Investor Letter

Quarter ended June 30, 2017

For the quarterly period ended 06/30/2017 (Q2-2017), 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, Europe equities (Total Return strategy), India equities (Total Return strategy), emerging and frontier market equities (Total Return strategy), and fixed income more than offset a slight decline in our Japan equities-currency hedged (Total Return strategy), gold, commodities and TIP positions.

During the second quarter of 2017, equity markets continued to move higher. Although U.S. equities performed well, non-U.S. equities, particularly in Europe and Emerging Markets, began to outperform U.S. equities, an occurrence not common since the Financial Crisis of 2008. This relative outperformance may be explained by a combination of factors, including investor concerns about stretched U.S. equity valuations, the potential for deepening dysfunction in both the Trump administration and U.S. Congress and further evidence of European economic growth rates coming in above market expectations. Equities in Europe strengthened further following the French election of Emanuel Macron in early May.

Recently, we have become a bit more cautious in our outlook for equities in general as our model research is now indicating the potential for lower projected risk-adjusted rates of return for global equities in the future. After the recent meeting of the world's central banks in Portugal, it now appears that the U.S. Federal Reserve, the European Central Bank and the Bank of England will be moving ahead with a coordinated effort to normalize their monetary policies, unwinding the unprecedented quantitative easing that has been in place for many years. Even though it isn't clear exactly when each of these central banks will begin to implement their normalization plans, what does seem clear is their intention to signal to the markets that unwinding of quantitative easing is imminent. In fact, just the suggestion of normalization has recently begun to push bond yields higher. The Bank of Japan, however, is signaling that they are content to diverge from the world's major central banks and have signaled their intention to continue with extraordinary monetary policy for the time being. The potential for monetary policy divergence could contribute to a further weakening of the Japanese yen, which could help Japan's export-driven companies and in turn its economy to grow and possibly move Japan's inflation rate to a more satisfactory level.

Another potential cause for concern for the global equity markets going forward is the shifting nature of what has likely driven recent gains. Our analysis indicates that equity markets have more recently been responding to investor behavioral factors (i.e. positive market performance drawing more cash from the sidelines, leading to higher prices in a positive feedback loop) rather than economic and fundamental factors. This can lead to a riskier environment since there always exists the potential for these behavioral factors to not only fade rapidly under certain circumstances, but to reverse course, leading to self-reinforced selling. Of course, there could also be surprises to the upside if, for example, the upcoming U.S. corporate earnings season turns out to be stronger than expected, thereby supporting further gains in U.S. equities.

Looking ahead into the third 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, a continuation of narrow (favorable) credit spreads and positively-sloped yield curves, all of which could support higher equity markets. However, a risk to further equity market appreciation is the future direction of central bank policy decisions during the remainder of 2017. Should the recent pronouncements by the U.S. Federal Reserve, the European Central Bank and the Bank of England begin to materialize into actual policy action, this could prove to be a formidable headwind for equities for the remainder of 2017. Further, continued failure to enact pro-growth U.S. fiscal policies and tax reform, a slowing of U.S. GDP growth, a reduction of loan and credit growth, rising credit spreads and flattening or inverted yield curves could also signal the onset of an unexpected credit contraction and the potential for an equity market correction.

Although our model research has recently indicated lower projected risk-adjusted rates of return for equities in general, equities (both U.S. and ex-U.S.) on a projected risk-adjusted return basis continue to be ranked more favorably than other major asset groups including fixed income, real assets and cash at this time.

We are continuing to watch a myriad of potential risks to investors including the geopolitical tensions between North Korea and the U.S., particularly in the aftermath of North Korea's launch of an ICBM on July 4^{th}. The current tense situation in the Korean peninsula also involves many other countries including South Korea, China, Japan and Russia. Additional risks to the global capital markets include the potential for scandals involving the Trump administration as well as legislative gridlock which stymies attempts to enact fiscal stimulus and tax reform legislation. We will also be closely monitoring how any additional rate hikes and the potential for the unwinding of quantitative easing may 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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