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# VIEWPOINT

## Newsflash

A new month and the 88th issue of Viewpoint from **Financial Partners**.

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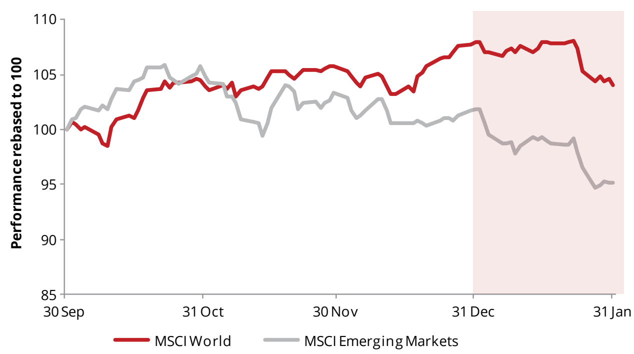
## Market Commentary

Emerging market woes, which came to the fore after the Federal Reserve's first tapering comments in May 2013, finally spread to developed markets in January. The problems of the fragile five (Turkey, Brazil, India, Indonesia and South Africa) spread much more widely in January, as concerns about reduced dollar liquidity, the withdrawal of funds from developing countries, slowing growth across much of the developing world and country specific issues combined to produce sharp falls in EM currencies and stock markets. This, together with some slightly disappointing growth data from the US, led to a risk off period globally, with developed market equities also falling sharply as the month progressed.

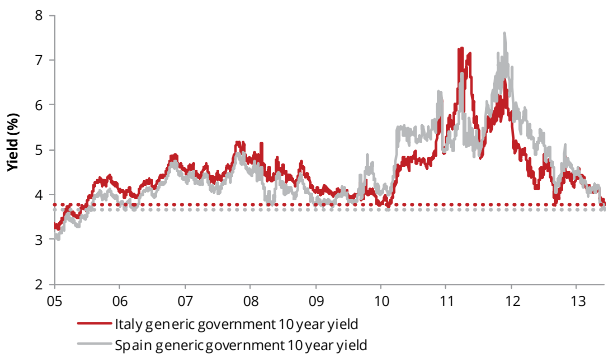
*Figure 1: Global equity markets fall back at the start of 2014*




Equity markets suffered their worst start to a calendar year in five years, with the MSCI World index declining by 3.7% and the MSCI Global Emerging Markets index down by 6.5% (with Latin America falling by almost 10%). All markets suffered in the sell-off, although Japan was the weakest of the majors (-6.3% in yen terms) while Europe and in particular peripheral Europe held up relatively well (-1.6% in euro terms). Meanwhile the US and the UK both fell by 3.6% in local currency terms.

As equities suffered, traditional safe haven government bonds instead rallied. 10 year treasuries, which ended 2013 with yields of over 3%, saw yields fall back to 2.7%, despite the decision by the US Federal Reserve to continue tapering its asset purchase programme by a further USD 10 billion. The JPMorgan Global Government Bond index returned 1.6% in January, with all major markets producing similar returns other than peripheral Europe, which performed particularly well as yields on Spanish and Italian bonds fell to levels not seen for eight years.

*Figure 2: Investor appetite for Spanish and Italian government bonds*




The positive performance of government bonds (which provide a reference rate for all other fixed income securities) prompted gains in credit markets, with investment grade bonds in the US returning 1.8%. High Yield, on the other hand, did less well amidst rising risk aversion, returning 0.7%, while emerging market debt fell by 1.6% to continue its poor performance from 2013.

Gold saw renewed interest from investors, with a return of 3.2% during the month, and the price appears to have found support at around USD 1,200. In contrast, other commodity markets fell as fears grew about growth in the developing world (oil -3.1%; copper -5.9%; aluminium -5.3%).

Currency markets were dominated by sharp falls for EM currencies. The South African rand depreciated by 5.6% versus the US dollar (Turkish lira -4.8%; Russian rouble -6.5%), while in Argentina the central bank took the decision to devalue the currency by the biggest amount in 12 years, as its foreign exchange reserves continued to decline. The yen, in contrast, was seen as a safe haven and rallied by 3.2% versus the dollar, a move which appears to have caught out many hedge fund managers who had been short the yen and long the Japanese stock market.

There was a series of bad news for developing countries – some specific such as the ongoing slowdown and weak data in China, mining strikes in South Africa, the devaluation of the Argentinean peso, political crises in Ukraine, Turkey and Thailand – but the big underlying issue remained (and remains) the challenge posed by the withdrawal of excess dollar liquidity. This has brought into sharp relief the critical need for structural reforms and rebalancing in many countries. Several countries, notably India, Brazil and Indonesia, had already raised interest rates in the course of 2013 but many more elected to hike rates in January, including Turkey (from 4.5% to 10%), South Africa and India. Inevitably this will lead to tougher economic conditions in 2014 across much of the developing world.

Data from the US has also slightly disappointed, although the picture is mixed and recent activity levels have undoubtedly been affected by severe winter weather conditions. PMIs have slipped slightly and December payrolls disappointed at only 75,000, while housing was weak but perhaps affected more than most industries by the weather.

There were more positive signs for Europe (although debt levels and unemployment both remain extremely high), as Ireland exited its bailout programme and several weaker members of the eurozone successfully raised debt funding in the markets.

The UK stands out as the best economic performer in Europe, with growth accelerating and spreading more widely. Job creation has been a notable feature of the economy, with the

*Source: Bloomberg. Returns in US dollars unless otherwise stated. January 2014.*

strongest jobs growth since 1999, bringing unemployment down close to the central bank's 7% target.

The fall in markets in January will no doubt blunt investors' optimism at the start of 2014. Many pundits had entered the new year forecasting a continuation of the strong performance from developed market equities and poor performance from bonds. The reverse has happened. Equity markets rose strongly in 2013 and price moves have at times outperformed underlying earnings. There are undoubtedly severe problems to overcome in the emerging world but we see opportunities being created by this setback and are looking to add to positions in hard currency EM debt as well as into equity markets on further weakness. The least risky opportunities remain in the developed world but as the year progresses there will be opportunities in emerging markets where valuations have fallen to increasingly attractive levels on a longer term horizon.

*Source: Bloomberg. Returns in US dollars unless otherwise stated. January 2014.*

# Market Performance

| Asset Class/Region | Index | To 31 January 2014 | | |
|---|---|---|---|---|
| | | Currency | Month | Year to date |
| **Equities** | | | | |
| UK - All Cap | MSCI UK NR | GBP | -3.6% | -3.6% |
| UK - Large Cap | MSCI UK LARGE CAP NR | GBP | -4.1% | -4.1% |
| UK - Mid Cap | MSCI UK MID CAP NR | GBP | -1.1% | -1.1% |
| UK - Small Cap | MSCI SMALL CAP NR | GBP | -1.4% | -1.4% |
| United States | S&P 500 NR | USD | -3.5% | -3.5% |
| Continental Europe | MSCI Europe ex UK NR | EUR | -1.6% | -1.6% |
| Japan | Topix TR | JPY | -6.3%* | -6.3%* |
| Asia Pacific (ex Japan) | MSCI AC Asia Pacific ex Japan NR | USD | -5.1% | -5.1% |
| Global developed markets | MSCI World NR | GBP | -3.1% | -3.1% |
| Global emerging markets | MSCI EM (Emerging Markets) NR | GBP | -5.9% | -5.9% |
| **Bonds** | | | | |
| Gilts - All | BofA Merrill Lynch Gilts TR | GBP | 2.1% | 2.1% |
| Gilts - Under 5 years | BofA Merrill Lynch Gilts TR under 5 years | GBP | 0.4% | 0.4% |
| Gilts - 5 to 15 years | BofA Merrill Lynch Gilts TR 5 to 15 years | GBP | 2.3% | 2.3% |
| Gilts - Over 15 years | BofA Merrill Lynch Gilts TR over 15 years | GBP | 3.1% | 3.1% |
| Index Linked Gilts - All | BofA Merrill Lynch Inflation-Linked Gilts TR | GBP | 1.6% | 1.6% |
| Index Linked Gilts - 5 to 15 years | BofA Merrill Lynch Inflation-Linked Gilts TR 5 to 15 years | GBP | 1.8% | 1.8% |
| Index Linked Gilts - Over 15 years | BofA Merrill Lynch Inflation-Linked Gilts TR over 15 years | GBP | 1.7% | 1.7% |
| UK Corporate (investment grade) | BofA Merrill Lynch Sterling Non Gilts TR | GBP | 2.3% | 2.3% |
| US Treasuries | JP Morgan United States Government Bond Index TR | USD | 1.6% | 1.6% |
| US Corporate (investment grade) | Barclays Capital U.S. Corporate Investment Grade TR | USD | 1.8% | 1.8% |
| US High Yield | Barclays Capital U.S. High Yield 2% Issuer Cap TR | USD | 0.7% | 0.7% |
| Euro Government Bonds | Citigroup EMU GBI TR | EUR | 2.2% | 2.2% |
| Euro Corporate (investment grade) | Barclays Capital Euro Aggregate Corporate TR | EUR | 1.4% | 1.4% |
| Euro High Yield | BofA Merrill Lynch Euro High Yield Constrained TR | EUR | -1.5% | -1.5% |
| Global Government Bonds | JP Morgan Global GBI | GBP | 2.3% | 2.3% |
| Global Bonds | Citigroup World Broad Investment Grade (WBIG) TR | GBP | 1.7% | 1.7% |
| Global Convertible Bonds | UBS Global Focus Convertible Bond | GBP | 0.4% | 0.4% |
| Emerging Market Bonds | JP Morgan EMBI+ (Hard currency) | GBP | -1.0% | -1.0% |

** estimate*

*Source: Bloomberg*

# Market Performance

| Asset Class/Region | Index | To 31 January 2014 | | |
|---|---|---|---|---|
| | | Currency | Month | Year to date |
| **Property** | | | | |
| UK Direct Property | UK IPD All Property TR | GBP | 0.0%* | 0.0%* |
| Global Property Securities | S&P Global Property USD TR | GBP | -0.3% | -0.3% |
| **Currencies** | | | | |
| Euro | | GBP | -1.2% | -1.2% |
| US Dollar | | GBP | 0.7% | 0.7% |
| Japanese Yen | | GBP | 4.0% | 4.0% |
| **Commodities & Alternatives** | | | | |
| Commodities | RICI TR | GBP | -0.6% | -0.6% |
| Agricultural Commodities | RICI Agriculture TR | GBP | -0.1% | -0.1% |
| Oil | ICE Crude Oil CR | GBP | -2.5% | -2.5% |
| Gold | Gold Spot | GBP | 3.9% | 3.9% |
| **Interest Rates** | | | **Current rate** | **Change at meeting** |
| United Kingdom | 9 January 2014 | GBP | 0.5% | - |
| United States | 29 January 2014 | USD | 0.3% | - |
| Eurozone | 9 January 2014 | EUR | 0.3% | - |
| Japan | 4 April 2013 | JPY | 0.1% | - |

# Asset Allocation Dashboard

Positive | Neutral | Negative

| Asset class | View |
|---|---|
| **Equities** | |
| Developed equities | Neutral |
| UK equities (relative to developed) | Neutral |
| European equities (relative to developed) | Neutral |
| US equities (relative to developed) | Negative |
| Japan equities (relative to developed) | Neutral |
| Emerging market equities | Positive |
| **Fixed Income** | |
| Government | Negative |
| Index-linked (relative to government) | Negative |
| Investment grade (relative to government) | Neutral |
| High yield | Neutral |
| Loans | Positive |
| Emerging market debt | Positive |
| Convertible bonds | Neutral |
| **Alternatives** | |
| Commodities | Neutral |
| Property (UK) | Neutral |
| **Currencies** | |
| Dollar | Neutral |
| Euro | Neutral |
| Yen | Negative |
| Emerging market currencies | Neutral |

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