Q1 2016 MARKET REVIEW

& MARKET DRIVERS REPORT

LEXINTA GROUP

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MARKET DRIVERS

LETTER FROM THE PRESIDENT, CEO & FOUNDER

Firstly, as is now customary and rightly so, I would like to take this opportunity to thank our clients for their continued trust in Lexinta, to safeguard their investment needs for today and future generations. Also the Lexinta team needs a special mention for their unwavering commitment and diligence towards meeting our client's investment expectations.

We are currently living in an investment world of higher volatility and lower returns, which means we need to maintain our policy of being proactive in regards to risk management to maximize opportunities of diversification when they present themselves. Effectively our client's investment goals can be achieved by adopting a strategy of investing in a broader range of asset classes to smooth the effects of asset class volatility.

Sincerely

Bismark Badilla
President, CEO & Founder of the Lexinta Group

FORWARD



We are delighted to present to you the Lexinta Q1 2016 Market Review & Market Drivers Report. This has been a collaborative effort between Lexinta Research and Lexinta Trading, involving staff from various world locations.

This document has been developed to provide the reader with spotlights of information and therefore should not be considered as a comprehensive report. However, that said, the document has been written to provide the main themes from which the reader can extract key information.

Obviously markets change and as such the information contained herein can never cover every aspect of what awaits in the future but we hope you find the information of interest in relation to both strategic and tactical asset allocation.

Sincerely



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Q1 2016 MARKET REVIEW

We have seen a very turbulent start of the year 2016. The S&P 500 Index lost 11.44 % until it reached its low of 1810.10 (11-Feb-16). The Chinese Index CSI300 reached a bottom of 2821.21 (29-Feb-16) down 24.38 % since its close of 3731.005 (31-Dec-15). Crude oil declined to a low of 26.21 USD. Starting mid-February the global stock markets began to recover significantly, led by a strong bounce in crude, which carried the S&P to end flat for the quarter. The MSCI World Energy Sector Index (MXWO0EN) at 185.88 is up 25 % (31-Mar-16) from its January lows of 148.67 and year to date +4.23 %.

Although we believe the fears over China's hard landing are overdone, we definitely see a bumpy landing as the country shifts from an investment driven economy to a consumption driven economy. The volatility in the Chinese equity market has put downward pressure on the global stock market and across commodities as a whole.

The global financial volatility contributed to the tightening on monetary conditions in the US, which in conjunction with disappointing Q4 growth and depressed oil prices led to a risk-off environment, as evidenced by the downtrend in the famous FANG technology stocks (Facebook, Amazon, Netflix and Google).

Fears of a prolonged supply glut in the oil market did not produce a corresponding positive signal for consumption as expected, as the short-term impact of the depressed prices on investment and employment in the sector outshone any positive effect on consumption. Concerns surrounding the oil market fed into the financial sector, whose business model was further threatened by the Fed's promises of a more moderate rate increase for 2016. In addition, the worries about the health of the European banking system reinforced the downtrend of the financial sector.

AMONG THE MOST SIGNIFICANT EVENTS OF 1Q 2016:

– The Bank of Japan surprised the markets by implementing negative interest rates at the end of January.

– Agreement between Saudi Arabia, Russia, Qatar and Venezuela to freeze the outputs at current levels pushed the oil price higher.

– European Central Bank is expanding the monetary easing to EUR 80 billion per month. They have cut the main refinancing rate by 5 basis points to 0.00% and the interest rate on deposit facility has been decreased by 10 basis points to -0.40 %.

– Federal Reserve left the rates unchanged upon foreseen weak global growth.

– Evidence of China's slowdown vis-à-vis the lower than expected industrial output that caught investors by surprise; confidence in the government was eroded following a currency devaluation.

– Oil reached a multiyear low on fears of China's slowdown and persistent oil supply glut.

– China has been deploying capital overseas on record multibillion-dollar acquisitions.

MARKET DRIVERS

EQUITY – INVESTOR SENTIMENT REBOUNDS

The market is telling us things aren't as bad as people thought they were. Furthermore, the messages coming out of the major central banks have been stock supportive.

BRITAIN VS. THE EU

A significant driver of uncertainty in the coming quarters will be borne by the coming referendum on Britain's inclusion in the EU. We believe this will have a dampening effect both on the real economy and financial markets in Britain and across the EU as investment is postponed and investor's retreat in the face of the increased risk profile of the country. PwC has estimated that in the worst case scenario a disorderly exit would cost the economy upwards of £100bn, or 5 % of GDP, and 950k jobs by 2020. Ultimately we do not believe the Out-campaign will be successful, however as the summer brings an increasing flow of immigrants into the Eurozone, this position might be reversed should populist sentiment become more prevalent.

EMERGING MARKETS VS. CHINA AND THE FED

Emerging markets currently command attractive valuations, however they are at the mercy of two primary factors; the slowdown in Chinese industrial production and an increasingly hawkish Fed talking up an imminent rate rise. We expect the former to continue to be a drag on EMs as it moves towards a terminal growth rate of 5 % and struggles to balance debt worth 230 % of GDP, copious overcapacity in asset heavy industries and the reforms required to successfully transition from an investment driven economy to a consumption driven one. EMs with both current account and budget deficits are especially vulnerable. As for the US, the current strength in their labor market leads us to pay close attention to the FOMC's minutes for surprise hawkishness, however this risk factor is mitigated by the Fed's clear consideration of global market volatility and financial weakness in its decision making process.

US HIGH YIELD (USHY) MARKET

With improving oil prices, the US high yield (USHY) market should get a breather. We continue in our expectation that USHY will perform well during this year, namely because of the reduced probability of more than two Fed Fund rate increases.

DRAGHI VS. INFLATION

ECB's Draghi seems to play one of his last cards to avoid deflation and boost the economy. The central bank has notably pivoted in its core goal from weakening the currency and boosting exports to promoting banks to issue more loans, thereby stimulating investments and GDP growth. The big question is if these measures will suffice in overcoming a lack of a capital market union, political fragmentation and large quantities of non-performing loans on banks' balance sheets.

Easing measures by Draghi have turned the very low yields in Europe's "risk-free" market into what is actually a "return-free" market. According to Markit research a tiny rise in German 10-Y papers will erase the next 12-months return.

FOREIGN EXCHANGE (FX) – USD OUTLOOK

In it´s most recent statement the Federal Reserve lowered its projections for the number of rate hikes due to the downside risks of growth from global financial markets, we should expect 2 more hikes to bring rates least 50 basis point higher by the end of the year. The highflying dollar rally has taken a pause even as the ECB announced rate cuts that were less aggressive than expected. Unless we see a more aggressive rate hike from the FED this year the dollar rally could stall and correct lower versus major currencies.

CRUDE VS. S&P 500 INDEX (SPX)

For the past 15 years the correlation of the Bloomberg Commodity Index versus the S&P 500 Index has been -0.08. So far this year that correlation has been 0.88, surprised many participants in the financial markets. The commodity became a bellwether for aggregate demand and expected GDP growth, however we believe that relationship will be broken in the coming months as the oil market rebalances itself and investors begin to look to the traditional signals to forecast economic growth.

METALS VS. CHINA

China's iron ore imports are likely to peak this year and demand boost from India will not match China's scale and may be 10 to 15 years down the road. This suggests that seaborne iron ore volume may be in permanent decline as of 2017. Paired with the continuous reduction in production costs for major iron ore producers and their access to low-cost iron ore deposits, we imagine that the floor for iron ore prices has not been hit yet.

Recent higher copper prices face an uncertain future over China's consumption of the metal. The country is responsible for more than 40% of global demand and is likely to increase it by 0.6 % this year, down from 3.8% in 2015, according to research group CRU in London. Copper is considered a key barometer for China's economy, due to its use in wiring, cables and construction.

Despite the government's numerous stimulus programs to reduce China's housing supply there are still 13 million vacant homes, according to Reuters. But the efforts, albeit crucial, are anything but straightforward. Prices bounced back in major top-tier cities, but dropped in all the remaining cities. In recent years, these accounted for 90 % of new construction.

One offsetting factor that could offer support to metals is China's infrastructure program, announced one year ago in the colossal amount exceeding US$ 1 trillion.

IMPORTANT INFORMATION

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