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Newsflash

A new month and the 101th issue of Viewpoint from **Financial Partners**.

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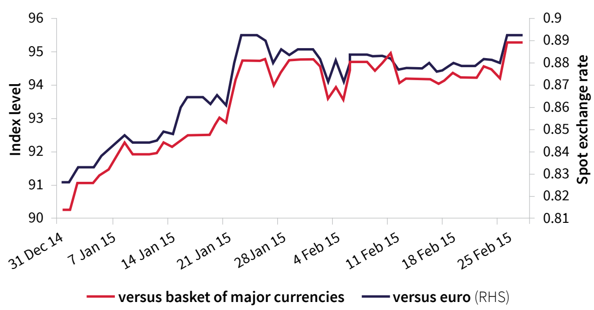
Market Commentary

Markets continued their strong start to the year in February. Equity indices in the US and UK hit all-time highs, while European stocks soared ahead of full-scale quantitative easing in the common currency bloc. On the other hand, US Treasuries fell by 1.8% and UK gilts fell by 4.4% in sterling terms. The ten-year yield on US and UK government bonds rose intra-month to 2.1% and 1.8%, respectively. Emerging markets also lagged, as the US dollar continued to strengthen against a basket of major currencies and in particular the euro.

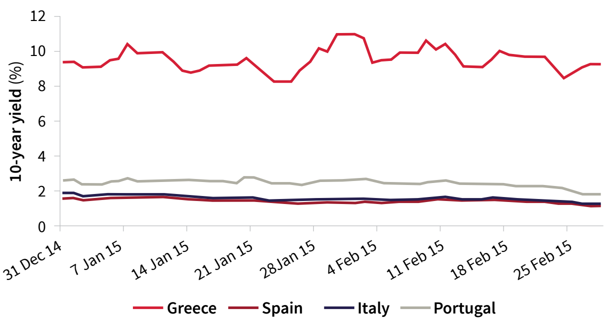
Figure 1: US dollar continues to strengthen



At the start of the month, negotiations between the newly elected Greek government and other European leaders took centre stage. The austerity conditions attached to the current Greek bailout programme have led to a seismic political shift in Greece towards the anti-austerity Syriza party. After a landslide election victory, the leftist party is now under intense pressure to deliver on pre-election promises to ease austerity, but going into the negotiations European leaders and in particular Germany held the upper hand. Greeks continued to withdraw savings from domestic banks (according to Moody's, seven to eight billion euros were withdrawn in January alone) resulting in a reliance on the European Central Bank's (ECB's) emergency lending facilities. Moreover, Greece would have defaulted on its debt repayments within a matter of weeks had the bailout transfers been halted. In the end, a four-month extension of the current programme was eventually agreed. This will give Greece the opportunity to re-negotiate some of the bailout terms while continuing to draw on emergency funding from Europe. The first round of negotiations has certainly illustrated how fraught these further discussions will be.

Greek 10-year bond yields fell from 11.1% to 8.6% after the agreement was reached, only to bounce back up at the end of the month. Equities on the Athens stock exchange also rose following the news but have steadily declined since. It is clear that significant uncertainty still remains around Greece's position in the euro area, but it is worth noting that Spain, Portugal and Italy were left unaffected by the political turmoil. Since the euro-crisis of 2012, European leaders have put in place solid contingency plans to prevent contagion across the region, should a 'Grexit' occur. It appears that markets are becoming increasingly comfortable with these arrangements.

Figure 2: Yield is Greece versus yields in other European 'periphery' countries



Across the Atlantic, economic data prints in the US continued to be mixed as the fourth quarter GDP print for 2014 disappointed (2.2% versus initial estimates of 2.6%) and month-on-month retail sales figures fell by more than expected. It has been gains in payrolls and unemployment numbers that have dominated market sentiment, however, as both prints continue to surprise on the upside. Wage growth has lagged behind somewhat but remains healthy, and expectations of a Federal Reserve (Fed) rate hike are starting to increase. Chair of the Fed, Janet Yellen, continued to use the word "patient" to describe the Fed's approach to a first rate rise in February, and markets will be watching closely to see if it continues to feature in the Fed's FOMC meeting minutes.

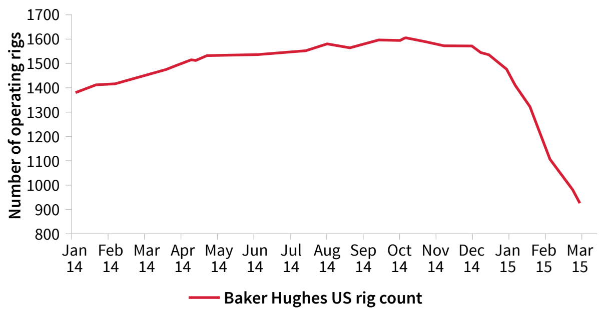
The slowing Chinese economy also remained an important theme over month. China's Purchasing Managers' Index (PMI) fell below 50 for the first time since September 2012, consistent with a contraction in factory activity. The indicator fell 0.3 points, to 49.8 in January and rebounded to a mere 49.9 in February. China's trade surplus has now hit its highest level on record (USD 60 billion versus expectations of USD 48.9 billion) highlighting diminishing domestic demand. Imports surprised significantly on the downside in February, printing -19.7% year-on-year, versus an expectation of -2.3%. In response, the Chinese authorities cut the Reserve Requirement Ratio for all banks by 0.50 percentage points, and the People's Bank of China (PBoC) announced a quarter percentage point cut to its benchmark deposit rate and cut its one-year lending rate by the same amount. The PBoC had already cut rates in November, but weak growth and falling inflation are clearly starting to worry the Chinese leadership.

Brent crude gained a notable 18.1% in February. This was oil's highest monthly gain for six years, and brought the price back up to $53 a barrel. Supply by US shale producers has been scaled back at an incredible pace in 2015: according to Baker Hughes, there are now 922 oil rigs operating in the US, down from circa 1,600 in December last year. Despite this, inventories are filling up quickly as overall supply continues to increase, leaving less opportunity for those looking to

Source: Bloomberg. Returns in US dollars unless otherwise stated. February 2015.

buy and store oil. This has been seen in the US in particular, causing the price between WTI and Brent crude to widen recently, as supply is being soaked up less quickly. On the other hand, demand for oil is increasing steadily as the US economy improves and the depressed oil price boosts demand. The US saw increased gasoline consumption and automobile sales in February.

Figure 3: Number of operating rigs in the US



We expect equity markets to continue to deliver decent returns over the medium to long term. Markets face challenges, however, as Russia's behaviour remains unpredictable and the Islamic State, Ebola and even North Korea's recent sabre-rattling serve as a salutary reminder that many risks remain in global markets. By their nature, many of these risks are inherently unpredictable – which emphasises the need for diversification and prudent risk controls in investors' portfolios. In the coming months we expect to see markets continue to be dominated by central bank and political rhetoric. Much time will be devoted to forecasting the path of US interest rates and predicting the course of action in Europe with respect to Greece, while the European Central Bank looks to speed up growth in the euro area.

Source: Bloomberg. Returns in US dollars unless otherwise stated. February 2015.

Market Performance

Asset Class/Region	Index	To 27 February 2015		
		Currency	Month	Year to date
Developed markets equities				
United States	S&P 500 NR	USD	5.7%	2.5%
United Kingdom	MSCI UK NR	GBP	3.3%	6.1%
Continental Europe	MSCI Europe ex UK NR	EUR	6.9%	15.2%
Japan	Topix TR	JPY	7.7%	8.3%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	3.2%	4.7%
Global	MSCI World NR	USD	5.9%	3.9%
Emerging markets equities				
Emerging Europe	MSCI EM Europe NR	USD	9.6%	5.7%
Emerging Asia	MSCI EM Asia NR	USD	2.4%	4.9%
Emerging Latin America	MSCI EM Latin America NR	USD	4.2%	-2.2%
BRICs	MSCI BRIC NR	USD	4.4%	5.6%
Global emerging markets	MSCI EM (Emerging Markets) NR	USD	3.1%	3.7%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	USD	-1.8%	1.1%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	-1.3%	2.0%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	-1.0%	2.0%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	2.4%	3.1%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	-4.4%	0.8%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	-2.7%	1.9%
Euro Government Bonds	Citigroup EMU GBI TR	EUR	0.7%	3.0%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	0.6%	1.5%
Euro High Yield	Barclays European HY 3% Issuer Constraint Total Return Index Value	EUR	2.1%	3.1%
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	-0.7%	-0.7%
Australian Government	JP Morgan Australia GBI TR	AUD	0.2%	2.3%
Global Government Bonds	JP Morgan Global GBI	USD	-1.3%	-1.0%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	USD	-0.8%	-1.2%
Global Convertible Bonds	UBS Global Focus Convertible Bond	USD	2.5%	1.5%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	0.7%	1.3%

** estimate*

Source: Bloomberg

Market Performance

Asset Class/Region	Index	To 27 February 2015		
		Currency	Month	Year to date
Property				
US Property Securities	MSCI US REIT NR	USD	-3.6%	2.8%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	2.9%	10.8%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	2.3%	4.3%
Global Property Securities	S&P Global Property USD TR	USD	0.3%	4.5%
Currencies				
Euro		USD	-0.8%	-7.5%
UK Pound Sterling		USD	2.5%	-0.9%
Japanese Yen		USD	-2.4%	0.0%
Australian Dollar		USD	0.6%	-4.4%
South African Rand		USD	-0.1%	-0.8%
Commodities & Alternatives				
Commodities	RICI TR	USD	3.8%	-1.8%
Agricultural Commodities	RICI Agriculture TR	USD	2.5%	-4.3%
Oil	Brent Crude	USD	18.1%	9.2%
Gold	Gold Spot	USD	-5.5%	2.4%
Hedge funds	HFRX Global Hedge Fund	USD	1.8%	1.6%
Interest Rates			**Current rate**	**Change at meeting**
United States	12 March 2015	USD	0.25%	-
United Kingdom	12 March 2015	GBP	0.50%	-
Eurozone	12 March 2015	EUR	0.05%	-
Japan	4 April 2013	JPY	0.10%	-
Australia	3 March 2015	AUD	2.25%	-
South Africa	12 March 2015	ZAR	5.75%	-

* *estimate*

Asset Allocation Dashboard

Positive | Neutral | Negative

Asset class	View
Equities	
Developed equities	Neutral
UK equities (relative to developed)	Positive
European equities (relative to developed)	Neutral
US equities (relative to developed)	Negative
Japan equities (relative to developed)	Neutral
Emerging market equities	Positive
Fixed Income	
Government	Negative
Index-linked (relative to government)	Neutral
Investment grade (relative to government)	Neutral
High yield	Neutral
Loans	Positive
Emerging market debt	Positive
Convertible bonds	Neutral
Alternatives	
Commodities	Neutral
Property (UK)	Neutral
Currencies	
GBP	Neutral
Euro	Neutral
Yen	Negative

For more information, please contact your adviser or alternatively contact:

Financial Partners Ltd.
泛柏資產管理有限公司
24/F, Kinwick Centre
32 Hollywood Road
Central, Hong Kong

Tel +852 2827 1199
Fax +852 2827 0270
client.services@f-p.hk
www.f-p.hk
A Member of Wealthnet

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