# REVIEW & Outlook

Q1 2015
Q2 2015

## Global Financial Markets

BIAS

INVESTMENT MANAGERS - SECURITIES ANALYSTS

MARCH 31, 2015

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## Review Q1 2015



## Outlook Q2 2015

# World Markets Quarterly Review

**March 31, 2015**


*The S&P Global 1200 Index gained 2.2 percent for the quarter ended March 31, 2015. All returns are expressed in US dollars.*

| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| 1 | DJIA | 0.3% | 3 | BSX | 0.2% | 7 | UK FTSE | -0.2% | 11 | Nikkei | 10.2% |
| 1 | S&P 500 | 1.0% | 4 | Bolsa | -2.0% | 8 | CAC | 4.7% | 12 | Hang Seng | 6.0% |
| 1 | NASDAQ | 3.9% | 5 | Bovespa | -15.5% | 9 | DAX | 7.7% | 13 | Straits Times | -0.8% |
| 2 | TSX | -6.0% | 6 | Merval | 22.4% | 10 | Kospi | 5.4% | 14 | ASX | 2.9% |

# Stock, Bond, Currency Overview

## Global Stock Markets

- Global equity markets closed the First Quarter in positive territory as developed market central banks maintained their accommodative stance towards growth.
- In the US, investors remained selective and showed a preference for sectors with earnings growth and positive economic catalysts.
- In Europe, stocks were lifted by expectations of improving regional growth and outperformed the global benchmark in US dollar terms, more than offsetting the euro depreciation.

## Bond Markets

- Treasury yields fell amid low inflation expectations and on overseas demand for relatively better yielding assets.
- Yields on sovereign bonds in the eurozone fell as the region's central banks started buying bonds under the ECB's quantitative easing programme.
- The central banks in Canada and Australia cut their benchmark rates in the quarter citing weaker growth outlooks for their respective economies.

## Currency Markets

- The US dollar advanced against all major currencies but the Swiss franc on speculation the Fed was moving closer to raising interest rates while counterparts in Europe and Asia eased monetary policy.
- The euro weakened as the ECB initiated a bond purchase programme to push inflation back to the central bank's target of close to two percent.
- The Canadian dollar weakened on concern the sharp decline in crude oil prices will affect the nation's economic growth.

# North American Stock Markets

| Indices | 31 Dec 2014 | 31 Mar 2015 | Total Returns Local Curr. | Total Returns US$ |
|---|---|---|---|---|
| US Dow Jones Industrial | 17,823.07 | 17,776.12 | 0.3% | 0.3% |
| US S&P 500 | 2,058.90 | 2,067.89 | 1.0% | 1.0% |
| US NASDAQ | 4,736.05 | 4,900.89 | 3.9% | 3.9% |
| Canada TSX | 14,632.44 | 14,902.44 | 2.6% | -6.0% |
| S&P Global 1200 | 1,897.82 | 1,927.26 | 2.2% | 2.2% |

*Source: Bloomberg*

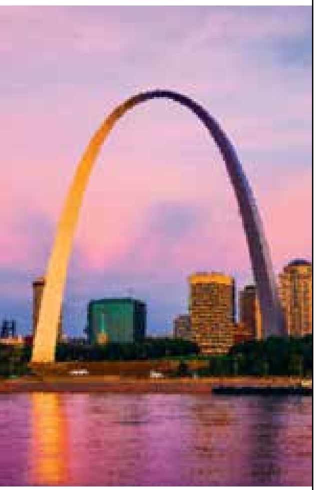
*Healthcare and consumer stocks led gains in the US in First Quarter 2015.*

- **On January 16** Forex Capital Markets (FXCM), the largest US retail foreign exchange broker, announced it would be unable to comply with capital requirements imposed by the industry regulator. The announcement came against the back drop of the Swiss central bank's unexpected decision to remove the cap on the Swiss franc against the euro which led to a rally in the Swiss franc. This in turn caused significant losses for FXCM's clients. Shares of FXCM plummeted 92 percent before trading in the stock was halted. The company negotiated a rescue by Jefferies, an investment bank owned by Leucadia National Corp., and a rescue package was confirmed on January 20 with Jefferies injecting $300 million in FXCM.

- **On February 3** Staples Inc. and Office Depot Inc. confirmed they were in talks for a possible merger. The deal would result in the largest office supply retail chain in the US. In 1997, Staples had tried to acquire Office Depot but the Federal Trade Commission (FTC) termed the transaction anticompetitive and the deal consequently fell apart. Last year, however, the FTC did approve a merger between Office Depot and OfficeMax, the industry's second and third-largest chains, after the retailers argued that there was adequate competition from online retailers. As the possible merger was announced, Staples jumped 13 percent and Office Depot surged 21 percent.

- **On February 12** the US Patent and Trademark Office rejected the renewal of a Johnson & Johnson (J&J) patent arguing that it did not add anything new to earlier patents covering the same type of drug. The patent under question is used in one of J&J's best selling drug, Remicade, which generates about $7 billion of sales annually. J&J can appeal the decision to a board within the agency and, if that does not work, to a court specializing in patent law. The patent remains valid during that process. On the day of the rejection shares of J&J declined 3.2 percent in New York trading.

- **On March 25** Kraft Foods Group announced a merger with H.J. Heinz led by investment firms 3G Capital and Warren Buffett's Berkshire Hathaway Inc. The combined entity, The Kraft Heinz Company, will be the fifth largest food company in the world and third largest in the US. The deal is worth $46 billion and expected to be transacted in stock and cash. Kraft shareholders will receive 49 percent of stock in the combined entity and a one-time cash dividend of $16.5 per share while Heinz shareholders will retain a 51 percent stake. Investors expect drastic cost cutting following the merger and value to be driven from combined operations. Kraft shares soared 36 percent to close at $83.17 in New York after the announcement.



# Latin American Stock Markets

| Indices | 31 Dec 2014 | 31 Mar 2015 | Total Returns Local Curr. | Total Returns US$ |
|---|---|---|---|---|
| Mexico Bolsa | 43,145.66 | 43,724.78 | 1.5% | -2.0% |
| Brazil Bovespa | 50,007.41 | 51,150.16 | 2.3% | -15.5% |
| Argentina Merval | 8,579.02 | 10,837.23 | 26.3% | 22.4% |
| Chile IPSA | 3,850.96 | 3,916.92 | 1.7% | -1.2% |
| S&P Global 1200 | 1,897.82 | 1,927.26 | 2.2% | 2.2% |

*Source: Bloomberg*

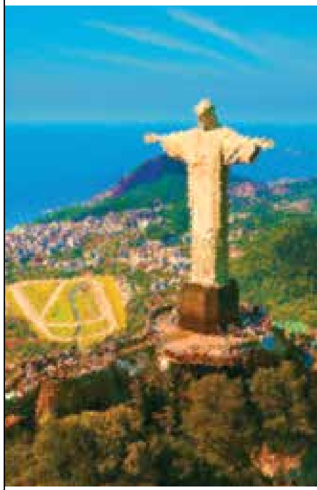
- **On January 8** Colombia's state-controlled oil company Ecopetrol SA said it was exploring to sell its stake in Invercolsa, SA, a natural gas and liquified petroleum gas distribution company, in a bid to divest non-strategic assets. Ecopetrol was also seeking the sale of other stakes, in particular Empresa de Energia de Bogota SA and Interconexion Electrica SA ESP stakes. The three sales may raise as much as $1.1 billion and allow Ecopetrol to focus on the core business in response to the slump in global crude oil prices. Ecopetrol shares fell five percent on the day of the announcement.

- **On January 26** AT&T Inc., agreed to buy NII Holdings Inc.'s Mexican wireless assets for $1.88 billion. The acquisition would include companies that operate under the name Nextel Mexico, spectrum licenses, and network assets. Nextel Mexico's network covers about 76 million people and the purchase gives AT&T an opportunity to not only capture more customers in Mexico but also in the US who have friends and family living across the border. The deal is expected to close in mid-2015, subject to regulatory approval by Mexico's telecom regulator and by the US Bankruptcy Court. NII Holdings' shares, which trade on the OTC exchange, rose 135 percent in the quarter.

- **On January 29** Petrobras, a semi-public Brazilian energy company, signaled a potential dividend cut as a result of involvement in Brazil's biggest ever corruption scandal. The corruption probe has blocked the company's access to debt financing and Petrobras now plans to use more than half of its cash holdings to cover investments and expenses, including debt service costs. Petrobras' shares fell 2.9 percent in the quarter.

- **On February 23** British American Tobacco plc announced it was considering buying out the minority stake in the company's Brazilian unit Souza Cruz SA. The transaction is estimated at about $3 billion and would be transacted in cash. The deal would enhance better cooperation on new product development and is considered strategically attractive as Souza Cruz has a market share of 78 percent in Brazil. Souza Cruz shares rose 9.9 percent on the announcement while British American Tobacco shares gained two percent in London.

*Currency headwinds marred returns in Latin American markets.*



# European Stock Markets

| Indices | 31 Dec 2014 | 31 Mar 2015 | Total Returns Local Curr. | Total Returns US$ |
|---|---|---|---|---|
| UK FTSE | 6,566.09 | 6,773.04 | 4.7% | -0.2% |
| Germany DAX | 9,805.55 | 11,966.17 | 22.0% | 7.7% |
| France CAC 40 | 4,272.75 | 5,033.64 | 18.0% | 4.7% |
| Spain IBEX 35 | 10,279.50 | 11,521.10 | 13.0% | 0.2% |
| S&P Global 1200 | 1,897.82 | 1,927.26 | 2.2% | 2.2% |
| S&P Europe 350 | 1,401.41 | 1,624.37 | 16.8% | 3.6% |

*Source: Bloomberg*

*European stocks gained from expected improvements in the economy.*

- **On January 11** Dublin based Shire plc announced a merger agreement with NPS Pharmaceuticals Inc. Shire markets, licenses, and develops prescription medicines while NPS is a biopharmaceutical company focused on the development of treatment options for patients with rare gastrointestinal and endocrine disorders. Shire acquired all the outstanding shares of NPS Pharma for $46 per share in cash, a total consideration of approximately $5.2 billion. The acquisition was completed on February 21. In the quarter, Shire rose 18.6 percent while NPS rose 33.8 percent up until the date of acquisition.

- **On February 26** medical device makers Sorin SpA and Cyberonics Inc. agreed to merge in order to expand in the area of cardiac surgery and heart failure. The new company will be based in the UK and will seek listings on the Nasdaq and the London Stock Exchange. Equity value of the new holding company will be about $2.7 billion with 54 percent ownership by Cyberonics shareholders and 46 percent by Sorin shareholders. In the quarter Sorin rose 18.5 percent and Cyberonics gained 32.7 percent.

- **On March 12** Banco Sabadell SA, one of Spain's largest banks, announced that it was considering a takeover of TSB Banking Group, Britain's seventh-biggest bank, for about £1.7 billion. Sabadell is well known for its business lending heritage and ability to efficiently integrate acquisitions. The transaction should help Sabadell build an international presence following a contraction in local business owing to Spain's recession. TSB's stock rose 25 percent in London trading after the announcement while Sabadell shares fell seven percent in Madrid.

- **On March 13** the Italian oil and gas company Eni Spa announced a dividend cut and the suspension of its share buyback program. According to Eni's CEO, rationale for the dividend cut was to save funds to spur future production growth while attempting to increase Eni capabilities to sustain a period of lower crude oil prices. Eni's shares fell 4.6 percent on the day of the announcement.

- **On March 30** Swiss company Dufry AG announced plans to acquire Italian rival World Duty Free SpA for $2.8 billion. After buying 50.1 percent stake from a company controlled by the Benetton family, Dufry said it would also make an offer for the rest of World Duty Free. Shares of Dufry AG gained 8.5 percent on the news, the most since 2009.

# Pacific Rim Stock Markets

| Indices | 31 Dec 2014 | 31 Mar 2015 | Total Returns Local Curr. | Total Returns US$ |
|---|---|---|---|---|
| Japan Nikkei | 17,450.77 | 19,206.99 | 10.7% | 10.2% |
| Hong Kong Hang Seng | 23,501.10 | 24,900.89 | 6.0% | 6.0% |
| Hang Seng Red Chip | 4,331.52 | 4,650.05 | 6.9% | 6.9% |
| Korea Kospi 100 | 1,915.59 | 2,041.03 | 6.6% | 5.4% |
| Singapore STI | 3,366.11 | 3,447.01 | 2.8% | -0.8% |
| Taiwan TWSE | 9,268.43 | 9,586.44 | 3.0% | 4.2% |
| Australia ASX 200 | 5,416.63 | 5,891.51 | 10.3% | 2.9% |
| S&P Global 1200 | 1,897.82 | 1,927.26 | 2.2% | 2.2% |
| FTSE Pacific ex-Japan | 458.79 | 470.15 | 3.3% | 3.3% |

*Source: Bloomberg*

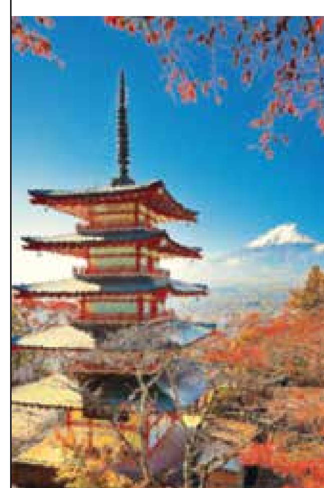
- **On January 9** Hong Kong billionaire Li Ka Shing announced a $24 billion restructuring of his companies, Cheung Kong Holdings and Hutchison Whampoa. Real Estate assets in each company would be spun off into a separate entity by the name of Cheung Kong Property Holdings while non-property assets would be integrated under CK Holdings. The deal would simplify Li's empire and allow investors to choose a pure play property business or an expanding global company. In reaction to the news, share price of Cheung Kong Holdings and Hutchison Whampoa gained 24.3 and 22.6 percent, respectively.

- **On January 22** the Japanese machine tool maker DMG Mori Seiki launched a takeover of German partner DMG Mori Seiki AG, in which the Japanese company already owns a stake of almost 25 percent. The companies have been cooperating since 2009 and eventually adopted similar names as part of their alliance. The proposed takeover would be one of the biggest to-date of a German company by a Japanese peer. Seiki shares rose ten percent in Tokyo trading while the shares of the German partner jumped 12 percent on the news.

- **On February 4** Alibaba Group Holding Ltd., China's biggest internet retailer, announced the testing of drone deliverers. The trial was limited to areas within a one-hour flight of Alibaba's distribution centers in Beijing, Shanghai, and Guangzhou. The technology will speed up deliveries and boost the budding commercial drone industry in China. Key regulations regarding flight altitude and accountability for accidents, however, have not been established yet. Investors did not buy into the company's innovation with shares falling 19.9 percent in the quarter.

- **On March 11** Japan's Brother Industries Ltd. agreed to buy Domino Printing Sciences plc in the UK. Brother produces communications and office equipment including digital copy machines, label printers, and word processors, while Domino is a developer of inkjet printing and laser printing products. The acquisition would allow the Japanese company to expand its industrial printing range as home printer demand has fallen due to the higher use of smart devices. On the day of the announcement Brother Industries' shares fell 12.5 percent while Domino's shares rose 44.5 percent.

*Pacific Rim markets gained on economic improvements in Japan and expected stimulus in China.*



# Bermuda & Cayman Stocks

| Benchmark Indices | 31 Dec 2014 | 31 Mar 2015 | Total Returns Local Curr. | Total Returns US$ |
|---|---|---|---|---|
| BSX Index | 1,357.12 | 1,346.38 | 0.2% | 0.2% |
| BSX Insurance Index | 1,535.40 | 1,543.73 | 0.5% | 0.5% |
| S&P Global 1200 | 1,897.82 | 1,927.26 | 2.2% | 2.2% |
| **Stocks** | | | | |
| ACE Ltd. | 114.88 | 111.49 | -2.4% | -2.4% |
| Ascendant Group Ltd. | 5.40 | 5.20 | -2.4% | -2.4% |
| Butterfield Bank | 2.00 | 1.98 | 0.0% | 0.0% |
| Caribbean Utilities | 10.71 | 11.11 | 5.9% | 5.9% |
| Consolidated Water Co. | 10.64 | 10.27 | -3.1% | -3.1% |
| XL Capital Ltd. | 34.50 | 36.80 | 7.6% | 7.6% |

*Source: Bloomberg*

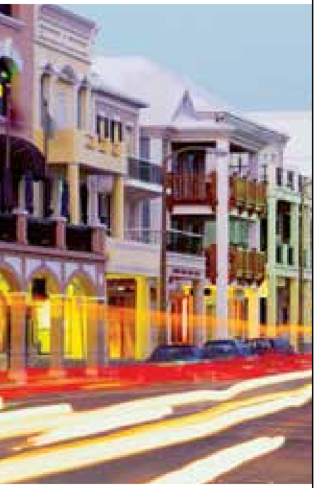
*Local shares underperformed the global benchmark in the quarter.*

- **On January 9** XL Group plc announced the acquisition of Bermuda-based Catlin Group Ltd. The combined business is expected to have a leading presence in the top ten global specialty insurance and reinsurance markets and will operate under the trade name XL Catlin. The transaction will involve stock and cash exchange with XL acquiring all Catlin common stock and Catlin shareholders receiving 388 pence in cash and 0.13 shares of the new entity for each share they own. This represents a transaction equity value of nearly $4.1 billion. Shares of XL and Catlin returned 7.6 and 9.2 percent in the quarter.

- **On January 25** Axis Capital Holdings Ltd. and PartnerRe Ltd. announced a $11 billion merger to create one of the world's largest reinsurers. The deal is an all-shares agreement where PartnerRe shareholders will receive 2.18 shares of the new entity while Axis shareholders receive one share for each share they own. The transaction is expected to close in the Second Half 2015. On the day of the announcement, Axis stock advanced 4.9 percent and PartnerRe rose 0.6 percent.

- **On March 2** RenaissanceRe completed an acquisition of Platinum Underwriters Holdings Ltd. for $1.9 billion. The deal was announced on November 24, 2014. About two-thirds of Platinum employees based in Bermuda were offered either a permanent or temporary position at RenaissanceRe. Not all employees accepted the offer with around 50 percent of the original workforce expected to integrate with RenaissanceRe. Shares of RenaissanceRe and Platinum rose 2.9 and 4.2 percent in the quarter.

- **On March 17** Consolidated Water Co. Ltd. announced 2014 financial results. Net income decreased 27 percent to $6.27 million for the year ended December 31, 2014, compared to $8.59 million for the year ended December 31, 2013. Revenues increased by three percent attributable to higher sales from the retail and services business segments. However, higher plant and equipment maintenance costs in the Cayman operations also increased which forced gross profits to decline to approximately $23.1 million (35 percent of total revenues) in 2014 from  $23.5 million (37 percent of total revenues) in 2013.



# Global Bond Markets

| Indices | (Yield to Maturity) 31 Dec 2014 | 31 Mar 2015 | Total Returns Local Curr. | US$ |
|---|---|---|---|---|
| US 2 Year | 0.66% | 0.56% | 0.52% | 0.52% |
| US 10 Year | 2.17% | 1.92% | 2.60% | 2.60% |
| US 30 Year | 2.75% | 2.54% | 4.97% | 4.97% |
| Canadian 10 Year | 1.79% | 1.36% | 5.56% | -3.31% |
| Australian 10 Year | 2.74% | 2.32% | 4.97% | -2.33% |
| UK Gilt 10 Year | 1.76% | 1.58% | 1.73% | -3.22% |
| German Bund 10 Year | 0.54% | 0.18% | 4.15% | -7.62% |
| Japanese 10 Year | 0.33% | 0.40% | -0.44% | -0.73% |
| **Citigroup** | | | | |
| 3-7 Year Treasury Index | 1,369.51 | 1,393.51 | 1.75% | 1.75% |
| 7-10 Year Treasury Index | 1,737.81 | 1,781.73 | 2.53% | 2.53% |
| 1-10 Year US Corp. Bond Index | 1,649.40 | 1,678.14 | 1.74% | 1.74% |
| World Gov't 7-10 Yr. Bond Index | 1,196.59 | 1,151.02 | -3.81% | -3.81% |

*Source: Bloomberg*

- **Japanese investors** were net buyers of overseas sovereign debt in January underscoring their appetite for higher overseas returns as the Bank of Japan's unprecedented monetary easing suppressed Japanese yields. Japanese net purchases of Canadian sovereign bonds rose to ¥99.5 billion, the most since May 2010. The Japanese also bought a net ¥469.7 billion of French government bonds, the largest amount in seven months, and ¥182.9 billion in Belgian securities, the most on record back to January 2005. In total, about ¥1.9 trillion yen were invested in overseas sovereign debt in January adding to the downward pressure on yields in both Canada and Europe.

- **On February 3** Australia's central bank (RBA) cut the benchmark interest rate to an all-time low of 2.25 percent citing a weaker growth outlook for the nation's economy. The cut marked a sharp turnaround from the bank's previous meeting in December when the bank signalled a period of stability for monetary policy. However, following a rush to ease by central banks in Europe and Canada, the RBA had to follow suit if only to stop the Australian dollar from rising to uncompetitive levels. Following the cut to the benchmark rate yields on the nation's 10-year government bonds dropped to a record low of 2.36 percent.

- **On February 6** FIH Erhvervsbank in Denmark announced plans to charge retail customers to hold money in their deposit accounts. The rare move came after Denmark's central bank cut rates to minus 0.75 percent to defend the Danish krone's peg against the euro. The bank's CFO Palle Nordahl said "If people want to put their money with us in our deposit bank, we at least don't want to lose money on it." According to Mr. Nordahl some of the bank's 26,000 retail customers have already left the bank following the decision to charge interest on deposits. Other larger Danish banks said they may charge interest to depositors if interest rates drop further or stay below zero for longer.

- **On March 9** the European Central Bank started buying government bonds under the expanded quantitative-easing (QE) plan designed to boost inflation in the region. People with knowledge of the transactions said the ECB along with national central banks bought German, Italian, French, and Belgian securities on the first day of QE. The QE purchases resulted in yields falling across the region, with yields on longer-maturity bonds declining the most.

*Yields fell in most developed nations on central bank action.*

# World Currency Markets

**Value of Currency** — US$1 = value in local currency

| Currency | 31 Dec 2014 | 31 Mar 2015 | Change |
|---|---|---|---|
| Australian Dollar | 1.2232 | 1.3146 | -7.0% |
| Brazilian Real | 2.6576 | 3.1967 | -16.9% |
| British Pound | 0.6420 | 0.6749 | -4.9% |
| Canadian Dollar | 1.1621 | 1.2686 | -8.4% |
| Euro | 0.8266 | 0.9318 | -11.3% |
| Japanese Yen | 119.7800 | 120.1300 | -0.3% |
| Swiss Franc | 0.9943 | 0.9727 | 2.2% |

*Source: Bloomberg*

*The US dollar advanced against most major currencies in the quarter.*

- **On January 15** the euro tanked 15 percent against the Swiss franc after the Swiss National Bank (SNB) removed a three-year old exchange rate cap that kept the franc weak against the euro. The euro initially plunged 30 percent in chaotic early trading and Swiss stocks plunged over ten percent on the day on fears for the export-reliant Swiss economy. The Swiss central bank's move came a week before the ECB was expected to unveil a bond-buying programme to counter deflationary pressure. Expectation is that the quantitative easing scheme from the ECB would be so big that the SNB would have struggled to defend the exchange rate cap.

- **On February 23** The Brazilian real touched a decade low against the US dollar as analysts surveyed by the nation's central bank projected a deeper contraction in Latin America's largest economy. In addition to poor economic growth, the nation's fiscal weakness raised concern of a sovereign credit rating downgrade. In the quarter the real weakened 16.9 percent against the US dollar.

- **On March 11** the euro fell to $1.0560, the weakest level against the dollar since March 21, 2003.  The drop in the euro came as the ECB's quantitative-easing programme entered its third day. In the quarter the euro weakened 11.3 percent against the dollar amid ECB purchases of sovereign debt.

- **On March 13** the pound Sterling fell to the lowest level since 2010 against the dollar amid concerns over the outcome of UK's May elections. Additionally, comments about the pounds relative strength from Bank of England Governor Mark Carney spurred speculation that the Bank of England may be slower to raise borrowing costs than previously thought. In the quarter the Sterling weakened 4.9 percent against the dollar.

- **The Canadian dollar** weakened to the lowest level against the US dollar in six years on March 13 after a report showed the Canadian economy lost jobs in February as the impact of the sharp decline in oil prices reduced jobs in Alberta. The province of Alberta, home to the bulk of Canada's oil reserves, posted a 14,000 decline in employment and raised concern the Canadian economy was beginning to see the impact of lower oil prices. In the quarter, the loonie weakened 8.4 percent against the US dollar.

- **The US dollar** advanced against all major currencies but the Swiss franc in the First Quarter on speculation the Federal Reserve was moving closer to interest-rate increases as counterparts in Europe and Asia eased monetary policy. Overseas demand for relatively better yielding US assets further added to dollar strength. The trade-weighted dollar rose 7.1 percent in the quarter.

# Outlook
## FOR THE SECOND QUARTER 2015

**We expect global growth to remain modest as major economies move through the current recovery cycle aided by low interest rates and accommodative central bank policies.**

- The US economy should stay ahead of other developed markets on the back of higher contribution from consumption.
- Inflation expectations remain muted as commodity and input prices stay depressed.
- While global growth receives a boost from lower oil prices, this may be offset by investment weakness if diminished demand persists.

**We expect higher interest rates in the US later this year as the Fed tightens monetary stimulus. Near term, however, we expect Treasury yields to stay low on overseas demand for relatively better yielding assets.**

- We expect the Fed to raise rates by 25bps in September on the back of gradually improving economic data.
- Overseas demand could possibly push yields in the US lower, even if the Fed raises rates, especially at the longer-end of the yield curve.
- Gilt yields are likely to gradually rise on the back of an improving economy and as the Bank of England is expected to be next in line after the Fed to raise rates.

**We expect the dollar to continue to strengthen against most major currencies as the developing monetary policy divergence story retains traction.**

- The dollar is supported by robust domestic economic data, expectations of interest rate hikes, and developments overseas.
- The euro weakness should continue led by monetary policy divergence between the ECB and the Fed and continued risks surrounding Greece.
- The outlook for commodity currencies remains bleak as we expect oil prices and commodities generally to stay low this quarter.

**We do not view commodities positively as an investment option given the expected appreciation of the US dollar.**

- Crude oil markets face further risks and we do not expect a 'V-shaped' recovery in prices near term.
- Gold and silver face increasing pressure from US dollar strength and subdued global inflation.
- In base metals, we maintain a positive view of aluminium and nickel as data indicates their markets remain in a supply deficit.

**We have a positive view of global equities relative to bonds as interest rates remain historically low, corporate earnings maintain an upwards trajectory, and valuations seem contained within a historical range.**

- Monetary policy divergence story retains traction and currencies maintain their importance in equity investing.
- In the US, we prefer to hold positions where growth is aligned with long term themes and valuations are reasonable relative to growth.
- In Europe, our investment case is predicated on ECB's monetary stimulus and the resulting financial asset inflation.

# ECONOMICS

*"We do see considerable underlying strength in the U.S. economy and in spite of what looks like a weaker first quarter, we are projecting good performance for the economy."*

Janet Yellen,
Fed Chair, FOMC
Press Conference,
March 18, 2015

## The World

We expect global growth to remain modest in the Second Quarter 2015 as major economies move through the current recovery cycle aided by low interest rates and accommodative central bank policies. We highlight the US economy as a bright spot which should stay ahead of other developed markets and reiterate our case for monetary policy divergence. Inflation expectations are muted as commodity and input prices remain depressed. Furthermore, on the demand side, we do not expect meaningful pressure which would warrant higher end product prices. The lower crude oil price continues to demand attention as its impact varies by region. IMF noted in their latest economic publication that while global growth receives a boost from lower oil prices, this may be offset by investment weakness if diminished demand persists. Global GDP growth in the current year is expected at 2.76 percent, revised slightly lower from the last quarter, as per Bloomberg estimates.

## North America

We maintain our positive view of the US economy with Second Quarter 2015 annualized GDP growth expected at three percent. We note some seasonality should come into play as we move away from the cold winter and move into spring. For the year, Bloomberg estimates suggest a three percent growth rate, unchanged from the last quarter.

Broad data points in the US indicate a recovery in the economy. JP Morgan estimates suggest that year-on-year improvement in GDP growth will come on the back of higher contribution from consumption. This is supported by rising consumer sentiment and improving employment data with unemployment at cycle-lows and initial claims on a downward trajectory. Improvements have, however, been meagre in some areas. Average hourly wage growth is in the two percent range which puts a question mark on the increased purchasing power of consumers. Recently, however, Walmart, TJ Maxx and other large retailers have announced increases to base hourly wages, which may be an early catalyst for wage inflation.

Positive economic metrics will generate a debate regarding the Fed's decision to raise interest rates but low inflation, a stronger dollar and monetary easing abroad will force the Bank to remain cautious, in our opinion. Recent commentary has also reinforced our view that the Fed remains data dependent and cognizant of the global macro environment which reduces the risk of an early economic derailment.

Canada's economy is expected to grow at 1.7 percent annualized in the second quarter and 2.1 percent in 2015, revised downward from previous estimates of 2.5 percent. The brunt of lower crude oil prices will pressure the country's main export, but impact on the economy does not stop there. We reiterate a spillover effect in capital investment, employment, and the housing sector – especially in the oil driven Alberta province. An accommodative central bank and weaker currency should support the manufacturing sector but it may not entirely offset commodity related declines.

## Europe

After the announcement of Quantitative Easing by the ECB, expectations have risen regarding growth in the eurozone. A consensus of Bloomberg analysts suggests that growth will pick up in the Second Quarter 2015 with GDP expected to rise 1.2 percent. Full year GDP growth is expected at 1.3 percent – revised upwards from prior estimates. Much of the improvement is expected to come on the back of investment spending as the currency weakens, which should aid exporters. Germany would be the primary beneficiary in this scenario, in our opinion, where GDP growth is expected to lead eurozone peers. However, we highlight that the road to recovery in the area is not a straight and clear path. Historically low interest rates and the limitation of economic improvements solely led by monetary policy pose reservations with regards to the efficacy of bond buying by the ECB. The eurozone, specifically Greece and the peripheral nations, still have chronic problems in the labour market as well as fiscal and balance of payment imbalances, which necessitate structural reforms to resolve. In the near term, we do not foresee such a resolution and expect the status quo to hold.

We maintain our outlook for the UK with Second Quarter and Full Year 2015 GDP growth estimates of 2.5 percent and 2.6 percent, respectively. With general elections looming in May, we expect UK's budget deficit, which still runs over five percent of GDP, to be at the center of political debates. Coming out of the elections we may expect a gradual improvement in the budget gap as the new Government addresses the issue. Furthermore, the economy should be aided by continued low interest rates as inflation, as for most developed economies, stays below the central bank's target rate.

## Pacific Basin

We highlight improvement in the Japanese economy – albeit at a gradual pace, with Second Quarter 2015 annualized GDP growth of 1.9 percent and full year growth of one percent. Economic data suggests improvement in Japan is primarily coming on the back of a weaker yen and sustained low crude oil prices. Morgan Stanley notes a cyclical recovery and points to three areas of growth. Firstly, export volumes, led by capital goods shipments, are on the rise with support from improved competitiveness tied to the weaker yen. At the same time, personal consumption is showing positive signs as household sentiment recovers on the back of improving wage and employment conditions. Secondly, capital investments are expected to trend upwards amid corporate expectations of a continued recovery. And finally, sustained low crude oil prices should deflate the import bill and increase household and corporate real incomes. All these point towards an overall positive outlook for the Japanese economy.

For China, 2015 continues to be a year of moderating growth. The world's second largest economy revised full year GDP growth downwards to seven percent, which is now more in line with IMF and World Bank estimates. The model continues to be a transition away from infrastructure spending and towards more sustainable growth of domestic consumption. The key risk still remains the PBOC's ability to stimulate the economy to land safely. Chinese policies also impact the commodity based Australian economy, where Second Quarter 2015 annualized GDP growth is expected at 2.2 percent with a further pick up expected later in the year as lower interest rates and a depreciated currency take effect.

## Latin America

Latin American growth has witnessed a significant downward revision with GDP growth in 2015 expected at 0.99 percent compared to previous Bloomberg estimates of 1.86 percent. The lowered estimates come on the back of deteriorating growth in Brazil and Venezuela, which ties in with our Atlantic vs. Pacific bloc thesis. Recall that we presented the idea of countries in the Atlantic bloc underperforming their Pacific peers. We fear the worst for Brazil may not be over and mismanagement of the Rousseff government may further diminish business sentiment and encourage capital outflows. At the same time, Brazil's lack of commitment to support its currency should pose further risk to the downside.

*"Exports will probably continue to be the main driver for Japan's economy in the first half of this year."*

Minoru Nogimori, Economist at Nomura Securities Co Ltd, Tokyo, March 19, 2015

# BONDS

*"Even once rates start to go up, they may not reach long-term 'normal' levels for some time."*

Janet Yellen,
Federal Reserve Chair,
March 18, 2015

Most major central banks are easing monetary policy in light of low inflation and weak global growth, forcing interest rates lower. We could see higher interest rates in the US later this year driven by improving economic data and as the Fed tightens monetary stimulus. Near term, however, we expect Treasury yields to stay low on overseas demand for relatively better yielding assets. In fact, the 10-year spread between US Treasuries and German bunds is at its highest level in 25 years, increasing the attractiveness of US debt and demand for the US dollar.

We agree with market consensus and expect the Fed to raise rates by 25bps in September on the back of gradually improving economic data. The Fed has communicated that their next move is an increase in interest rates but the timing will ultimately depend on realized and expected progress towards the central bank's dual mandate of maximum employment and stable prices. The former is measured by the unemployment rate which currently stands at 5.5 percent but targeted by the Fed at 5.0 to 5.2 percent. The latter is measured by inflation which stands at 1.6 percent with a target of two percent.

Importantly, there are at least two major factors holding back a sharp increase in yields despite expectations of the Fed raising rates. Firstly, reinvestment of the Fed's sizeable bond portfolio acquired under the quantitative easing programmes will continue in the near term. Secondly, with the ECB's QE in full swing overseas, the difference in interest rates between US Treasuries and German 10-year bunds is at the highest level in a generation. The substantial yield pick-up for investors holding Treasuries instead of German bunds will result in continued overseas demand for Treasuries and keep yields in the US low. In fact, overseas demand could possibly push yields in the US lower, even if the Fed raises rates, especially at the longer-end of the yield curve as long as inflation is contained.

In the eurozone, the ECB's large-scale quantitative easing programme will effectively soak up supply of the region's sovereign bonds and push yields lower still. In Germany, yields on sovereign bonds out to seven years maturity are already negative while Spain can now borrow at a cheaper rate than the US for ten years. The ECB has acknowledged that it will not buy debt yielding less than minus 0.20 percent, possibly putting a limit to how low yields can go. Negative interest rates will undoubtedly force flows out of the region as investors reach for relatively better yielding assets elsewhere, such as in the US.

In the UK, gilt yields are likely to gradually rise on the back of an improving economy and as the Bank of England is expected to be next in line after the Fed to raise rates. However, the central bank has placed emphasis on wage data in determining when to raise interest rates. Many compensation negotiations are due in April and should provide an indication of spare capacity in the economy and wage growth, providing clarity on the BOE's eventual path. We do not expect strong overseas demand near term for gilts as we do for US Treasuries as the UK faces an uncertain outcome of the election on May 7.

We expect the Bank of Canada to cut interest rates by another 25 bps in the second quarter to try to get ahead of deteriorating economic conditions following the sharp drop in energy prices over the past six months. An interest rate cut will keep the loonie weak - a boost for exports and the manufacturing sector. Additionally, lower interest rates should provide support to non-oil related business sentiment and investment. These tailwinds should offset some of the negative impact of lower oil prices on Canada's economy.

# CURRENCIES

We expect the dollar to continue to strengthen against most major currencies in 2015 as the developing monetary policy divergence story retains traction. In the US, the Fed is expected to raise interest rates on the back of an improving labour market; meanwhile, in Europe the ECB recently started an asset purchase programme aimed at weakening the euro and improving the regions competitiveness. In Japan, investors appear structurally inclined to reduce Japanese assets putting pressure on the yen. Weaker Chinese growth and low oil prices are likely to keep commodity currencies, such as the Australian and Canadian dollars, subdued.

The trade-weighted dollar has rallied since late 2014 but is far from historical highs and has room to appreciate, in our view. More importantly, while the dollar is supported by robust domestic economic data and expectations of interest rate hikes, developments overseas are likely to be the major catalysts for a continued US dollar rally near term.

The euro weakness should continue led by monetary policy divergence between the ECB and the Fed and continued risks surrounding Greece. The ECB's most recent stimulus is a powerful driver of portfolio flows out of the euro and into any country not at immediate risk of having to ease as well.

Sterling is one of the currencies that could benefit from portfolio flows out of the eurozone as the Bank of England is expected to be the next central bank after the Fed to raise interest rates. Near term, however, we expect Sterling to weaken against the dollar and be flat against the euro amid uncertainty ahead of the UK election on May 7. Additionally, recent economic data has showed a lack of wage growth and inflation in the UK economy, reducing pressure on the Bank of England to raise interest rates sooner.

The Japanese economy has started to show signs of revival with economic growth improving and inflation finally picking up albeit it still remains very muted. This should strengthen the currency eventually but near term we expect the yen to stay weak against the dollar as Japanese investors appear to favour foreign bonds and equities. This is in line with the Government Pension Investment Fund's (GPIF) change to their targeted levels of Japanese assets. In November 2014 the GPIF's allocation target of foreign bonds and equities was reset upwards at 40 percent. The GPIF has taken a gradual approach to reaching the new target and at December 31, 2014 the allocation was 32.7 percent in foreign assets. Hence, while the Bank of Japan may not ease monetary policy further and the economy improves, continuous longer-term asset flows out of Japan are likely to prevent the yen from appreciating against the US dollar.

The outlook for commodity currencies remains bleak as we expect oil prices and commodities generally to stay low this quarter, mainly affecting Canada and Norway, while relatively weak growth in China will impact the Australian economy. Central banks in the aforementioned nations are dovish and could deliver further interest rate cuts to stimulate their economies. This would further weaken their currencies against the US dollar.

In light of the above, we have hedged out the risk of euro and Japanese yen depreciation in the BIAS funds.

*"We expect we'll continue to see the dollar strengthen, however it will probably be at a much more gradual pace."*

Michael Sneyd, FX strategist BNP Paribas, London, March 19, 2015

# COMMODITIES

*"For better or worst, US shale is assuming the role of swing supplier."*

Mike Wittner,
Head of Oil Research,
Société Générale,
New York,
March 27, 2015

We do not view commodities positively as an investment option given the expected appreciation of the US dollar. Headwinds from the moderate global growth environment and negative sentiment created from the crude oil price decline reinforce this view.

We reemphasise the importance of crude oil in our outlook and believe that the absence of action from OPEC has fundamentally changed the nature of the market. The lack of a moderator should force prices to be driven more by demand/supply fundamentals. This involves a gradual phase out of high cost production, which in the current case is some North American shale output, before prices can find an equilibrium. At the same time we do not expect respite from the OPEC nations; some are debt burdened and count on oil revenues to balance their economies. In most instances, we may even see supply increase as these nations try to meet their revenue targets at the existing low price. The crude oil markets, therefore, face further risks and we do not expect a 'V-shaped' recovery in prices near term.

In precious metals, overriding fundamentals still point to lower prices in the Second Quarter 2015. We may see some support as investors price in a slower rate hike path by the Fed but inflation expectations remain subdued and the dollar strong. Also, while US Treasury yields may be at their historical low, they continue to provide a healthy yield pickup over their European peers, which indicate potential upside in US Treasuries – a headwind for gold.

In base metals, we maintain a positive view of aluminium and nickel as data indicates their markets remain in a supply deficit. For aluminium, this comes on the back of multiple years of restructuring on the supply side where production has moderated following sustained low prices. Also, on the demand side, robust automobile industry growth in the wake of fresh regulation for more fuel efficient cars should be supportive of prices. For Nickel, the deficit comes from Indonesia's ban on ore exports a year back. Chinese smelters actively manage inventory but a demand shock could catalyse prices in this undersupplied market.

In other metals, copper and iron ore largely stay tied to Chinese growth, which is tapering off to more moderate levels. While the rest of emerging Asia may soften the price decline, we do not believe the smaller regional economies will be able to offset the lower Chinese demand. The metals may witness short term price upside correlated with news related to easing credit conditions and stimulus efforts in China, but the long term trajectory appears sluggish.

# EQUITY STRATEGY

We have a positive view of global equities relative to bonds as i) interest rates remain historically low, which buoys equities as investors hunt for yield, ii) corporate earnings maintain an upwards trajectory, despite downward revisions in the Energy sector, and iii) valuations, although high on a forward price to earnings basis, seem contained within a historical range.

We reiterate our case for monetary policy divergence between the developed market central banks and subsequently the increased importance of currencies in equity investing. This is central to our equity strategy moving forward as well. In terms of broad asset allocation, we believe monetary stimulus in Europe will further depress bond yields in the region and force capital allocation changes. Some of these should enter European equities as investors hunt for yield while some could also spill over the Atlantic into US equity markets where equities, on average, continue to yield more than bonds. As detailed in our bond outlook, US Treasuries should also receive net inflows as they still offer the highest yield pick up over German sovereign debt in over 25 years.

We keep an overweight stance in the US as companies are well positioned to gain from underlying strength in the economy. Furthermore, balance sheets remain strong and stock returns should be lifted by mergers and acquisitions and share buybacks. On the flip side, broad index moves may be limited as S&P 500 valuations are at the high end of the range and Large Cap stocks remain vulnerable to US dollar strength. We, therefore, prefer to hold positions in pockets of the US market where growth is aligned with long term themes and valuations are reasonable relative to growth.

Healthcare and Information Technology remain our preferred sector plays due to secular growth trends, upside from innovation, and reasonable valuations. In the Healthcare sector, we continue to see upside in the biotechnology and life science tools industry. Biotech industry should also get a boost from M&A activity as large pharmaceuticals search for targets to augment growth. In the Information Technology sector, we anticipate a long term trend developing in the cyber security space which is our preferred area of growth in the sector.

As the US economy improves, we believe further attention to cyclical plays is warranted. We view the transportation industry, which reflects cyclical trade growth in North America, favourably. Additionally, fundamentals in the home construction and renovations area seem ripe and an improving labour market, gasoline savings, pent up demand and US dollar strength should all contribute towards this trend.

In Europe, our investment case is predicated on ECB's monetary stimulus and the resulting financial asset inflation. We note that assets should appreciate in local currency terms and, therefore, have hedged out the impact of euro depreciation against the US dollar in our funds. We anticipate gains to be broad but biased toward exporters and yield payers, which leads to our preference for dividend paying exporters in the euro area with an overweight in Germany.

In Japan, we hold a similar investment thesis where monetary stimulus by the central bank should lead to financial asset inflation in local currency terms. We, therefore, maintain broad exposure to Japan on a hedged currency basis. Our economic outlook in Japan further confirms this view as the weaker yen has translated to higher capital goods shipment and tightened slack in the labour market. Furthermore, low oil prices aid the Japanese markets by lowering the import bill while increasing consumer and corporate real incomes.

*"Central Banks are still a critical aspect of equities as an asset class."*

Ian Williams,
Market Strategist,
Peel Hunt LLP,
London,
March 27, 2015

# CONCLUSION AND STRATEGY POINTS

## EQUITIES

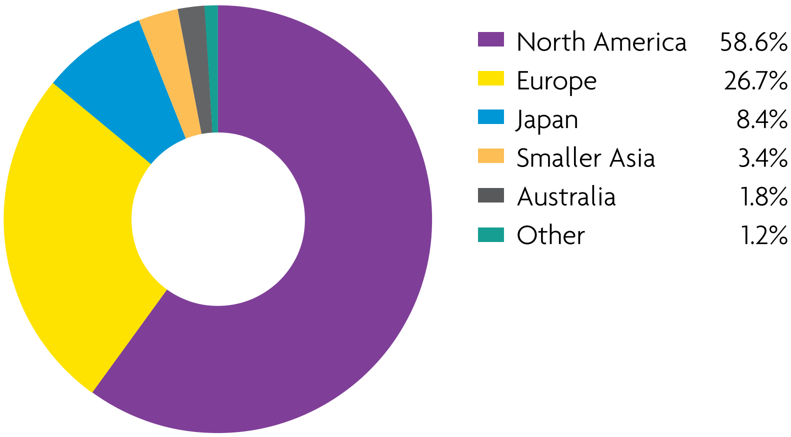
### Regional Strategy

- Overweight US at 58.3 percent (versus an index weighting of 54.9 percent).
- Overweight Japan at 8.4 percent (versus an index weighting of 7.7 percent).
- Slightly overweight Europe at 26.7 percent (versus an index weighting of 26.0 percent).

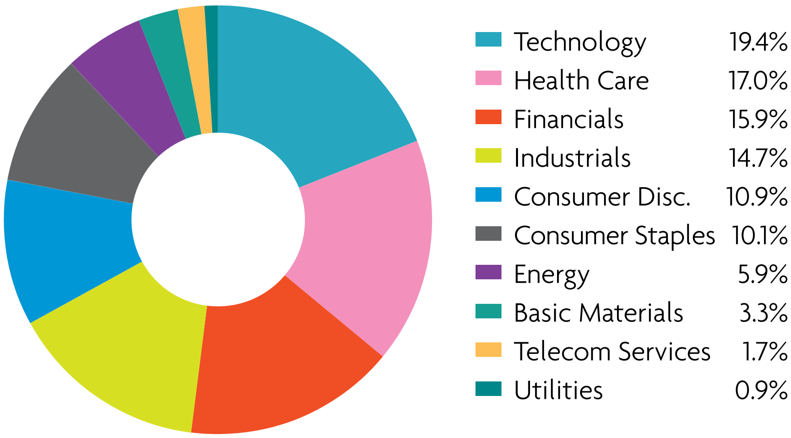
### Sector Strategy

- Overweight Information Technology at 19.4 percent (versus an index weighting of 14.2 percent).
- Overweight Healthcare and Industrials at 17.0 percent and 14.7 percent (versus an index weighting of 12.9 percent and 10.8 percent, respectively).
- Slightly overweight Consumer Staples and slightly underweight Consumer Discretionary at 10.1 and 10.9 percent (versus an index weighting of 10.0 percent and 12.1 percent, respectively).
- Underweight Financials, Utilities, and Telecom at 15.9, 0.9, and 1.7 percent (versus an index weighting of 20.6, 3.1, and 3.7 percent, respectively).

Geographic Allocation



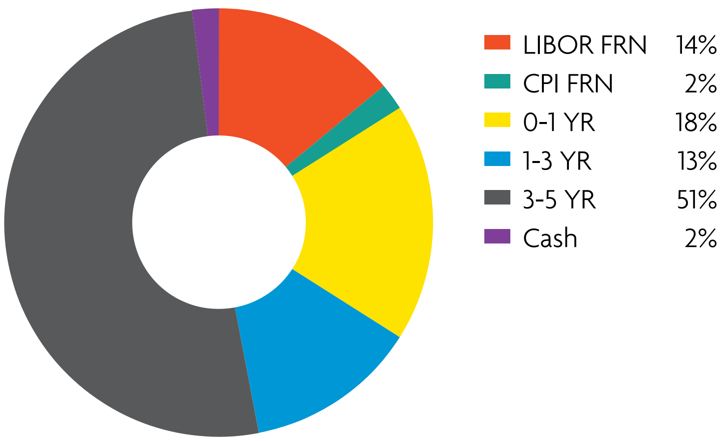

Sector Allocation



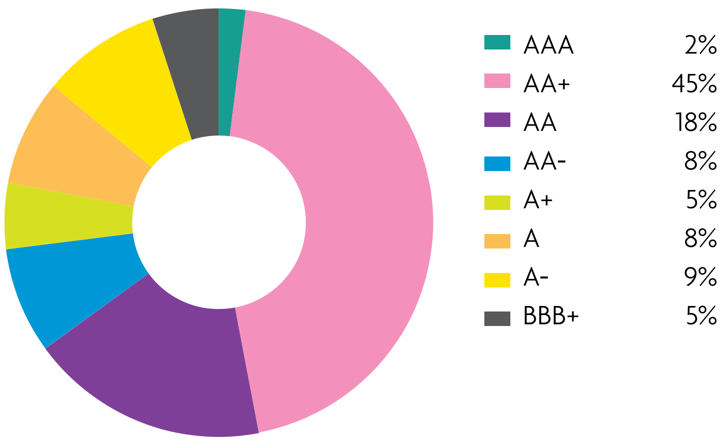
## BONDS

- Opportunistically add Treasuries maturing in four-to-five years for roll-down along the yield curve.
- Hold shorter-dated investment grade corporate bonds for their relative yield advantage over Treasuries.
- Hold floating-rate notes for when the Fed starts raising interest rates.

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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