ATRAM

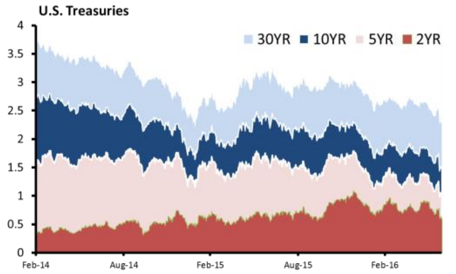
Investment Outlook

Global economy and markets

After a rocky start, global risk markets rallied for the good part of the first half of 2016, until June 23rd when British voters narrowly approved a referendum to leave the EU. "BREXIT" reignited uncertainty and volatility in global markets. Global bond yields fell to record lows, the British pound fell to a 31-year low versus the dollar. Global equity markets plunged post-BREXIT but within a little over a week gained back much of what they lost. We expect global markets to remain volatile in the third quarter. The rally in global equities can be mostly attributed to an expansion in valuation multiples (ie P/E, P/B ratios). Given the current trend of declining corporate earnings growth, the upside to global stocks remain limited. For stock prices to go even higher, investors need to see an improvement in the corporate earnings outlook. Meanwhile, long-term global bond yields at multi-decade lows show no signs of turning any time soon. With various central banks still with an easing bias (via negative interest rates), any U.S. rate hikes are likely to cause the dollar to appreciate significantly. Despite better U.S. economic growth, higher inflation and a tighter labor market, we do not expect the Fed to be in any hurry to raise interest rates once again. While global economic growth remains lackluster however, the probability of a U.S. recession remains low.

Developed Market Bonds

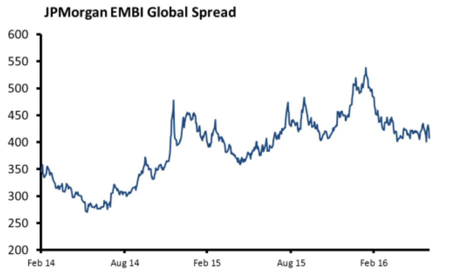
Bond markets were broadly up in the second quarter due to investor risk aversion, with US 10-year yields reaching 3-year lows and German 10-year yields reaching negative territory in late June for the first time. We expect to see continued downward pressure on US Treasury bond yields in response to the increasingly desperate efforts of central banks to engineer growth. In this lower-for-longer global interest rate environment, investment grade corporates are preferable to developed market sovereign debt due to the incremental spread. The key risk is upward pressure on US inflation which can trigger one Fed rate hike in the second half of the year.



Source: Bloomberg

Emerging Market Bonds

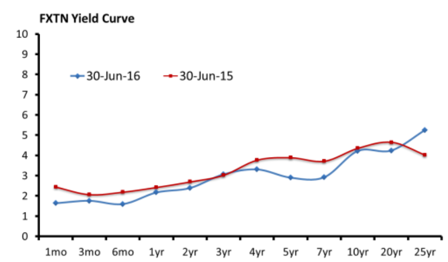
Extremely loose global monetary policy should intensify the search for yield among investors and emerging market (EM) dollar bonds should continue to benefit. A key risk would be a sudden tightening of U.S. monetary policy. Yields of local EM debt have followed the lead of US Treasuries this year, accounting for roughly 2/3 of the year-to-date return on the asset class. Similarly, we do not expect a significant further rally in local yields but we also see limited risk of rising yields. Local currency strength have the potential to become a significant driver of positive returns for local EM debt in the coming months.



Source: Bloomberg

Philippine Bonds

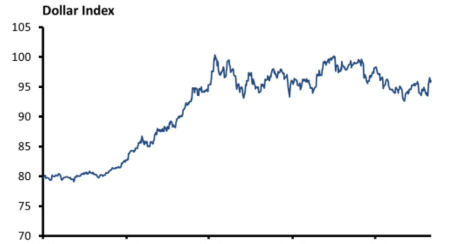
There is no compelling reason for the Bangko Sentral ng Pilipinas (BSP) to change policy settings anytime soon. Growth is expected to be better than in 2015 with domestic demand supported by fiscal spending and private sector investments. Liquidity remains adequate with continued oversubscription of the term deposit auctions introduced by the central bank in the second quarter. While inflation has been well within the BSP's 2-4% target for the year, cost-push pressures from the supply side and fiscally-induced price pressures may force the BSP to adjust its policy stance. We see the most relative value in medium-tenor issues among Philippine Government Securities.



Source: Bloomberg

Currencies

The Philippine Peso reversed previous gains and weakened by 2% against the US dollar in the second quarter of 2016. The exchange rate hit a low of 47.24 pesos to the US dollar amid some panic selling prior to the national elections in May. It bounced back close to the 46 level on the back of a landslide victory and strong popular mandate of new President Rodrigo Duterte. The trend of a weaker USD against Asian currencies may persist in the short term but we believe the long-term theme of broad-based USD strength remains intact and see a weaker PHP at 47-48.



Source: Bloomberg

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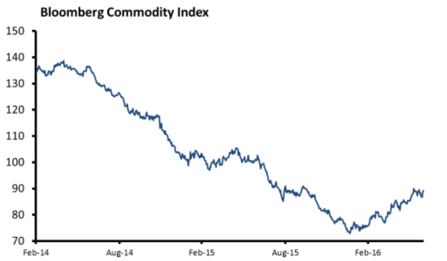
Global economy and markets

Commodities

Oil markets remain on track to tighten up in the third quarter, despite the short-term concerns about growth following the UK's BREXIT vote. While the first half of 2016's imbalances have tightened up following a surge in unplanned outages, the bigger-picture shift underway to tighter market conditions will be driven by structural, rather than temporary, factors in the third quarter. For base metals, prices traded above expectations, seemingly immune to weaker Chinese macro data, higher production and export rates and BREXIT. Looking forward, for this quarter, further global monetary easing remains a potentially large upside risk.



Source: Bloomberg

Developed Market Equities

Fundamentals need to improve to sustainably push the S&P 500 Index past all-time highs. US equities could grind higher on multiple expansion alone but we are less optimistic with the business cycle in its later stages and political risks looming. Meanwhile, strong returns in Europe's sovereign and corporate bond markets this year have not trickled into their equity markets. Even after the bounce in global equities post BREXIT vote, European stocks continue to look very cheap on many measures, especially compared to U.S. stocks, and European earnings remain below peak levels with potential room to improve.

Source: Bloomberg

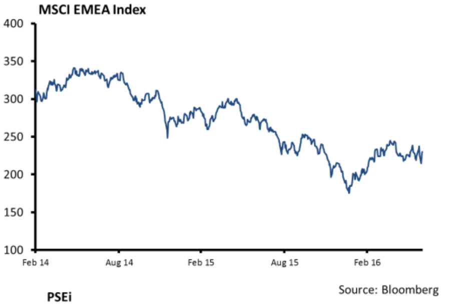
Asia ex-Japan (AxJ) Equities

Asian stocks have stabilized after panic selling ensued summer last year on a surprise depreciation by the People's Bank of China (PBoC) and as concerns that higher interest rates in the U.S. will erode credit in emerging markets. We see Asian stocks consolidating while slowly drifting upward in the third quarter as money flows back into the market on the region's value proposition. As fears of a Chinese hard landing dissipate and as more economic data show that the Chinese economy is stable, equity markets in the Asian region as a whole should benefit.

Source: Bloomberg

Emerging Market Equities

A positive result of the BREXIT vote is that EM, despite fragile investor sentiment and uncertainty, performed relatively well. EM equities, as represented by the MSCI EM Index, were up just under 1% in the last quarter and have generated respectable returns in 2016, up more than 6%. In contrast, developed markets, represented by the MSCI EAFE Index, have fallen more than 4% this year. The rebound in EM equities since February has been driven in part by a rebound in local currencies, itself a result of the recovery in commodity prices. Attractive valuations can be found in EM but commodity prices remains a key risk, alongside political issues and weak corporate earnings.



Source: Bloomberg

Philippine Equities

The Philippine Stock Exchange index (PSEi) rallied 7.35% last quarter on the back of the successful and relatively clean national elections. The new administration was successful in reassuring investors about its intention to focus on infrastructure spending, and tax reform. Property, infrastructure and consumer sectors stand to benefit the most in the medium term. Based on technicals, the index may continue to test the all-time high of 8,127 given the strong foreign fund interest in the country. Negative market catalysts such as central bank actions and earnings disappointments may cause a correction in the prevailing uptrend.

Source: Bloomberg

Index/Currency	Price as of Jun 30	Percent Change		
		QoQ	YTD	YoY
MSCI World Index	1,653.2	0.3%	-0.6%	-4.7%
MSCI AC Asia ex Japan Index	503.67	-0.8%	0.7%	-14.2%
MSCI EMEA Index	230.71	-2.1%	9.8%	-16.7%
PSEi	7,796.3	7.4%	12.1%	3.1%
USD / PHP	47.16	2.6%	0.5%	4.6%
USD / JPY	103.20	-8.3%	-14.2%	-15.8%
EUR / USD	1.1106	-2.4%	2.2%	-0.4%

Source: Bloomberg

Security	Yield as of Jun 30	Change in Yield (bps)		
		QoQ	YTD	YoY
US Treasuries 2YR	0.58	-14	-47	-6
US Treasuries 5YR	1.00	-21	-76	-65
US Treasuries 10YR	1.47	-30	-80	-88
US Treasuries 30YR	2.28	-33	-73	-84
PHIL. FXTN 2YR	2.39	-108	-160	-31
PHIL. FXTN 5YR	2.90	-56	-103	-99
PHIL. FXTN 10YR	4.22	-47	12	-14
PHIL. FXTN 20YR	4.24	-99	-128	-41

Source: Bloomberg

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