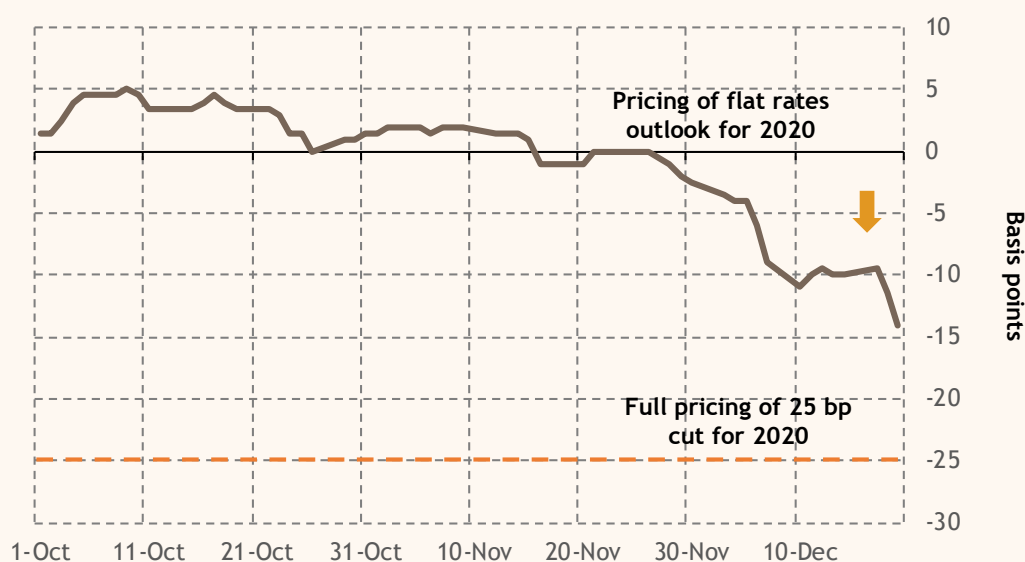


Key Economic Figures/Events of the Week

- This year's last Fed meeting scheduled for 19 December 2018 was the central event for the markets this week. The interest rate was raised by 0.25% to 2.5% in line with the expectations. Analysts found the commentary from Jerome Powell a bit less dovish than they would like it to be, as the Fed chief reaffirmed commitment to further rate hikes and continued balance sheet reduction. Nevertheless FOMC members lowered their expectations toward two rate hikes in 2019 and one more hike in 2020, while market prices a rate cut in 2020. Our base-case scenario for the next year is the same: we expect two rate hikes of 0.25% each.

Market began to price in FED rate decrease in 2020



- The US treasury yields responded by taking a big dip, with the 10-year and 30-year treasuries closing Thursday (20 December) below 2.81% and 3.05%, respectively. Euro strengthened against US dollar and closed Thursday above 1.144. Credit spreads narrowed a bit on the back of general market optimism, with the prices for many bonds going up by 1-2%.
- Italy reached a deal with the European Commission over its 2019 budget. The parties agreed on the deficit target of 2.04%, down from the 2.4% initially asserted by Rome. This sparked a rally in the Italian debt market, with the 10-year sovereign bond yields dropping to 2.7% from the mid-November high of 3.6%. We have moderate exposure to Italian bonds and are set to benefit from the achieved compromise.

Weekly Investment Insights

- On 18 December, Fitch downgraded Oman's credit rating to BB+, one notch below the investment grade. In its commentary, the rating agency noted that despite a recovery in oil prices the country's high budget deficit continues to drive the sovereign debt up. As a result, Oman's bond prices dropped by an average of 3%. Oman's bonds account for roughly 2% of our total allocations. We will continue to hold them expecting to see renewed support for the bonds from the EMBI inclusion slated for January 2019.

- On 19 December, the US Department of the Treasury's Office of Foreign Assets Control (OFAC) announced its intention to terminate the sanctions imposed on Rusal, En+ Group and EuroSibEnergO in 30 days. "These companies have committed to significantly diminish Deripaska's ownership and sever his control," the statement says. Even though Oleg Deripaska remains under the US sanctions, this step is likely to boost the investment case of Russian bonds which had been previously shunned by international investors due to the risk of further US sanctions. Our exposure in this segment remains stable at 10-15% offering a yield to maturity of 5% for the instruments with four-year duration. In our opinion, such returns are commensurate with the risk.

Strategy

This week, we purchased USD denominated bonds of Enel, an Italian energy company (BBB+/Baa2), maturing in 2039 and offering a yield to maturity of 6.0%. Enel's bonds had dropped by over 10% amid the Italian crisis. We believe that they have a significant upside potential now that the budget deal has been reached between the EU and Italy.

Starting next week and until the beginning of January, liquidity will be hard to come by in the markets due to the upcoming holidays. We would like to take this opportunity to wish you all a merry Christmas and happy New Year! Our next review will be released in January.

We hope you find this information useful and will be glad to answer your questions

AXIOMA Wealth Management AG
Bleicherweg 45, CH-8002 Zurich
Tel.: + 41 43 305 07 10
info@axiomag.ch
www.axiomag.ch



Verband Schweizerischer Vermögensverwalter | VSV
Association Suisse des Gérants de Fortune | ASV
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