Centre Funds Insight – Fall/Winter 2015 Market Review & Outlook – Multi-Asset Fund

For the one year period ended September 30, 2015, Fixed Income as an asset class contributed positively to the Fund's return as did Real Estate Linked Securities. U.S. Equities, Non-U.S. Equities and, in particular, Commodity-Linked Securities as asset classes performed poorly over the period as they were negatively impacted by a strengthening U.S. dollar and concerns over global economic growth, particularly in heavy resource consuming foreign economies, most notably in the emerging markets. During the period, our tactical allocation to Fixed Income and non-Equities was increased and our exposure to Commodity-Linked Securities, except for those linked to the price of gold, was eliminated. We also eliminated our exposure to Real Estate-Linked Securities as we've seen their correlation to other asset classes increase and valuations reach levels that we deemed unattractive.

Our process in managing the Fund remains flexible and allows us to opportunistically shift emphasis to each of the various asset classes as conditions warrant based upon the ability for each asset class to perform best during particular market environments. For example and as noted, during the period we increased our exposure to Fixed Income and eliminated our exposure to all industrial Commodity-Linked securities. Incorporating asset classes such as Commodity-Linked ETNs[1] and ETFs[2], Real Estate Investment Trusts, and ETNs and ETFs with returns linked to REIT[3] Indexes, that are sometimes inversely or less correlated to U.S. stocks and bonds held within more traditional balanced funds, offers enhanced diversification benefits and the ability to take advantage of the changes in asset class performance that may take place with changes in different inflationary or deflationary environments. The Fund is designed to help reduce the level of risk that comes from concentrating in a single asset class. Additionally, we aim to emphasize asset classes we believe are poised to perform best based on our understanding of how different asset classes respond to the level of inflation or deflation and changes in economic conditions. The result is a broadly diversified portfolio that may be used as a core flexible balanced type holding or as a complement to existing equity or fixed income strategies. Also, given that certain historical correlations between asset classes tend to change, particularly during periods of market stress, the Fund is able to take defensive positions in an attempt to respond to adverse market, economic, political, or other conditions when deemed tactically prudent.

With competing inflationary and deflationary forces in a "tug of war", namely ultra-accommodative monetary policy now in its seventh year and aging demographics with the baby boomer generation just beginning to retire in earnest, respectively, we think the longer-term risk of inflation is higher than it has been in quite some time. However we also recognize that short- and intermediate-term market signals such as an appreciating U.S. dollar, economic weakness globally and slack industrial capacity have given deflationary pressures the upper hand and will continue to do so. The irony is that we expect inflation to increase only after a sustained period of deflation which may result in a change in central bank and fiscal policies that target nominal growth with, perhaps, a near abandonment of inflation stability.

In our view, the failure of U.S. fiscal policy to stimulate growth has caused dependency on this unprecedented and massive monetary easing that shows no sign of abating. The U.S. Federal Reserve has continued to postpone the normalization of its ultra-accommodative policies. On a positive note, monetary policy has allowed the U.S. financial sector to heal distinct from the tremendous restructuring undertaken by business and consumer focused corporate America. That said, it is unlikely that monetary policy will

[1] An exchange traded note (ETN) is a type of unsecured, unsubordinated debt security that was first issued by Barclays Bank PLC. This type of debt security differs from other types of bonds and notes because ETN returns are based upon the performance of a market index minus applicable fees, no period coupon payments are distributed and no principal protections exists.

[2] An ETF, or exchange traded fund, is a marketable security that tracks an index, a commodity, bonds, or a basket of assets like an index fund.

[3] A security that sells like a stock on the major exchanges and invests in real estate directly, either through properties or mortgages. REITs receive special tax considerations and typically offer investors high yields, as well as a highly liquid method of investing in real estate.

suddenly transmit growth stimulus to the real economy (as opposed to financial assets) when it has not in the past seven years given the collapse in monetary velocity[4]. The vast bulk of the Federal Reserve's bond purchases have made their way right back in the form of bank reserves deposited at the Federal Reserve and the nearly 300 percent increase in the money supply has been offset by the collapse in velocity. If velocity should turn up however, the outlook for inflation should rise and do so substantially. At the present time, this seems unlikely given the weak demand for credit and the riskless option afforded to banks to earn interest on their capital reserves placed on deposit with the Federal Reserve.

On the deflationary side, in a number of industrialized countries, including the U.S., on the assumption that fertility remains at or close to present levels, populations will start to decline and, in some cases, do so quite rapidly in the near future. The impact on developed societies will be decreasing demand for goods and services and increasing pension liabilities. This can be crushing in terms of taxation on younger workers and a potential source of unrest and political disruption. Japan, the pathfinder of this phenomenon as it embraced Western family planning even before Europe and the U.S. and where adult diapers now outsell those for children, shows the debilitative impact from an aging society and need to resort to new radical inflationary macroeconomic policies to combat its ill effects. No developed world country is immune from this significant problem which is just starting to be felt in Europe, the U.S., and elsewhere. With regard to near-term relevance to Federal Reserve policies, we see that the U.S. Civilian Labor Force Participation Rate has dropped below a level that we last saw thirty years ago, when women began to join the workforce in earnest. A large part of the current fall in the unemployment rate has been due to this "dropping out" of the labor force, either due to discouragement, early retirement, or more generous public assistance programs. This collapse in the civilian workforce participation rate and increase in the number of persons on government dependency since the economic recovery began in 2009 have never happened before during previous recoveries. In addition, productivity now is at the lowest levels seen since the late 1970's. Furthermore, the growth in average hourly wages has fallen significantly as inflation has slowed and competition for jobs domestically and from overseas is limiting consumer consumption. This is evidenced by the latest drop in consumer spending being consistent only with past recessions.

Current market conditions and trends have created a myriad of possible outcomes over the next few years that are likely to contribute to a rise in the level and volatility of long-term inflation expectations, but only after a sustained period of deflation. This is due to the negative macro circumstances being unlike any in the past and our lack of confidence in the ability of public officials to manage them given the unprecedented fiscal and monetary policy employed thus far and without the expected efficacy as seen in the past. The Centre Multi-Asset Real Return Fund will attempt to deliver on maintaining investor purchasing power of today's dollar in nominal terms plus a positive real return on capital by using its tactical flexibility across broad asset classes with the added ability to take defensive positions under volatile market conditions and when the potential for large drawdowns is perceived to be highest.

[4] The rate at which money is exchanged from one transaction to another, and how much a unit of currency is used in a given period of time. Velocity of money is usually measured as a ratio of GNP to a country's total supply of money.

Centre Funds

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Disclosures

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