FLEURUS INVESTMENT ADVISORY

November 4, 2015

Overview

During the month of October the US equity markets rallied from 5.6% to 8.4%. The S&P's 500 Total Return Index rose 8.4%, the Russell Mid Cap Index was up 8.1% and the Russell 2000, 5.6%. Similarly, a major market rebound across international markets caused developed and emerging markets indices to shoot up anywhere from 6.0% to 7.5%. US Bonds prices were mostly flat across sectors.

Our four target portfolios rose from 3.3% to 4.9%. On a YTD basis, our performances across portfolios range from 1.6% to 2.0%, net of fees. This compares to a 1.9% YTD performance for a portfolio consisting of 50% S&Ps' 500 Total Return Index and 50% US bond aggregate.

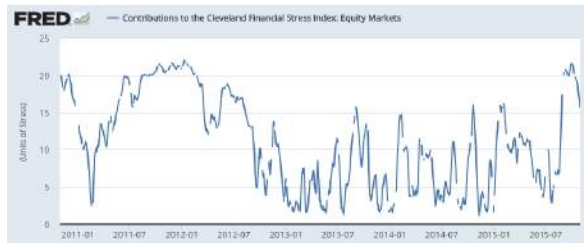
Market developments

An 8% monthly rebound in equities is a rather exceptional occurrence. It is particularly interesting to note that this violent upswing started during the very last days of September, when a not-insignificant number of market pundits were discussing the beginning of a bear market. The future will tell whether we are in one or not, but it sure does not feel like it right now.

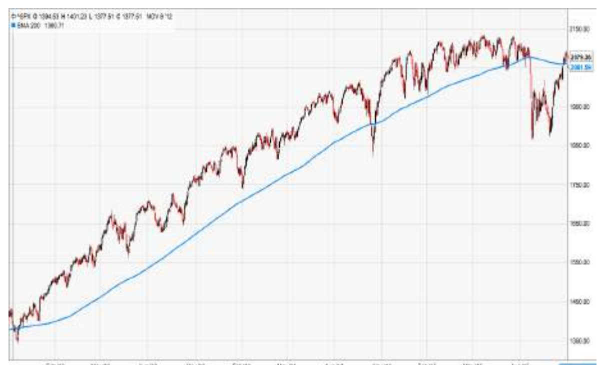
When we try to make sense out of this market action it seems that a confluence of fundamental and technical factors combined to make this unexpected market surge possible.

As far as fundamental factors are concerned, we can point at the following: Oil prices rose meaningfully in the first week of the month causing emerging market currencies to rally. Adding to this positive sentiment, the views on China's economy gradually shifted from "very negative" to "may be not so bad after all". Central Banks around the world, from China to the ECB and the Bank of Japan, either implemented or talked of more easing measures. Finally, quarterly earnings came in without significant negative surprises and offered even some very positive ones in the technology sector (Amazon, Microsoft, Apple).

As a result, the level of risk in equity markets has dropped significantly, as illustrated by the Federal Reserve Stress Index chart below:



As far as technical factors are concerned, part of the explanation for the October rebound may be found in the chart below.



At the end of August, the S&P's 500 dropped to a level of about 1860-1870 (first leg down) before bouncing back just before the Fed's decision on interest rates of September 16. It dropped again to that level at the end of September (second leg down). On both occasions, the rebound took place around the low of October 2014, 1850.

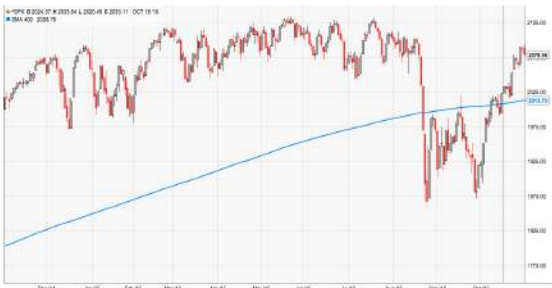
Could a chartist have anticipated this rebound? Yes. Could it have been anticipated with a sufficiently high degree of confidence that would have caused us to redeploy cash right then and there? No.

A support level is only a support level until it is no longer one!

That said, by mid-month, the combination of fundamental and technical factors was sufficiently robust in our eyes to justify a prudent reallocation to equities.

Tilts and Allocations

Specifically, we started redeploying cash to equities when the S&P's 500 broke its 400 moving average level (at the intersection of the vertical line and the blue line below):



Once that technical level was broken we started buying the Russell Mid Cap Growth Index with a view to bringing our US equity allocation to target. As of this writing, we are mid-way there and will continue buying over the next weeks if the uptrend endures.

We followed the same approach with international equities and started buying anew EZU (Eurozone ETF) and deploying cash to Japan via EWJ, an ETF that tracks the performance of large Japanese equities. Both ETFs are on key technical levels as illustrated below.

We bought EZU when it crossed its 50-days moving average (blue line) and anticipate doing more buying once it crosses the orange line (100 day moving average).

We moved in a similar fashion with EWJ, as illustrated below:

We will increase our exposure if and when the 100-day moving average is broken to the upside.

Concluding Remarks

We are in a volatile environment! When markets go down by close to 10% and up by as much in the space of a few weeks, it is crucial to integrate technical and behavioral factors into one's thinking before taking any investment action, hence our unusually high reliance on charts this past month. We expect technical factors to inform most of our actions throughout the rest of the year.

This volatile state of affairs results in good measure from the diverging policies conducted by the Fed and other central banks in the world. While we, in the USA, are positioned to tighten monetary policy (albeit very slightly), the ECB, BOJ and Bank of China are in a loosening mode. This causes currency movements and capital flows that fluctuate with the slightest central banker's utterance.

The resulting market volatility is likely to endure until the Fed finally moves, hopefully in mid-December. Once this is out of the way we expect volatility to subside and markets to become somewhat more predictable.

Meanwhile, the US economy is chugging along, the nihilistic faction in Congress seems to be (temporarily) under control, allowing for some basic and sensible pieces of legislation to pass and the Eurozone is showing signs of life. In that general context, we remain prudently optimistic and plan to reallocate to equities as opportunities arise.

As usual, please feel free to provide your feedback.
All the best.