GUARDIAN ASSET MANAGEMENT

2016 MARKET OUTLOOK

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Market Outlook

Once again markets did not fail to excite in 2015, with most major markets enduring swings of over 20% from their high and low points in 2015. After a six year winning streak the US bull market came to a halt in 2015, declining by 0.73%. Global equity markets were even more dismal with a few exceptions in Europe and Asia, however even those returns on a USD basis were eroded by currency losses.

One silver lining was the positive performance of regional equity. The local Trinidad & Tobago Composite Index gained 0.99%, driven mainly by Cross Listed stocks as the Jamaica stock market delivered a stellar year, helping investors hit new highs with gains of over 80%, topping global stock markets in 2015.

INDEX	PRICE AS AT 31-Dec-15		YTD Return	2015 HIGH %	2015 LOW %	Change
GLOBAL STOCK MARKETS						
TTSE Comp	1,162.30	↑	0.99%	1.47%	-2.44%	3.92%
S&P 500	2,043.94	↓	-0.73%	3.68%	-9.32%	13.00%
MSCI World ex US	774.36	↓	-6.90%	9.52%	-11.56%	21.09%
MSCI Europe	410.97	↓	-5.72%	9.88%	-11.60%	21.48%
MSCI Asia Pacific	131.96	↓	-4.29%	14.16%	-12.49%	26.65%
MSCI BRIC	220.96	↓	-15.68%	18.67%	-18.46%	37.12%
LONDON	6,242.32	↓	-4.93%	8.48%	-12.15%	20.63%
PARIS	4,637.06	↑	8.53%	23.66%	-3.59%	27.25%
FRANKFURT	10,743.01	↑	9.56%	26.36%	-4.90%	31.26%
MOSCOW	1,761.36	↑	26.12%	34.15%	2.44%	31.71%
SAO PAULO	43,349.96	↓	-13.31%	17.13%	-13.61%	30.75%
MUMBAI	26,117.54	↓	-5.03%	9.18%	-9.48%	18.66%
HONG KONG	21,914.40	↓	-7.16%	21.11%	-12.91%	34.03%
SHANGHAI	3,539.18	↑	9.41%	60.08%	-11.87%	71.95%
TOKYO	19,033.71	↑	9.07%	20.07%	-4.92%	24.99%
SYDNEY	5,295.90	↓	-2.13%	10.83%	-9.27%	20.10%

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2015 Market Recap

Trinidad & Tobago

The economic and political landscape shifted in Trinidad & Tobago in 2015. With oil prices declining from above US$100 per barrel in June 2014 to less than US$50 per barrel in January 2015 the government was forced to revise budget allocations and projections. In April the first negative action on the country's credit rating came as Moody's downgraded Trinidad & Tobago's credit rating to Baa2 from Baa1 and changed the outlook from stable to negative. In September the government changed with the People's National Movement returning to power after a five year hiatus.

In October the much anticipated Trinidad & Tobago NGL IPO concluded and shares began trading on the Trinidad & Tobago Stock Exchange (TTSE). In December the government announced the appointment of a new Central Bank Governor after the dismissal of the former governor, under whom the Repo rate was raised from 2.75% in July 2014 to 4.75% by December 2015. Also in December a second credit rating agency Standard & Poor's revised its credit rating outlook on T&T to negative from stable, citing the expectation of prolonged low oil prices and lower GDP growth prospects in addition to the potential for an increasing debt burden.

Internationally

The year started off with the surprise action by the Swiss National Bank which in January abandoned its 1.20 currency floor against the euro. The action in Europe continued in the first quarter when the European Central Bank (ECB) announced its EUR 60bn per month quantitative easing program, causing the euro to plunge to the lowest level in more than a decade.

In the second quarter bond markets sold off on prospects of higher US interest rates and stronger European growth. In June after jumping 150% over the prior 12 month period and over 60% year to date the Chinese equity market finally peaked.

As the second quarter ended and the third began markets were rife with volatility as "Grexit" was the hot topic with Greece coming close to leaving the Eurozone, causing the S&P 500 Index to give up all gains for the year and European stock prices to plunge. In August, China allowed its currency, the Yuan, to depreciate by 3%, flaming fears of an impending 'currency war'.

Later in the third quarter volatility spiked to levels not seen since 2008. China's stock market tumbled over 70%, taking many emerging and commodity based markets with it, as fears over China's slowing growth mounted. Emerging market currencies also took a beating in the third quarter and concerns over the Syrian refugee crisis in Europe heightened.

In the fourth quarter Europe and the rest of the world were shocked by brazen attacks on civilians in Paris by the Islamic State. OPEC met and decided to make no changes to oil supply, leaving oil producing countries to continue to feel the squeeze of lower oil prices. In mid-December the Fed met and decided to raise interest rates for the first time in over six years.

2016 Themes:

Belt Tightening Time…

Locally we expect to see the economy grapple with recession as oil prices remain low at below US$50 per barrel and revenues earned from the oil and gas sectors decline. We also expect to see unemployment in the energy sector and downstream sectors rise. Foreign reserves may also decline from current 11 months cover of imports, and the exchange rate may come under pressure, trending down towards TTD/USD $7.00/$1.00.

Given the lower gas and oil revenues we expect the government to seek additional avenues to cut spending and raise revenue which will be announced at the midyear review in March/April. As such the gas subsidy may be further reduced. This subsidy cut along with the introduction of VAT on previously non-vatable items and the higher cost of imported goods may stoke inflation pressures in 2016.

Despite our expectations for rising inflation we do not foresee the continued rise in the Repo rate. In January 2016 we saw the CBTT pause for the first time since the raising cycle began in September 2014. Given weakening growth prospects we believe the Central Bank will become accommodative and seek other means to stem capital flight, which in the past was cited as a reason for increasing the Repo rate.

Weaker growth prospects and a growing debt burden however may result in Trinidad & Tobago losing its “A” credit rating from S&P in 2016. A downgrade could have a further impact on USD denominated Government of Trinidad & Tobago (GOTT) bonds, causing yields to rise to reflect the higher perceived credit risk. The prices of internationally traded GOTT bonds have been under mounting pressure since the second half of 2015 as the decline in oil prices intensified.

We anticipate 2016 will be a tough year for local stocks, in 2015 the All T&T Index fell by 1.75%. We expect the decline in 2016 to possibly worsen as earnings of energy related stocks fall in line with oil and gas prices. Also blue chips such as the banks and conglomerates are expected to earn lower revenues as consumers and businesses reduce borrowing and spending.

Whilst there isn’t much to be optimistic about, the possibility of new stock listings coming to the market, as a way for the government to shore-up revenue to fund its budget deficit, may offer some alternatives for investment.

Another silver lining on the local market may once again be cross listed shares. The prospects for Jamaica and Barbados may rise as their energy bills are reduced. Also the global recovery may benefit their tourism industries as international consumers are now more likely to opt for tropical vacations given higher disposable incomes and lower airline transportation costs.

Investment Idea: Diversify out of Trinidad and Tobago dependent equities; buy Cross-listed stocks or local equities which have external revenue streams.

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The wait isn't over yet…

With oil prices at decade lows, inflation in the US is poised to stay low, giving the US Federal Reserve little impetus to raise interest rates in any meaningful way before the end of 2016. The fragile state of commodity producing countries and emerging markets dependent on Chinese growth will also tie the Fed's hands. As such we do not anticipate any further increases from the US Fed before the second half of 2016. Also globally most developed nations and many developing nations remain on pause or are in easing mode, this accommodative stance is expected to be supportive of equities in general. Nonetheless we do anticipate volatility to remain rife as investors remain sensitive to changing global dynamics and volatile oil prices.

Investment Idea: Asset Allocation: Equal weight equities- trade on volatility; Underweight Long-term Fixed Income, favour short durations.

Dollar reign to continue…

The dollar will continue to hold its own against other developed market currencies such as the GBP, EUR, YEN and CAD. The Canadian and Pound will be affected by slower GDP growth on lower oil prices. Canada may quite possibly slip back into recession as oil prices stay at these low levels over the next year as demand and supply forces try to find equilibrium. UK GDP will also suffer, though to a lesser extent from the loss of revenues and corporation taxes from North Sea oil operations. Also the pound will remain under pressure as uncertainty over the "Brexit", the risk of the UK exiting the Eurozone, grows. As a result both the Bank of Canada and the Bank of England are likely to remain accommodative to help sustain or rejuvenate economic growth. The Euro and the Yen will also continue to wane as their respective Central Banks remain ready to add stimulus as necessary to support their lethargic recoveries. The Yen may however appreciate during times of heightened risk aversion as investors seek the comfort of the Yen, which is viewed as a safe haven.

Investment Idea: Long Dollar

Where's the bull…

After taking a break from its six year bull market, analyst consensus expects the US equity market to continue to rally in 2016, albeit mildly to around 2,160 (as measured by the S&P 500 Index) based on an 8% growth on 2015 earnings and an 18 times P/E multiple. We agree with this view. US corporate earnings were negatively impacted in 2015 by lower exports due to a stronger dollar and the drag of reduced Capex spending from energy sector companies which may continue to be felt in 2016. However, we think that the positives of increased employment, stabilizing oil prices and returning consumer confidence will outweigh these negatives which have been worrying investors. From current levels of between 1,890 to 1,930 we think US equities are attractively valued.

Investment Idea: Equal weight US equities – buy the dips, sell on exuberance.

Easy Money…

In January 2016 the Bank of Japan surprised the markets by joining the European Central Bank in adopting a negative interest rate. In theory financial institutions must now pay to place deposits with these Central Banks thus further incentivizing banks to make low cost loans to businesses and consumers for consumption and capital expenditure in hopes of strengthening economic growth. The BOJ's pledge to keep increasing the monetary base at an annual pace of 80 trillion yen ($663 billion), primarily by continuing to purchase Japanese government bonds, exchange-traded funds and real estate investment trusts, is also supportive of Japanese equities.

Investment Idea: Favourable on Japan and developed Europe equities in the international space.

Zika and other maladies...

Latin America will continue to underperform in 2016 as a bevy of maladies impact the region, slowing demand from China being a main source of weakness to this commodity rich region. Brazil will suffer another lack luster year, even while hosting the 2016 Olympics. The emergence of the Zika virus in Brazil and the spread to the rest of Latin America will be an added toll on the region's already strained position.

Investment Idea: Underweight/ Short Brazil and Latin America.

Year of the Monkey (2016)...

In the Chinese zodiac it is said that people born in the year of the Monkey are more optimistic. Likewise we think that China while having several issues at its door steps has the wherewithal and institutional support to muddle through without entering into a hard-landing situation where growth falls to less than 5%. That said there will be further bouts of global volatility stemming from lower Chinese growth and trading partners of China in Asia such as members of ASEAN, Taiwan and South Korea, will suffer the effects. Globally emerging market countries in Latin America and Africa will also be impacted by lower China growth. Therefore in the emerging market space China with its 3 trillion in USD reserves and moderate debt-to GDP ratio of 40% is well equipped to handle the reoccurring volatility and prevent a systemic decline, the fear of which sent panicking markets into tailspins in January this year.

Investment Idea: Opportunistic on China as valuations become more attractive

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Crumbling BRIC…

India's economy is the only of the BRIC nations which has not shown signs of crumbling in recent turmoil. Rather India continues to grow at a pace and is benefiting from the rout in energy prices. India's expanding middle class and growing reliance on domestic demand to propel growth has insulated it somewhat from the upheaval that other emerging markets have felt in response to slowing China.

Investment Idea: Overweight India in the emerging market sphere

Are we there yet…

Have we seen the bottom of the commodities cycle? Maybe not, but we are getting there. The IMF expects Chinese growth to slow to 6.3% in 2016 and 6.0% in 2017 from an estimated 6.9% in 2015, so there may still be some pain to be endured in commodity prices, particularly iron ore and other base materials.

Oil prices have sunk to 12 year lows but may be close to the bottom as oil producers shutter operations and cut back on planned CapEx spending, thereby reducing production. Many analysts expect the price of WTI oil to rebound to above US $45 per barrel by the end of 2016. However the true impact of the addition of Iranian oil to the market and the commitment of OPEC members to maintain January production levels are possible game changers. Gold prices meantime may receive a reprieve in 2016, already the precious metal has gained 5% in the first month of 2016, gold prices may remain stable and benefit safe haven buying during future bouts of volatility and also as the increase in US Fed rates are expected to be gradual.

Investment Idea: Underweight commodities. Watch from the sidelines until the dust has cleared.

Risks to Outlook:

- Locally, the midyear budget review reveals a worse than expected fiscal position.
- Heightened geopolitical risk, should tensions in the Middle East (Israel/Palestine conflict, ISIS incursion into Syria) worsen.
- Further terrorist attacks on Europe or other developed nations.
- Refugee crisis in Europe grows.
- Volatility within US stock market exacerbated by US elections in November.
- Economic crisis in large oil dependent nations such as Russia, Venezuela, Nigeria etc should oil prices remain low or dip further.
- High yield debt defaults rise due to falling oil prices, causing risk aversion and volatility.
- Increase in US interest rates faster than expected, which may cause a sell-off in US equities.
- Deflation in the euro zone, hampering the recovery in that region.
- Greece/UK exiting the euro zone.
- Lower Chinese growth than expected, "hard-landing" scenario.