KBC Invest Newsletter

4th Edition, 2018

Welcome to the final 2018 edition of our KBC Invest Newsletter

2018 has been a year of seismic shifting events from around the world – from Trump's tirades, trade wars, Brexit, and yield curves. These issues have many investors wondering how they can better protect themselves against growing uncertainty and still reach their financial goals. But all is not doom and gloom - we're currently in one of the longest running bull markets in history. In this newsletter, we'll discuss what investors can do in these times of volatility including diversification and managing emotions, but first, an update on what's happening out there.

Brexit: How did we get here?

The UK voted to leave the EU in 2016; invoked Art.50 and is now due to leave the EU on 29th March 2019.

If an agreement on exit terms cannot be arrived at by the March deadline, there will then be a total severance between the EU & the UK – a so called 'hard' Brexit. This means that, overnight, the UK would no longer be a member of the EU.

Prime Minister Theresa May has managed to negotiate a Brexit deal with the EU, under which, the UK will pay a 'farewell premium' to EU and remain part of a customs union until the end of 2020 with the ability to further extend this. A special regime would also apply to Northern Ireland (the 'backstop') meaning that a hard border would not be needed.

Resistance to this deal within the governing party has led to dismissals and resignations of ministers, the postponement of a vote on the deal and now, a vote of no confidence in the Prime Minister. So the going is definitely tough!

Hard Brexit

With a hard Brexit, trade in goods would fall back on regulations within the World Trade Organisation rules. What this means is:

- Higher import costs on goods,
- A likely fall in the value of the British Pound,
- Restrictions on labour mobility and investment

A hard Brexit could have an extremely negative impact on the UK economy, between -5% and -7.8% of Gross Domestic Product according to the IMF. Within the EU, Ireland would be particularly affected; with Belgium and Central Europe also more affected due to volumes of trade and proximity.

Our View

The chance of a hard Brexit seems limited but is increasing; we think that the possible impact on the British economy is too great to run this risk. But, time is ticking and approval in the British Parliament is proving extremely difficult. New negotiations with EU are highly unlikely so it's really a matter of whether or not Prime Minister May can weather the storm and gather support for the current proposal.

We view a 'soft but not so smooth Brexit' as most likely at this stage, i.e. a last minute approval and long transitional period.

Inverse yield curve

Due to uncertainty surrounding inflation and economic growth, bond investors typically look for higher yields on longer maturities so you'd expect the yield on a 10 year bond to be higher than on a 2 year bond. In recent days, the difference between the two has narrowed to 0.13%. Historically, when the 2 year yield exceeds the 10 year, a recession has followed so the short distance between them has caused nervousness.

In historical terms, however, any sharp slowdown in growth follows on average 21 months after such an event. A downturn in growth is therefore not imminent. Economists also question whether the yield curve is still a good predictor of a recession. Due to bonds being bought by the central banks, the long-term rate is lower than normal, while ageing and the continued low level of inflation are also putting pressure on rates.

The trade conflict

This remains the number one problem for the markets. Any communication about it – whether positive or negative – always leads to sizeable reactions on the stock markets.

The biggest dispute continues to be the China/America trade relationship. A breakthrough was expected at the G20 summit in Argentina. The 'ceasefire' agreement between Trump and Xi Jinping was initially positively received by the markets, but the sentiment reversed the more it was interpreted as a non-deal.

We expect tensions between America and China to persist. They clearly have an impact and weigh on the prospects for growth, but are not such as to trigger a global recession.

KBC

Summary

We have Brexit marked as one of the main risks which are discussed/reviewed monthly (more often if required). Our current view is that Brexit will continue to create uncertainty but a deal will be reached. Additionally, we have a negative recommendation on GBP and UK government bonds also as a result of the Brexit risk.

Elsewhere, the global economy continues to be strong, which for the time being is still the most important indicator for the stock markets. The US is by far the strongest growing region, with fears of a recession appearing unfounded in the light of the economic data. However, we need to continue paying very close attention to developments in the trade conflict. The turnaround in sentiment prompted a very sharp correction on the stock markets. Combine the above with what are still very robust operating results, and the stock markets still look quite attractive. The positive fundamentals, therefore, enable us to see through the problems in Europe and the trade conflict and lead us to a rather positive view of shares, with an emphasis on Europe.

Diversification, diversification, diversification …

Diversification is possibly the most overused word when it comes to investing – but what is it and how does it help? You've probably heard the phrase "don't put all your eggs in one basket" – well, that's really all that diversification means. At its core it's the simple idea that by spreading your money across a number of different things, you can help reduce the degree of the inevitable up and downs that will occur over time.

Traditionally, investments diversify by spreading your money across asset classes (for example, shares, Bonds, cash etc.) and also within those asset classes (different company shares, bonds from different governments and companies, different currencies). For example, a standard balanced investment fund with KBC can comprise of around 3,000 different components. This approach can really help limit the effect that an underperforming stock can have on the value of your money.

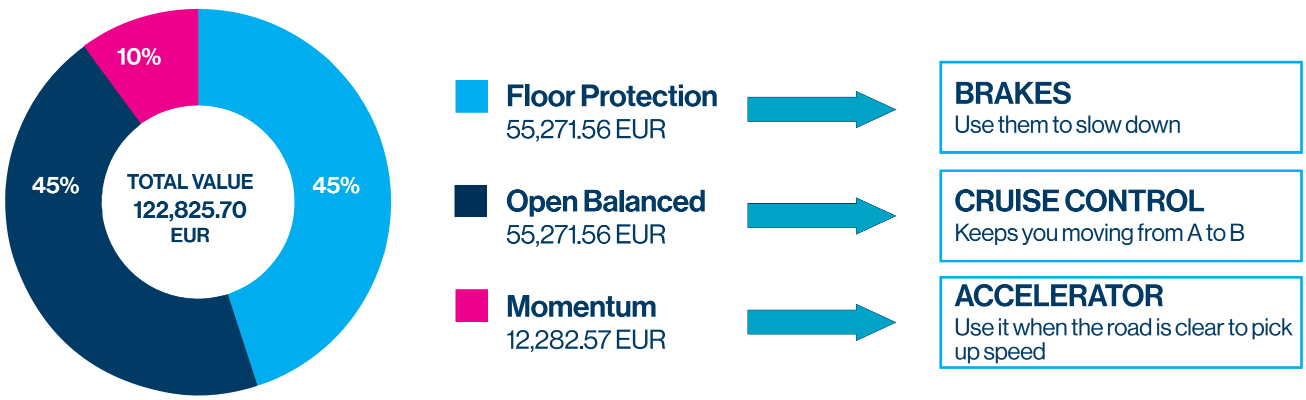
At KBC, we believe in the power of diversification so strongly that we have taken it to a new level. As well as the traditional diversification approach, we also encourage investors to diversify across different management styles. Investors who take this approach have a much better chance of staying within their individual comfort zones while they invest for the medium to long term.

Broadly speaking, we have three different families of funds – Open Balanced, Floor Protected and Momentum, each of which has a different job to do depending on whether markets are rising, falling or even a bit flat. You can think of them in terms of a car:

Open Balanced – This is like your cruise control, keeping you moving on a clear road without requiring much input from you.

Floor Protected – This is like your brake pedal – at times where you may be a little more cautious, this technique can help you slow down a little.

Momentum – This is like your accelerator which can help you get to your destination a little sooner – when the road conditions are good!



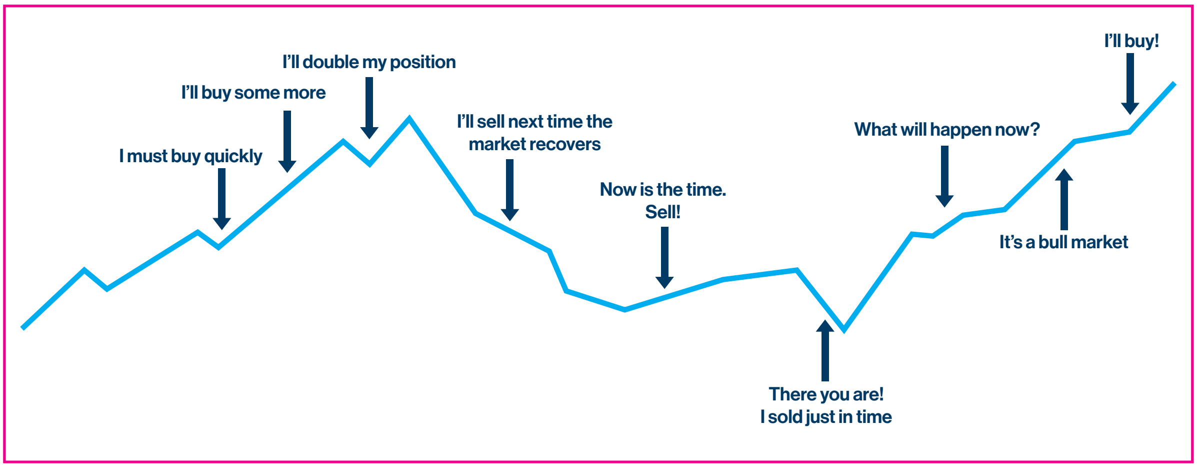
It's important to realise that the goal of diversification isn't to maximise your returns but rather to limit the extent by which the value of your investment may rise or fall. A well thought-out investment will use diversification to help ensure that you strike the right balance between being comfortable with your investment and making a return.

Investing and emotion

Sometimes, when it comes to money, it's easy to forget that we are all human. If we only thought about investments from a purely financial view, we would only invest our money when the markets fall because buying things when they are cheap is better than buying the same things when they are expensive.

However, we are not emotionless when it comes to money – especially money that we may have worked hard to earn. When confronted with a volatile market, it takes a great degree of courage and faith to make the decision to invest. All too often, instead we wait for markets to return to strong growth before we're comfortable to make the leap.

The illustration below shows the path that many investors take:

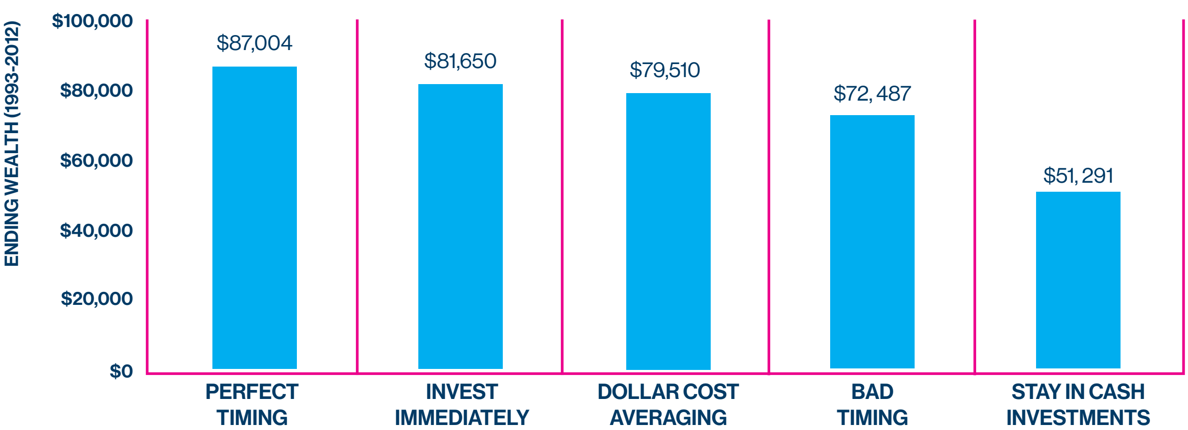


Of course, it's very hard, if not impossible, to change human nature and, besides, even if we could, retaining a sense of emotion is not necessarily a bad thing – it's part of who we are and should be considered an important part of investing. There are, however, a few things that we can do to increase our chances of reaching our investment goals while remaining comfortable during our investment timeframe.

The illustration below shows how an investor given $2,000 to invest each year in the S&P 500 index over a 20 year period would have fared out in different scenarios. The first investor picked the perfect time to invest every year, the second invested all the money immediately, the third spread it out in equal amounts during the year, the fourth picked the worst time every year and the fifth didn't invest at all – preferring to remain in cash.

We can pretty much discount numbers 1 & 4 as it's virtually impossible to pick the perfect/worst times correctly for 20 years in a row. Of the remaining two investors, the person who invested immediately did get a better return but not by a huge amount and, bear in mind, they may have had to make some brave decisions to invest over that 20 year term as we see above.

The regular investor "dollar cost averaging" was a very close runner up and, in making the decision to feed the money in regularly over the period, also reduced the likelihood of being influenced by emotion. By investing small amounts regularly, you can smooth out your returns over time and avoid many of the emotional pitfalls associated with investing.



Want to learn more? Now may be a good time to speak with one of our investment specialists about ways to prepare your portfolio for 2019.

November Privileged Portfolio Pro Reset

After management fee and other ongoing charges. Source of data: KBC Asset Management.

	31st October 2017		31st October 2018		
Fund Name	**NAV**	**Floor Level**	**NAV**	**Floor Level**	**Change**
Privileged Portfolio PRO 95 November	316.10	300.30	303.48	288.31	-3.99%
Privileged Portfolio PRO 90 November	335.44	301.90	315.74	284.17	-5.87%
Privileged Portfolio PRO 85 November	363.20	308.72	338.99	288.14	-6.67%

Our November Tranche of the Privileged Portfolio Pro Funds reset downwards on 31st October. Despite a challenging calendar year which saw much volatility and some heavy falls, all three funds delivered on their primary objective of protecting their floors becoming fully invested once more on 1st November.

Call in to one of our investment specialists and see how adding floor protection to your investments can help you weather times of uncertainty.

What to do next

Would you like to find out more about Savings and Investments but aren't sure where to start? Contact your local investment specialist.

Pop in to a Hub

1800 51 52 53

kbc.ie

The investment strategy described in this document relates to all investment funds (undertakings for collective investment) managed by KBC Asset Management NV, which make explicit reference in their investment policy, as laid out in the prospectus, to KBC Asset Management's investment strategy. The stated strategy is not, therefore, altered in the case of other investment funds, the investment policy of which does not refer directly to KBC Asset Management's investment strategy. It is possible that these investment funds are managed in a way that differs from the investment strategy. You should always read the prospectus and the Key Investor Information Document for the relevant investment fund.

Warning: Past Performance is not a reliable guide to future performance

Warning: This fund may be affected by changes in currency rates

Warning: If you invest in this product you may lose some or all of the money

Warning: The value of your investment may go down as well as up

The term "fund" refers to a sub-fund or a Bevek under Belgian law, a sub-fund of a Sicav under Luxembourg law or a mutual fund under Belgian law. Performance figures are based on investment returns. The calculation of past performance includes all charges and fees, except taxes and entry charges. The assets of this fund may be used for the purposes of securities lending in order to earn an additional return of the fund. While securities lending increases the level of risk within the fund, it can also provide an opportunity to increase the investment return.

Tax: Investors should note that the tax legislation which applies to the Fund may have an impact on the personal tax position of your investment in the Fund. KBC Bank Ireland plc is regulated by the Central Bank of Ireland.