WAVERTON

INVESTMENT MANAGEMENT

WAVERTON CAUTIOUS INCOME FUND

OUTLOOK FOR 2017

Political Risks

As we look around the world, 2017 looks to be another year whose outcome will be dominated by political rhetoric and action (or lack thereof, as the case may be).

In Europe, the Brexit process will roll on, with the Supreme Court yet to come to its decision as to whether Article 50 can legally be enacted without prior Parliamentary approval, and detailed withdrawal negotiations – yet to begin – likely to be a protracted affair. In addition, by GDP, more than 40% of Europe goes to the polls in 2017 to vote in their respective leaders. France may well see the appointment of (generally) pro-business Mr. Fillon, while Merkel in Germany must push back against AfD's anti-immigration stance. Will 2017 see an extension of the anti-establishment stance, or will cooler heads prevail? It would be intellectually dishonest to say we knew the answer, however the ensuing months will provide further policy details and the public's reaction thereto, which in turn will offer us analysable information from which we can determine how best to position the fund.

The key political risk to the global economy seems to be President Elect **Trump**, and despite an unusually high-profile pre-inauguration period, important questions remain, namely:

(1) Will domestic policy (infrastructure and tax cuts) dominate foreign policy (China-stealing-our-jobs, trade policy, Mexican immigrants) in the minds of investors? and
(2) Can Trump even implement what he has indicated he will?

The domination of domestic policy over foreign policy will mean strong risk-asset performance, particularly in the US, while Trump being able to implement effectively will intensify the effect. However, concerns about foreign policy may make investors waver, and any indication that Trump will struggle to implement policy will only heighten uncertainty. Trump's first 100 days will provide a lens through which we will get a glimpse of a future with Mr. Trump as President. They will provide important information to financial markets, and we will be watching closely.

Asia and Emerging Markets also see political risks, some as a result of their own political topography, some by virtue of their relationships with China and the US in particular. For commodity-producing nations, China will remain the marginal buyer of product (Trump has proposed $1tn of infrastructure spending over 10 years, China spent this in the first 9 months of 2016 alone). In addition, for many EM and Asian companies China is often either the final destination for goods and services or a key node in the supply chain. Political risks also abound as regards US trade policy; will the new administration enact trade barriers? Will trade agreements be abandoned or rewritten, and if the latter, how so? What will the effect of a protectionist policy be on the Dollar, and how, in turn, will this effect emerging economies and companies? Again, Trump's first 100 days will be telling.

Economic Risks

Economic risks also abound in 2017. Indeed, many of the risks of 2015 and '16 remain, despite being less prominent in the financial press. **China's** credit problems coupled with slowing growth, dependence on property and infrastructure investment and continued pressure on the capital account (in turn affecting the Yuan and China's foreign exchange reserves) are risks to China's and, by extension, the global economy (China remains the largest direct contributor to global growth, while its position within the global supply chain makes its health all the more important to the global economy).

If for any reason global growth is weak, it is likely that **Europe** will suffer, principally as a result of its economic structure but also due to the boost that "alternative" political parties will gain from the perception that the status quo isn't working for Main Street.

Further risks lie in US rising interest rate policy in particular, and the effect of a stronger Dollar on Emerging Markets in particular.

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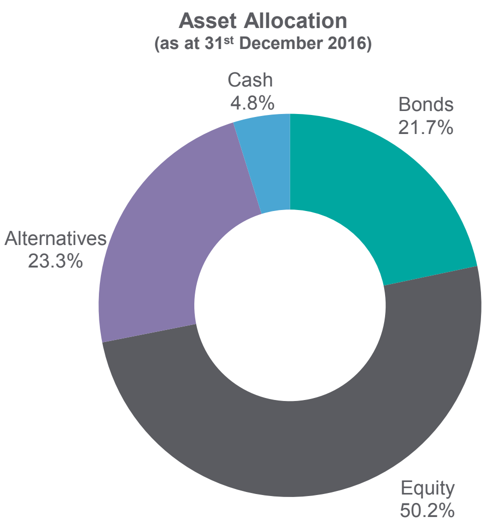
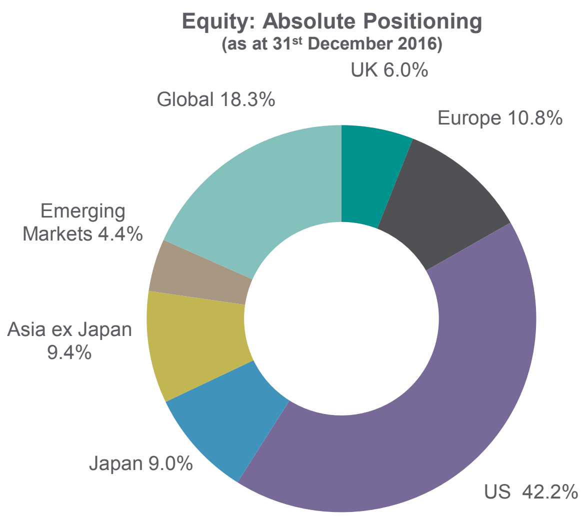
In the Cautious Income Fund …

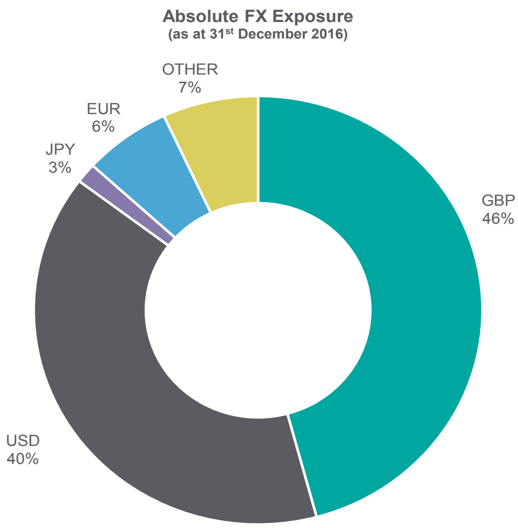
Thematically, c.22% of the fund is positioned to outperform in a pro-growth, reflationary world, while the remainder of the fund is broadly defensively positioned.

In the Cautious Income Fund we currently hold 50.2% in Equity, 42% of which (i.e. 21.2% of the Fund) is in the US, taking the view that the Trump administration will be able to accomplish substantially most of its intended domestic policies, in particular its infrastructure spend and corporate tax cuts.





Across all asset classes, we are currently 40% exposed to the Dollar and 46% to Sterling (including cash holdings).



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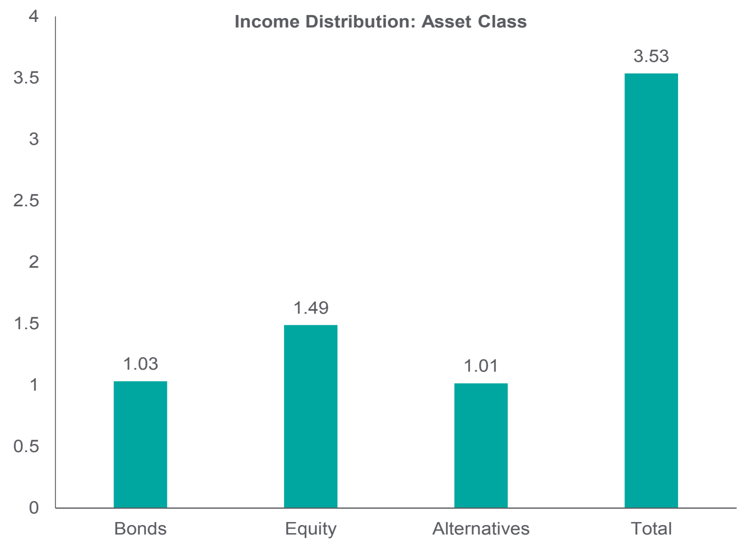
Within fixed income we hold 3% in direct Gilts and ETFs, with the majority of the remaining 22.7% allocation in short-dated securities, thus limiting the overall duration of the fund. This benefitted us during the bond-market sell-off, and given our outlook for 2017 we expect to maintain similar positioning throughout.

Within Alternatives, we hold non-yielding hedging positions, and to diversify across our High Volatility, Low Volatility and Asset Backed buckets, with a preference for the latter (16% of the Fund). We continue to see interesting opportunities in the Alternatives space and highlight the importance of the asset class in diversifying both capital and income sources for the fund.

As regards income, we project a 3.5% income yield in 2017 according to current allocations (04/01/2017)*.



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*Investors should note that yields on investments may fall or rise dependent on the performance of the underlying investment and more specifically the performance of financial markets. As such, no warranty can be given that the expressed yields will consistently attain such levels over any given period.
Changes in the rate of exchange may have an adverse effect on the value, price, or income of an investment. For full details of investment risks please refer to the Prospectus. A copy of the full prospectus and the KIID is available from Waverton Investment Management or Administrator, RBC Investor Services. (Ireland)