REVIEW & Outlook

Q2 2014
Q3 2014

Global Financial Markets

BIAS
INVESTMENT MANAGERS - SECURITIES ANALYSTS

JUNE 30, 2014

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World Markets Quarterly Review

June 30, 2014

1	DJIA	2.8%	3	BSX	1.0%	7	UK FTSE	5.9%	11	Nikkei	4.1%
1	S&P 500	5.2%	4	Bolsa	6.6%	8	CAC	2.4%	12	Hang Seng	6.9%
1	NASDAQ	5.3%	5	Bovespa	7.8%	9	DAX	2.3%	13	Straits Times	4.3%
2	TSX	10.1%	6	Merval	22.8%	10	Kospi	5.9%	14	ASX	2.6%

The S&P Global 1200 Index closed up 5.2 percent for the quarter ended June 30, 2014. All returns are expressed in US dollars.

Stock, Bond, Currency Overview

Global Stock Markets

- Global equity markets advanced in the Second Quarter after a weak start as First Quarter earnings results and economic indicators were mixed following severe weather in North America.
- In the latter half of the quarter, a gradual consolidation in stocks and confirming economic indicators led US outperformance versus the global benchmark. The growth centric NASDAQ came up on top returning higher than the S&P 500 and the Dow Jones index.
- Emerging Markets led regional returns as re-structuring continued in China and anticipation of political change drove stock prices higher in Brazil.

Bond Markets

- Treasury yields fell in the Second Quarter on mixed economic data, increased hostility in Ukraine and tension in Iraq.
- The European Central Bank (ECB) cut the benchmark interest rate to address deflationary threats and stimulate economic growth which sent yields lower in the eurozone.
- Shorter-maturity yields in the UK rose on expectations the Bank of England will raise rates sooner than previously expected following strong economic data.

Currency Markets

- The dollar advanced versus the euro in the Second Quarter as the US Federal Reserve continued paring bond purchases, thus reducing monetary stimulus, while the ECB increased monetary stimulus.
- The Canadian dollar advanced versus all major currencies as economic growth improved in the US (Canada's largest trading partner) and inflation picked up.

North American Stock Markets

Indices	31 Mar 2014	30 Jun 2014	Quarterly Change Local Curr.	US$
US Dow Jones Industrial	16,457.70	16,826.60	2.8%	2.8%
US S&P 500	1,872.34	1,960.23	5.2%	5.2%
US NASDAQ	4,198.99	4,408.18	5.3%	5.3%
Canada TSX	14,335.30	15,146.00	6.4%	10.1%
S&P Global 1200	1,858.14	1,937.67	5.2%	5.2%

Source: Bloomberg

US markets rose, led by the growth centric Nasdaq.

- **On April 28** Bank of America shares declined 6.3 percent after the company suspended plans for a dividend increase and $4 billion of share repurchases due to an error in its stress-test submission to the Federal Reserve. Bank of America incorrectly estimated its Tier 1 capital ratio after finding erroneous accounting on structured notes issued by Merrill Lynch. The Bank consequently notified the Fed and agreed to resubmit a revised capital plan.

- **In the quarter** Tyson Foods Inc. and Pilgrim's Pride Corp. made multiple offers to takeover Hillshire Brands Co., the maker of Jimmy Dean sausages and Ball Park hot dogs.

  Pilgrim's Pride made a first bid on May 27 which was followed by a higher bid of $50 per share from Tyson Foods on May 29. Pilgrim's Pride increased their bid to $55 only to be raised again by Tyson Foods to $63. Tyson Foods still remains the key contender to takeover Hillshire which has low debt levels and strong cash flows as well as a range of value-added packaged foods.

- **On May 28** Apple Inc. agreed to buy Beats Electronics LLC for $3 billion. The deal was Apple's largest acquisition to date and gave the company access to a nascent subscription music-streaming business as well as a line of popular headphones. As sales of digital music downloads decline, Beats will give Apple a foothold in internet-based streaming, where Google's YouTube, Spotify Ltd. and Pandora Media Inc. dominate. The deal shows CEO Tim Cook's willingness to use Apple's $150 billion cash reserve to acquire smaller companies to grow more aggressively, a departure from predecessor Steve Job's playbook of acquiring smaller companies for technology and talent. Apple investors responded favourably with the stock up 21.2 percent in the quarter.

- **On June 18** Amazon.com Inc. announced entry in the smartphone market with a handset called the Fire Phone. The phone will offer a 4.7 inch display, 3-D viewing and image recognition technology which will make it simpler for users to buy items from Amazon's web store. The Fire Phone will join the company's eco-system of e-readers, tablets and TV set-top boxes, as a way to get Amazon's online store and digital services more directly in front of customers. AT&T will be the exclusive carrier. The phone will list for $649 without a contract. Shares of Amazon rose 2.7 percent in New York on the day of the announcement.

- **On June 24** Chipotle Mexican Grill announced plans to purchase more than 20 million lbs of locally grown produce for its restaurants this year, up from the 2013 goal of 15 million lbs. As the only national restaurant company with a significant commitment to serving local produce on a large scale, Chipotle has steadily increased the supply of locally sourced produce since beginning the program in 2008. The stock is one of our premier plays in the healthy living space and rose 4.3 percent in the quarter.

Latin American Stock Markets

Indices	31 Mar 2014	30 Jun 2014	Quarterly Change Local Curr.	Quarterly Change US$
Mexico Bolsa	40,461.60	42,737.20	6.0%	6.6%
Brazil Bovespa	50,414.90	53,168.20	5.5%	7.8%
Argentina Merval	6,373.82	7,887.33	24.8%	22.8%
Chile IPSA	3,772.76	3,875.73	2.7%	2.1%
S&P Global 1200	1,858.14	1,937.67	5.2%	5.2%

Source: Bloomberg

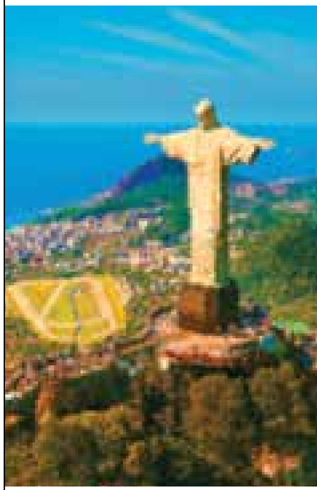
- **On April 22** America Movil, Mexico's largest mobile operator, filed an injunction request against the Federal Telecommunications Institute (IFT). The IFT was created in response to constitutional reform aimed at curbing dominance in the Telecommunications sector. In March, America Movil was ruled to be a dominant player due to the company's 70 percent share of the Mexican mobile market, and 80 percent share of the fixed-line market. The IFT imposed tougher roaming and billing rules for fixed and mobile operations requiring America Movil's mobile unit to stop charging customers more expensive roaming charges and to separate charges made for telecom and non-telecom services. Shares of America Movil rose 3.9 percent in the Second Quarter.

- **On June 20** Cencosud, Chile's largest retailer, announced the signing of a credit card joint venture agreement with Banco de Nova Scotia (Scotiabank) in which the Canadian based bank will hold a 51 percent majority stake in Cencosud's retail credit card business in Chile for $280 million. The Canadian bank and its local unit, Scotiabank Chile, will also finance the retailer's credit card portfolio for around $1 billion, in a business arrangement between the retailer and bank that is to last 15 years. The deal could help Cencosud reduce debt levels and maintain an investment-grade credit rating. Regulators in Canada and Chile need to approve the deal which Cencosud expects will be completed by year-end. Shares of Cencosud rose 0.33 percent in the Second Quarter.

- **Data released on June 23** showed that Argentina's economy slid into recession in the first quarter of 2014. A recession is often defined as two consecutive quarters of declining gross domestic product (GDP). The decline in the GDP in the third largest Latin American economy was due to declines in industrial output and consumer spending. This decline comes as the country wrestles with one of the world's highest inflation rates, falling central bank reserves and an ongoing legal fight with creditors who insist on full payment of debt that the sovereign nation defaulted on in 2002. Despite the downturn in the economy in the First Quarter, the Argentina Merval rose 23.75 percent for the Second Quarter as investors searched out growth opportunities in emerging markets.

- **On June 25** Petroleo Brasileiro SA (Petrobras) announced a decision to pay $6.8 billion (15 billion reais) through 2018 for new deep-water oil rights. The company expects to produce as much as 15 billion additional barrels from a region that holds the giant Buzios field in the deep waters of the South Atlantic. Petrobras, the most indebted publicly traded oil company, is considering selling assets and restructuring projects in order to meet the costs. Petrobras expects to start producing under the contract in 2021 and reach a peak of one million barrels a day in 2026. Shares of Petrobras rose 9.6 percent in the quarter.

Latin American markets advanced following a weak First Quarter.



European Stock Markets

Indices	31 Mar 2014	30 Jun 2014	Quarterly Change Local Curr.	Quarterly Change US$
UK FTSE	6,598.37	6,743.94	3.3%	5.9%
Germany DAX	9,555.91	9,833.07	2.9%	2.3%
France CAC 40	4,391.50	4,422.84	3.0%	2.4%
Spain IBEX 35	10,340.50	10,923.50	7.2%	6.6%
S&P Global 1200	1,858.14	1,937.67	5.2%	5.2%
S&P Europe 350	1,361.41	1,400.88	4.5%	3.9%

Source: Bloomberg

Most European markets lagged the global benchmark on weak economic growth in the region.

- **On April 16** Credit Suisse Group AG, the second biggest Swiss bank, reported a slump in first quarter earnings as a drop in fixed income trading weighed on investment banking profit. Net Income of the bank fell 34 percent to 859 million francs from a year earlier, missing the 10.9 billion franc consensus estimate. European banks across the board have witnessed lower revenues from investment banking and bond trading amid low interest rates in the current soft monetary policy environment. Credit Suisse stock declined as much as 2.8 percent in Swiss trading following the results announcement.

- **On April 24** Bloomberg reported that General Electric (GE) was in talks to buy Alstom's energy unit which builds power plants and transmission gear. The potential transaction valued Alstom at $13 billion which was 25 percent more than the market value at the time. The stock surged 18 percent in Paris on the announcement, the biggest jump since 2004. Subsequent to the announcement, the French government raised concerns and encouraged the German group Siemens to make a counter offer.

  After much debate, the deal was announced on June 23 after the French government agreed to terms whereby the French state will become Alstom's main shareholder with a stake of 20 percent. This ensured jobs would be retained and decision-making would stay with the French government.

- **On April 28** US drug maker Pfizer Inc. proposed to buy European company AstraZeneca Plc for $98 billion in what would rank as the industry's biggest takeover, surpassing Pfizer's $64 billion purchase of Wyeth in 2009. AstraZeneca spurned the offer as too low. AstraZeneca rose 14 percent to £46.67 in London, the biggest one day advance since 1993 while Pfizer climbed 4.2 percent to $32.04 in New York.

  On May 19 Pfizer increased the takeover offer to $117 billion for AstraZeneca only to be rejected again by the company's board. In a follow-up to the offers, Pfizer announced on May 26 that it will no longer pursue the take over.

- **On June 11** Airbus Group suffered the biggest ever order cancellation in the company's history as Gulf airline, Emirates cancelled a deal for A350 planes valued at $16 billion. Emirates ordered 50 A350-900s and 20 larger 1000s in 2007 which were scheduled to be delivered in 2019. The company assured shareholders that other airlines have inquired about taking up the vacant delivery slots and there should be no problem selling the planes. The stock, however, reacted negatively to the news and declined 4.3 percent on the day in France.

Pacific Rim Stock Markets

Indices	31 Mar 2014	30 Jun 2014	Quarterly Change Local Curr.	Quarterly Change US$
Japan Nikkei	14,827.83	15,162.10	2.3%	4.1%
Hong Kong Hang Seng	22,151.10	23,190.70	6.8%	6.9%
Hang Seng Red Chip	4,161.24	4,369.01	6.6%	6.7%
Korea Kospi 100	1,985.61	2,002.21	0.8%	5.9%
Singapore STI	3,188.62	3,255.67	3.4%	4.3%
Taiwan TWSE	8,849.28	9,393.07	6.5%	8.6%
Australia ASX 200	5,394.83	5,395.75	0.9%	2.6%
S&P Global 1200	1,858.14	1,937.67	5.2%	5.2%
FTSE Pacific ex-Japan	483.42	506.26	5.6%	5.6%

Source: Bloomberg

- **On April 1** Singapore based Overseas China Banking Corp. offered $5 billion to buy Wing Hang Bank Ltd. in the biggest takeover of a Hong Kong lender since 2001. The acquisition will give OCBC more access to China related business in Hong Kong and will provide a foothold to catch up with competitors such as DBS Group Holdings. OCBC shares rose 0.4 percent in Singapore while Wing Hang shares rose 0.2 percent in Hong Kong.

- **On May 7** Chinese company Alibaba Group Holdings filed for US initial public offering to raise as much as $20 billion. The company was founded by a former English teacher, Jack Ma by selling a few dozen items on the website which has now grown to become a thriving online marketplace selling everything from forks to forklifts. On current valuation, the total company is estimated at $168 billion which makes it the 34th largest company in the world by market capitalization.

- **On May 8** stock prices of Macau gaming and casino companies declined amid concerns that a crackdown on illegal money transfers will pare demand. Wynn Resorts declined 8.5 percent in the day while MGM China Holdings Ltd. and Galaxy Entertainment Group Ltd. fell 8.2 percent and 7.6 percent, respectively. Macau may tighten visa policies after police investigated a series of irregularities pointing to overseas money laundering, capital flight and illegal bank card use. The Macau gaming industry has been at the center of controversy in the past but regulatory action has seldom followed investigations.

- **On May 16** Narenda Modi's opposition bloc came to power with the biggest Indian election win in 30 years defeating the Gandhi dynasty, which was accused of sluggish economic growth and corruption. Modi's Bharatiya Janata Party captured 283 of the 543 seats up for grabs setting up the biggest single party victory since Gandhi's Congress won 404 seats in 1984. The election also hosted the highest ever voting turnout in India. The result boosted Indian stocks the most in five years and lifted the Indian Rupee.

- **On May 22** Chinese online retailer JD.com Inc. which handled more than $20 billion of purchases in 2013 debuted on a New York stock exchange. Demand for the initial public offering was larger-than-expected and the stock gained ten percent on the first day to close at $20.90. Internet spending is expected to boom in China as the middle class grows, urban migration continues and the economy focuses on internal consumption.

Pacific Rim markets rose led by Hong Kong and Taiwan.

Bermuda & Cayman Stocks

Benchmark Indices	31 Mar 2014	30 Jun 2014	Quarterly Change Local Curr.	Quarterly Change US$
BSX Index	1,389.16	1,391.91	1.0%	1.0%
BSX Insurance Index	1,435.20	1,468.69	2.3%	2.3%
S&P Global 1200	1,858.14	1,937.67	5.2%	5.2%
Stocks				
ACE Ltd.	99.06	103.70	4.7%	4.7%
Ascendant Group Ltd.	7.34	6.50	-10.5%	-10.5%
Butterfield Bank	1.98	1.99	1.0%	1.0%
Caribbean Utilities	10.26	10.45	3.6%	3.6%
Consolidated Water Co.	12.79	11.77	-10.1%	-10.1%
XL Capital Ltd.	31.25	32.73	5.3%	5.3%

Source: Bloomberg

Local shares underperformed the global benchmark in the quarter.

- **On May 8** Cayman based Caribbean Utilities Company announced unaudited results for the quarter ended March 31. Net earnings for the First Quarter 2014 totalled $3.4 million, an increase of $0.5 million when compared to $2.9 million for the First Quarter 2013. The increase was driven by higher electricity sales revenues and lower depreciation costs. Sales were positively impacted by growth in customer numbers and warm weather conditions resulting in higher customer air-conditioning load when compared to the same period last year. The average monthly temperature in Cayman during the first three months of the year was 80 degrees Fahrenheit compared to an average monthly temperature of 79.3 degrees in the first three months of 2013. Shares of Caribbean Utilities Company rose 1.9 percent for the Second Quarter.

- **On May 20** Moody's Investors Service downgraded the government-guaranteed preferred stock rating of The Bank of N.T. Butterfield and Son Limited to A1 from AA3. All other ratings were reaffirmed including, short and long term deposit ratings of A3 and Prime-2 and financial strength rating (BFSR) of D+. The outlook on the ratings is stable. The ratings reflect the bank's good liquidity and strong capital position while taking into account risks associated with Butterfield's high level of non-performing assets, which is due to the bank's large concentration in Bermuda real estate and sizable exposures to single borrowers. Shares of the Bank of N.T. Butterfield rose 0.5 percent for the Second Quarter.

- **On June 17** Bermuda based insurer BF&M, announced First Quarter 2014 net income was $11.4 million compared to $4.4 million for the three month period a year earlier. The increase in net income was driven by slightly improved core operating earnings as well as several one-off items such as the timing of certain revenues and one–time gains. Gross premiums for the period were $79.9 million, a two percent increase from 2013. Investment income reflected a $7.7 million increase in the value of investments as interest rates and credit spreads fell. The Board of Directors also announced that the dividend will be increased from 20 cents to 22 cents per share for shareholders on record at 30 June 2014. Shares of BF&M rose 4.4 percent for the Second Quarter.

Global Bond Markets

Indices	(Yield to Maturity) 31 Mar 2014	30 Jun 2014	Total Returns Local Curr.	US$
US 2 Year	0.42%	0.46%	0.24%	0.24%
US 10 Year	2.72%	2.53%	2.66%	2.66%
US 30 Year	3.56%	3.36%	5.21%	5.21%
Canadian 10 Year	2.46%	2.24%	2.56%	6.20%
Australian 10 Year	4.08%	3.54%	5.70%	7.62%
UK Gilt 10 Year	2.74%	2.67%	1.22%	3.91%
German Bund 10 Year	1.57%	1.25%	3.71%	3.13%
Japanese 10 Year	0.64%	0.57%	1.07%	2.97%
Citigroup				
3-7 Year Treasury Index	1,337.19	1,353.77	1.24%	1.24%
7-10 Year Treasury Index	1,635.77	1,676.68	2.50%	2.50%
1-10 Year US Corp. Bond Index	1,607.80	1,633.80	1.62%	1.62%
World Gov't 7-10 Yr. Bond Index	1,232.31	1,271.13	3.15%	3.15%

Source: Bloomberg

- **On June 5** the European Central Bank (ECB) cut the benchmark interest rate to a record low of 0.15 percent from 0.25 percent. The central bank also imposed a fee on funds deposited by financial institutions with the Bank, replacing interest on balances. The ECB's goal is to discourage banks from stockpiling cash and create an incentive to make loans that could stimulate the region's weak economy. Following the ECB's announcement, yields on Belgian, French, Irish, Italian and Spanish bonds fell to all-time lows and Germany's five-year yields dropped to the lowest since May 2013.

- **All but the** very shortest Treasury yields fell in the Second Quarter on mixed economic data, increased hostilities in Ukraine and tension in Iraq. As expected, the Fed continued to reduce asset purchases in the quarter, citing an improving economy. However, on June 18 Fed Chair Janet Yellen emphasized the Federal Open Market Committee's view that rates are likely to stay low for a considerable time and dismissed a faster-than-forecast rise in the US consumer price index as "noisy" data.

- **In the week** ended June 20 yields on UK 10-year government bonds rose to a three-month high of 2.77 percent after Barclays Plc analysts, contrary to consensus, projected an increase in the Bank of England benchmark interest rate before year-end following strong economic data. Earlier, analysts at Credit Suisse Group AG and Deutsche Bank AG had also brought forward their estimates for the central bank to act in 2014. The change in analysts' expectations was in line with comments on June 12 from Bank of England Governor Mark Carney, who said the central bank's first interest rate increase "could happen sooner than markets currently expect."

- **Investment grade** corporate bonds generally outperformed US Treasuries in the quarter amid high demand for their relatively better yields in the current low interest rate environment. However, decreased liquidity resulting from lower corporate bond inventory at banks led to volatile pricing on individual corporate bonds in the quarter. For the quarter, Citigroup's 1-10 year 'A' corporate bond benchmark was up 1.6 percent while Citigroup's 1-10 year Treasury benchmark rose 0.9 percent.

All but the very shortest Treasury yields fell on mixed economic data and increased hostilities in Ukraine and Iraq.

World Currency Markets

Value of Currency US$1 = value in local currency

Currency	31 Mar 2014	30 Jun 2014	Change
Australian Dollar	1.0794	1.0601	1.8%
Brazilian Real	2.2719	2.2143	2.6%
British Pound	0.6002	0.5846	2.7%
Canadian Dollar	1.1050	1.0649	3.6%
Euro	0.7263	0.7303	-0.6%
Japanese Yen	103.2300	101.3300	1.9%
Swiss Franc	0.8846	0.8869	-0.3%

Source: Bloomberg

Canada's dollar advanced versus all major currencies as the Canadian economy picked up steam.

- **The dollar advanced** against the euro in the Second Quarter on diverging central bank paths. In the quarter, the European Central Bank (ECB) cut the benchmark interest rate to stimulate growth and boost inflation in the region. The Fed, on the other hand, kept reducing monetary stimulus by paring back bond purchases as economic data showed the US economy was improving. For the quarter, the dollar advanced 0.6 percent against the euro.

- **In the week** ended June 20, Sterling advanced to the strongest level in over five years against the dollar and reached a 20-month high versus the euro on bets that the Bank of England is moving closer to increasing the benchmark interest rate, which fuelled demand for the currency. Appreciation of the pound was consistent with the strength of economic data reported in the quarter which demonstrated that the UK economy is recovering. In the quarter, Sterling advanced 2.7 percent against the dollar and 3.1 percent against the euro.

- **Canada's dollar gained** against all major currencies in the Second Quarter as investors boosted wagers on higher interest rates as the economy is picking up steam. Both retail sales and inflation picked up in the quarter. In particular, higher inflation data was seen as a potential trigger for the central bank to significantly change the forecast for the economy. The Canadian dollar advanced 3.6 percent against the US dollar in the quarter.

- **On June 19** the Norwegian krone plunged by 2.3 percent against the euro and 2.1 percent versus a basket of the krone's most traded peers after Norway's central bank said they are ready to cut interest rates. A rate cut should protect Western Europe's largest oil producer from an investment slump as offshore energy investments abate and record household debt weighs on consumers. Prime Minister Erna Solberg, who pledged to protect the Norwegian oil industry from political interference and supports increased exploration, also backed the central bank's concern. In the quarter, the krone weakened 1.9 percent against the euro and 2.4 percent against the dollar.

- **The Japanese yen** advanced against the dollar in the Second Quarter on signs Prime Minister Shinzo Abe's efforts to put the economy on a solid growth path is making progress. In May the economy added 370,000 jobs (mainly in the private sector) from a year earlier. Inflation also picked up in the quarter and reached 1.4 percent in May. In the quarter, the yen advanced 2.29 percent against the dollar.

Outlook
FOR THE THIRD QUARTER 2014

Global GDP growth is set to re-accelerate in the second half of the year as weather related one-offs normalize, pent up demand is released, and productivity resumes.

- In Developed Markets (DM), we expect recovery to continue, albeit more moderately than anticipated.
- In Emerging Markets (EM), structural reforms remain the key theme, as these economies re-orient their growth drivers.
- As a downside risk, tensions in the Middle East may raise energy prices higher hindering growth for EM economies with weak balance sheets.

We expect upward pressure on interest rates as global growth picks up.

- The increase in yields is likely to be gradual and modest as inflation remains low across the developed world, keeping central bank policy accommodative.
- The Fed Funds rate is likely to stay unchanged near zero this year and into next year as inflation is low.
- We do not expect the ECB to cut rates further and only see full-blown quantitative easing if growth and inflation in the region fall sharply.

The dollar is likely to strengthen against the euro as the two central banks are on diverging paths with regards to monetary policy

- Sterling could strengthen further against the dollar as economic growth is strong and the Bank of England is expected to raise the benchmark rate before the Fed.
- The prospect of strong oil prices is likely to be beneficial to the Canadian dollar.
- We are bearish on the Japanese yen as the Bank of Japan is likely to add more monetary stimulus to the economy.

We maintain a neutral tone for commodity prices as markets approach a more balanced supply-demand state following a multi-year bear cycle.

- Copper may trade sideways in the quarter as economic data from China does not give clear indication of demand pickup in the industrial metal.
- Gold is likely to remain out of favour as an investment as economic growth improves and inflation remains benign.
- Oil prices will stay firm as the US enters a period of strong seasonal summer demand and robust consumer spending.

We expect global equity markets to continue on their positive trajectory as global economic recovery expands.

- We see newer themes in global equities emerging which are gaining traction and should force valuations and consequently stock prices higher.
- Economic results will set the stage for improving fundamentals in US stocks.
- Risks in Emerging Asia appear to be abating as China remains in-line with their economic guidance.

ECONOMICS

"Our current view is that the global economy is experiencing a soft patch within an ongoing expansion."

Ned Davis Research Group, Market Digest June, 2014

The World

We maintain our positive view on global economic growth for the Third Quarter 2014. Global GDP growth is set to re-accelerate in the second half of the year as weather related one-offs normalize, pent up demand is released, and productivity resumes. In Developed Markets (DM), we expect recovery to continue, albeit more moderately than anticipated. In Emerging Markets (EM), structural reforms remain the key theme, as these economies re-orient their growth drivers.

Geopolitical concerns continue to pose downside risk to our outlook. Tensions in the Middle East may raise energy prices higher hindering growth for EM economies with weak balance sheets. Nonetheless, we assign a low probability to this kind of non-systematic risk. We remain cautiously optimistic and expect a 2.8 percent global growth expansion for 2014 in accordance with World Bank estimates.

North America

Our longer term growth outlook for 2015 and 2016 remains largely unchanged following a strong economic rebound in the Second Quarter. Despite the dismal annualized 2.9 percent GDP contraction in the First Quarter 2014, Bloomberg consensus estimates forecast 3.1 percent growth in the Third Quarter and 2.2 percent for the year. A flurry of economic indicators, including those that measure employment, consumer spending, and industrial production, indicate that the US economy is picking up steam. With data currently driving monetary policy, we could also see a less dovish Federal Reserve if economic conditions continue to improve as projected.

GDP growth in Canada is set to match the pace of the US, rising 2.2 percent for the year 2014, while trailing the nation's southern neighbour in the Third Quarter at 2.4 percent. External demand for Canada's goods is central to the country's economic growth. Aided by a historically weaker Canadian dollar, broad based global growth would support prospective Canadian output gains.

Europe

GDP in the eurozone is expected to expand 1.1 percent in the Third Quarter and 1.1 percent for 2014. Our view is that the eurozone will continue to improve modestly and we remain confident that growth will gradually gain momentum in the second half of 2014 and in 2015. Should growth deteriorate and deflation become a threat, the European Central Bank (ECB) has indicated willingness for further action, including Quantitative Easing (QE) measures.

Notably, GDP growth in Ireland is forecast to considerably outperform the eurozone in 2014, with consensus pointing to a yearly increase of 1.9 percent. Countries such as Italy and France, who have yet to implement major economic reforms, appear to be stuck in stagnation.

UK growth continues to impress, surpassing that of continental Europe as well as beating growth projections discussed in our prior reports. Consensus GDP growth forecasts have yet again been revised higher to 2.9 percent for the Third Quarter and 3.0 percent for year 2014. As we predicted in our last Outlook report, growth in the first half of 2014 was impressive. Lower inflation, an improved labour market and robust housing market activity have been supportive of consumer spending in the country. Inflation forecasts have been revised slightly lower due to a stronger Sterling, leading to further upward revisions for real income and consumer spending forecasts in the coming quarters.

On geopolitics, the security crisis in Ukraine now looks set to be more protracted. Recent positive developments which include the IMF programme and successful presidential elections have helped to reduce tensions. Nonetheless, given the strong economic ties between Germany and Russia, downside risks remain. The escalating crisis in Iraq has also raised concerns over higher oil prices and fears of potential supply disruptions. Again, we do not place significant weight on these risks materializing.

Pacific Basin

The Pacific Basin is bifurcated into Developed Markets —Japan, Australia and New Zealand, and Emerging Markets —China, Korea, India, Indonesia, and the Philippines.

Our longer term economic outlook for Japan continues to be positive given Japan's commitment to continued economic stimulus and structural reform. In the near term, we are more uncertain about the pace of recovery. Preliminary reports suggest a bigger drag on private spending by the consumption tax hike than previously anticipated. Summer economic data will confirm the extent of the adverse impact of the hike on growth in Japan. Moreover, progress on the reforms we discussed in our previous report has been mixed, with corporate governance reform moving rapidly, government reform underway, labour market reform inconclusive, and agriculture reform progressing slowly.

Australia is forecast to be among the three fastest growing DM economies this year with consensus projections for GDP growth in 2014 at 3.15 percent. Following a strong start to the year, we expect a softer growth momentum in the second half of the year. We see headwinds from weak commodity prices, a slowdown in China, and a tighter fiscal policy landscape. Should the Australian dollar continue to strengthen from current levels as a result of yield-seeking global markets, trade-exposed sectors on which GDP growth in Australia largely depends could experience some strain. Correspondingly, we see a greater probability of the Reserve Bank of Australia moving to an easing bias in coming months.

Amid tighter financial conditions, GDP growth in China is projected to be 7.4 percent in 2014 which is slower than historical averages. In the second half of the year, we expect to see an escalation of easing measures aimed at boosting the sluggish economy. Chinese policy-makers will likely expend the bulk of their efforts on cushioning the impact of a correction in an overheated property market. However, we still expect financial reforms that address China's credit-fuelled investment boom to continue at a fast pace.

Latin America

As a whole, Latin America is projected to grow 2.18 percent in 2014 based on Bloomberg consensus estimates. However, a pronounced GDP growth divide persists between the Atlantic Bloc (Brazil, Argentina, and Venezuela) and the Pacific Bloc (Mexico, Colombia, Chile, and Peru). Collectively, GDP in the Atlantic Bloc is projected to remain well-below one percent, in stark contrast to the Pacific Bloc's 4.2 percent average projected growth.

Combined, members of the Pacific Bloc, also known as the Pacific Alliance, make up 39 percent of Latin America's economy. Each of the countries within the block has taken initiatives to export a greater range of goods and services and to maintain economic stability alongside high productivity gains as well as keep their economies open to investment.

We expect GDP growth in Brazil, the largest member of the Atlantic Bloc, to slip further. Weak domestic demand, a dragging industrial sector, and high inflation will continue to hamper growth in the Second Half 2014. Economic conditions in Venezuela and Argentina are also challenging. A deepening political crisis in Venezuela has led to civil violence and additional economic instability while the Argentine economy faces further contraction in coming quarters.

"Japan's economy will pick up, but there's uncertainty about the pace of recovery,"

Norio Miyagawa,
Senior Economist at Mizuho Securities Research and Consulting Co, Tokyo.
July 1, 2014

BONDS

"The US central bank is slowly building a case for normalization, but it is still far from signalling that the first rate hike is nigh."

Credit Suisse, US Economics Digest. June 18, 2014

As global growth picks up in the Second Half 2014 and into 2015, we expect upward pressure on interest rates. However, the increase in yields is likely to be gradual and modest as inflation remains low across the developed world, keeping central bank policy accommodative.

The Fed will end the bond purchase programme in the fall of 2014 as economic data improves. However, the Fed Funds rate is likely to stay unchanged near zero this year and into next year as inflation is low. The Fed has an annual inflation goal of two percent and any contribution to inflation from an improvement in economic growth is likely to be offset by an appreciating dollar and modest wage growth as more people rejoin the workforce.

We expect yields in the euro area to be little changed as inflation keeps running close to the deflation threshold. As such, the ECB will likely stick to the "rates at present levels for an extended period" mantra in the foreseeable future. We do not expect the ECB to cut rates further and only see full-blown quantitative easing, including large-scale purchases of government bonds, if growth and inflation in the region fall sharply. Growth in the eurozone has improved, but is weaker than that in the US and the UK, and is mainly led by the German growth engine while growth in the peripheral nations is still vulnerable.

Strong economic growth will push UK yields higher and we expect the Bank of England to be the first major central bank to raise the benchmark rate. Business confidence in the UK has surprised on the upside, investment and employment intentions are strong, and elevated housing market activity has supported consumer spending. While the Bank of England will be the first major central bank to raise rates, we expect a slow and gradual tightening cycle as the economic recovery is still fragile and a highly leveraged household sector is sensitive to higher interest rates.

We expect a modest rise in interest rates in Canada as inflation has finally picked up and the economy is gradually improving, largely led by improvement in the US. However, Canada's central bank is not likely to raise the benchmark rate anytime soon as growth is sluggish. For this reason, the rise in yields is likely to be less than that in the US.

Yields in Australia are likely to trade sideways or even fall in the near future. We expect the central bank to keep rates on hold until late 2015 and to adopt an easing bias as growth and inflation have surprised on the downside. Further adding to downward pressure on yields is the fact that Australia has relatively higher interest rates than most major economies. This is likely to attract investors to the nation's bonds in search for yield.

On the corporate bonds side, strong corporate financial health will continue as the economy improves and corporate balance sheets are in good shape. Investment grade corporate bonds will generate excess returns relative to Treasuries owing to their relatively better yields, but lack of liquidity in the corporate bond market may cause pricing to be volatile.

CURRENCIES

We expect the dollar to continue to strengthen against the euro as the two central banks are on diverging paths with the Fed reducing monetary stimulus and the ECB increasing stimulus. We do not expect any sudden dollar strength in the near term, but rather a slow and steady appreciation. As we get closer to a first interest rate hike, however, we expect the dollar appreciation to gather immediate momentum. Should economic data in the US start to come in stronger than expected, market expectations of an interest rate hike will be brought forward and dollar strength will come sooner.

Sterling could strengthen further against the dollar in the near term as economic growth is strong and the Bank of England is expected to raise the benchmark rate before other major central banks. However, given the extent of the Sterling rally so far in 2014 and the fact that the market is already pricing in an 80 percent probability of an interest rate hike in November, we believe upside for Sterling versus the dollar is limited near term. Also, the Scottish referendum in September could lead market participants to reduce Sterling positions, thus weakening the currency.

We are bearish on the Japanese yen and expect the yen to weaken against the dollar in the Second Half 2014. The Bank of Japan is likely to add more monetary stimulus to the economy to boost growth and inflation. Additionally, Japanese investors appear to be favouring higher yielding Australian assets as evidenced by portfolio flows in the First Half 2014. We expect this trend to continue unless the political turmoil in Ukraine and Iraq escalates – which would prompt Japanese investors to move their investments back home.

The prospect of strong oil prices as suggested in our Commodities Outlook is likely to be beneficial to the Canadian dollar. The loonie has historically had a strong correlation to oil prices which, for two reasons, may strengthen going forward. Firstly, the weight of crude oil in Canada's energy exports has increased steadily in the past ten years and is now reaching all-time highs of close to 26 percent, last seen pre-recession. Secondly, the prospect of improvement in US growth might support demand for Canada's oil exports. Diverging paths of the Fed and the Bank of Canada with regards to their monetary policy can potentially offset appreciation of the loonie versus the US dollar.

Unlike the loonie, the commodity affecting the Australian dollar the most is iron ore prices. While we believe further downside to iron ore prices is limited, the demand side (read China) needs to improve for the commodity to give a boost to the Australian dollar. We do not believe this will happen near term. Further adding to Australian dollar weakness is the diverging path of the central banks. The minutes from the Australian central bank's meeting on June 3 expressed more uncertainty than before about the sustainability of non-mining domestic demand, and since the meeting, economic data has surprised to the downside. Overseas flows, particularly from Japanese investors, to relatively better yielding Australian bonds could partly offset the weaker outlook from low iron ore prices and the dovish central bank.

"As markets increasingly price for hikes by the BoE and the Fed, we think AUDUSD will converge with the direction of interest rate spreads."

Credit Suisse,
FX Compass.
June 18, 2014

COMMODITIES

"Gold is pretty much unloved because investors seem to be mesmerized by other assets,"

Michael Gayed, Chief Investment Strategist at Pension Parnters LLC, New York July 1, 2014

We maintain a neutral tone for commodity prices in the Third Quarter as markets approach a more balanced supply-demand state following a multi-year bear cycle. The global economic growth story remains intact with the US close to achieving critical economic momentum and Europe improving on a sequential basis. We highlight an upside risk from emerging markets with post-election reforms in India, Indonesia and Brazil in the second half of the year and Chinese demand picking up earlier than expected.

In base metals, copper prices have bottomed out, in our opinion, after they approached the marginal cost of production, as highlighted in our previous commodity outlook. Copper may trade sideways in the quarter as economic data from China does not give clear indication of demand pickup in the industrial metal in the near-term. We highlight the ongoing probe in China regarding copper backed bank financing. Bloomberg analysis reveals that there may be limited downside to prices, but owners may move inventory to London Mercantile Exchange (LME) storages outside of China, which currently stand at record lows. This will moderate inventories held at Chinese ports eligible for bank financing.

Nickel supply fundamentals shifted significantly after Indonesia banned nickel-ore exports earlier in the year. While Chinese companies are well stocked at the moment, gradually depleting inventories may trigger a multi-year rally in the metal. Furthermore, demand for nickel products i.e. stainless steel is also expected to remain strong on industrial pick-up in the US.

For precious metals, we expect our stance from the previous commodity outlook to continue to play out. We expect gold to remain out of favour as an investment as economic growth, specifically in the US and Europe, improves and inflation remains benign. There is upside risk from geopolitical risk in Iraq but a significant move may only come if energy supplies are disrupted and prices rise significantly. In the absence of that case, we have precedence from last quarter's Ukraine-Russia crisis that prices react immediately but correct thereafter. Gold, therefore, should trade along long-term support and underperform other asset classes, such as equities and credit.

In energy, risk of supply disruptions from OPEC countries, primarily Iraq, has increased the risk premium in crude oil prices. While reports from Morgan Stanley confirm that oil assets are safe in the well-fortified northern Kurdish area and Shia-majority areas in the south-east of the country, we remain cautious and foresee further escalation before things eventually resolve in the region.

Additionally, longer-term demand dynamics for energy products continue to strengthen which will keep prices ticking up. The US enters a period of strong seasonal summer demand and a recent string of strong US consumer retail data consolidates our view of robust energy spending. In non-OECD countries, China and India remain the highest consumers and an indication of further improvement in these economies will also support prices. At this point, we must highlight that excessively high crude oil prices pose a risk to recovering economies with fragile balance sheets but currently we assign a low probability to a non-systematic price event.

In grains, historically higher soybean returns versus corn has forced an acreage shift in South America. The increased soybean supply will match recently depleting inventories and prices should remain soft. Corn prices are also expected to stay weak as shrinking acreage is expected to be offset by higher yield and modest consumption growth.

EQUITY STRATEGY

We expect global equity markets to continue on their positive trajectory as global economic recovery expands. Equity valuations expressed in forward price/earnings multiples have expanded in anticipation of improving earnings growth ahead. As long as profits are delivered equities should broadly tick higher. Additionally, low global interest rates and easy monetary policy is also supportive of economic expansion and advancing equity markets.

We also see newer themes in global equities emerging which are gaining traction and should force valuations and consequently stock prices higher. One of these is the ongoing global Merger and Acquisition (M&A) activity. Worldwide M&A has reached $1.74 trillion year-to-date, a pace of $10 billion a day. Drivers for this are excess cash availability for corporations, opportunities to buy global growth, and "tax inversion" incentives for US based companies re-domiciling in lower tax countries. Later, as global companies see stronger sales growth and improved earnings results, we expect investment in organic growth to resume. The other noticeable theme is the pace of share buyback plans currently in place. They indicate that valuations in equity markets are reasonable and prices may stay buoyant as companies engage programs if prices capitulate.

We expect economic results will set the stage for improving fundamentals in US stocks. However, we do notice that as indices hit successive highs, fewer companies are hitting their respective 52 week highs. We think this distinction among stocks price movements is important and prefer selective pockets of the US market with long term secular themes. We stay overweight in the Health Care sector with a preference for biotech stocks on their growth story coming from innovation. We also maintain a positive view on the internet retail segment in Consumer Discretionary and healthy living trends in the Staples sector. In the Energy sector, we believe the theme of North American energy independence is gaining traction and subsequent infrastructure growth will follow.

Eurozone equity markets will be driven by monetary policy, in our opinion. A search for yield in European equities has moved Utilities and Staples stocks year-to-date but is likely nearing an end. As we enter the second half, we remain cautious regarding returns in Europe and believe equity markets will lag those in the US as broad based growth in the region is still elusive.

United Kingdom is experiencing strong economic growth driven by an expanding housing market and an improved jobs market. However, companies based in the UK equity markets derive 77 percent of their revenues globally and are more biased toward Energy, Staples and Materials. We believe global integrated energy companies may be close to completing their operational turnaround following the BP oil spill scare but Materials companies wait a clear indication on Emerging Market growth before gaining traction. Nonetheless, positive economic data and improving real incomes should translate to higher equity returns, in our opinion.

Risks in Emerging Asia appear to be abating as China remains in-line with their economic guidance. In the most recent period, China's PMI has improved toward expansion following weaker results early in 2014. We await a clear inflection point before returning to a more neutral position. In Latin America, we maintain our preference for Mexico and remain positive on economic recovery and advancing stock prices as reforms remain underway and the fundamental story stays intact.

We also highlight potential volatility from increased violence in Iraq. An escalation in the Middle East and higher crude oil prices may raise demand for safer assets at the expense of equities.

"Global equities rally, particularly in U.S. and Europe, should remain on track as recovery in developed economies strengthens."

Mark Haefele,
Global CIO of UBS AG's wealth management unit, Singapore.
July 1, 2014.

CONCLUSION AND STRATEGY POINTS

EQUITIES

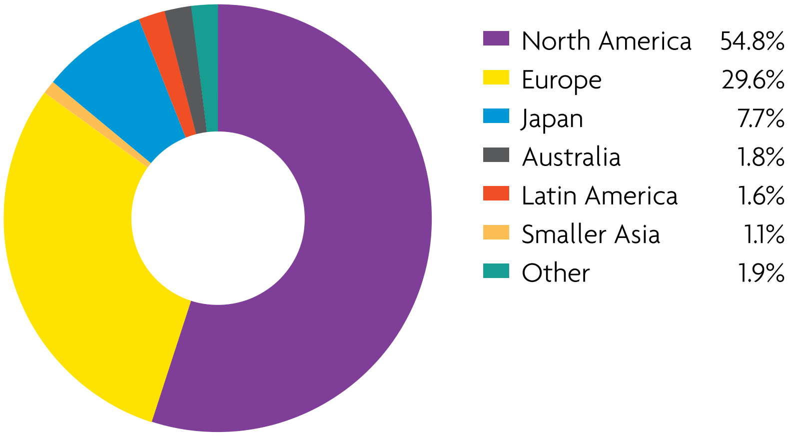
Regional Strategy

- Overweight US at 53.3 percent (versus an index weighting of 52.1 percent).
- Overweight UK at 8.7 percent (versus an index weighting of 7.8 percent).
- Underweight Emerging Asia at 1.1 percent (versus an index weighting of 3.8 percent).

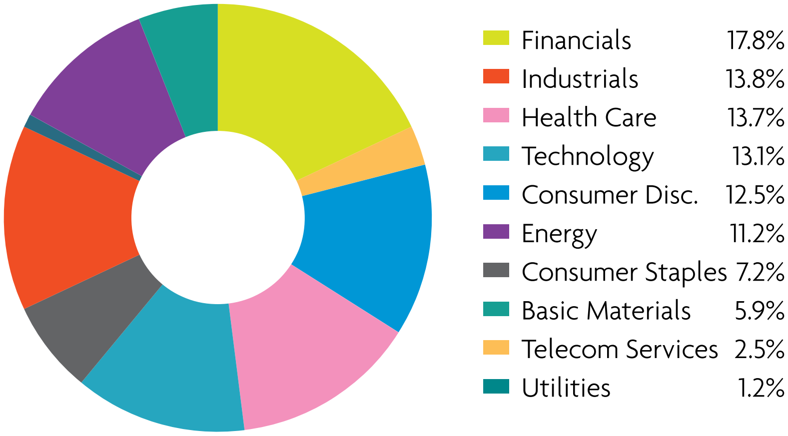
Industry Sector Strategy

- Overweight Industrials at 13.8 percent (versus an index weighting of 11.0 percent).
- Overweight Health Care at 13.7 percent (versus an index weighting of 11.1 percent).
- Overweight Energy, Consumer Discretionary, and Information Technology at 11.2, 12.5, and 13.1 percent, respectively (versus index weights of 9.8, 11.3, and 12.5 percent, respectively).
- Underweight Consumer Staples, Financials, Utilities, and Telecoms at 7.2, 17.8, 1.2, and 2.5 percent respectively (versus index weights of 10.2, 20.8, 3.3, and 3.9 percent respectively.)

Geographic Allocation



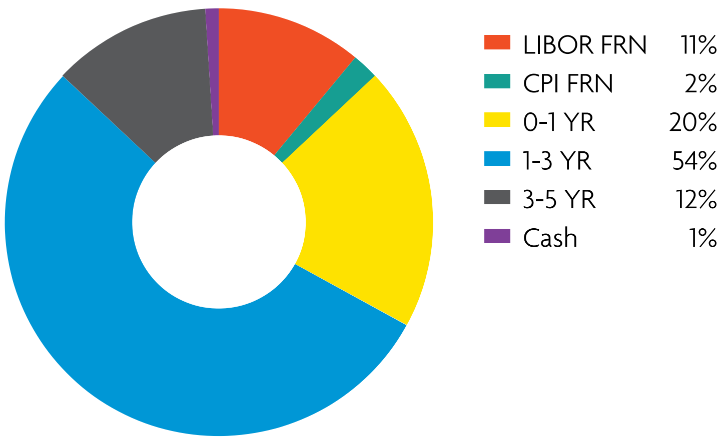
Sector Allocation



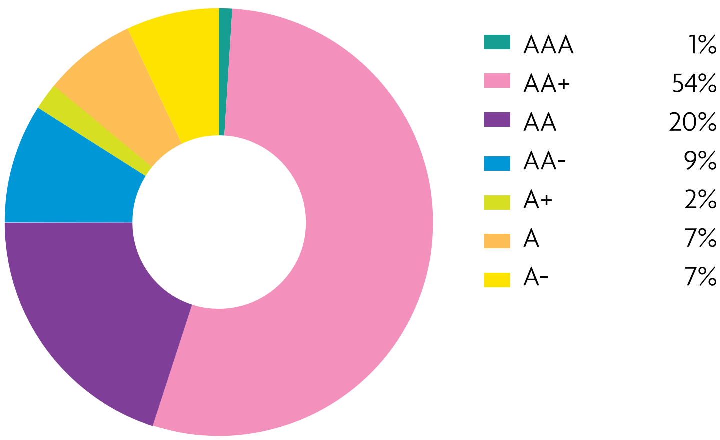
BONDS

- Stay short duration as interest rates gradually rise.
- Hold floating rate notes to take advantage of rising interest rates.
- Hold shorter-dated investment grade corporate bonds for their relative yield advantage over US Treasuries.

Bonds Strategy Allocation



Credit Ratings



BIAS structures portfolios according to the needs and risk profile of a specific investor. Some systematic risks should be acknowledged over which BIAS and other asset managers have no control including: trading on exchanges not regulated by any US Government agency, the Bermuda Monetary Authority, or the Cayman Islands Monetary Authority; possible failure of brokerage firms or clearing exchanges; illiquid markets which may make liquidating a position at a given price more difficult. For more details on these and other risk factors, please refer to BIAS' Form ADV as files with the US Securities and Exchange Commission.

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