SALMANN
INVESTMENT MANAGEMENT

Investment Report – 30th September 2015

Autumn storms above the rooftops[1]

With the change of season, a cold front has also hit the exchanges. Contrary to Reinhard Mey's song from 1972, the "autumn storms above the rooftops" in this case isn't about love, rather the frustration of investors at the rekindling volatility and losses on financial markets. The third quarter lived up to its historically notorious reputation once again. Hardly any asset class managed to escape falling prices.

China has replaced Greece as the spoilsport

Investors were initially worried about the (slight) devaluation of the Renminbis and a massive plunge on the Chinese exchanges, however, this then evolved into great uncertainty about the future economic development of the Middle Kingdom. Two points are worth mentioning here; firstly, Chinese equities experienced a fulminant bull market during 2014 and the first half of 2015. During its course, the Shanghai Index rose by 162 percent between March 2014 and June 2015. Since June 2015, however, quotes have dropped by about 41 percent. They are now back to the levels of December 2014, although still leaving prices up about 55% above the lows of March of that year.

Average **growth and inflation forecasts** from "The Economist's" September poll of economists:

	Real GDP Growth		Inflation	
	2015	2016	2015	2016
Germany	1.7%	2.0%	0.4%	1.6%
Euroland	1.4%	1.7%	0.2%	1.2%
United Kingdom	2.5%	2.4%	0.2%	1.5%
Japan	0.8%	1.5%	0.7%	1.0%
Switzerland	0.7%	1.3%	-1.0%	-0.1%
USA	2.4%	2.6%	0.4%	2.0%

Secondly, no pundits following the Chinese economy could seriously have expected growth rates of 7 and more percent to be maintained ad infinitum. In the past, China's expansion has been strongly driven by capital investment. This rate, and with it, growth, has to, and will, slow in future as China mutates into a consumer-driven economy. At a recent speech given in Zurich, Philipp Hildebrand, the former president of the Swiss National Bank and currently Vice-Chairman of the fund manager, Black Rock, went even further, saying that the world would indeed have had something to worry about, had China not heralded in the transformation to a consumer-driven economy, and had growth not begun to slow. Had this not taken place, the high growth rates would have continued to be driven by capital investments that are neither sustainable nor productive in the long term.

Change in **Equity Markets since the beginning of the year:**

		Dec. 2014	Sept. 2015	Change[2]
Asia ex Japan	DJ STOXX A/P	486.7	398.6	**-18.1%**
Germany	DAX	9,805.6	9,660.4	**-1.5%**
Europe	DJ STOXX 600	342.5	347.8	**1.5%**
Japan	TOPIX	1,407.5	1,411.2	**0.3%**
Switzerland	SPI	8,857.0	8,679.8	**-2.0%**
USA	S&P 500	2,058.9	1,920.0	**-6.7%**
World	MSCI World Index	417.1	381.7	**-8.5%**

The second major uncertainty was on account of the US Central Bank (Fed). As ironic as it may sound, its waiver of a first interest rate hike in September has caused quite a stir. Apparently, and according to the interpretation of participants in the market, the American economy is not in good enough shape for interest rates to be tightened. Further, this holding pattern feeds the fear that the Fed is demonstrating too little independence and is following the leads given by World Bank and IMF (International Monetary Fund) too closely. Shortly before the Fed meeting, both institutions warned against higher US rates. In our view, it is the warning given by the latter institution that upset the apple cart for the financial markets. On the whole, the US economy looks to be in good shape. The trends of many indicators are rising, such as for example cyclical consumption, weekly hours worked, housing starts, car sales, consumer confidence, and many more. As previously, unemployment continues to fall as well.

[1] Original title "Herbstgewitter über Dächern" by the German chansonnier Reinhard Mey

[2] Development of index in local currency. Exceptions Asia ex Japan and World in USD

Investors are anticipating the next course with pleasure

More of the same, i.e. cheap money and quantitative easing, is apparently not to the liking of investors anymore. Maybe it's now time to serve the next course. Whether or not this may cause digestive problems nobody knows, and clearly nobody wants to be the first to start the experiment. Anyhow, the USA has two more chances in the current year to ring in the normalisation of interest rates. At the end of October and in mid-December, the Fed's directors are planning to put their heads together once again. It's quite possible that then, the next course will be served rather than another extra serving.

The **equity funds employed by us** achieved since the beginning of the year the following returns[3], with some beating their benchmarks:

Aberdeen Asia Pacific (USD)	-15.9%
JB Japan Stock Fund (CHF hedged)	-0.6%
JB Japan Stock Fund (EUR hedged)	0.6%
Performa Asian Equities (USD)	-15.5%
Black Rock Swiss Small & Midcap Opp. (CHF)	4.8%
Raiffeisen Futura Swiss Stocks (CHF)	-3.5%
iShares ETF MDAX-Index (CHF)	2.3%
Performa European Equities (EUR)	2.9%
iShares ETF Core S&P-500-Index (USD)	-7.2%
Performa US Equities (USD)	-1.8%

Asset Allocation:

At its meetings, the Investment Committee decided on the following changes to the asset allocation for medium-risk balanced Swiss-Franc portfolios, not subject to client's restrictions (mandates in different reference currencies at times display different nominal weightings and weighting changes):

Money Market: Due to the equity sales described below (see Equities Europe and Equities USA), the money market allocation has increased slightly. From a return perspective, this investment segment remains static. Nevertheless, it is a valuable buffer against the high volatility in other asset classes, particularly during unsettled periods.

Bonds: The zero interest rate policy of many central banks, combined with the massive bond purchasing programme of the European Central Bank (ECB), has kept yields on government bonds, and those of prime debtors, in consistently very low or even negative territory. Correspondingly, investing in this sector proves rather challenging. In the lower credit qualities, both volatility and spreads (yield differentials between different quality classes) have increased. Funds we hold in this segment have correspondingly lost ground. We have made no active changes to the position.

Since the beginning of the year, **yields on 10-year government bonds** developed inconsistently:

	Dec. 2014	Sept. 2015	Change
Europe	0.54%	0.59%	9%
United Kingdom	1.76%	1.76%	+/-0%
Japan	0.33%	0.36%	9%
Switzerland	0.32%	-0.12%	-137%
USA	2.17%	2.04%	-6%

Equities Switzerland: Even though the Swiss equity market has experienced less strong autumn storms than other countries, it has nevertheless been under the influence of a cold front. The Swiss Performance Index (SPI) lost 2.7% during the third quarter, and now stands 2% below the year-end 2014 level. Our directly-invested Swiss Stock Portfolio (SSP), however, managed a positive performance (including dividends) of 3.79% to 30th September. This was helped by the fact that this selection consisting of 20 stocks is tilted towards medium to small capitalised companies. On the one hand, these experienced less selling pressure, and on the other, they account for a larger share in our portfolio than in the index.

The annual total return of the SSP since 2010 totals 9.05% p.a., significantly above the performance of the benchmark at 7.83%. Transaction costs and taxes at source

[3] Performance in fund currency. Source: Bloomberg or respective fund company

have already been deducted from the SSP figures. In contrast, these costs are not included in the benchmark index. The funds Raiffeisen Futura Swiss Stocks and Black Rock Swiss Small & Midcap Opportunities diverged in their performance. Whereas the Raiffeisen Fund with its focus on large capitalised companies (exceptionally) lagged behind the Index, the Black Rock vehicle, with its focus on mid and small capitalised companies, managed to beat the SPI. Neither allocation nor individual investments where changed.

Other funds employed by us developed as follows[4]:

Acatis IfK Value Renten Fond (EUR)	-2.3%
Acatis IfK Value Renten Fond (CHF)	-3.8%
Lyxor ETF Euro Corp. Bond Fund (EUR)	-2.1%
New Capital Wealthy Nations Bond Fund (EUR)	2.2%
New Capital Wealthy Nations Bond Fund (CHF)	1.6%
New Capital Wealthy Nations Bond Fund (USD)	2.4%
Pictet CH-CHF Bond Fund	1.9%
Swiss Rock Absolute Ret. Bond Fund (EUR hedged)	-1.8%
Swiss Rock Absolute Ret. Bond Fund (CHF hedged)	-2.9%
UBAM Corporate USD-Bonds (EUR hedged)	-0.7%
UBAM Corporate USD-Bonds (CHF hedged)	-1.5%
ZKB ETF Gold (USD)	-7.5%

Equities Europe: All of a sudden, here too a fresh breeze is blowing in the face of exchanges. As a consequence, the DJ Stoxx 600 Index had to hand back nearly 9%, and with that, nearly all the gains achieved earlier in the year. Compared to January, it just managed to hold on to a plus of 1.5% by the end of the third quarter, nevertheless making it the winner amongst the major established markets. Due to the deteriorating economic outlook and the fuzzy technical state of the exchanges, we have reduced the European stock allocation slightly. In particular, it did not appear advantageous after the summer break to have a targeted allocation to German "Mittelstand" companies, which is why we sold the MDax Certificate.

From the directly-invested European Stock Portfolio (ESP), we sold the stocks of Antofagasta (mining), Standard Chartered (bank), as well as Aggreko (electricity and cooling equipment rental). These stocks hit a system-defined stop loss limit that triggered this move. The shipping stock, AP Moeller-Maersk, has been added. Overall, the selection is putting up a good show. It achieved a gross performance of 5.45% to the end of September, compared to a 3.85% total return by the Dow Jones Stoxx 600 Index. Net after cost and taxes, the ESP performance achieved 4.60% and with that result, still beats the index.

The medium annual net performance of the directly-invested portfolio amounts to 8.74% since 2004, compared to 6.61% of the benchmark. The figures for the European Stock Portfolio include transaction costs and taxes at source, whereas the reference index operates without costs. You will find the performance and benchmark comparisons of the ESP and SSP updated on our website www.salmann.com (under the tab "Produkte").

Equities USA: Here we implemented two changes. On the one hand, we sold the units in the Janus Perkins US Strategic Value Fund, reinvesting the proceeds in the Performa US Equity Fund. This was after the first fund's performance has been unable to keep pace for some time now. In view of the higher and rising fundamental valuations, as well as increasing nervousness on the markets, we reduced the iShares Core S&P 500 position later in the quarter to take the USA weighting to a near neutral position.

Equities Asia (excluding Japan): Asian markets have suffered most from the distortion. Apart from the maelstrom of China, the nagging worry that rising US interest rates and a strengthening US Dollar might stress the funding side of companies increasingly lodged itself in the heads of investors. In addition, the fear that a flight of capital from the region towards America might ensue as a result, made the rounds. The position remains unchanged. With about 5%, the weighting amounts to a roughly neutral allocation.

Equities Japan: The Land of the Rising Sun was unable to escape the weak state of the Asian markets. There were no changes in the positions. Its size is similar to the Asian one and it is slightly overweight. The Yen is hedged in clients' reference currencies.

[4] Performance incl. re-invested dividends where applicable

Alternative Investments: Unchanged, this category is covered by a 3% position in a gold ETF.

Summary of our current **Asset Allocation**[5]**:**

Investment Category	
Money Market	overweight
Bonds	underweight/short duration
Equities Switzerland	overweight
Equities Europe	neutral
Equities USA	slightly overweight
Equities Asia	neutral
Equities Japan	slightly overweight
Alternative Investments	underweight

Conclusion / Outlook

We expect the growth of the global economy to come in slightly weaker than previously expected, but will ultimately be able to supply positive impulses. The first interest hike in the USA might come this year, and is rather more likely to calm markets. Generally, equities remain more interesting than bonds.

Measured on the **price/earnings ratio**[6] using the latest 12 months profit figures, all equity markets have become more attractive:

	Dec. 2014	Sept. 2015	Change
DAX Index/DE	17.2	15.3	**-11%**
DJ STOXX 600 Index/EU	21.3	20.4	**-4%**
MSCI World Index	16.9	16.3	**-4%**
S & P 500 Index/USA	18.2	17.0	**-7%**
SPI Index/CH	19.5	17.2	**-12%**
TOPIX Index/JPN	16.1	14.7	**-9%**

[5] For a Swiss Franc referenced portfolio

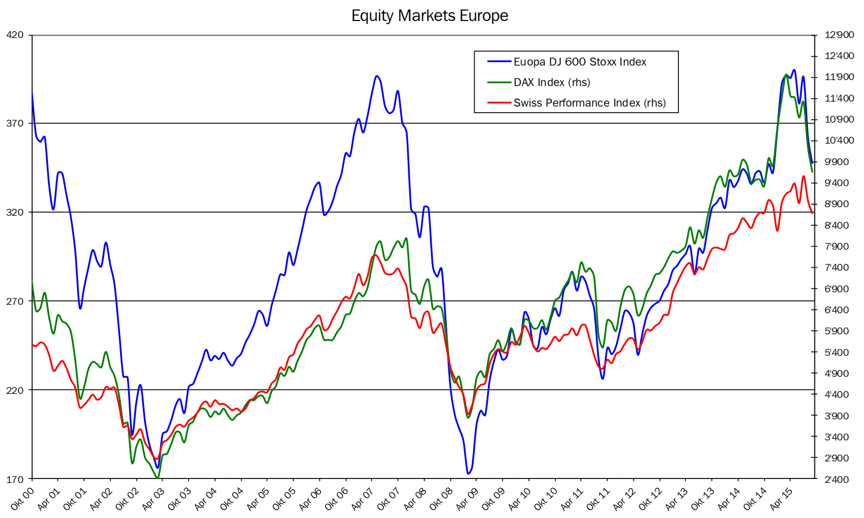
Price/Book and **Dividend Yield** of major equity markets:

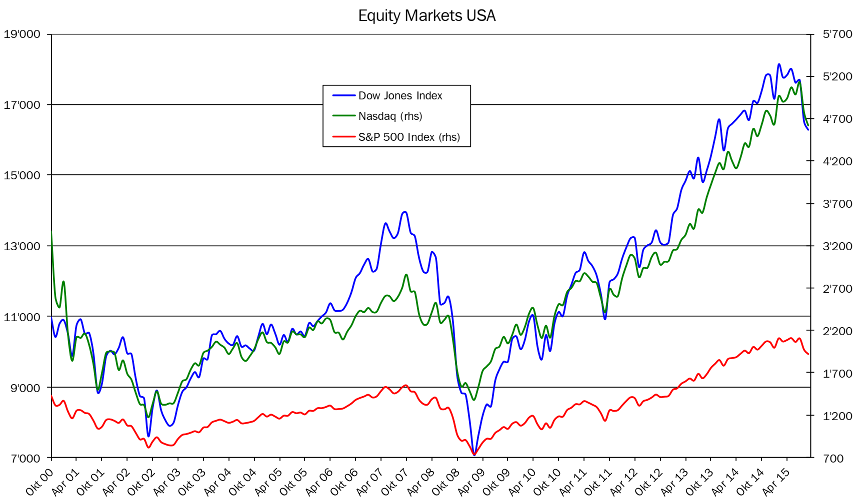
	Price / Book	Div. Yield
DAX Index/DE	1.5	3.1%
DJ STOXX 600 Index/EU	1.7	3.7%
MSCI World Index	1.9	2.7%
S & P 500 Index/USA	2.6	2.3%
SPI Index/CH	2.3	3.3%
TOPIX Index/JPN	1.2	1.9%

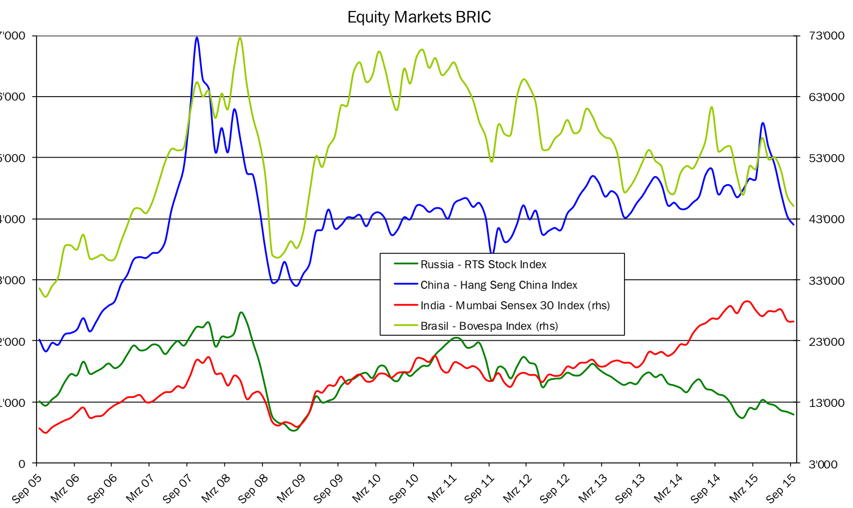
We thank you for the trust placed in us and wish you many golden autumn days.

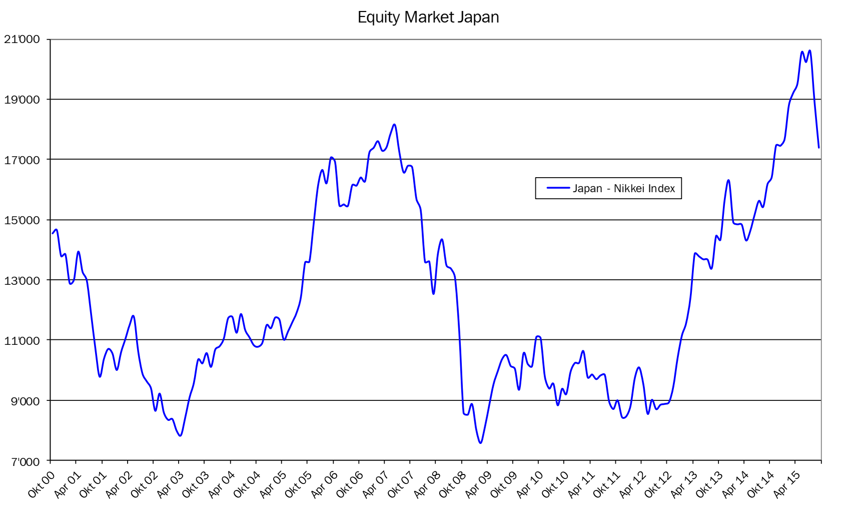
Alfred Ernst
Vaduz/Zurich, 30th September 2015

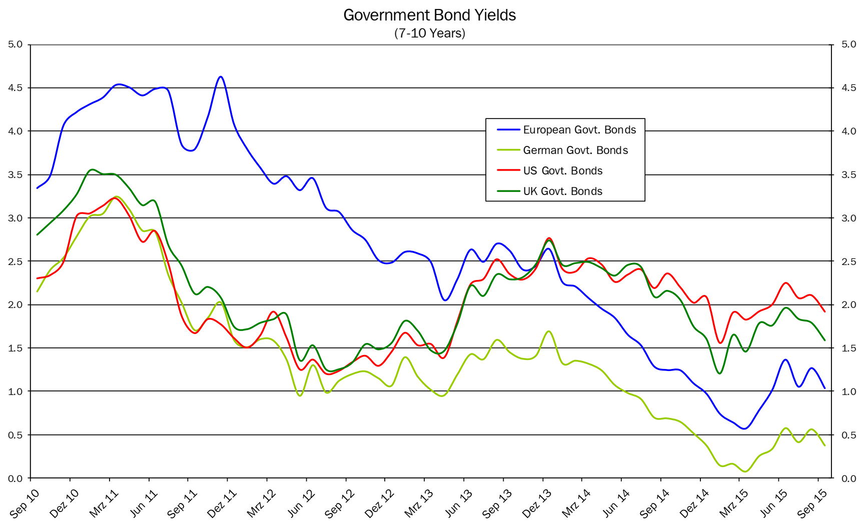
[6] Source: Bloomberg

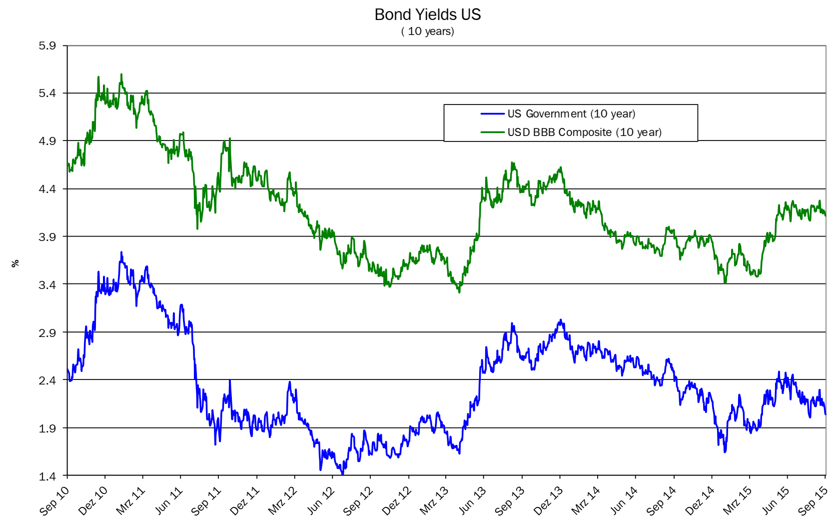

Equity Markets Europe
Euopa DJ 600 Stoxx Index
DAX Index (rhs)
Swiss Performance Index (rhs)

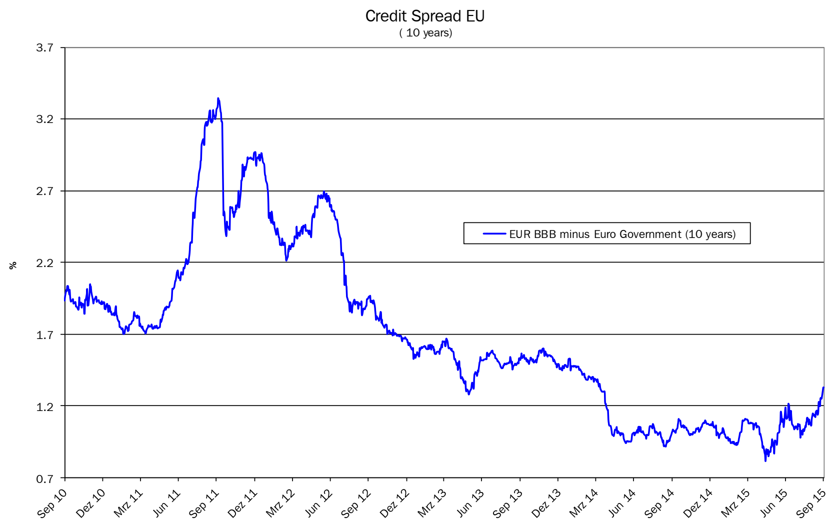

Equity Markets USA
Dow Jones Index
Nasdaq (rhs)
S&P 500 Index (rhs)

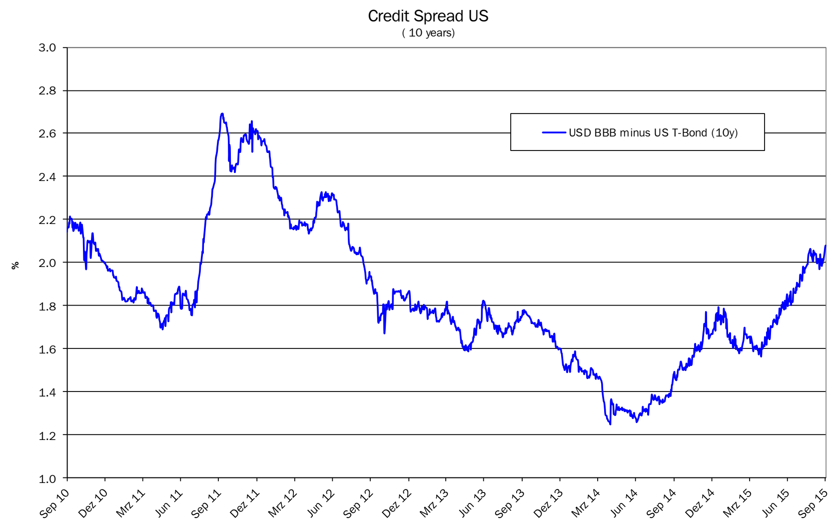

Equity Markets BRIC
Russia - RTS Stock Index
China - Hang Seng China Index
India - Mumbai Sensex 30 Index (rhs)
Brasil - Bovespa Index (rhs)


Equity Market Japan
Japan - Nikkei Index


Government Bond Yields
(7-10 Years)
European Govt. Bonds
German Govt. Bonds
US Govt. Bonds
UK Govt. Bonds


Bond Yields US
(10 years)
US Government (10 year)
USD BBB Composite (10 year)
%


Credit Spread EU
(10 years)
EUR BBB minus Euro Government (10 years)
%


Credit Spread US
(10 years)
USD BBB minus US T-Bond (10y)
%