Check-Up

Reichmuth & Co Private Bankers Client Newsletter
Integral Investment Management | January 2018

Editorial

In 2017, perhaps the biggest surprise was that – despite numerous political uncertainties – there were no surprises. And so we are able to look back on 2017 as a good year in terms of business and investment.

Will 2018 be along the same lines? In this environment, having a comprehensive overview of assets is particularly critical as it allows risks to be identified and opportunities seized. This integral overview (see page 7) was instilled in us by Karl Reichmuth with the ultimate goal in client identification since the bank was first founded. Preserving the culture is something to which new unlimited liable partner Remy Reichmuth feels obliged, when he takes up the reins in 2018 (see page 8).

To you, dear clients, we wish to express our sincerest thanks. The trust you place in us is what motivates us to continue to be active for you as a partner in the future too.

Jürg Staub,
Unlimited liable partner

MULTIPOLAR WORLD

Somewhat less stable, but good economic prospects

One year after the election of new US President Donald Trump, it is becoming increasingly evident that Pax Americana – the stable post-war order with western dominance under US leadership – is coming to an end. The world now appears multipolar, and somewhat less stable as a result.

For this reason, a number of regions and powers are wrestling for their system's pre-eminence. Alongside Russia, the Islam-dominated Middle East countries and emerging world power China, this is becoming clear in Europe as well.

New balance of power in Europe
With the Brexit vote, a strong country in the north of Europe took the decision to leave the EU. The long phase of defiance in the withdrawal negotiations is giving way to a pragmatic approach. This was probably only possible following the results of the extraordinary election year for Europe. The UK will remain in Europe in the future, and they will continue to trade with each other. For the stability-oriented countries in northern Europe, the UK's withdrawal from the EU represents a greater loss, however, since their share of the EU population will fall from 35% to 25%.

Visegrad Group insists on sovereignty
The former eastern states of central Europe, known as the Visegrad Four (Poland, the Czech Republic, Slovakia and Hungary) are becoming increasingly stronger. Similar to the way of thinking in the UK, they too do not want to relinquish any of their sovereignty to Brussels. They only reclaimed their sovereignty back in the 1990s. In terms of European migration policy, too, they are rallying against the EU's solutions. It is interesting that the winner of the Austrian elections, Sebastian Kurz, is also expecting to find new allies here. But the Visegrad Group is likely to increase its resistance to stronger EU centralism.

Southern Europe is groaning under the euro
To become more competitive, the countries in the south of the eurozone are missing an outlet: they are unable to

Continued on the next page

depreciate. For this reason, their economies must adapt while feeling the huge pinch from their membership of the European single currency. This austerity policy has already been likened to a kind of chemotherapy. The European Central Bank (ECB) has attempted to relieve this pain with plenty of cheap money, through the bond purchasing programme. The hope of the ECB is that higher inflation in Germany will strengthen the competitiveness of the countries in the south. Only withdrawals from the Euro or a transfer union, i.e. payments from the north to the south, ultimately remain as alternatives.

Franco-German leadership role?

With Emanuel Macron's election victory in France, the EU appeared to have found new momentum. He set out the vision of an EU with greater centralisation and a shared budget. But the elections in Germany put a dampener on this idea. Angela Merkel's CDU/CSU was weakened and the coalition negotiations have not yet yielded any results. Because the FDP withdrew from the "Jamaica coalition", there is no brake on redistribution. Should there be a repeat of this large coalition, it is likely that things will head in the direction of a transfer union.

The ECB and Eurogroup

Portuguese Finance Minister Mário Centeno has just been appointed the new head of Eurogroup. This means that both the ECB and Eurogroup are headed up by southern Europeans. We predict that this combination will be temporary since Mario Draghi, President of the ECB, is being replaced in 2019. This indicates to us that we could have a German ECB President for the very first time, bringing the presidency right back to the heart of the EU. Monetary policy would then be increasingly decoupled from EU policy again. Political questions around the Euro would be a matter for the Eurogroup, which is democratically legitimised. The ECB is once again focusing more on its actual duty, which is performed by technocrats with no democratic legitimacy. We therefore expect a recovery on the part of European monetary policy. Policy issues, are expected to be "muddling through" in light of the new balance of power. This is no bad thing for the economy. The high pace of new orders is likely to ease off and the economy will be able to grow more freely.

Flexible exchange rates as an outlet

Taking Russia and Saudi Arabia as examples, the various effects of fixed or flexible exchange rates are clear to see. When the oil price lost half of its value three years ago, the incomes of oil-exporting countries in USD plunged. At the same time in Russia, the ruble fell by 50%, while the cost/income ratio for Russian oil companies remained relatively stable. The situation was entirely different in Saudi Arabia whose currency is pegged to the US dollar. Incomes dwindled, and the public deficit surged, which affected political stability. Of course, Saudi Arabia could have let the currency float freely. This would have made imports more expensive, which would have impacted Saudi Arabia more than Russia. An oil price shock triggered by political unrest in the Middle East would be a plausible scenario. If the oil price reached a certain level, the US fracking industry would probably be in a position to cushion this somewhat.

Successful financial repression

Very low, or even negative central bank interest rates in times of positive inflation are considered financially repressive. It is seen as successful and people get used to it. Two-year government bonds of countries in northern Europe are yielding minus 0.8%, while nominal growth is at around 4.5%. This is leading to debt reduction compared with gross domestic product (GDP). For example, Germany's government debt is still at around EUR 2 billion, but has fallen from 80% (2010) to 66% of GDP. Since central banks worldwide are effectively playing a game of pick-up-sticks, i.e. carefully taking their first normalisation measures in the hope of not moving any other indicators, monetary policy will remain expansive in 2018.

Dynamic economic growth

The economy is enjoying good growth worldwide and is even likely to gain momentum in 2018. For the new year, we expect a good environment for the economy, and there are barely any clouds visible on the financial markets either. Only the valuations are high, which is down to the abundant money supply and the very low interest rates. A normalisation of interest rates would weigh on valuations. In the long term, interest rates should approximate nominal growth, which they have not done for some time already. Interest rate growth must be monitored closely, however. In particular in the US, there is first and foremost likely to be a clear sign when this growth cycle comes to an end – even before the market cycle. On European and Asian stock markets, we are seeing more potential partly because both the margins and valuations are still showing potential here, and because interest rate normalisation is still some way off. For this reason, shares remain the heavyweight of our investment strategy. We expect the following asset allocation shifts over the coming years. The high equity weighting will be reduced in favour of cash; then bonds are likely to become attractive again and one will certainly expect a surprise or two, which, with a little nerve, can be exploited. The specific implementation always comes down to the individual environment, which is why we look forward to a face-to-face meeting with you.

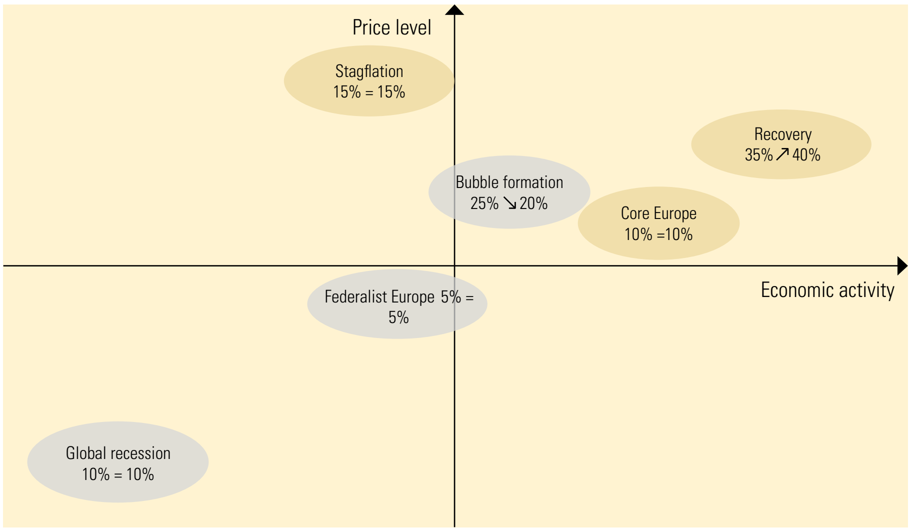
Christof Reichmuth, unlimited liable partner

«Alea iacta est»

See our 2018 Market Outlook in a recording at the KKL Luzern on **www.reichmuthco.ch.**

GLOBAL EXPANSION IS MARCHING ON

Our take on the future



Yellow = the scenarios described below

Summary

- Global growth recovery continues to gain momentum. PMIs at a very high level
- Central banks are planning a cautious withdrawal from expansive monetary policy – like a game of pick-up-sticks played from a dizzying height
- Political uncertainties are no longer an issue – delays in the forming of a coalition in Germany is temporarily inhibiting core European countries

Recovery: global growth momentum is accelerating

The global economy is gaining momentum. Businesses are increasingly launching new investment projects. In the US, this trend is fuelled by the tax reforms. This, coupled with positive consumer sentiment, is having a positive effect on consumer spending, which is key for the US economy. Central banks are only slowly cutting back their purchasing programme and are cautiously tackling the cycle of interest rate rises. Wages are increasing, but only slowly thanks to efficiency gains through automation and digitalisation, while inflation remains under control. In China, Xi Jinping's power has been strengthened and reforms are being pursued. Progress is being made with its transformation from an export to a consumption model. In Europa too, economic recovery is quickening its pace.

40% Probability 3–6 months

Investment ideas

- Overweight shares (more cyclicals)
- Avoid fixed-income investments
- Foreign currencies are attractive

Stagflation: central banks are spending too long on the sidelines

The Fed is anxious to nip the emerging economic growth in the bud and waiting too long to increase interest rates. Tax relief and an expansive fiscal policy are leading to wage pressure in spite of a contracted labour market. This is having a negative effect on the margins of businesses and growth is declining. Infrastructure projects that are underway and the tax reforms are also negatively affecting the US budget. The USD is weakening and the US is importing inflation. Inflation rates are increasing beyond the target range of 2%. The weaker USD is having a positive effect on individual emerging markets. Southern Europe is continuing to struggle with competition problems and the stronger EUR against the USD is putting new pressure on countries with poor cost structures.

15% Probability 3–6 months

Investment ideas

- Underweight developed market equities
- Underweight nominal values
- Overweight hedge funds
- USD underweight
- Gold overweight

Core Europe: strong core with flattened margins

In the wake of pragmatic negotiations between the EU and the UK, Europe is proceeding with reforms that are long overdue. Following the successful forming of a coalition in Germany in the spring of 2018, there will be an open debate in Europe on establishing a core eurozone including a fiscal union. Germany, France and the Netherlands will be at the centre of this debate. The new EU would have a strong core with flattened margins. The centrifugal forces could therefore be reduced and the EU would become somewhat more flexible. Ideally, the structurally weak countries in the eurozone would leave of their own accord. The most important pillar of the new core Europe, besides the fiscal union, are the jointly regulated migration policy and the common financing and implementation of a military strategy (new NATO).

10% Probability 3–6 months

Investment ideas

- Equities in northern Europe underweight
- EUR overweight/ CHF underweight
- Avoid nominal investments in EUR

THE GLOBAL ECONOMY IS PICKING UP SPEED

Trend reversal for inflation?

Patrick Erne,
Head of Research

Global economic forecasts are good and corporate earnings are on the rise. In spite of the positive leading indicators, however, interest rates are scarcely moving and the central banks are continuing to signal a cautious approach. It is possible that the disinflationary trend due to technological change and global labour markets has been overestimated, however, and a trend reversal for inflation is just around the corner. Improved growth prospects and ongoing expansive central banks are a fertile breeding ground in this respect.

Economic recovery still intact

The global economic outlook for the next few months is positive. Economic growth – particularly in Europe – accelerated in 2017. Leading indicators such as the purchasing managers' index are near past highs and point to further expansion. In Germany in particular, investment and consumer spending are likely to increase further and fuel the current construction boom. In the US, a tax deal with positive implications for investment spending by businesses and consumers is looming. In China, following on from the party's National Congress, important reforms are being initiated in order to choke high credit growth and improve credit quality. Growth momentum is therefore falling somewhat. China will grow in the next year too, however, at around 6%. Other markets such as Japan or most emerging markets should also grow in the wake of the three major economic blocs (Europe, China and the US). Without an exogenous shock, global economic growth is likely to be somewhat higher in 2018 than in the past year.

GDP growth expectations	GDP current growth	Growth expectation 12 months
USA	2.3%	2.5–3.0%
Europe	2.6%	2.5–3.0%
Switzerland	1.2%	1.5–2.0%
Japan	2.1%	1.5–2.0%
China	6.8%	6.0–6.5%

Good economic forecasts barely reflected in the yield curves

In spite of the rosy economic outlook, the US Federal Reserve has signalled only three interest rate hikes for 2018. The market is not even expecting two further increases for 2018. The US Federal Reserve is starting with a cosmetic reduction of its balance sheet and a possible tax deal is likely to increase the deficits further in the future. In spite of this, the US yield curve has flattened out over the past 12 months. The long maturities have moved sideways. A further flattening out towards an inverted yield curve would be a warning signal that the economic cycle could turn. Are the interest rate markets therefore in contradiction to the positive economic outlook?

In light of the globally high debt levels of and debt sustainability, the question arises as to the extent to which interest rates may rise overall, in particular in the event of below-average growth rates. With the improved economic outlook as well as signs of a property asset bubble, there is growing pressure to raise interest rates somewhat in order to keep the loss of purchasing power for savers due to negative real interest rates under control. Even if this balancing act is likely to become more difficult in the medium term, we see room for improvement for US interest rates in light of the good economic climate. In our base scenario, we assume that the long US interest rates will initially rise and only reach a possible turning point at a later stage. The economy, inflation outlook, declin-

Interest rate expectations	3-m rate (Libor)	Expectation in 3 – 6 m	10-year swap	Expectation in 3 – 6 m
USA	1.5%	higher	2.4%	rising
Europe (D)	-0.4%	stable	0.8%	rising slightly
Switzerland	-0.8%	stable	0.2%	rising slightly
Japan	-0.02%	stable	0.2%	unchanged

ing central bank purchases and increasing fiscal spending are in our view indicative of higher interest rates at the long end of the yield curve. Deciding factors are likely to be how fast the other large central banks couple themselves to the US Federal Reserve and reduce the interest-rate advantage of US bonds.The ECB is continuing to be very conservative and signalling only a decline in bond purchases. Interest rate hikes over the next three to six months are therefore extremely unlikely. This is also the case for the Bank of Japan, which – in addition to its QE programme – is keeping interest rates nailed down at the long end ("yield anchoring"). Even if there is speculation that interest rates at the long end could be set slightly higher, monetary policy in Japan continues to be extremely expansive. Switzerland's central bank is having the pressure taken off somewhat due to the weaker CHF. Based on the improved economic climate in Europe, there is no appreciation pressure for now, but interest rate increases are unlikely at present. In real terms, bonds in Switzerland and Europe continue to yield negatively and remain unattractive. The situation is somewhat different in China, where the key interest rate is of secondary importance. What is key is regulating bank lending, which China wants to handle in a more restrictive and targeted way in the future. The credit shortage has meant that interest rates have risen in China lately. Of the large economic blocs, China has the highest real interest rates (around 4% nominal interest rates, with around 2% inflation).

High earnings growth for businesses

Corporate earnings (EPS basis) rose in practically all regions in 2017. A combination of a more attractive global economy, barely any inflation pressure and low financing costs have resulted in an increase in earnings. The good earnings growth is likely to continue into 2018. The decisive question for equity investors is how much of this has already been priced in on the equity markets. The valuations are challenging and offer little in the way of leeway for disappointments. In addition to the valuations, there are a number of different sector trends in particular that are creating crowding in individual sectors and shares. This trend is being further reinforced by the booming ETF sector and is making the market susceptible to sector rotations. Since central banks are continuing to signal a very cautious path in terms of interest rate normalisation and keeping interest rates below inflation, the outlook for equity markets for the next three to six months remains positive overall. The risks for temporary price setbacks have risen, however, and are barely reflected in the current low volatility levels. From a valuation perspective, the markets in Europe, Japan, and emerging markets are more attractive than in the US. On a sector basis, energy and bank shares continue to have catch-up potential.

International equity valuations and expectations

Market	Index level (15.12.17)	Price/ earnings	Price/ sales	Price/ book value	Div./ yield	Expectation 3–6 months
S&P 500	2 676	19.0	2.2	3.3	1.9	sideways
DAX	13 104	13.7	1.0	1.9	2.5	rising
SMI	9 395	18.1	2.2	2.6	3.3	rising
TOPIX	1 793	15.9	0.9	1.4	1.8	rising
China H-Shares	11 366	8.5	1.0	1.0	3.7	rising

What will 2018 bring?

We see an opportunity in equities and alternative investments. Our strongest convictions for 2018 are:

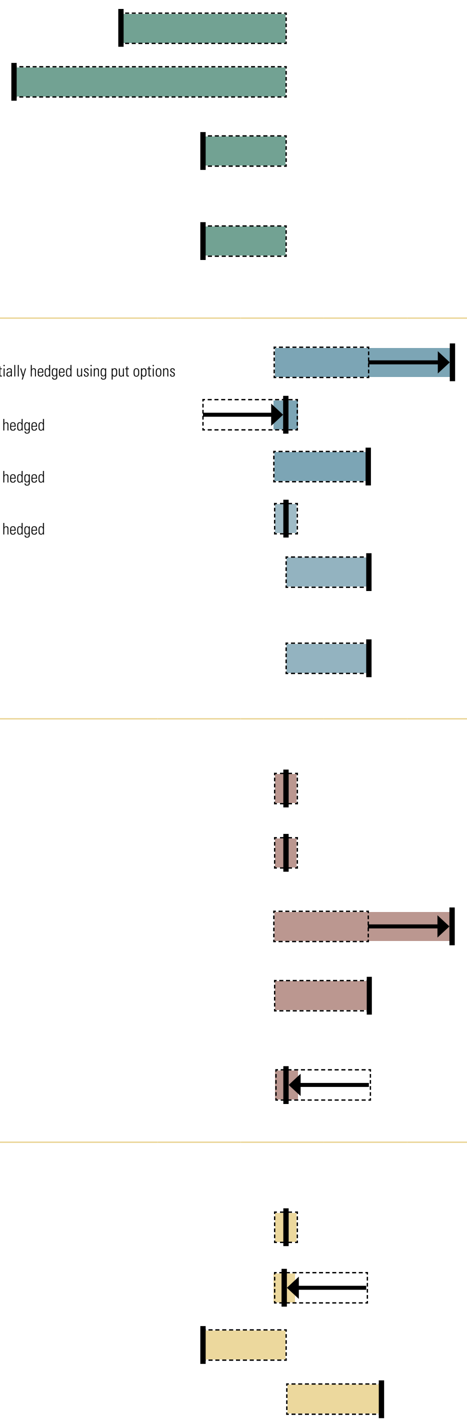
- **Asian small & mid caps:** Asia is a structural growth market with a fast-growing middle class and relatively attractive valuations.
- **Energy shares:** Oil prices have recovered and show a continued upward trend. Energy equities, on the other hand, have barely reacted and in a positive economic environment have upward potential.
- **Insurance-linked securities:** We expect to see higher premiums on the reinsurance market for 2018. This makes it an attractive time to invest in this uncorrelated asset class.
- **Japan:** Shareholder value reasoning is slowly but surely also being adopted in Japan. Thanks to high net liquidity, we continue to see a lot of potential in Japanese shares.
- **Alternative investments:** Volatility strategies, but also strategies that rely on higher divergence in the market, namely investment topics that are difficult to implement, but offer good portfolio protection should the mood on the financial markets turn.

OVERVIEW – ASSET CLASSES

Increase in the tactical share weighting with partial hedging

Asset class | **Positioning** | **Change since last investment decision**

Min. — – 0 + ++ Max.



Bonds

Government bonds

Corporate bonds

Emerging markets

Since interest rates in the main investment markets have barely any downward potential, we are keeping weightings as low as possible and maturities short. We are selectively adding government bonds from emerging markets in the local currency. We prefer alternative investment options with a fixed-interest character to traditional bond markets.

Equities

Partially hedged using put options

USA 1/3 hedged

Europe 1/3 hedged

Switzerland 1/3 hedged

Japan

Asia/emerging markets

We prefer the Europe, Asia, and Japan regions due to their more favourable valuations and good growth prospects.

Well-positioned, medium-sized companies in Europe and Switzerland should benefit from the upturn.

Within emerging markets, we are focusing on countries with a fast-growing middle class.

Alternative investments

Hedge funds

Insurance-linked securities

Raw materials incl. gold/silver

Real estate

Event-driven and Asian long/short equity strategies remain attractive. As part of portfolio hedging, we favour Global Macro issues.

Following on from an intense hurricane season, we expect significant repricing with respect to (re) insurance; an ideal time to replenish.

Real estate valuations in Switzerland seem somewhat overheated. Reduction to neutral.

Currencies

USD

EUR

CHF

Other

Our currency ranking:
1. XAU, EUR, NOK, EM Ccy
2. CHF, USD, GBP, JPY, AUD, CAD, SEK

We have tactically increased our USD exposure at the expense of EUR.

If you would like to receive a copy of our detailed Investment Policy publication with in-depth market assessments, please contact your relationship manager or register at nadine.vonwyl@reichmuthco.ch.

YOUR PERSONAL INTEGRAL OVERVIEW

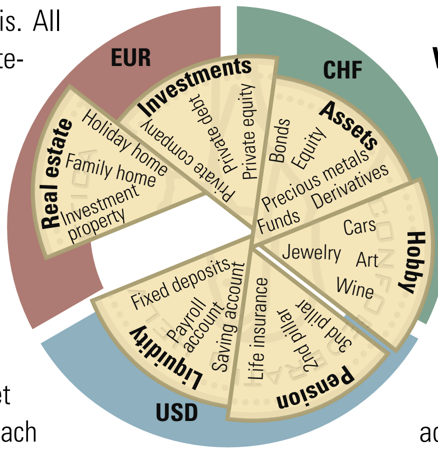
The best basis for holistically coordinated decisions

Comprehensive overview

Assets are often only consolidated once a year as part of the tax declaration. However, this balance sheet is often incomplete since, for example, key components – such as pension fund assets from the second and third pillars – are not included or certain investments are disclosed at too low a value (e.g. real estate). For the comprehensive overview, as a basis for strategic decisions, there is also no overview of asset allocation according to category or currency. Risks as well as potential for optimisation are difficult to identify.

Integral view generate transparency

The integral overview provides you with real-time consolidation of all assets. Liquidity, securities, real estate, mortgages, privately held investments, loans, pension fund assets, art, jewellery, cars etc. can be factored into this. All values are grouped together in an asset statement and divided into the usual investment categories and currencies. The statement contains a detailed overview of equities by industry and region, and bonds by maturity and credit quality. In addition to risk monitoring, this overview of assets also allows for a performance measurement with the same calculation basis for all existing relationships with other banks and asset managers – individually consolidated for each mandate which offers a general overview with optimisation potential for structures when it comes to tax (private assets, retirement provision, company etc.). Reimbursement of foreign withholding tax could also be better coordinated in this way, whilst the efforts and costs involved kept to a minimum. Real-time key risk figures on rating, duration, currency, and sector allocation or bulk positions make it possible to act quickly in the face of severe events.



Anytime, anywhere

For this reason, the integral overview can be accessed at any time through our e-connect via your PC, tablet, or smartphone, and is also available in good old paper form. Reichmuth & Co will be happy to help you analyse the consolidated overview as your specialised contact partner.

Find out more about the integral overview:

Thurs	**15 March 2018**	**at 6 p.m.**	**in Lucerne**
Tues	**20 March 2018**	**at 6 p.m.**	**in Zurich**
Tues	**27 March 2018**	**at 6 p.m.**	**in St. Gallen**

We would be delighted if you could attend. For any questions or registrations, our relationship managers will be happy to hear from you.

Interview with Philipp Achermann Founding partner for BZ Bank and Avaloq banking software

Mr Achermann, why is the consolidation of your assets so important to you?

I have always consolidated my assets using Microsoft Excel. The overview of my risks, viewed in terms of all assets, incl. pension funds, privately held participation rights, or even real estate, is important to me in order to make decisions on new investments or to manage risks. Opportunities and the need to act arise time and time again, especially in times of high market fluctuations. When this happens, it must be possible to make decisions quickly, without losing sight of the big picture and for the long term. The basis for this is the general overview, which should be accessible and up to date at all times.

Why did you replace the old, tried-and-tested Excel list with Reichmuth's integral overview?

The error rate is much lower and easier to use and to maintain. Data from three banks is consolidated in one. I have all relevant key risk figures available at the touch of a button, and the overview can now be called up from anywhere with consistent performance measurements. My administrative work has therefore decreased enormously.

How do you use the integral overview from Reichmuth & Co?

I access it through online banking. Before, I had to go through the tedious process of logging into various systems of different banks in order to get information about my overall assets. Today, I only have to worry about logging in once! I also meet with my relationship manager on a quarterly basis in order to discuss tactical changes and to bring overall allocation of asset classes and currencies in line with my market view and that of Reichmuth & Co.

Tobias Pfrunder,
Head of Advisory, partner

PRESERVING VALUE CULTURE

Remy Reichmuth – new partner with unlimited liability

Remy Reichmuth, you are a new unlimited liable partner (uhG), along with Christof Reichmuth and Jürg Staub. How long have you been with Reichmuth & Co and what was your role until now?
After studying economics in Zurich, I gained professional experience at a private equity firm in Beijing. Back in Switzerland, I was employed by other banks in the realm of asset management. After these years I spent travelling, I pushed forward with the opening of our branch in Zurich for Reichmuth & Co. around 10 years ago. As a relationship manager, I was able to build up my own client base and later assumed a leadership role as Chief of Private Banking Switzerland. I have been a member of the Board of Directors for two and a half years. Since the client is always the focus of our activity, I will primarily act as a relationship manager in my role as unlimited liable partner too.

How do uhG benefit clients?
We believe an owner-managed family business with unlimited liable partners offers maximum security for our clients. Anyone whose accepts liability on their private assets will keep a long-term view and deal with clients, partners and colleagues fairly. I am delighted and honoured to contribute here as an unlimited liable partner.

What does it mean for you, being an uhG?
One selects a bank based on trust. That's why I find value based culture to be so important in our industry. "Individual responsibility" is the most important value, not only in financial matters but in all walks of life. Having "unlimited" liability as a family business and private banker is underpinned by this willingness to take individual responsibility. I would like to offer our clients the best possible solution for them. Every client should be certain that I will take responsibility for everything we do and that I would even give them the shirt off my own back.

What does this step mean for you privately and for your family?
My job is my calling and has always gone hand in hand with my private life. This is also the case for many of my friends who are partners or relationship managers. The step towards unlimited liability was something my wife and I discussed together, and so she too is ready to take on liability. My three children are too young to understand the responsibility that comes with my role, which is a good thing.

Why did Karl Reichmuth step down from the role of uhG?
"Always leave before you have to leave" is what my father used to say. So he already stepped down from his role of President of the Board of Directors two and a half years ago, although we would have liked to see him in this role longer. From his perspective, it was time and he made way for someone younger to implement their ideas and assume responsibility. He placed his trust in us for some time, let us make mistakes and stayed out of all operating decisions himself. By stepping down, he made this clear to those outside the company too. This has let many of us mature and take a huge step forward. In hindsight, I think the time he chose was ideal.

Does Karl Reichmuth no longer have a role at the bank?
As the founder, a long-standing with unlimited liability partner, President of the Board and still an "honorary" President today, he will always have ties with the bank. All the more so since with him there was scarcely any difference between his job – or rather his calling – and his hobby. So he will still often be at the bank, working there, bringing his own ideas and proposing "non-binding recommendations", as he likes to call them.

What can we expect from you as an uhG in the future?
Today our bank is completely healthy and has an attractive offering for private clients, families, businesses, more senior managers, and institutional clients. I am there to ensure personal relationships based on trust. A high level of individualisation and flexibility is important to me. The banking industry is still in a state of upheaval and I am in no doubt that, with our offering, our structure and our values, we will be able to make the most of any opportunities that may present themselves. I will undertake everything to ensure that we continue down this path in order to earn our clients' trust afresh each day.

Remy Reichmuth (lic. oec. publ. and CFA) is married and father to three children between the ages of 6 and 12. He lives in Lucerne and cites "sport & music" as his hobbies.

Remy Reichmuth,
Partner with unlimited liability