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Newsflash

A new month and the 107th issue of Viewpoint from **Financial Partners**.

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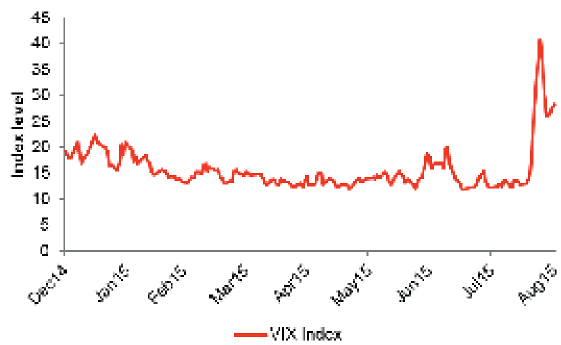
Market Commentary

The implications of China's profound economic problems finally spilled over into a full-scale global market rout in August. China's stock market collapsed by 8% on 'Black Monday' and virtually all other markets suffered almost equally sharp falls in conditions of near panic. The VIX index of implied volatility, often referred to as the 'Wall Street Fear Index", also spiked sharply higher.

Figure 1: The VIX index of implied volatility



In developed markets, the cumulative peak-to-trough decline since May reached -12% in August, representing the biggest correction since 2011. In emerging markets, equities have now fallen by 28% since April in an acceleration of the bear market which started in mid-2011. China, the immediate cause of the latest falls, has fallen by an extraordinary 43% since mid-June, wiping out a large part of the equally extraordinary bull run of the previous twelve months.

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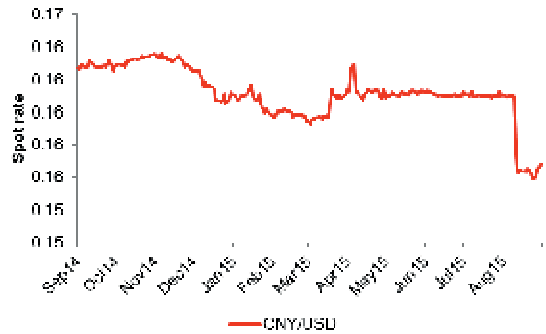
Notably, the sell-off in risk assets did not coincide with a great flight to safety. US Treasuries, the world's most important safe haven asset, saw little change in prices and rates, a pattern repeated across other high-quality government bond markets. The US dollar, usually the beneficiary of a big market sell-off, weakened against the euro and yen, while gold enjoyed a modest rally that was not sustained into the end of the month.

Figure 2: Asset class returns year-to-date.

The trigger for the falls was the surprise decision by China's authorities to devalue the renminbi by circa 3% over a period of three days in early August. Aside from raising questions around currency wars and the competitive impact on other countries, especially its Asian neighbours, the policy shift highlighted the deep seated economic problems in China and the difficulties faced by the ruling Communist Party in maintaining growth near the target of 7%.

China's economic slowdown will undoubtedly impact global growth, but much of the damage is expected to be limited to China itself and to commodity-producing nations, which have been the greatest beneficiaries of China's boom over the past 20 years. In the developed world falls in commodity prices triggered by China's reduced demand are in fact having and will continue to have a beneficial impact on consumer spending by keeping inflation low and providing a boost to real incomes.

Figure 3: China devalues the yuan



Moreover, sluggish economic growth globally means central banks are likely to keep monetary policy loose for longer. In the case of the European Central Bank and Bank of Japan, policy might even be loosened further, a possibility hinted at by both central banks recently. China's central bank has also loosened policy following the sharp market falls, cutting interest rates and lowering the reserve requirement ratio, and there is a strong likelihood that policy will be eased further in coming months.

It seems that investor expectations have rapidly adjusted to events in China. The process of adjustment has and will continue to be painful in some sectors and countries, but in our view its impact on the developed world is much less than the sharp falls in stock markets and other risk assets would suggest.

With valuations now materially lower than three months ago, we view this as a good opportunity to add to risk in portfolios, something we have been implementing on a gradual basis during this period of weakness. We recognise that markets have the hurdle of the Federal Reserve's first rate rise on the way and there will likely be further volatility going forward, but we remain firmly of the view that the bull market has considerably further to run in this particularly long business and market cycle.

Source: Bloomberg. Returns in US dollars unless otherwise stated. August 2015.

Market Performance

Asset Class/Region	Index	To 28 August 2015		
		Currency	Month	Year to date
Developed markets equities				
United States	S&P 500 NR	USD	-5.3%	-2.5%
United Kingdom	MSCI UK NR	GBP	-6.1%	-2.6%
Continental Europe	MSCI Europe ex UK NR	EUR	-8.0%	9.5%
Japan	Topix TR	JPY	-6.6%	11.2%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	-9.6%	-11.2%
Global	MSCI World NR	USD	-5.9%	-1.7%
Emerging markets equities				
Emerging Europe	MSCI EM Europe NR	USD	-7.1%	-5.6%
Emerging Asia	MSCI EM Asia NR	USD	-9.1%	-11.4%
Emerging Latin America	MSCI EM Latin America NR	USD	-9.5%	-22.3%
BRICs	MSCI BRIC NR	USD	-10.0%	-10.7%
Global emerging markets	MSCI EM (Emerging Markets) NR	USD	-8.9%	-12.7%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	USD	0.2%	1.0%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	-0.7%	-0.3%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	-0.6%	-0.8%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	-1.9%	0.0%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	0.3%	1.2%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	-0.7%	0.0%
Euro Government Bonds	Citigroup EMU GBI TR	EUR	-0.8%	0.1%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	-0.7%	-1.0%
Euro High Yield	Barclays European HY 3% Issuer Constraint Total Return Index Value	EUR	-0.9%	1.7%
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	0.2%	-0.3%
Australian Government	JP Morgan Australia GBI TR	AUD	0.4%	2.3%
Global Government Bonds	JP Morgan Global GBI	USD	0.7%	-2.2%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	USD	0.4%	-2.6%
Global Convertible Bonds	UBS Global Focus Convertible Bond	USD	-1.7%	-0.6%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	-0.5%	1.1%

** estimate*

Source: Bloomberg

Market Performance

Asset Class/Region	Index	To 28 August 2015		
		Currency	Month	Year to date
Property				
US Property Securities	MSCI US REIT NR	USD	-4.1%	-5.5%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	-4.6%	5.1%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	-7.3%	0.0%
Global Property Securities	S&P Global Property USD TR	USD	-5.3%	-4.2%
Currencies				
Euro		USD	1.8%	-7.5%
UK Pound Sterling		USD	-1.5%	-1.2%
Japanese Yen		USD	1.8%	-1.7%
Australian Dollar		USD	-1.8%	-12.2%
South African Rand		USD	-4.7%	-13.0%
Commodities & Alternatives				
Commodities	RICI TR	USD	-3.3%	-15.2%
Agricultural Commodities	RICI Agriculture TR	USD	-3.4%	-13.3%
Oil	Brent Crude	USD	-4.1%	-12.7%
Gold	Gold Spot	USD	3.4%	-4.3%
Hedge funds	HFRX Global Hedge Fund	USD	-2.2%	-1.0%
Interest Rates			**Current rate**	
United States			0.25%	
United Kingdom			0.50%	
Eurozone			0.05%	
Japan			0.10%	
Australia			2.00%	
South Africa			6.00%	

* *estimate*

Asset Allocation Dashboard

🟢 Positive 🟡 Neutral 🔴 Negative

Asset class	View
Equities	
Developed equities	🟡
UK equities (relative to developed)	🟢
European equities (relative to developed)	🟡
US equities (relative to developed)	🔴
Japan equities (relative to developed)	🟡
Emerging market equities	🟡
Fixed Income	
Government	🟡
Index-linked (relative to government)	🟡
Investment grade (relative to government)	🟡
High yield	🟢
Loans	🟢
Emerging market debt	🟢
Convertible bonds	🟡
Alternatives	
Commodities	🟡
Property (UK)	🟡
Currencies	
GBP	🟡
Euro	🟡
Yen	🟡

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