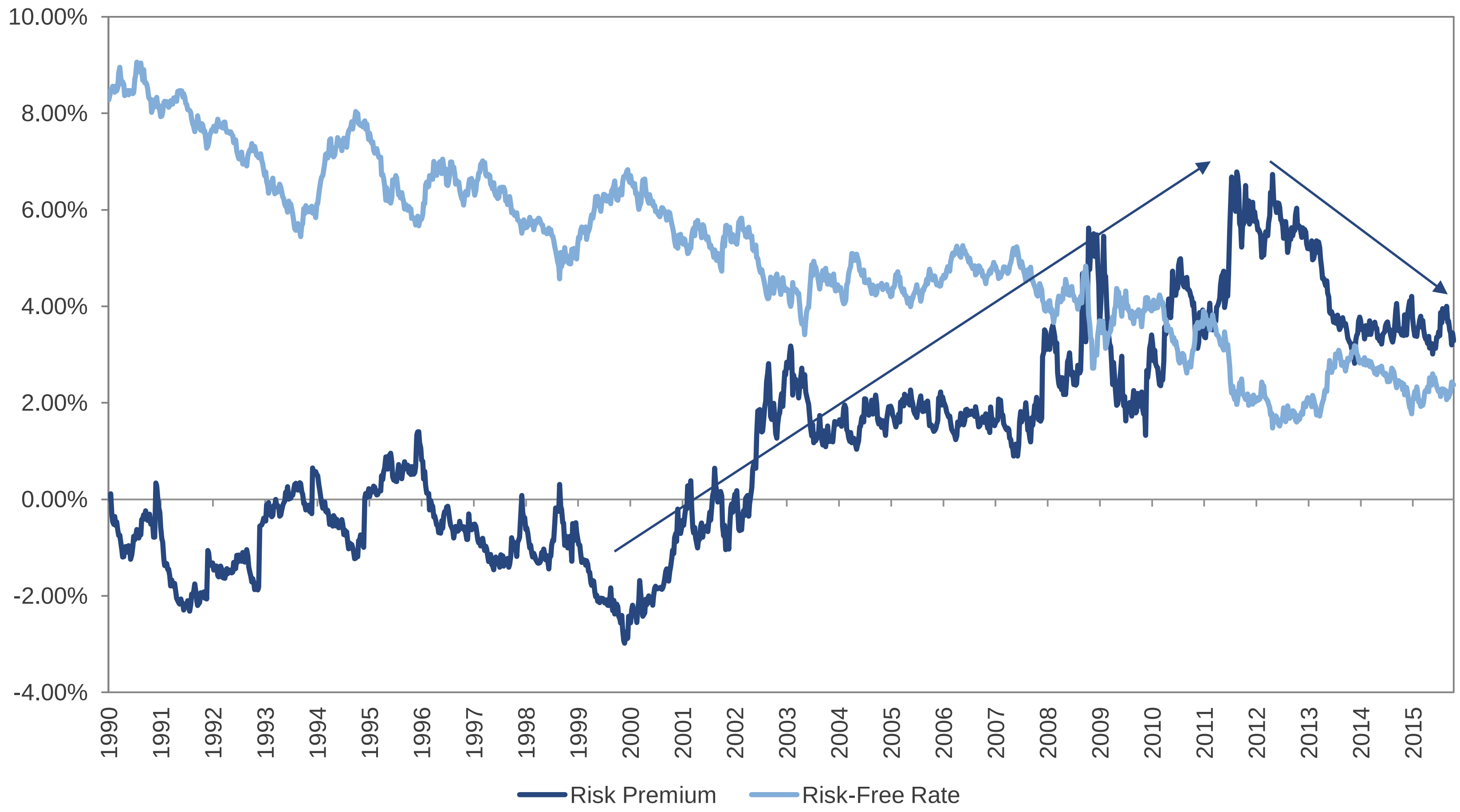
Taylor rule as a guide



- According to the **"Taylor Rule"**, which derives the nominal interest rates as a function of inflation and economic output potential, **Fed rates** should be at an estimated level of **0.92%**
- However, it remains **uncertain** whether the economy is currently running **close to full capacity**, defined by a non-accelerating inflation rate of unemployment (NAIRU) at 5%, or if on the contrary **there is still slack**, as the number of Americans who remain **out of the labor market**, and hence not included in unemployment statistics, is larger than ever

Source: Bloomberg

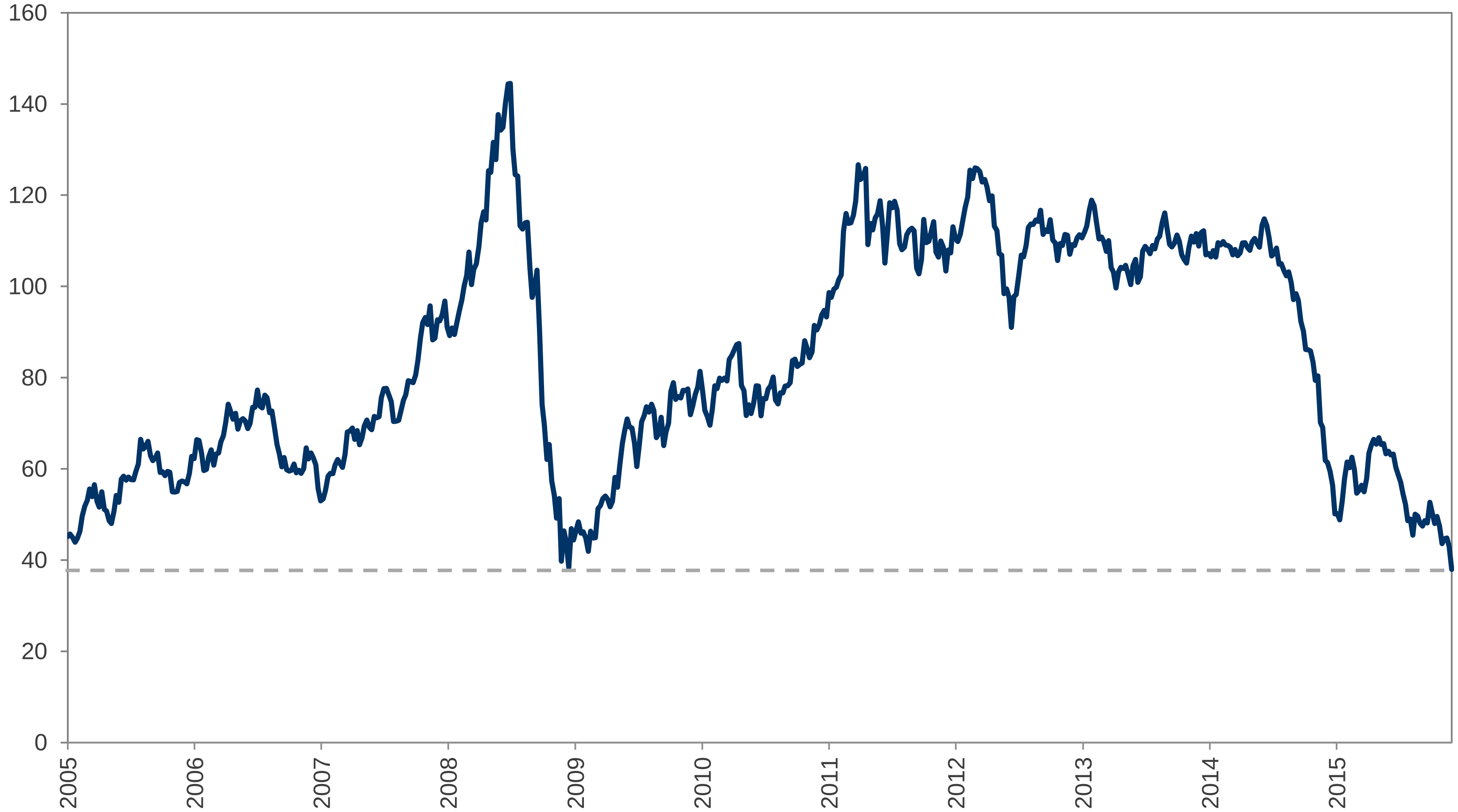
Low rates magnify market sentiment's impact



- As central banks have embarked into **ultra-expansive monetary policies**, the **relative importance** of the risk premium – driven by **market sentiment** – has markedly **increased**
- Nonetheless, **the market has increased the risk premium** over the monetary loosening period, which can be seen as a reflection of **prudence** over how long can interest rates remain that low. However, **since 2012 the risk premia has started to shrink** as stock prices have kept rising faster than earnings

Source: Bloomberg. Risk premium is defined as the difference between the earnings yield and the 10-year Treasury Bond yield. Discount rate is defined as the sum of both.

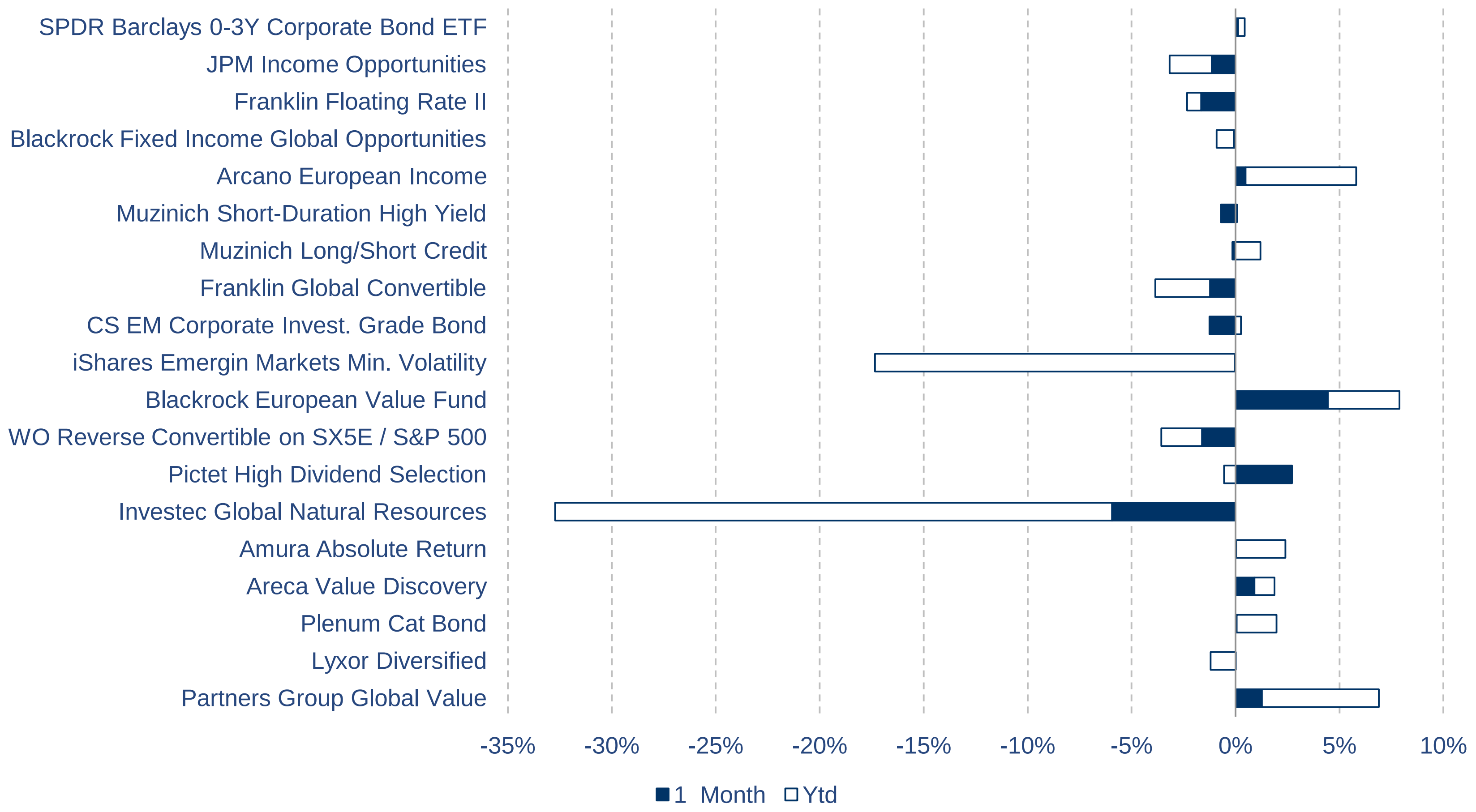
Oil trading at 2008 levels



- The barrel of Brent is trading at its lowest since 2008. This is -39% from a year ago and -73% from its peak in 2008. We have moved from talking about **"Peak Oil"** to the **"Oil Glut"** in a mere few years
- If oil price is a **leading indicator** of the economy, we should be heading to a massive economic slowdown, Two alternative factors could be playing a role; first we might be witnessing the **end of the OPEC** as supply from non-members grows. Second, producers may be reckoning that the **"Carbon Transition"** may take fewer years than initially expected

Source: Bloomberg

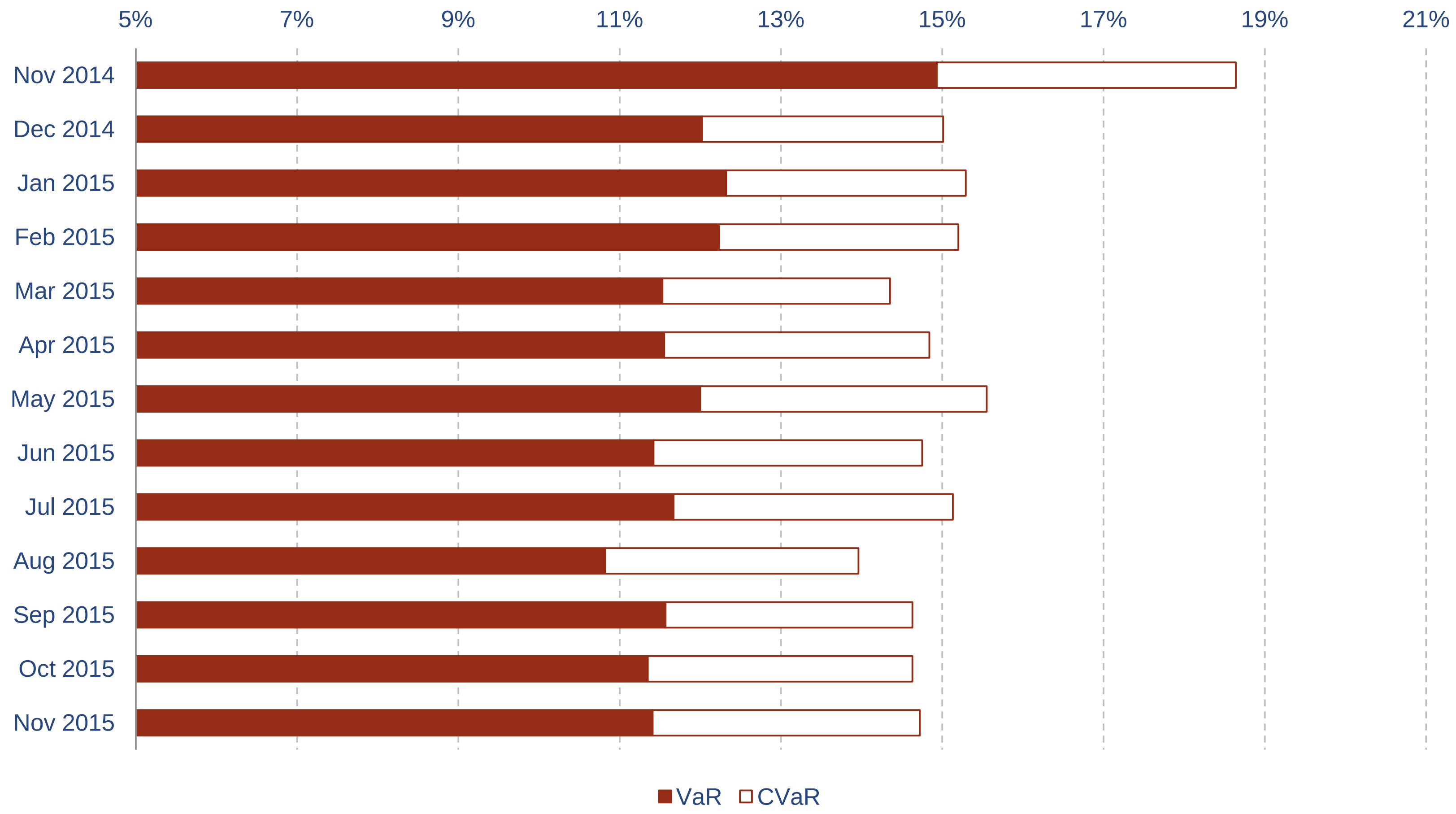
A bad month for credit



- November was another **bad month for credit,** with only **investment-grade** performing positively within the fixed income allocation
- **Equity** performance was **positive**, with the **exception** of **commodity-related** companies
- **Alternative investments** overall added to November's performance

Source: Bloomberg as of November 6, 2015

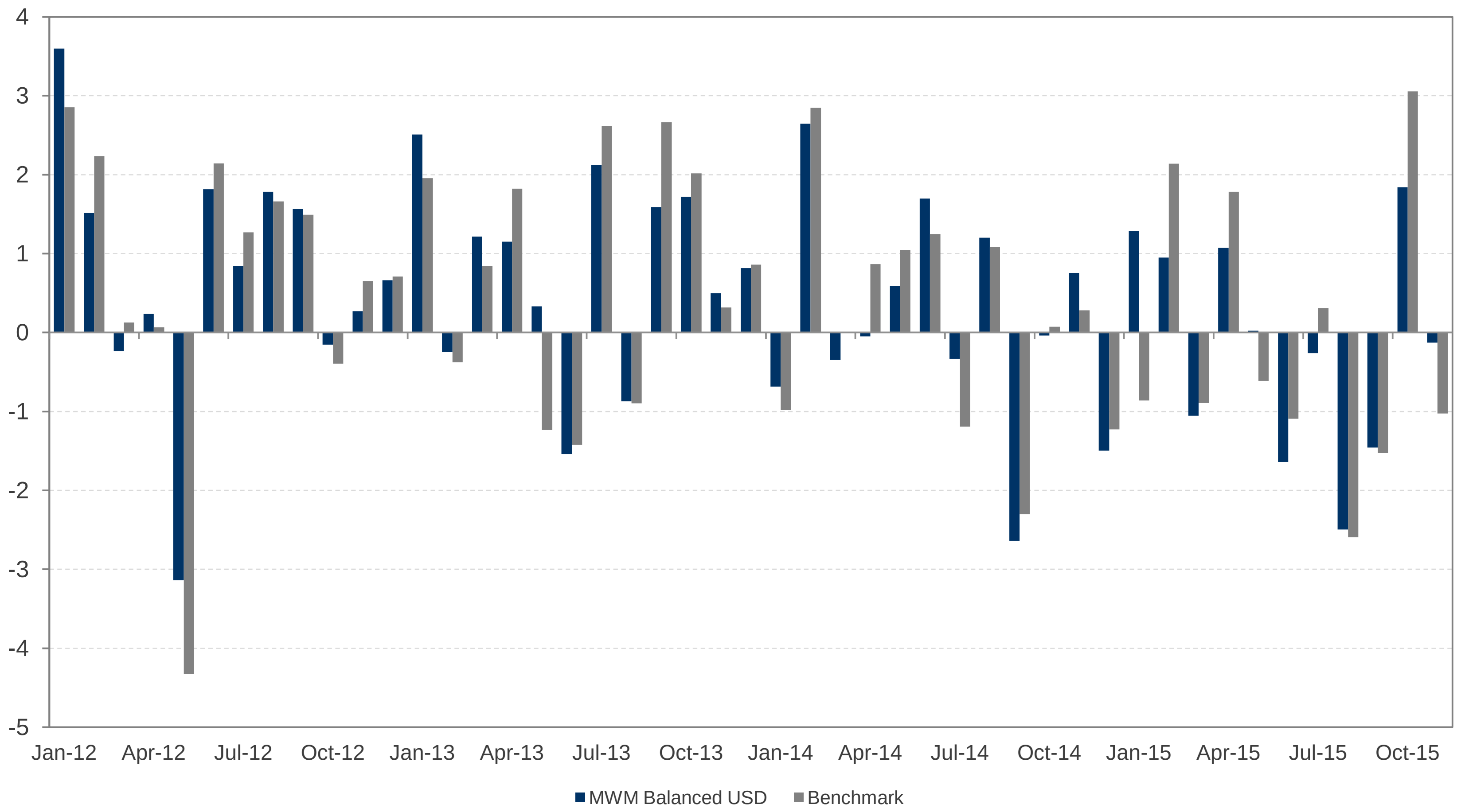
Model portfolio de-risking process continues



- Since **one year ago** the model portfolio has been significantly **de-risked**
- Since **August's** market correction, we have **further taken out risk** from the portfolio; a process that should **continue in the months to come**

Source: Bloomberg as of November 6, 2015

MWM Model Portfolio - Historical performance (2)



- **Standard Deviation** (1 year[1]): **4.28%** vs. **5.45%** Benchmark[2]
- **Downside Risk** (1 year[1]): **3.15%** vs. **3.90%** Benchmark[2]
- **Sharpe Ratio** (1 year[1]): **-0.82%** vs. **-0.45%** Benchmark[2]
- **Var 95%** (1 day[1]): **-0.46%** vs. -**0.56%** Benchmark[2]

[1] As of November 30, 2015

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

Three broad scenarios

MORA WEALTH MANAGEMENT

	Scenario 1 Global economic slowdown	Scenario 2 Muddling through	Scenario 3 Inflation surprise
Drivers	• Global economic slowdown led by a hard-landing in China • Fed delays rate rises indefinitely • Strong deflationary scenario due to a combination of low growth and structural factors (demographics, low aggregated demand, deleveraging)	• Chinese authorities stabilize the market and halts economic rebalancing (weaker yuan, higher IP). US, Japan and Europe continue exhibiting low but stable growth • Fed rise rates at an accommodative pace • Low inflation due to structural factors (demographics, low aggregated demand, deleveraging)	• Growth concerns dissipate, with economic activity accelerating in Europe and Japan • Inflation in US unexpectedly increases • The Fed is behind the curve and is forced to rise rates aggressively
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 to remain depressed	• Equities recover moderately, particularly in Europe • Credit spreads remain stable as the credit cycle is further elongated • Sovereign and IG suffer as monetary policy is progressively normalized • USD appreciate moderately due to higher interest rate differentials • Commodities remain weak in short term, but rebound in long-term as supply and demand balance out	• Correction in equities due to higher rates. Impact will be mitigated if higher inflation is the consequence of an acceleration in growth • 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	35% ↑	45% ↓	20%

Short-term catalyzers
Chinese QE, Fed delays lift-off, macro-data (particularly in China) showing resilience

Other risks
Commodity prices lead to political destabilization (Russia, Saudi Arabia, Iran, Venezuela, etc.), Greece, Terrorism, Brexit…

Tactical positioning

- We remain extremely cautious in **fixed income** due to a very unattractive combination of risk and return, **favoring credit exposure** over **interest rate risk**. However, since August's market correction we have reduced our exposure to High Yield and Emerging Markets in favor of **investment grade bonds**.
  - **Diversification** is key to obtain a yield pick-up through credit exposure (**High Yield, EM, Convertibles**)
  - **Flexibility** and active management preferred over buy and hold
  - **Low duration** limits the impact of interest rate rises
  - **Currency hedging** is needed. Unusually high volatility erodes diversification benefits from FX exposure
- Central banks have created an environment where **valuations** are largely **dependent on interest rates to remain low for long**. Hence, the incoming normalization in US monetary policy is causing **investor anxiety**. From a **valuation** perspective, we favor **European equities**, **EM equities** and **high-dividend stocks**
- **Alternative investments** offer a much needed source of **diversification** and (partially) **uncorrelated returns**. We recommend allocating a significant part of the portfolio to Multi-Strategy Hedge-Funds, Private Equity, Cat Bonds, Commodities and derivative strategies (covered-calls)
- A **larger than usual cash allocation** is advisable as the **opportunity cost** of holding cash has decreased dramatically, and it offers **flexibility** to enter the market in an opportunistic manner

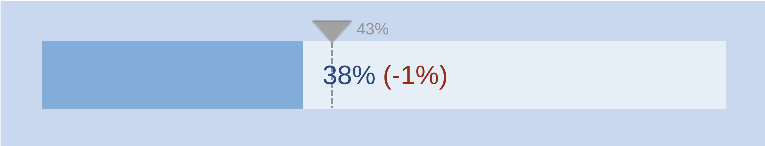
MWM Investment Policy

MORA WEALTH MANAGEMENT

Cash

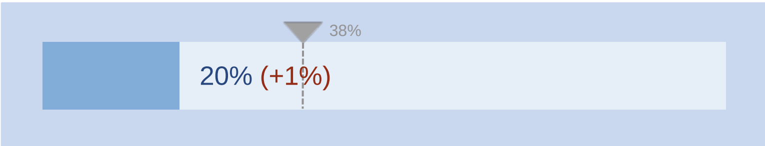
- In the current interest rate environment cash has become an investment asset class (returns on cash are higher than those of many sovereign bonds)
- Waiting for good investment opportunities is a prudent investment strategy since the opportunity cost of holding cash has considerably decreased

Fixed Income



- Highest-quality fixed income currently offers a very unattractive combination of risk and return, as the current low yields offer little cushion for price fluctuations, particularly in the longer maturities
- Only high-yield, emerging markets, convertible bonds and short-term corporate debt offer an acceptable carry that can help absorb losses from rises in interest rates

Equity

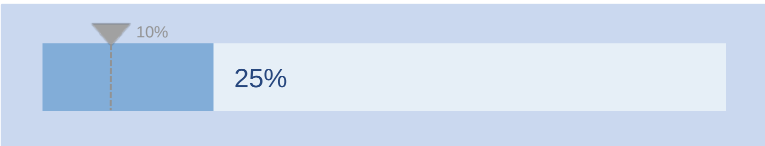


- Valuations remain attractive only if very low interest rates are used for discounting future revenues. A potential normalization of interest rates poses a risk of returning to lower valuation multiples
- In relative terms, Europe looks still more attractive than US and Asia

Commodities

- Commodity prices seem to have reached a bottom, in tandem with the USD
- Weak correlation with other asset classes confer commodities diversification benefits

Alternative investments



- Alternative investments as a source of low volatility and uncorrelated returns are more attractive than ever in the wake of the current latent risks in the market
- However, double digit returns cannot be expected in the current interest rate environment

Strategic Asset Allocation

MWM Model Portfolio

MORA WEALTH MANAGEMENT

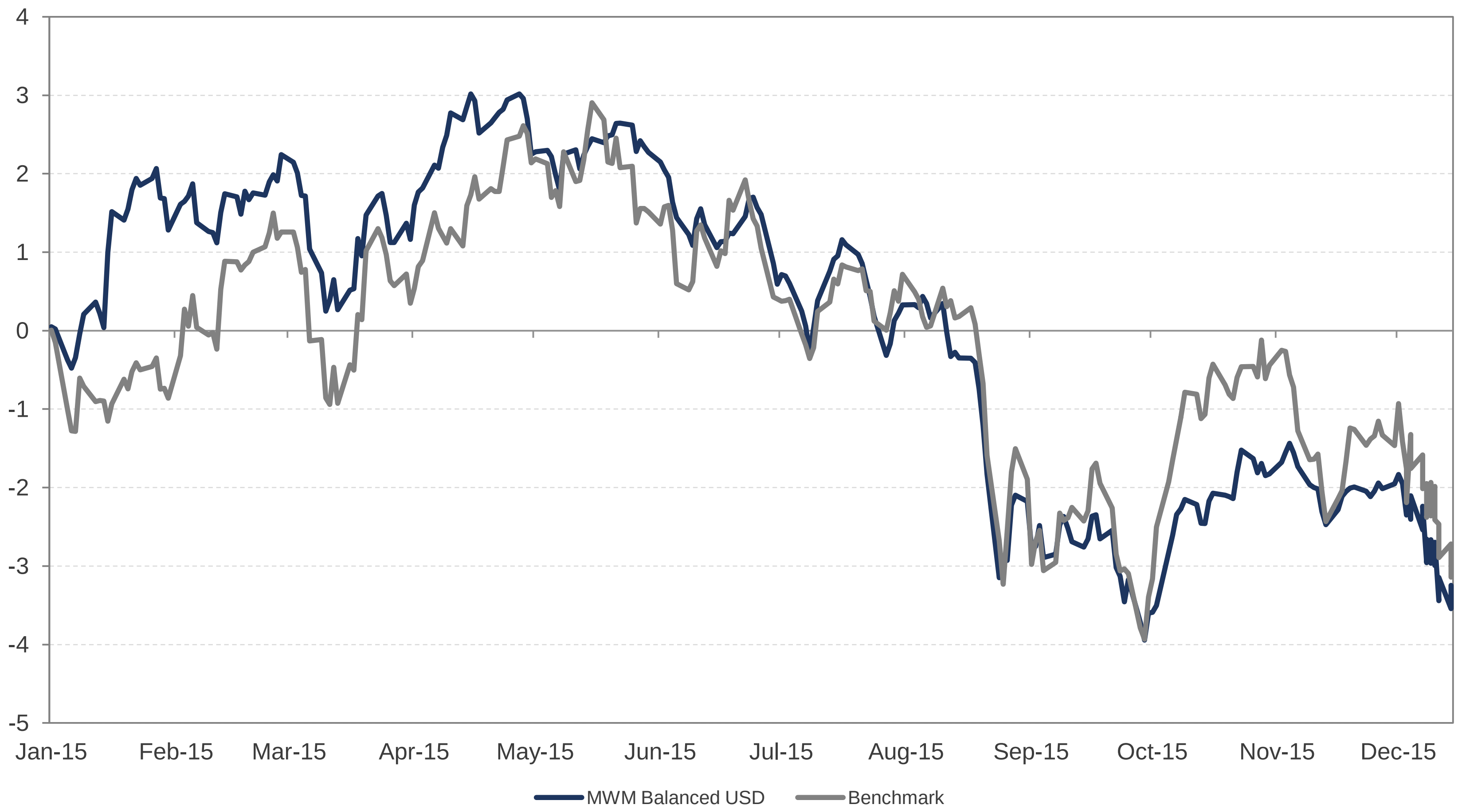
Cash	Cash	• Cash	6%	14%
	Money market	• Mora Money Market	4%	
	Enhanced Money Market	• JPM Income Opportunities	4%	
Fixed Income	Short-Term Corporate Bonds	• SPDR Barclays 0-3Y Corporate Bond ETF	6%	37%
		• iShares USD Short Duration Corporate Bond	6%	
	High Yield US	• Muzinich Short Duration High Yield	4%	
	High Yield Europe	• Arcano European Income	5%	
	High Yield Absolute Return	• Muzinich Long/Short Credit Yield	4%	
	Emerging Markets	• CS EM Corporate Investment Grade Bond	4%	
	Leveraged Loans	• Franklin Floating Rate II Fund	5%	
	Convertible Bonds	• Fundlogic Salar Convertibles	3%	
Equity	Europe	• Blackrock European Value Fund	3%	20%
		• THEAM Quant Equity Europe Income	3%	
	Volatility	• Reverse Convertibles on Blue Chips	6%	
	Emerging Markets	• iShares MSCI Emerging Markets Minimum Volatility	3%	
	High Dividend Yield	• Pictet High-Dividend Selection	5%	
Commodities	Diversified	• Investec Global Natural Resources	4%	4%
Alternative Investments	Multi-Strategy	• Lyxor Diversified Fund	5%	25%
	Multi-Strategy	• Amura Absolute Return	5%	
	Relative Value	• Areca Value Discovery	5%	
	Cat Bonds	• Plenum CAT Bond Fund	5%	
	Private Equity	• Partners Group Global Value	5%	

MWM Investment Profiles

	Conservative	Balanced	Growth
Cash	16% (▼ 5%)	14% (▼ 5%)	6% (▼ 5%)
Fixed Income	50% (▼ 64%)	37% (▼ 43%)	26% (▼ 22%)
Equity	12% (▼ 24%)	20% (▼ 38%)	32% (▼ 52%)
Commodities	2% (▼ 2%)	4% (▼ 4%)	6% (▼ 6%)
Alternative Investments	20% (▼ 5%)	25% (▼ 10%)	30% (▼ 15%)

▼ Strategic Asset Allocation

MWM Model Portfolio – Ytd performance (Net)



- **Total Return** (Ytd[1]): **-3.44%** vs. **-2.47%** Benchmark[2]
- **Standard Deviation** (Ytd[1]): **4.20%** vs. **5.50%** Benchmark[2]
- **Downside Risk** (Ytd[1]): **3.09%** vs. **3.92%** Benchmark[2]
- **Var 95%** (Ytd[1]): **-0.44%** vs. **-0.55%** Benchmark[2]

[1] As of December 14, 2015

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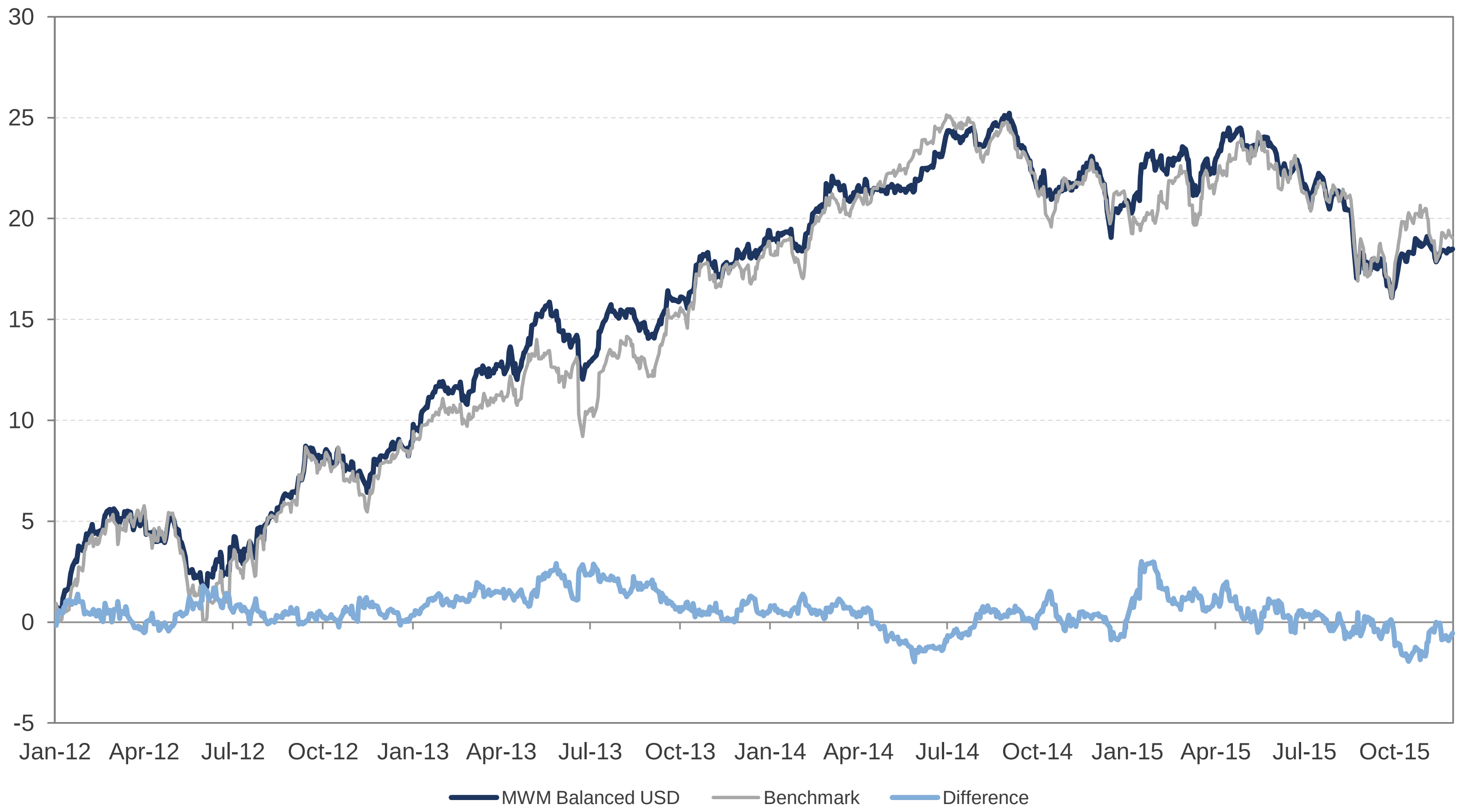
MWM Model Portfolio - Historical performance (1)



- **Total Return** (1 year[1]): **-3.55%** vs. **-2.56%** Benchmark[2]
- **Total Return** (3 year[1]): **7.22%** vs. **8.55%** Benchmark[2]
- **Total Return** (Since Jan 12[1]): **16.56%** vs. **17.52%** Benchmark[2]

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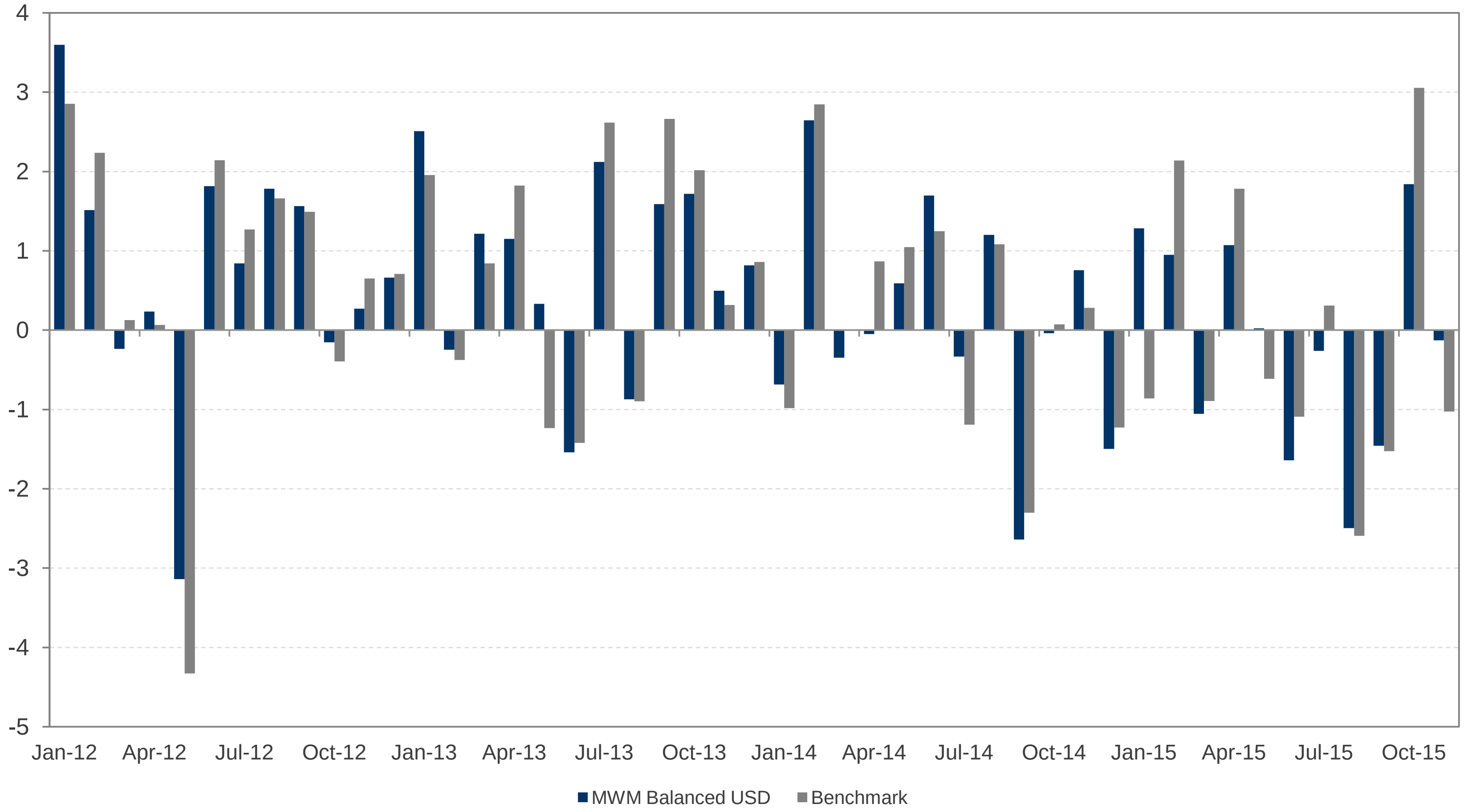
MWM Model Portfolio - Historical performance (2)



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