CORE CAPITAL

MARKET OPPORTUNITIES

June 2018

- European economic slowdown
- The political challenges are increasing

Core Capital Management S.A.

46 Place Guillaume II, L-1648 Luxembourg
info@corecapital.eu Tel:+352 2621 1969

www.corecapital.eu

It is not just the political risk that has increased during May. We have also seen weaker economic data, mainly in Europe.

What is actually happening? Industrial barometers in Europe have fallen every month this year, i.e. 5 consecutive months. We are now back at the levels from the beginning of 2017. It is a bit worrying that there has been no recoil, with a broad decline seen in several countries. The situation is not all dark. A mixed message was that German industry is record optimistic about the present, although they are worried about the future. We saw this on the IFO barometer. Barometers are surveys, but we also see a dampening in actual economic figures. For example the Economic Surprise Index has shown clear weaknesses in Europe, but also in Japan.

What is the explanation for the slowdown? We see three explanations:

1) The first is the previously high levels observed in 2017, which makes the comparison numbers tough to compete with. Then came trade concerns with the tariffs and Trump now again talking car taxes.

2) The second reason is currency. Europe's exporters have had a headwind from a fairly strong euro throughout the last year and early 2018. Japan has also faced recent headwinds from the currency.

3) The third reason is the high oil price. It affects those who are importers of oil and so are both Europe and Japan. According to the experts, we would not reach an oil price of 80 US dollars per barrel. It is clear that such a surprise has an impact.

In addition to the political unrest in Italy, we see other risks that may affect Europe. Should we point at one in particular, then the current situation is Turkey is worrisome. The country is vulnerable when US interest rates are rising. Companies in Turkey have big dollar loans which are now becoming more expensive, especially when their own currency has tumbled 25% so far this year against the dollar. The country has many underlying problems. To name another one, inflation is high and above 10%. And now they go to elections on June 24th. Turkey is close to Europe, with 80 million inhabitants and 4 million refugees. It is clear that a worsening crisis in Turkey could affect Europe.

What becomes the conclusion of all this? Well Europe is growing, but we see a clear dampening in different barometers while the political challenges are increasing. Stocks in Europe have been weak in May, and we continue to monitor oil prices and tariffs in the near future.

During late April, we have also reduced our exposure to European equities and instead increased our exposure to US equities. We have done that by selling the STOXX 600 ETF and added Morgan Stanley US Growth Fund.

Markets – May 2018

Equity indices	May-18	2018
MSCI ACWI	-0.18%	-0.83%
MSCI World	1.27%	0.95%
S&P 500	2.16%	1.18%
Euro Stoxx 50	-3.67%	-2.78%
DAX	-0.06%	-2.42%
FTSE 100	2.25%	-0.12%
NIKKEI 225	-1.18%	-2.47%
OMX 30	-1.32%	-1.71%
OMXC 20	0.71%	-4.50%

Bond indices	May-18	2018
Global Treasuries	-0.96%	-0.14%
Global High Yield	-1.51%	-2.08%

Currencies	Price	May-18
EUR/USD	1.17	-3.19%
EUR/SEK	10.31	-2.48%
USD/SEK	8.81	0.74%
USD/DKK	6.37	3.20%

Interests	May-18
US T-Bill 3M	1.87%
Euribor FIX 3M	-0.32%
Libor FIX 3M	0.60%
Stibor FIX 3M	-0.40%
Cibor FIX 3M	-0.30%

Other	May-18	2018
Gold	-1.28%	-0.33%
Oil crude. Brent	3.22%	16.03%
HFRX Index	+0.23%	-0.73%

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Portfolio update
Portfolio composition was not changed during May.

Market outlook
- Fixed income

Inflation continues to track higher in the US, helped by a rising oil price, and is likely to mean further interest rate hikes from the US Federal Reserve. With weaker economic data lately, European central banks appear to be adjusting to an easier monetary policy path. We are overweight convertible bonds and senior secured loans with a short duration, while being underweight more traditional fixed income including government bonds.

- Equities

We still expect equities to outperform other asset classes. The fundamental picture remains solid, and the outlook for corporate returns continues to be bright. Concerns over inflation, political turmoil, trade, and greater regulation of the tech sector could potentially hit sentiment. Overall volatility is expected to be more frequent during 2018. It can pay to buy when others are fearful and this strategy may work in the long run. We aim to increase our modestly overweight position in stocks when market panics.

- Currencies

After a 20% fall versus the euro between the start of 2017 and February 2018, the US dollar has been making a comeback. The recent drop in EURUSD, or more precisely broad USD strength, resulted from the unwinding of US short positions and uncertainty about European politics and growth. Overall solid global growth, which tends to run against the USD, and the unwinding of the ECB’s ultra-easy monetary policy should support EURUSD later this year. This is the most likely scenario since fundamentals still support a higher EURUSD, even with higher US interest rates.

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Holding of the Month
G Fund European Convertible Bonds

Convertible bonds is an attractive asset class because of its convexity. The G Fund has, historically, been more sensitive to equity upturns than downturns. This gives us an attractive long-term risk/return profile relative to equities.

The way a convertible bond work in the market can be explained as follows:
- In a bullish market, convertible bonds are exercised and exit the investment universe.
- In a bearish market, convertible bonds, except defaults, are redeemed at their nominal value.

Return year-to-date is +0.6%, net of fees.