3EDGE Asset Management

Investor Letter **Quarter ended March 31, 2017**

For the quarterly period ended 03/31/2017 (Q1-2017), both the **3EDGE Total Return Strategy** and **3EDGE Conservative Strategy** earned positive rates of return. Gains from our holdings in U.S. equities, global equities, Japan equities-currency hedged (Total Return strategy), India equities (Total Return strategy), emerging and frontier market equities (Total Return strategy), gold and fixed income more than offset a slight decline in our commodities position.

The U.S. equity markets began the first quarter on a strong note, reflecting the hope that following the U.S. elections in November, fiscal stimulus (tax reform, deregulation and infrastructure spending) could fuel a more rapid rise in economic growth. Our analysis also determined that narrowing credit spreads, a sufficiently steep yield curve and a stable U.S. Dollar could be supportive of equity markets. On March 15th, the Federal Reserve hiked short-term interest rates by 25 basis points, its third upward move since the financial crisis. Before the announcement, recommendations for a rate hike were telegraphed by members of the Fed, reducing the element of surprise. Fed chair Janet Yellen indicated that she still sees U.S. monetary policy as accommodative, and until the economy and inflation rise more rapidly, a gradual approach to monetary tightening is warranted. The equity markets responded favorably as investors interpreted the move as a "dovish hike".

Just after the U.S. elections, we expressed our view that the market was likely to enter a "hope phase" (based upon the perceived benefits of fiscal stimulus) followed by a "reality" phase, which could be unfavorable if the expected increase in economic growth failed to materialize. Given the failure of the new administration's first attempt to repeal and replace Obamacare, investors are beginning to doubt whether a fiscal stimulus package will be enacted by a gridlocked Congress, potentially harming the prospects of U.S. equities that were poised to benefit. At the same time, while the Fed is attempting to normalize monetary policy and tighten rates, the world's other major central banks are continuing their policies of monetary accommodation. Since the financial crisis of 2008, U.S. equity markets have significantly outperformed non-U.S. equity markets benefiting from an earlier and more sustained policy of monetary stimulus from the Fed. However, now that non-U.S. central banks are promoting monetary policies that are more accommodative than the Fed, non-U.S. equity markets may have an opportunity to reverse years of underperformance. In fact, many non-U.S. equity markets did begin to outperform U.S. equities during the first quarter of 2017, and we have continued to increase our non-U.S. equity allocation as a share of our overall equity holdings.

Investors continue to speculate whether so-called "animal spirits" may have finally taken hold of the global economy and capital markets, thereby helping to justify current equity market valuations. In our analysis, one important signal of the return of long-awaited animal spirits would be an increase in money velocity, which has not yet materialized. Money velocity is a measure of the degree to which money changes hands in the real economy. It collapsed during the financial crisis of 2008 and has remained low ever since. The potential for increasing money velocity and the rekindling of animal spirits is doubly important since it may not only reflect positive changes in the economy and the markets, but could also serve as a driver of both. In the face of rising equity markets since the election, particularly in the U.S., economic and financial data has remained somewhat mixed. The so-called soft data, such as consumer and business sentiment, has been encouraging, but the hard data such as GDP and other measures of economic strength have been inconsistent at best.

Looking ahead into the second quarter and the remainder of 2017, the case for a continuation of rising equity markets would be supported by a growing global economy, rising corporate profits, narrow (favorable) credit spreads and positively-sloped yield curves, all of which could attract more cash into the equity markets from the sidelines, thereby driving equity markets higher. History has shown that equity markets that may appear to be overvalued have the potential to extend their gains for longer than "rational" investors might expect. For example, the Fed declared in 1996 that the U.S. equity markets had become irrationally exuberant, however U.S. equities continued to rise sharply until peaking in March of 2000. However, history also shows that the higher the markets rise, particularly if the rise occurs in a compressed timeframe, the more painful the inevitable market correction may be. The failure of pro-growth U.S. fiscal policies to materialize, a slowing of U.S. GDP growth, and/or a reduction of loan and credit growth could signal the onset of an unexpected credit contraction, and the potential for an equity market correction. As of March 31st, our research favors global equities (both U.S. and ex-U.S.) on a risk-adjusted return basis over fixed income, real assets and cash.

We are continuing to watch a myriad of potential risks to investors including the following: potential legislative gridlock in Washington which stymies attempts at fiscal stimulus; the possibility of a foreign policy miscalculation given rising military aggression by North Korea, Syria, Russia, Iran, China and other parties; as well as the upcoming elections and referendums in France, Germany and Italy which could have major implications for the future viability of the European Union. We will also be closely monitoring how any additional rate hikes in 2017 affect expected real (inflation-adjusted) interest rates to gauge whether the U.S. Dollar is likely to strengthen in a sustained fashion or whether real assets may have an opportunity to appreciate.

The 3EDGE approach to portfolio management prioritizes risk management and seeks to limit potential portfolio drawdowns. We believe that investment portfolios need protection from a variety of possible "fat tail" or "black swan" events. However, we also believe that going forward, it will still be possible to generate attractive, risk-adjusted returns by continuing to follow our investment discipline of seeking to identify undervalued asset classes across the globe that may be poised to enter a period of market outperformance.

As always, please feel free to reach out to us if you have any questions, and thank you for the confidence that you have placed in our firm.

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