BANCA DEL SEMPIONE
SIMPLON BANK
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Investment Policy

April 2017 - 2. Quarter

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Press date: 15 April 2017

The year 2017 started off on an optimistic note, with share prices continuing along their path of recovery that began after the US presidential elections. Simultaneously and for the first time in a number of quarters, the economic indicators are also synchronised, in line with economic growth in Europe and the USA, as well as in the emerging markets, where China is less worrisome than one year ago.

During the quarter, the US Federal Reserve adjusted interest rates upwards for the third time since the end of 2015, and the market expects two additional increases in 2017, in the wake of a job market that has stabilised with a solid foundation. In Europe, the ECB continues to maintain an expansive policy, while reducing the monthly QE amount from here until year-end.

On the geopolitical front, the first appointment in the busy European electoral calendar was the defeat of the Eurosceptic front in the Netherlands. At the moment, the eyes of the entire world are focused on the French presidential elections, which, according to surveys, are not expected to take an anti-European turn. Meanwhile, the Brexit talks have been postponed until June, due to the early elections called by May, in order to take advantage of a broader consensus. Across the ocean, the first true attempt at reform (revision of Obamacare) has been momentarily suspended. However, the market has not reacted particularly negatively, showing overall confidence in expectation of the tax programme.

We maintain a pro-risk approach in equities, although we expect some pitfalls and volatility. With regard to foreign currencies and bonds, we reiterate our recommendation for a prudent approach, which requires opportunism and flexibility, not commonly associated with traditional buy-and-hold management. In fact, we believe the normalisation of US interest rates will undoubtedly affect all other bond segments, starting from the Eurozone bonds. We can obtain value from emerging market rates and currencies, selecting the countries carefully.

The US scenario in first quarter 2017

During the first quarter, the Fed proceeded with the third historic increase in rates since 2006, while maintaining a highly dovish stance: in fact, monetary policy continues to be accommodating. The market appears to have been surprised by this attitude, as expectations were for three further increases, rather than the two additional ones indicated by the Fed.
The first attempt at reform by the Trump administration in terms of healthcare was withdrawn in order to avoid parliamentary rejection. In the meantime, the real news in Trump's speeches after his inauguration - compared to those during the election campaign- is their more conciliatory tones and the call for unity, also noted by the most critical press.
The macroeconomic framework remains positive, with the PMI still in an expansive range. At the same time, the job market in the USA continues to show signs of solidity, and pressures on salary inflation are not yet cause for concern. The slight slowdown in GDP is not cause for worry, either.
Lastly, expansive fiscal policies should gradually replace monetary policy to support growth.

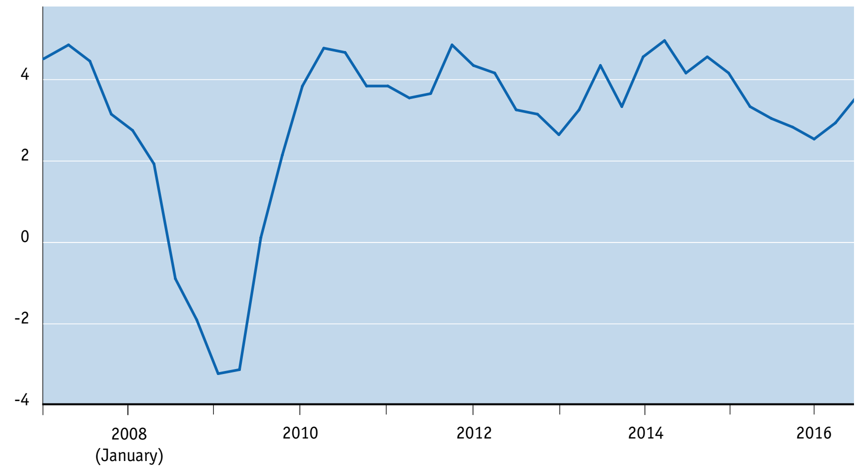
Normalisation of rates in Europe expected only around year-end

While it is already underway in the US, normalisation of rates is expected in Europe only at the end of the current year. Once the ECB is required to suspend the QE or, in any case, normalise monetary policy, we expect some volatility in bonds, perhaps sharper than the risks coming from the electoral front.
In fact, with regard to the presidential elections in France, the threat of a win by Le Pen appears to be less likely at the moment: Bayrou's support of Macron increases the probability of winning in the second round over the FN, easing a bit of uncertainty.
Lastly, the elections in the Netherlands, with the loss by extremist Wilders, were also a source of tranquillity.

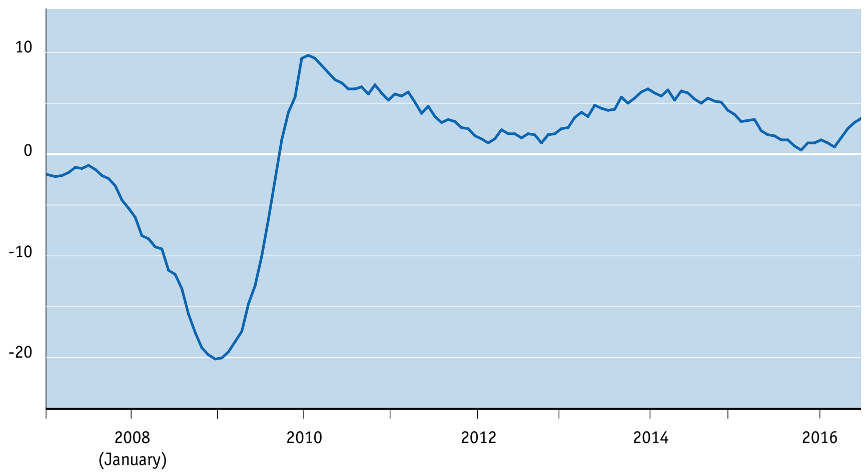
The process of "cleaning up" corruption in China

From the macroeconomic standpoint, the emerging markets continue to show signs of stabilisation of a positive growth trend, backed by the recovery in commodity prices and growth in consumption and investments.
In China, President Xi increasingly consolidated his position, placing trusted individuals in top military positions and in the various provinces. The four years of his mandate have been spent fighting widespread corruption at all levels and battling against oligarchic positions that damage state-owned enterprises (SOE): this "cleaning" process should end by the next congress, which is taking place this upcoming autumn.
After 7 years of decline, private investments are up as well, whereas public investments, which have buffered this phase of weakness, are down.
The PMI and job market appear to be headed in a positive direction. Contribution of consumption to GDP grew significantly, from 50% in 2011 to a current 70%, mainly thanks to growth of the middle class.

US quarterly GDP growth



Performance of leading indicators



Neutral on investment in USD

We have shifted to a neutral stance on the EUR-USD exchange rate, compared to the bearish attitude of the prior quarter. The reasons for a strong or weak Euro are the same. The "pro-Euro" arguments stem from an upcoming phase of normalisation of monetary policy by the ECB, supported by a macroeconomic scenario showing clear improvement and recovering inflation. On the other hand, the Euro bears focus on the interest rate gap between EUR and USD, and on the political risk of stability in the Eurozone (with the imminent French elections and the risk of victory by Le Pen).

Following the adjustment, the Norwegian Krone offers interesting investment opportunities

The Norwegian currency underwent a sharp adjustment during the quarter. The underlying reasons for this shift are mainly attributable to the downturn in oil prices and the disappointing consumption price trends (CPI yoy 2.5% compared to the expected 2.9%). The shift was magnified by the considerable positioning on "long NOK" trade. Devaluation has gone beyond the traditional adjustment, providing opportunities to increase the historic position or create a new one based on profitable prices.

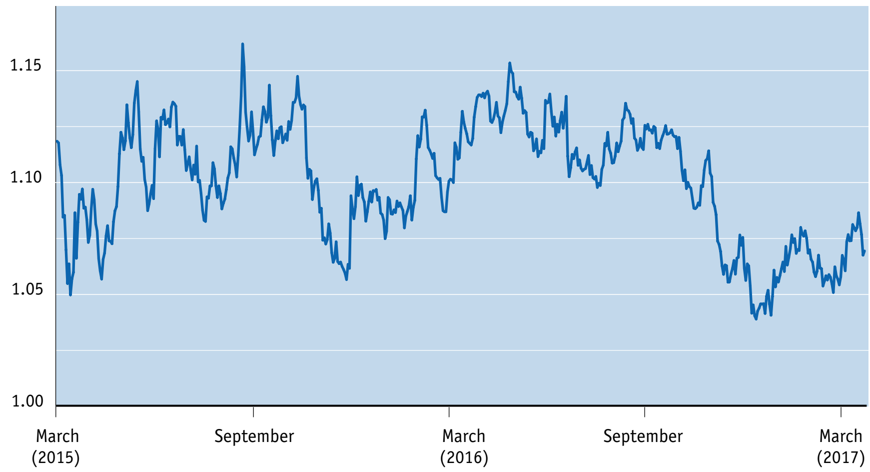
Even a long position on emerging currencies continues to be attractive

Emerging currencies continue to offer an attractive investment alternative. The interest rate upswing in the US, which has historically weighed on the performance of these currencies, appears to be largely over and no longer represents a threat. It is also true that the emerging currencies recorded good performance in the first quarter of the year, bringing prices to an essentially balanced position. Therefore, we maintain investment in these currencies, with manageable proportions and careful selection of the countries.
We are currently positive on the Mexican peso, Turkish lira and South African rand, while we prefer to refrain from investing in Russia or Brazil. Both the Russian rouble and Brazilian real have reached a level that provides more risks than opportunities. In particular, the geopolitical tensions related to the Syrian conflict could weaken the Russian currency.
The referendum in Turkey, with a victory by the YES votes, will grant greater powers to the prime minister. In fact, the currency underperformed the other emerging currencies in relative terms, due to this very event, and we believe that this performance gap may be recovered in upcoming months.

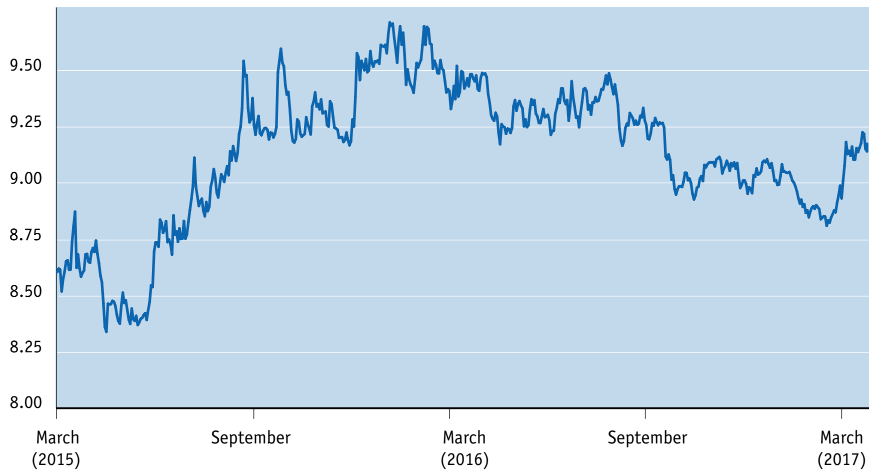
Japanese yen risks adjustment in the second quarter

The Japanese currency recorded good performance at the end of the quarter. The reason for this is the search for safe havens by investors which, to protect themselves from any anti-European repercussions in the upcoming French elections, have acquired three such safe havens par excellence: the Yen, gold and the German bund.
We are confident that Le Pen's defeat in the elections on 7 May will lead to a search for riskier assets, to the detriment of defensive ones, with a consequent devaluation of the yen.

EUR – USD Exchange Rate



EUR – NOK Exchange Rate



Context in first quarter 2017

During the first quarter, the Fed finally increased rates by 0.25, while maintaining a rather dovish wording for the rest of the year. Therefore, we are not at the beginning of a period of sharp increases like those of the years 2004 to 2006, during which Fed Funds grew from 1 to 5.25%! And this has clearly calmed the markets. US bonds have reacted moderately and recovered spread against German bonds.
Pressures on oil prices and Trump's defeat in congress in the attempt to change Obama's health reform have jointly created some volatility on the markets which has not, however, caused any significant movements. Markets are now questioning the capacity of Trumpenomics to truly achieve its objective of reflating economies. Whether the president will have to power to implement truly expansive tax policies is certainly food for thought. At the moment, these doubts are partially translating into partial profit-taking on themes which have performed well over the last few months (particularly stock indexes), but without any shocks.

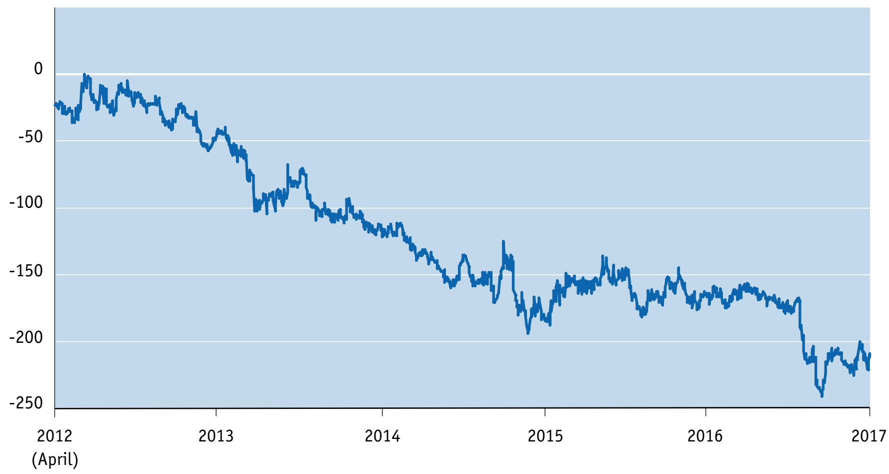
ECB support for the peripheral markets is a reason not to fear spreads' widenings

Another issue for analysis is how the ECB will handle the reduction in its purchases on the market. Many believe that a reduction in quantitative easing will lead to widening of the spreads in Europe, with the peripheral countries under pressure. We believe that at this point, the ECB's support of peripheral markets is implicit and long-term, regardless of quantitative easing. If Europe does not disintegrate (and this is by far our main scenario), debts will slowly become common, with uncertain methods and times. However, apart from moments of tension, we cannot imagine another way of managing European sovereign debt if not that of keeping spreads as compact as possible so as not to further penalise countries that are objectively weaker than others. With this underlying vision, we continue to bet on the core-periphery spread with a view to narrowing, without exaggerating the proportions.

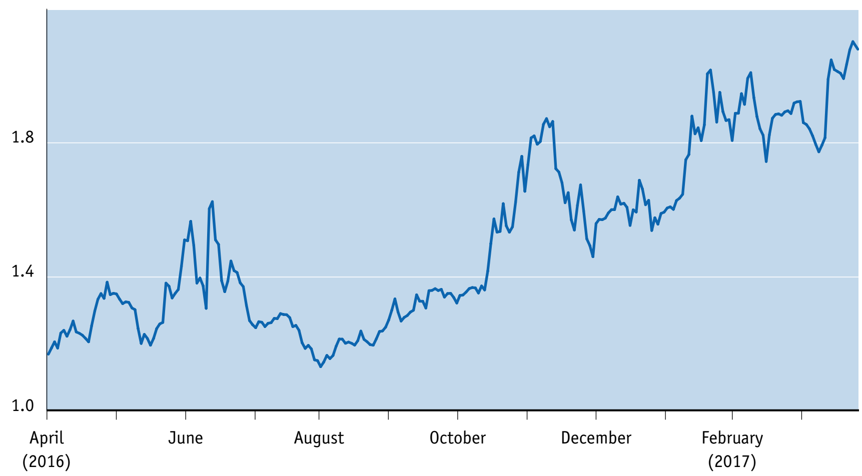
Our tactical bets

We continue to maintain our strategic ideas (short duration on the long German section, America-Europe spread, periphery-core spread, flattening on the Italian curve, long on the Mexican peso and Turkish lira), applying some tactical adjustments at key moments. Nevertheless, we recommend paying particular attention to exposure to the European periphery in terms of loans, due to an expected risk of increased volatility. This is also a result of limited opportunity that is forfeited, given the very low level of nominal and, in particular, real rates.
Taking a position on the local emerging segment appears interesting, with more attractive yields/rates and potential for appreciation of currencies.

US – Germany 10 year spread in basis points



BTP – BUND 10 year yield spread



US scenario in the first quarter

The difficulties of the Republican Party in finding an agreement in the US Senate on the health reform during the quarter have led investors to believe that the reforms pursued by the new US administration (starting with the tax reform) will undergo a more difficult parliamentary approval process than expected. Consequently, the market, which perhaps too quickly rejoiced at the implementation of said reforms, has taken a step back.

Growing earnings and valuations in the equity markets

We are still undergoing an expansion of the key macroeconomic indicators. Earnings are also expected to grow in the current year and in the next one, both in the USA and Europe, with a forecast P/E that is down compared to the current figure.
In terms of valuations, there is widespread and almost unanimous consensus that the European equity market is undervalued and to be preferred over the US market. Indeed, the recent upward shift of the European index is not in line with an expansion of multiples that decreased further (P/E at 19.1, having risen to slightly over 20 the prior month).

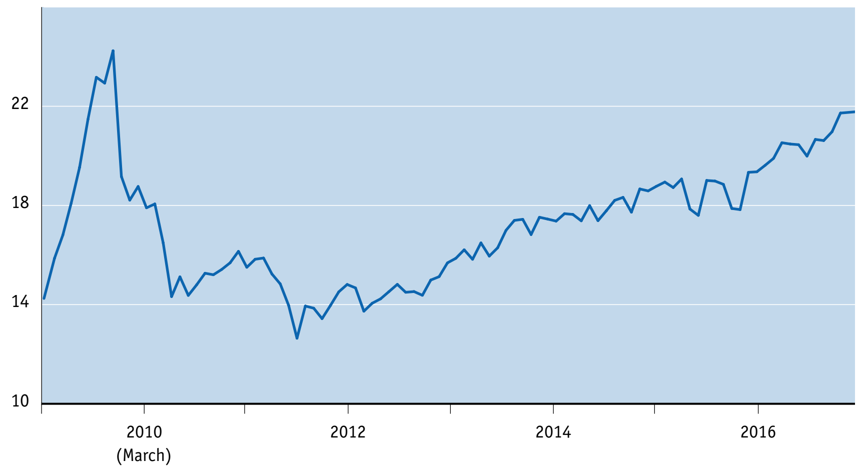
Favorite sectors include American small-mid caps and European banks

The US Small Cap sector should be favourably impacted by the tax reform and the desire to bring production back home.
At the same time, the sensitivity of small and mid-cap companies to trends in oil prices is important, given the exposure of the index to the oil sector. Therefore, although we do not consider it to be likely, if the current adjustment on WTI continues, the impact could be considerable.
On the European front, there is wide consensus on the fact that the banking sector could provide good results. This is largely due to the fact that government bond rates are supposed to rise, fuelled by QE and highly compressed due to fears of disintegration.

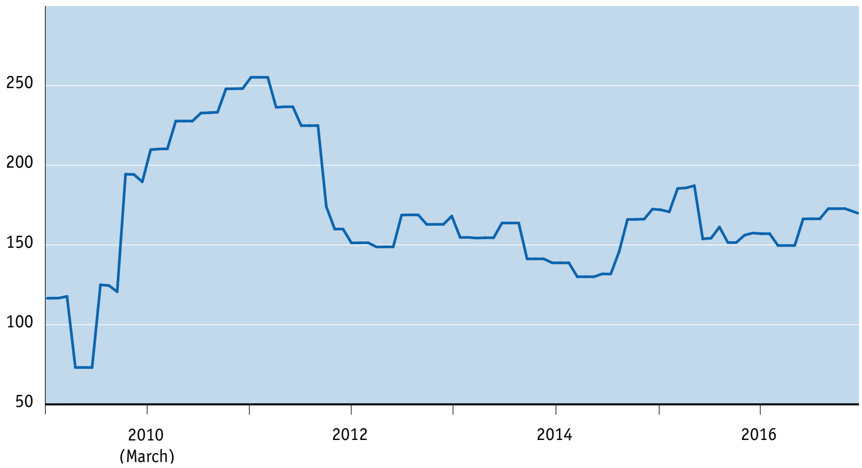
Chinese stock market attractive once again

In China, the fight against corruption and the introduction of regulation in the stock market have resulted in a sharp adjustment and in bursting of the bubble; however, the market appears to be recovering, as demonstrated by the recovery of IPOs in 2016.
But taking advantage of the Chinese market means paying close attention in the selection of equity sectors: New China (IT, Healthcare, Consumer) has heavily over-performed Old China (Energy, Materials and Industrials) and is still to be preferred over the latter, due to the SOE (state-owned-enterprise) structure of Old China.
Corporate debt, often mentioned as the cause of systemic risk in China, now appears to be less dangerous than feared: in fact, debtors partly include SOEs, and the state is therefore ready to resolve any issues, while the high percentage of savings means this debt can be financed locally, without resorting to foreign creditors.
China cannot be avoided over the medium to long-term, although attention must be paid to selecting the right sectors and stocks and, above all, the right manager!

Eurostoxx 50 historical EPS



S&P 500 historical P/E ratio



Goals

In a world characterised by increasingly squeezed yields expected for traditional risk categories (shares and bonds) and by more and more frequent market shocks, the objective set by Banca del Sempione's asset management is to achieve a real growth in capital in the medium-long term. To achieve this result we use the most advanced and innovative techniques accompanied by the healthy values of a Swiss tradition and culture which within the area of asset management can rely on people with an excellent level of professionalism.

Investment Philosophy

Our investment philosophy is based on five main principles:

- Composition of profits
- Drawdown reduction
- Discipline of the method, rather than "passivity" of the method
- Reduction of cognitive and emotional biases
- Limited presumption of market timing

Specifically, a reduction in drawdowns (i.e. negative fluctuations in asset values) combined with capitalisation of profits (defined by Einstein as the eighth wonder of the world), allows for triggering a snowball effect, through which profits are generated on profits , resulting in growth of invested capital over the medium-long term.

Portfolio Structure

		Maximum investment limits (%)					
Investment Profile	Risk category	Cash	Investment Grade Bonds (>=BBB-)	Non Investment Grade Bonds (<BBB>)	Equities	Other Funds*	Currency Diversification
Income	Low	100	100	0	0	5	15
Income Plus	Medium-low	50	100	15	15	15	15
Dynamic	Medium	30	100	20	30	25	25
Balanced	Medium-high	30	80	20	50	25	25
Growth	High	30	50	20	75	30	25
Equity	Very high	30	50	20	100	30	25

* Non-directional funds, total return funds, funds of funds

The limitation of drawdowns via compounding of profits - defined by Einstein as the eighth wonder of the world - permits the accrual of profits on profits, triggering a snowball effect that results in growth of capital invested in the long term. The main innovation of this approach is in the way of limiting losses: in the past, portfolio volatility was offset by investments in instruments considered to be free of risk, namely bonds. Today, the protection offered by such instruments is mostly limited, while in the medium/long-term, traditional investment in bonds could even increase portfolio risk, especially if we consider that over the recent period, stocks and bonds have increased in perfect harmony.

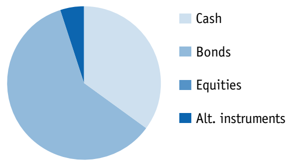
In our opinion, the implementation of systematic strategies allows for portfolio risk reduction and profit achievement whilst protecting invested capital, even in difficult markets. Due to their cold and mechanical approach, these strategies sharply mitigate the emotional component that drives and influences investment decisions and are based on the concept that it is preferable to participate in market trends rather than anticipate a shift or change in trend. On this basis, market prices are the best indicators of the current trend. As opposed to traditional ones, systematic strategies may also participate in market price downturns and, combined with a more traditional fundamental analysis approach, are able to offset sharp downward shifts such as those of 2008 or 2011.

In essence, common sense, systematic behaviour and discipline in making investments are the bases on which we build the portfolios of our clients.

Allocation by asset class

Income

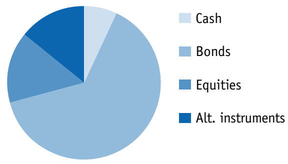
Cash	35
Bonds	60
Equities*	–
Alternative instruments	5
	100



Asset classes

Income Plus

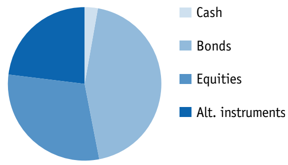
Cash	7
Bonds	64
Equities*	15
Alternative instruments	14
	100



Asset classes

Dynamic

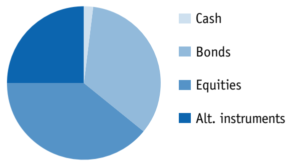
Cash	3
Bonds	44
Equities*	30
Alternative instruments	23
	100



Asset classes

Balanced

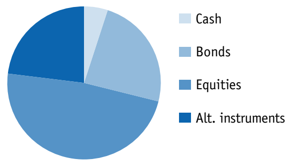
Cash	2
Bonds	34
Equities*	39
Alternative instruments	25
	100



Asset classes

Growth

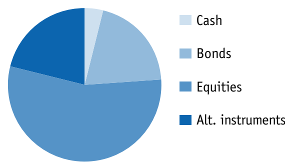
Cash	5
Bonds	24
Equities*	48
Alternative instruments	23
	100



Asset classes

Equity

Cash	4
Bonds	20
Equities*	55
Alternative instruments	21
	100



Asset classes

* Part of equity allocation is hedged with index options or futures

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