DYNAMIC TREE ASSET MANAGEMENT

MARKET REVIEW & OUTLOOK Q2 2019

AGENDA

A ROBUST FIRST HALF OF 2019 FOR OUR DT 15

The DT Top 15 continued its robust performance in the second quarter, advancing by +22.04% YTD in USD terms.

With this result, we have beaten the MSCI World and most global markets.

After their strong performance in April, Global stock markets fell significantly in May across all major regions. As the US/China trade war intensified dramatically, investors became very uneasy as to the future path of global growth. Global markets are essentially tracking U.S. President Donald Trump's Twitter account. His tweet on May 5th announcing a tariff increase on Chinese imports triggered the end of the equity market recovery from the late-2018 downturn. Trade talks between the US and China broke down and, as a result, the US government increased tariffs on USD 200 billion of Chinese goods from 10% to 25%, and China retaliated by increasing tariffs on USD 60 billion in imports from the US. Rattled by trade and economic concerns, the S&P 500 dropped 6.58% in May, from 2,945.83 at the end of April to 2,752.06 at the May close. The Euro Stoxx 50 Index – a major benchmark for the performance of European equities – fell by 4.90%. Despite the extremely negative investor sentiment during the month of May, the Swiss Market Index only fell by 2.52%, thanks to the high portion of defensive stocks in the index and the perceived safe-haven status of the Swiss Franc. Nestlé, for example, gained 1.53% in May and Novartis even appreciated by 3.47%, once again confirming Switzerland's status as a safe haven in times of panic. Switzerland continues to attract significant new money flows, despite the fact that a 10-year Swiss Government Bond currently yields negative 0.66% per year! In other words, if you want to place your money in safe, triple-A rated Swiss Government bonds, you need to pay money to do so. Even if you lend money to the Swiss Government for a 50-year term, the current yield is a mere 0.05% p.a.

After a dismal month of May, during which many once again believed that the world was coming to an end, global financial markets came roaring back with a vengeance. Global risky assets received help from central banks. Challenged with more downside risks to the general economic outlook and decreasing long-term inflation expectations, the Fed indicated that eight out of seventeen members think rate cuts are warranted this year. As a result of Fed chairman Jerome Powell's comment that "an ounce of prevention is worth a pound of cure", the market now expects more than 0.5% worth of rate cuts by the end of 2019, in sharp contrast to the 0.5% increase in interest rates it was expecting for 2019 back in September 2018. Meanwhile, 10-year US bond yields have fallen to below 2% in recent days.

The European Central Bank (ECB) was also concerned about renewed downside risks to the economic outlook in the Eurozone. ECB president Mario Draghi said that monetary policy would be loosened if the economy does not improve, and was thus trying to convince markets that the ECB still has irons in the fire if further quantitative easing is required, and that interest rates could fall even further into negative territory if necessary. There are still risks in Europe, however: negotiations on a U.S.-European Union (EU) trade deal are making little progress, with President Trump keeping alive his threat of tariffs on motor vehicles, and the US has threatened additional tariffs on European exports in response to a long-running dispute over EU subsidies to the European aerospace corporation Airbus. On the positive side, Italy – the problem child of the European Union – is making progress. The yield on 10-year Italian Government Bonds has fallen significantly of late. While the yield back in November 2018 stood at about 3.60%, it dropped to as low as 1.63% on July 4, 2019. In addition, the spread between the yield on 10-year Italian bonds and 10-year German bonds has fallen considerably, from 3.27% back in November to 2.03% today – an indication that markets are less nervous about Italy than at the end of last year. However, further political uncertainty and a renewed conflict between the Lega party and the European Commission over fiscal easing could generate renewed market nervousness. Nevertheless, Europe should get a boost from a trade thaw, and stands to be one of the main beneficiaries of significant policy stimulus in China.

Stock Markets

The Swiss Market hit a new all-time high toward the end of the quarter as Switzerland's political stability and steady dividend flow from companies such as Roche Holding and Nestlé attracted investors looking for a safe haven in the midst of an unresolved US/China trade war and numerous other risks in Europe and around the globe. Global investors have increasingly turned to Switzerland's equities and currency as the Swiss Market Index – the Swiss benchmark index – is considered less risky thanks to the heavy weighting of Roche, rival drug maker Novartis, and Nestlé, the Swiss food giant being among the SMI's top gainers.

Stock markets around the globe put in a solid performance in Q2 2019. The following table shows the performance of selected markets:

World Indices	Price Change Q2 2019 (%)	Price Change YTD (%)
S&P 500	+2.60	+17.35
NASDAQ 100	+2.27	+20.66
Toronto TSX	+0.95	+14.38
Euro STOXX 50	+2.61	+15.74
SMI Swiss Market Index	+3.78	+16.92
German DAX	+6.14	+17.19
Japanese Nikkei 225	-1.08	+8.76
MSCI World	+3.02	+14.50

Source: Reuters (in local currency terms)

The Fed ignited the renewed surge in gold prices during the quarter. Gold, an asset without yield or dividend payments, gains in attractiveness in times of loose monetary policy. Moreover, gold also serves as a sort of insurance against catastrophes and events such as the financial crises when its price rose from USD 750/oz to above USD 1,800/oz. More and more analysts are issuing bullish comments concerning the price of gold. Some analysts even forecast a rise to USD 1,800. We are cautious long-term investors, however, and prefer to avoid getting carried away by short-term waves of optimism. Nevertheless, we believe that the price of gold could increase further, especially given falling US rates and the US/China trade war that seems far from resolved. Moreover, technical analysis also seems to indicate a further rise in the price of gold, since it broke out of its trading range between USD 1,100 and USD 1,380. Against this backdrop, we intend to keep our gold allocation in our balanced mandates.

"Building wealth is a process of managing risk, not ignoring it."
Jon Duncan

International diversification helps to spread and diminish risks globally while exposing the portfolio to additional opportunities.

DT Top 15

In Q2 2019, our DT Top 15 strategy was up by 7.35%, beating its benchmark the MSCI Total Return Index by over 4%. For the first 6 months of 2019, our DT Top 15 Strategy gained 22%, outperforming all major equity indexes. Established at the end of April 2013, our DT Top 15 now has a six-year plus track record with a total gross return of 93.94%, or 11.34%, on an annualized basis.

The top performing stock within our DT Top 15 strategy in Q2 was Sony, advancing by 22%. Second came Sonova, which gained 12.8%. The worst performing stocks during the quarter were Merck and Salesforce, losing 8.7% and 5.9%, respectively. Below is an overview of some of our current holdings:

Microsoft - Microsoft develops, manufactures, licenses, sells and supports software products. The company offers operating system software, server application software, business and consumer applications software, software development tools, Internet and intranet software and mobile software. Microsoft also develops video game consoles, digital music entertainment devices and personal computer input hardware.

We bought Microsoft back in March of 2017 at around USD 65. Although we then believed that the stock had good upside potential, even we never anticipated that Microsoft would once again become the company with the largest market capitalisation in the world. As of July 4th, Microsoft's market cap stands at USD 1.05 trillion, ahead of companies such as Apple (USD 940 billion) and Amazon (USD 954 billion). Microsoft enjoys a near monopoly in personal computer operating systems and office productivity software, and has a global distribution network and presence. The company is currently experiencing strong momentum with its cloud services

and Commercial Office), and has transformed its business model to address the demand for cloud capacity. Broad-based strength, combined with continued strong cloud growth, characterized Microsoft's latest earnings report. We believe its above-average earnings growth will continue, particularly based on the continuing strong momentum in the cloud.

Vinci - Vinci SA is a French-based company involved in construction and engineering. It designs, builds, finances and manages facilities such as transport systems, public and private buildings, urban developments, and water, energy and communication networks. It divides its business into two sectors: concessions and contracting. The contracting sector includes Vinci Construction, a company with numerous subsidiaries in Europe, and a division dedicated to the management and execution of projects and the energy business line with Vinci Energies, Eurovia, which specializes in transport and urban development infrastructure. Concessions include Vinci Autoroutes, a motorway operator and Vinci Concessions, which specializes in the development and maintenance of transport infrastructures and public facilities, such as rail infrastructure, airports and car parks.

Vinci is one of the oldest holdings in our DT Top 15. We purchased the stock back in May 2013 at around EUR 36.60. Vinci currently trades at EUR 92, translating to a gain since inception of approximately 151%. We still like the story, as Vinci exhibits an attractive mix of concessions (about two-thirds of its annual EBIT) and contracting activities (about one-third). Its geographical business, along with its recurring income base from concessions, (about two-thirds of its annual EBIT) and contracting activities (about one-third). Its geographical business, along with its recurring income base from concessions, provides resilience to its revenues and cash flow. Vinci is also the largest toll-road operator in France.

Sony – Sony Corporation (Sony) is a technology and consumer goods conglomerate. Its key segments are: Imaging Products and Solutions (IP&S), Game and Network Services (G&NS), Mobile Communications (MC), Home Entertainment and Sound Sales (HE&S), Devices (including semiconductors), and Music, Pictures, and Financial Services (FS, including life insurance, damage insurance, banking and credit finance). Although Sony was one of the worst performers in our DT Top 15 in Q1 2019, it was the best performer in Q2 2019, growing by 22%. One of the reasons for the strong performance in Q2 was the announcement, on May 17, of a stock buy-back program whereby it will purchase as much as 4.8% of its outstanding shares, spending up to 200 billion yen (USD 1.8 billion). The move underscores a commitment to support its stock price, as Sony became the latest Japanese company to announce a buyback of at least USD 1 billion. The stock rallied as much as 8.8% on the day of the announcement. A second reason for the great performance in Q2 was an announcement made by Microsoft and Sony on May 16 that they have struck a partnership focused on improving the 'customer experience' in artificial intelligence and direct-to-consumer entertainment. The companies have long been adversaries as they produce the world's top two videogame consoles: Microsoft's Xbox and Sony's Playstation. "The two companies will explore joint development of future cloud solutions in Microsoft Azure to support their respective game and content-streaming services," the companies said in a press release. Sony and Microsoft will also collaborate on semiconductors and artificial intelligence, they said, using Sony's image sensor and Microsoft's Azure cloud platform to boost the offerings they provide to enterprise customers. In the first few days of July, Sony's stock rose another 4%. We like the recent developments and will remain with the story for the time being.

Sonova – Sonova provides hearing healthcare solutions. The company develops and manufactures hearing systems, such as wireless communication systems for audio applications and cochlear implant systems. Sonova also provides solutions for hearing protection. The company is greatly benefitting from the strong volume trends (aging population, emerging market growth) in the hearing aid market. We believe that those trends will continue and that Sonova, being a major player in this market, will benefit immensely in years to come. We bought Sonova back in April 2017 at around CHF 144.90. After rallying 22% in Q1 2019, the stock continued its run and gained an additional 12.80% in Q2 2019, bringing its year-to-date gain to a stunning 35%. As in Q1, there has not been all that much news on the stock. Nevertheless, we continue to like Sonova even at current levels, and will be on the lookout for further positive news.

Market Outlook

We expect global economic growth to stabilize during the second half of the year. A strong US employment report that was released in early July with non-farm payrolls coming it at 224,000 – well above market consensus – is an indication that the US economy is on solid footing. However, that same report also reduced market conviction that the Federal Reserve will need to cut interest rates by a full half-point when it meets at the end of July. We also believe that a full half-point reduction in US rates is off the table for the moment, but still anticipate that the Fed will cut its benchmark interest rate by 25 basis points at its next meeting, which should bode well for global risky assets.

US/China trade war tensions will remain a key risk to global markets over the next few months. China and the US failed to sign a deal in May, but after a meeting between Chinese President Xi Jinping and his US counterpart Donald Trump at the G20 summit in Osaka, they agreed to a trade war truce and to resume talks. When asked about the talks, Donald Trump said it was a "very, very good meeting, better than expected," while China's state news agency Xinhua said the two leaders had agreed to resume economic and trade negotiations, and that the US had said it would not impose any new tariffs on Chinese Products for the time being. It remains to be seen how long this truce will hold, however, and whether the two superpowers will be able to reach a mutually beneficial deal. Should negotiations drag on for too long without conclusion, global markets could be in for a setback. Conversely, a tangible deal could provide a further boost to global sentiment.

Oil prices are currently buoyed by escalating tensions surrounding Iran's nuclear programme. On the other side of the spectrum, it appears as though demand growth for oil is falling, putting pressure on oil prices. We believe there is no easy solution to the Iran conflict and that, as a result, oil prices should remain well supported despite the decrease in demand. Another reason for optimism is the fact that Saudi Arabia and Russia have agreed to extend their deal with OPEC to curb oil output by another six to nine months, as oil prices have come under renewed pressure from rising US supplies and a slowing global economy.

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"The trick is not to learn to trust your gut feelings, but rather to discipline yourself to ignore them. Stand by your stocks as long as the fundamental story of the company hasn't changed."

— Peter Lynch —

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