EB WEALTH

QUARTERLY REPORT
Q3 2017

GLOBAL OVERVIEW

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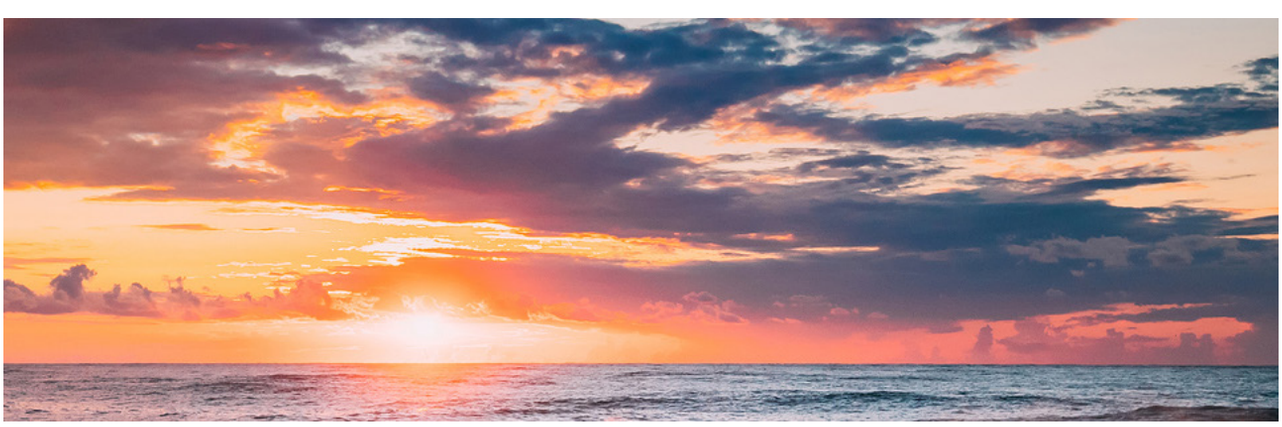
Global markets maintained their strong performance throughout 2017 with most major indexes registering gains over the quarter. Asian equities sustained their strong gains in the first half of 2017, with China the stand out performer this quarter. Equally, North American and European markets enjoyed strong gains whilst UK markets also nudged up over the quarter. On the commodities front, oil prices rocketed up, recovering their heavy losses from the previous quarter as well as some precious metals also performing well. Brazil had the best performing equities market with a notable mention for Russian equities also among the other top performers.

The main event that dominated this quarter was the geopolitical tension between North Korea and the USA which resulted in North Korea launching a missile over Japan in August. Tropical storm Harvey also influenced US equity markets. Towards the end of the quarter, markets drew strength from the continuing global economic upswing and the chance of major corporate tax cuts in the US.

Brexit negotiations are likely to continue over the next year along with Trump continuing with his new reforms in the USA. In Europe, the focus is on the upcoming European Central Bank governing council meeting in late October. In Japan, Prime Minister Shinzo Abe called a snap general election on the 22nd October with the lead up and result of this likely to have an impact on Japanese equities. For the rest of the world, corporate earnings and macroeconomic data is likely to weigh in on respective markets.



How will Political Tensions Between North Korea with North America and Japan effect Markets?

Tensions between the secretive North Korean state and the United States have been a topic of major global concern in the past few months. North Korea has been making a big show of what it perceives to be its military might, with a major display of troops and missiles taking place in Pyongyang to celebrate the nation's 105th anniversary.

In a major show of defiance to the international community, North Korea fired a ballistic missile over the northern Japanese island of Hokkaido in mid-September. This launch was the second to fly over Japan in less than a month, and the first since North Korea's sixth nuclear test and since new United Nations sanctions on the country.

North Korea is a Stalinist Communist state, and sees itself as an enemy of the USA, recently vowing that they will go to war with Trump's America if they have to. A statement from Kim Jong-un has been quoted as saying that "all the brigandish provocative moves by the US will thoroughly be foiled." Trump, however, has said that North Korea is a "problem that will be taken care of," and has flexed America's military muscle somewhat too, by ordering the USS Karl Vinson aircraft carrier to be dispatched to the Korean peninsula. North Korea also has issues with Japan, with missile tests performed by North Korea in March causing four military projectiles to enter the economic zone. Shinzo Abe, the Japanese Prime Minister, reacted by calling the move "an extremely dangerous action".

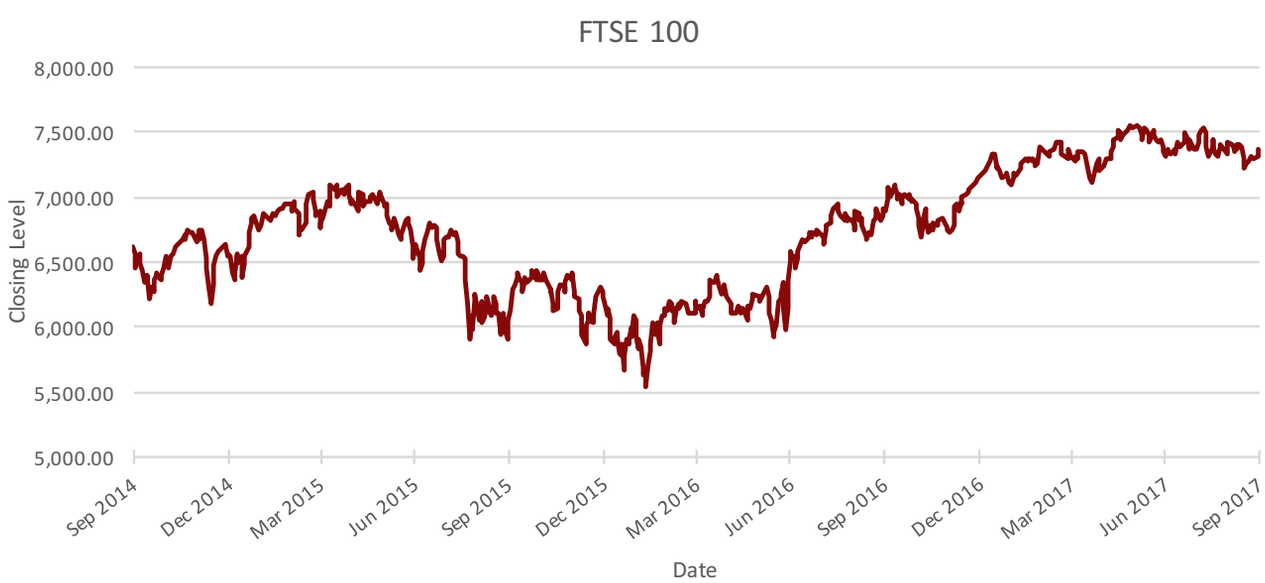
The political tensions could have a negative impact of Japanese equities. This is because the Japanese Yen is seen as a safe haven currency investment. The yen has increased in price against the South Korean won since early April, indicating that investors are seeing a need to put money into safe havens in the current climate. While this may sound like a good thing for Japan, Prime Minister Shinzo Abe has been striving for economic strategies that keep the price of the yen down in order to foster more export related growth. Therefore, if the Yen continues to creep up, it could have a negative impact on the earnings of the large exporting companies in Japan.

Another country that could be affected by these political tensions is China. Around 90% of North Korea's international trade is carried out with China, and so if China chooses to further restrict trade with them, then this could put a huge amount of pressure on Kim Jong-un. The effects of the North Korean situation on their trade, currencies and share dealing have an impact all over the world thanks to their dealings with China, Japan and South Korea, which have significant repercussions on international financial markets.
Equally, as the US seems to be preparing for the 'cold war' with North Korea turning quite quickly into an actual war, their economy—and therefore the economy of the West—is far from safe from significant North Korea related volatility.

Despite the political tensions, global markets have continued to perform well this year. However, the political tensions have caused short term volatility and if it continues to grow could have a negative impact on markets. The EB Partnership has had an overweight allocation towards Japan and Asia this year and our portfolios have benefited from the strong performance within these areas. However, given the current ongoing political tensions, we believe having a diversified portfolio will help to reduce the risk associated to specific regions that may be affected.

MARKET COMMENTARY

1. UK

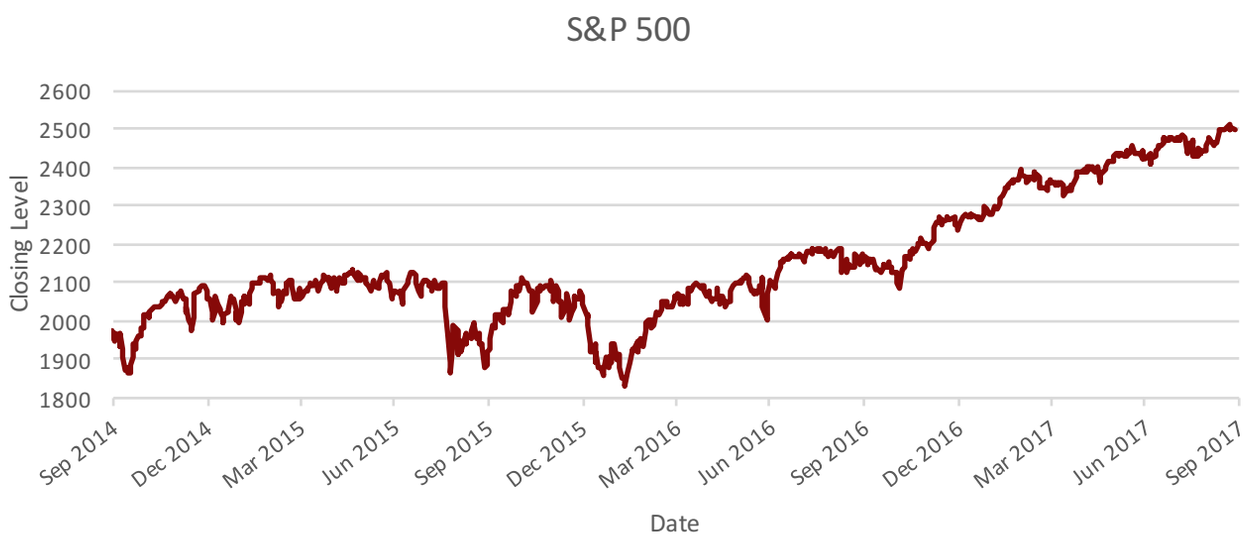


The Office for National Statistics (ONS) reported that UK GDP grew 0.3% during the third quarter of 2017 remaining the same as the previous quarter. UK unemployment fell by 75,000 in the three months to July, bringing the jobless rate down to 4.3% from 4.4% in the previous quarter. This quarter has also seen inflation, as measured by the Consumer Prices Index (CPI), increase by 2.9% year-on-year in August which is above the Bank of England's 2% target. However, weekly earnings increases including bonuses stayed the same at 2.1%.

UK equity markets remained broadly flat over the quarter, with the FTSE 100 ending slightly up 0.8% and FTSE All-Share up 1.2%. Growing tensions between US and North Korea added to nervousness in global markets and resulted in volatility in the UK markets. Although President Trump threatened to respond to North Korea's launch of a missile over Japan with "fire and fury" his actual response was muted which restored composure to markets. Sterling strengthened materially against the euro and the US dollar, particularly after the Bank of England (BoE) made clear its intention to 'ease its foot off the accelerator' with an expected interest rate rise in November which had a positive impact on UK markets. On the corporate news front, we saw profit warnings from WPP, Dixons Carphone and Provident financial which resulted in sharp share sell offs in their respective shares. On the other hand, JD Weatherspoon and Next released positively received updates.

UK markets have been fluctuating between the 7200 – 7500 over the last six months. Strength has come from the £ falling in value over the US $ with many of the large UK companies benefitting from their large revenues abroad. However, this effect has now been reflected in the UK markets and it is struggling to keep up with other regions. Although unemployment is falling, inflation is continuing to rise with wage growth not keeping up and economic growth is slowing. The EB Partnership therefore remains cautious and will maintain its underweight position on UK equities this quarter.

2. US



The US economy grew at an annual pace of 3.1% in the second quarter of 2017, faster than the 3% growth rate economists had been expecting. This is the highest since the first quarter of 2015 and followed a 1.2% pace rise in the previous quarter. August's 'non-farm payroll' rose by 156,000 which was well below the 180,000-economist consensus forecast. Interest rates remained constant at 1.25%. Inflation as measured by CPI increased at 1.9% in the year to August which was above the economists' forecast of 1.8%. The Labor Department said CPI rose 0.4% In August which is the largest in 7 months. The year-on-year wage growth was 2.5 % and has remained constant for a fifth consecutive month.

US equities performed well over the quarter with the S&P 500 up 4%, the Dow Jones up 4.9% and NASDAQ up 5.8%. Despite geopolitical tensions, the struggles of the Trump administration and Tropical Storm Harvey, the US equity market ended the quarter in positive territory. In August, unease spread amid rumours that President Trump's top economic adviser, Gary Cohen, would resign as chair of the National Economic Council. However, Mr Cohen, seen as one of the drivers behind President Trump's pro-growth agenda, did not resign. Instead it was controversial presidential adviser Steve Bannon who exited the White House, prompting an initial bounce in the US equity market. Market gains were propelled by the Republicans, unveiling a sweeping tax reform proposal aimed at lowering the corporate tax rate from 35% to 20%. The Fed said that it would stick with plans for further interest rate rises with another this year, probably in December, as well as 3 further increases in 2018. Financial, Energy and IT shares were the top performers this quarter, whilst Utility shares underperformed.

US equities are sustaining their impressive run. Economic growth bounced back this quarter and unemployment is continuing to fall albeit slower than forecasts. Inflation is picking up and is catching up to the stagnant wage growth. If Trump's proposed corporate reform is implemented, we expect it to increase profits for US companies and thus allowing firms to continue to expand their workforces. The Fed is planning further hikes in interest rates over the next year which is encouraging for the economy. Given the strong performance in US equities over the last few years, The EB partnership has concerns on whether this can continue. Therefore, we remain cautious on US equities but will be keeping a close eye on whether Trump is able to implement his tax reforms.

3. Europe

Eurozone equities performed well this quarter with the Paris CAC and German DAX both up 4% as well as the FTSEurofirst 300 Index up 2.2%. These gains were on the back of a string of encouraging economic data around Europe. GDP data from the second quarter 2017 showed Spain growing at its strongest pace in almost 2 years. Exports and investment have led France to its strongest continuous GDP expansion since 2011, while the Netherlands posted the fastest GDP growth since the end of 2007. Moreover, Italy, a country that has lagged behind its peers, is now showing encouraging signs and is expecting its GDP to increase by over 1% this year for the first time since 2010. From a sector perspective, healthcare and consumer goods performed well whilst consumer services and telecommunications underperformed.

On the macroeconomic front, Eurozone GDP remained robust at 0.6% in the second quarter, up from 0.5% in the first quarter. Eurozone GDP is now forecasted to rise 2.1% in 2017, up from 1.4% market consensus at the start of the year. The European Commission's economic sentiment indicator rose to 111.9, its highest level since July 2007. Unemployment in the eurozone remained at 9.1% in August - stable compared to July and the lowest rate since February 2009. August inflation figures were a step in the right direction with eurozone headline inflation climbing to 1.5% from 1.3% in the prior month. Core inflation (excluding volatile items) remained stable at 1.2%.

European markets have continued their strong performance this year. Economic growth has been promising and the smaller regions are also showing signs of optimism. With interest rates expected to increase in the UK the Euro dropped against the pound. Concerns over "Brexit" are ongoing and therefore The EB partnership remains neutral on Europe for this quarter but is encouraged by the fact that the smaller countries are producing strong growth figures to supplement the larger European constituents.

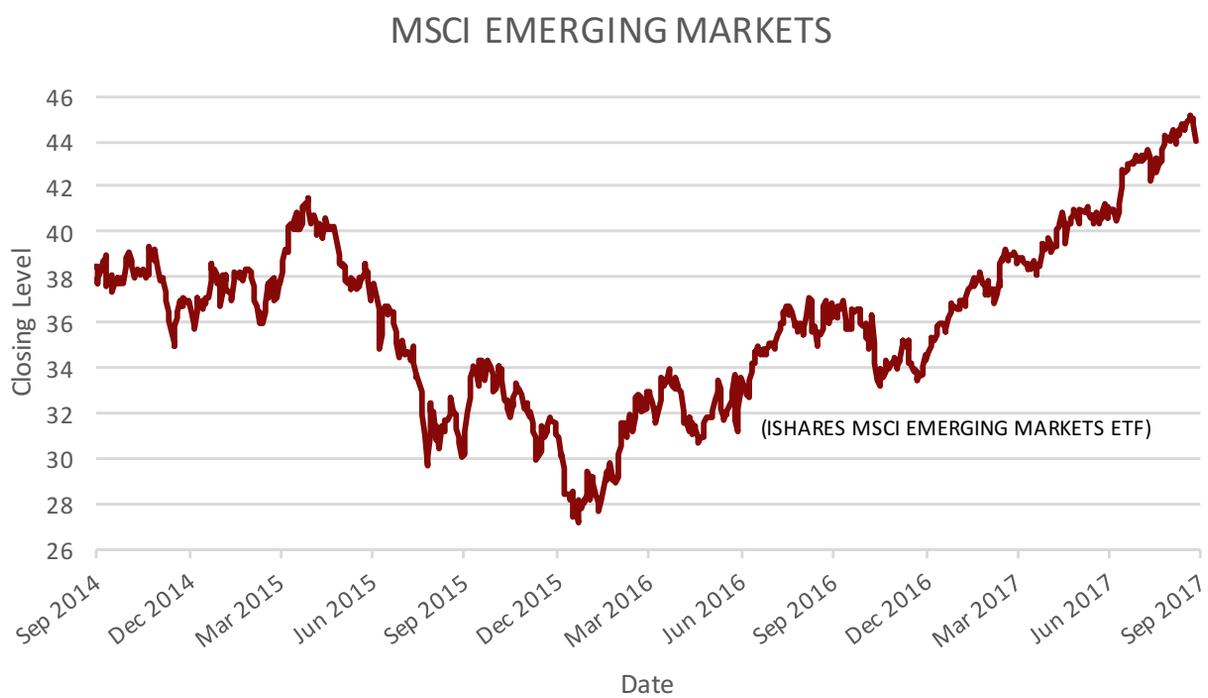
4. Japan

Japanese equities continued its upward trend this year with the Nikkei 225 up 1.6% in the third quarter of 2017. Although Japanese markets were under pressure early in August on renewed geopolitical risk on the Korean peninsula, which along with a decline in US Treasury yields resulted in Yen appreciation. However, the sell-off was short-lived and the market ended August with solid gains in local currency terms. Investor risk-appetite picked up again as US yields climbed and the Yen weakened. Markets climbed further after Prime Minister Shinzo Abe called a snap general election for 22 October, although the expected outcome is less certain now that Tokyo Governor Yuriko Koike has stepped forward to oppose Mr Abe as leader of a new party: The Party of Hope. Japan's equity market ended September marginally weaker due to tension between the US and North Korea and ongoing political uncertainty in the US. From a sector perspective, commodity-related and global cyclical sectors outperformed other areas of the market. On the other hand, the financial sector sharply underperformed.

On a macroeconomic front, statistics showed weaker than expected capital expenditure at large manufacturers in the second quarter, although manufacturing surveys remained positive. Industrial production increased by a good 2.1% month-on-month in August, while trade data showed that both imports and exports were strong. The Economy Watchers' Survey for August said that current conditions were steady, with some improvement in the outlook. Meanwhile, preliminary April-June real GDP was 4% quarter on quarter annualised, representing strong growth, well above the market consensus forecast of 2.5%.

Despite geopolitical tension between North Korea and the US, Japanese equities have continued with its bullish trend this year. With the Fed signalling another rate hike in the US before the end of the year as well as further hikes in 2018, the Yen is expected to continue to depreciate which is positive for the Japanese equities. The EB Partnership therefore maintains an overweight position but will be keeping a close tab on the build-up and outcome of the snap election result in October.

5. Emerging Markets



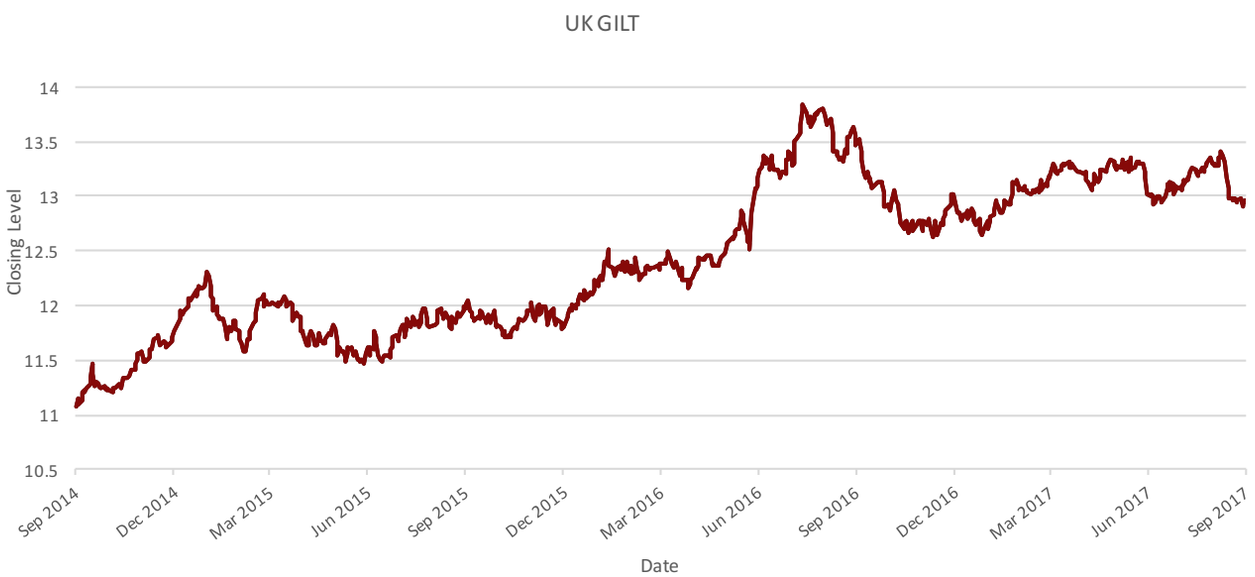
Emerging markets continued to outperform the rest of the world in the third quarter. Latin America led the gains, led by Brazil and Peru. Europe, Middle East and Africa equities also enjoyed stellar gains with Russia, Hungary and Poland being the individual winners. Asian equities were also positive but with greater volatility. China continued its upward trend while Korean markets bore the brunt of the unrest in the Korean Peninsula. Weakness was most pronounced in Greece and Turkey. From a sector perspective, financials and healthcare came out on top whilst telecoms underperformed.

Brazil's main index rocketed up over 18% during the quarter after macroeconomic data reaffirmed the growing view that the economy is finally back on the mend with retail sales, industrial production and employment numbers all above median expectations during August. Brazil's central bank reduced rates by 1% to 8.25% which provided further positive sentiment towards Brazil. The labour market continued to show signs of strength with new jobs being created and consumer confidence remaining stable at relatively high levels. On the political front, the dismissal of corruption charges against President Temer and the government's announcement to promote widespread privatisations were favourably received by financial markets. In Mexico, aside from a higher inflation figure, economic data was also generally upbeat as consumer confidence reached its highest level in the year and the unemployment rate fell to its lowest reading in over a decade. However, Mexico's returns were affected following 2 devastating earthquakes. Elsewhere in the region interest rates were cut by 0.25% to 5.25% in Colombia. Russian's main index also accelerated up over 13% on the back of a positive second quarter 2017 corporate earnings season and surging gas prices. Economic news from Russia was broadly positive with consumer inflation surprising on the downside with the headline rate falling to 3.9% versus consensus expectations of 4.3%. Russia's economic recovery appears to be gaining traction

with initial official estimates for quarter 2 GDP showing growth at 2.5% versus 1.7% expectations. Quarter 2 GDP growth also accelerated in the Czech Republic and marginally so in Poland but slowed in Hungary. South Africa's main index was up over 7% resulting from inflation falling to 4.6% from 5.1% and President Zuma surviving another vote of no-confidence, this time in a secret ballot. Equity performance in Asia was mixed with the Philippines and Thailand registering gains, whereas India and Taiwan both declined.

Emerging markets have continued to outperform developed areas for the fifth straight month. Economic news has continued to stay positive and corporate earnings has continued to impress. We are particularly impressed with the development of European emerging countries like Poland and Hungry and will be considering increasing our allocation to this area in the new year. We therefore maintain our 'overweight' position for this quarter.

6. Fixed Interest

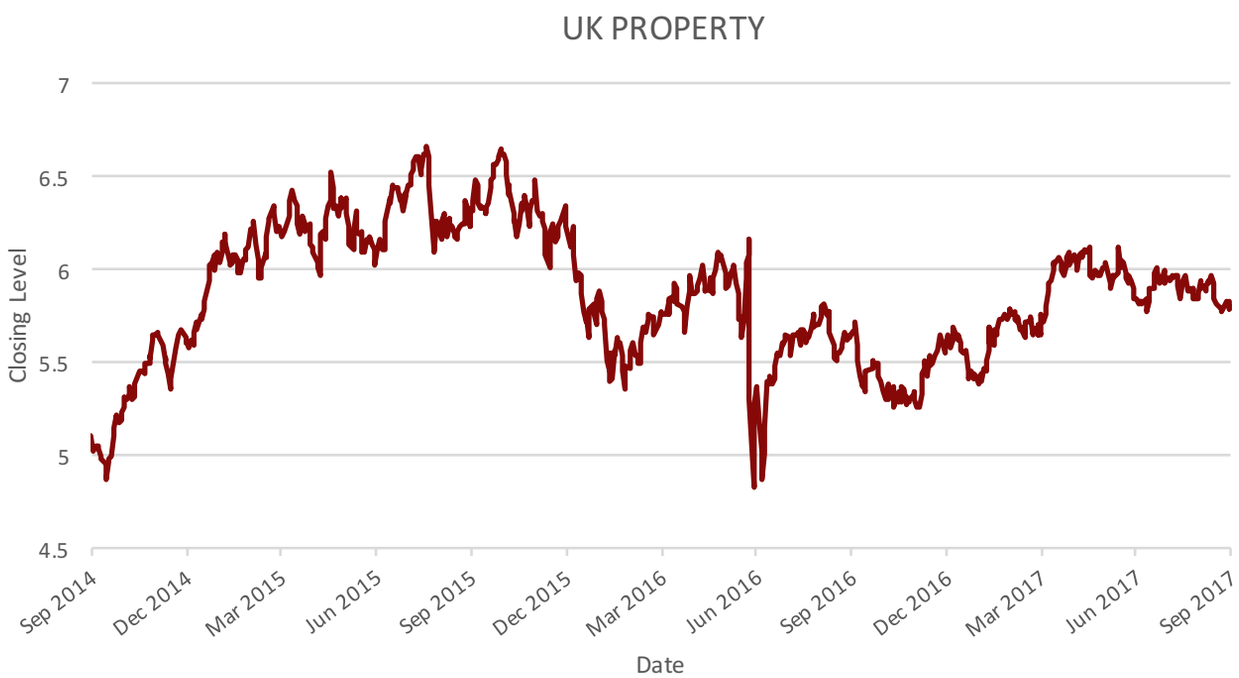


While Bond yields oscillated over the quarter, ultimately little changed thanks to a largely unchanged global economic backdrop. The one exception was the UK which sold-off sharply in September. Yields moved lower in July and August, precipitated by 'safe haven' buying, before reversing course once more in September as risk appetite returned. US 10-year yields began the period at 2.31% and finished at 2.33% with German Bund 10-year yields virtually unchanged from 0.47% to 0.46%. 10-year UK gilt yields rose 0.1% to 1.36%. The move reflected higher inflation and more hawkish central bank rhetoric. Corporate bonds made positive returns, outperforming government bonds. Global investment grade (IG) credit rose 1.14% and high yield bonds increased by 2.16%. The US investment grade bonds gained 1.37% and High Yield bonds 2.04%.

Various events and news impacted the bond markets over the quarter. The global economic upswing continued with data confirming the US second quarter growth rebound. The "Goldilocks" scenario of steady economic growth, rising asset prices combined with only moderate inflation remained in place. The Federal Reserve announced it will commence the reduction of its balance sheet at a rate of $10 billion a month from October. The European Central Bank (ECB) gave indications it is preparing to taper its quantitative easing. The quarter saw a marked escalation in tensions between the US and North Korea. The tensions were a key factor behind the temporary rotation into lower-risk assets in August. During the quarter however, there was little policy progress, although a framework tax reform plan, largely confirming plans for significant tax cuts, was unveiled in late September. For the UK, the economy showed clear signs of slowing down, while inflation picked up. The Bank of England struck a more hawkish note with Governor Carney and a number of members of the Monetary Policy Committee openly discussing rate rises. This occurred against a backdrop of above target inflation and low unemployment, leading to a significant increase in UK government bond yields.

Bond yields are marginally up over the quarter with corporate bonds outperforming gilt returns. However, the Bank of England and Federal Reserve are planning rate increases over the next year which are likely to have a negative impact on bond prices and yields. Therefore, we will continue with our 'underweight' position to fixed interest.

7. Property

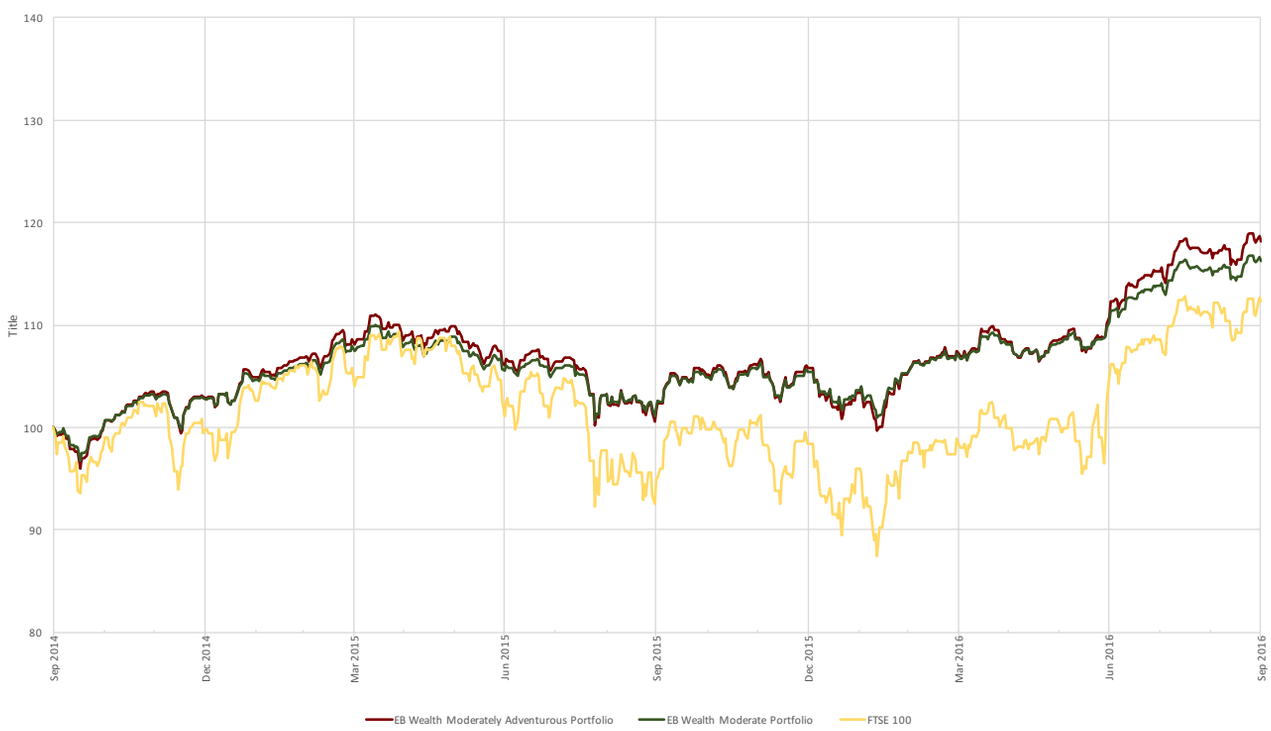


Commercial property showed a slight improvement relative to the previous quarter. Investor and occupier demand edged up over the quarter along with near term capital values and rental growth expectations more positive. Industrials are continuing to outperform whilst the retail market continues to struggle.

Tenant demand increased strongly across industrial space, and after falling in the office sector in the previous quarter it managed to stabilise this quarter. However, demand fell for a second consecutive quarter in the retail sector. Availability of leasable space declined over the quarter in the industrial sector, whilst hardly moving in the other sectors. Near term rent expectations point to firm growth in the industrial sector, and a broadly flat outturn for office rental values. In the retail segment, projections remain marginally negative at the headline level. London is again the exception, where negative projections in the office and retail sectors are cancelling out positive expectations for industrial rents. Over the year ahead, rental expectations are positive for both prime and secondary industrial space. The same is true for prime offices and to a lesser extent prime retail space. The outlook for secondary offices remains flat. Conversely, the results for secondary retail were firmly negative, with rents still anticipated to decline over the coming twelve months. With regards to the UK regional breakdown, short term rent expectations are generally positive across all sectors.

Although commercial property has performed better this quarter, sentiment and yields are generally very low and projections for the retail and office sub sectors are especially pessimistic. Therefore, we maintain our current 'underweight' position on property.

EB Wealth Portfolio Performance



The above graph shows the performance of our Self Invested Personal Pension (SIPP) portfolios including a 25% weighting into a basket of structured products which were recommended to clients over the same period.

Due to the close ended nature of structured products, not all clients can be invested into the same products and will therefore not have received the same returns. The graph above shows the average returns our clients would have received were they to have invested in our moderate or moderately adventurous portfolio, including the average returns they would have received from the structured product element of their portfolio.

OUR TACTICAL ALLOCATION

Sector	Forecast	Action	Morningstar Moderately Adventurous Allocation %	Tactical Overlay %	Final Allocation %
US	Unfavourable	Underweight	11	-2	9
UK Large Cap	Unfavourable	Underweight	22	-1	21
UK Mid Cap	Unfavourable	Underweight	8	-1	7
UK Small Cap	Unfavourable	Underweight	5	-1	4
Europe	Fair	Neutral	13	0	13
Japan	Favourable	Overweight	7	+3	10
Asia	Unfavourable	Underweight	4	-1	3
Emerging Markets	Fair	Overweight	9	+1	10
Commodities	Fair	Neutral	5	0	5
Global Fixed Income	Unfavourable	Underweight	2	-1	1
UK Gilts	Unfavourable	Underweight	2	-1	1
UK Corporate Bonds	Unfavourable	Underweight	2	-1	1
UK Inflation-Indexed	Unfavourable	Underweight	2	-1	1
Property	Unfavourable	Underweight	5	-1	4
Cash	Favourable	Overweight	3	+7	10

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