

Asset Allocation Dashboard

■ Positive
 ■ Neutral
 ■ Negative

Asset class	View	Comments		
Equities		Positive	Negative	Our view
Developed equities	■	<p>Corporates continue to generate healthy level of profits and, indeed, continue to often beat expectations. While gradually becoming less attractive, valuations are not overly stretched by historical standards. Recent M&A pickup also a returns driver for investors and additional central bank activity could provide a further impetus.</p>	<p>Risks remain and the global macroeconomic situation continues to be uncertain. Many developed markets are at, or around their nominal highs.</p>	<p>At these valuation levels we view a broadly neutral allocation as appropriate. Central Bank policy remains key for markets today. Short term noise could also be a result of increasing geopolitical tensions. An increase in volatility could provide interesting buying opportunities.</p>
UK equities Relative to developed	■	<p>Valuations are better than most developed markets thanks to a meaningful degree of underperformance of this market over recent months and there is less systemic risk than Europe.</p>	<p>The UK's economic outlook is, on the face of it, increasingly impressive but despite strong headline data, there remain areas of fragility and sources of risk especially the impending UK general election which could cause a degree of uncertainty in the coming months. The UK market remains disproportionately exposed to moves in the oil price.</p>	<p>The UK is reasonably attractive, but remains sensitive to political news both internally and to knock on effects from the EU. The UK is a mild 'green' status today especially in light of the relative underperformance of the rest of DM last year.</p>
European equities Relative to developed	■	<p>Sentiment remains low, which could have weighed on valuations disproportionately.</p> <p>The Central Bank is now committed to a large programme of 'full' QE which includes the outright purchase of sovereign debt. Moves such as these demonstrate the official sector's commitment to a positive outcome in Europe.</p> <p>Europe houses some excellent, global businesses.</p>	<p>Economic data continues to be weak and there is a growing risk of persistent deflation in the region. The intervention of the ECB has, on the whole, been well received, but their longer term efficacy remains to be seen. Given the recent move in oil, there is no reason to expect this to change any time soon.</p> <p>The possibility of 'Grexit' is once again on the table, which poses a significant risk to equity markets even if only in the short term.</p>	<p>Europe remains somewhat cheap, but does not qualify for the "fat pitch" that we look for, especially given the risk of negative growth in the region. Ultimately the weak macro story and the lack of a valuation extreme suggest caution in this region. Longer term, Europe needs some sort of political and banking consolidation, but the ECB is calming the waters for now.</p>
US equities Relative to developed	■	<p>The US economic outlook remains amongst the best of major economies. Economically significant sectors like housing, are recovering and the corporate sector remains in good shape. The consumer's confidence is improving thanks to improvements in housing and employment coupled with a low oil price.</p>	<p>The most expensive equity region, with low dividend yields and high investor expectations already priced in.</p> <p>US equity requires reasonable earnings growth to justify today's valuation.</p>	<p>Consistently the most expensive regional equity market (although this has moderated somewhat recently). Despite the better US news flow, it warrants an underweight. Investors can buy very similar companies elsewhere for less. But this is not a "fat pitch". Be cautious on sizing</p> <p>Monetary policy remains a key swing factor for the US.</p>
Japan equities Relative to developed	■	<p>Despite recent weakness, the market has responded well to Prime Minister Abe's attempts to bolster the economy and it is possible that his new mandate from the electorate will allow these reforms to come to fruition. Likely to see a continuation or increase in quantitative easing in order to stimulate the economy and inflation. This should be reflected in equity valuations.</p>	<p>Although Japan looks relatively cheap on a price-to-book basis, this can be justified by their lower historical ROE.</p> <p>Long term Japan remains in a difficult position with an ageing population and little or no economic growth.</p>	<p>The government's pro liquidity policies are welcome – and a weaker yen helps – but inconsistent data readings and a habit of not 'mean reverting' make this a difficult market to call. We rate this market as neutral today, but it is close to 'green'.</p>

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Equities		Positive	Negative	Our view
Emerging market equities	■	<p>Emerging markets have underperformed developed equity markets recently. Valuations remain attractive even on a cautious medium term outlook for the region.</p> <p>Investor sentiment is beginning to turn positive on the region and this, coupled with attractive valuations is an enticing combination. Falls in oil price should help the consumer.</p>	<p>The asset class continues to face near term headwinds including a strong US dollar and signs of a slowdown in Chinese growth may continue to weigh on markets.</p> <p>Oil price falls may disproportionately hit emerging markets equity index due to the large weight of the resources sector.</p>	<p>Valuations, in our opinion, are sufficiently attractive to justify an allocation.</p> <p>Care should be taken to ensure the strong valuation bifurcation between high and low quality stocks does not impact returns.</p> <p>Also, this is a volatile section of the equity market so care should be taken on position sizing.</p>

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Fixed income		Positive	Negative	Our view
Government	■	<p>A major withdrawal of monetary stimulus may still be some way off in the developed markets. With subdued inflation expectations, a significant sell off in sovereign bonds appears unlikely.</p> <p>High quality government paper remains the ultimate haven in times of elevated risk aversion. At current yields, these government bonds may offer investors an element of protection during a market sell-off.</p>	<p>Extraordinary monetary policy has brought about artificially low bond yields and long term government bonds remain expensive in our view.</p> <p>The real returns available to investors in a variety of '10 year safe haven' government bonds is likely to be negative even in a modest inflationary environment.</p>	<p>The ECB and BoJ have taken up the liquidity baton from the Fed and overall we continue to see extraordinary monetary stimulus, now a market feature since late 2008.</p> <p>On a medium term outlook government bond yields are not attractive and the asymmetry of potential returns from this asset class is stark.</p>
Index-linked Relative to government	■	<p>Present levels of inflation in the developed world are low and on a forward looking basis, inflation expectations are extremely muted.</p> <p>Given the historical stickiness of inflation at levels above breakeven inflation rates, linkers look like a more reasonable way of investing in government bonds than the fixed rate government bond market.</p>	<p>Linkers remain vulnerable to weak economic news flow.</p> <p>Real yields are still very low, or indeed negative and are expected to rise to more normal levels as monetary policy normalises.</p>	<p>Like their nominal counterparts, linkers are ultimately expensive. Nonetheless, compared to a conventional government bond, they could provide some protection against unexpected inflation, given that many market participants are expecting a relatively benign inflationary environment over the next few years.</p>
Investment grade Relative to government	■	<p>Investment grade spreads – a measure of relative value compared to government bonds – remain modestly attractive.</p> <p>Good quality corporates are able to access debt markets extremely cheaply – which bodes well for their future business prospects, as long as they do not become over reliant on cheap credit.</p> <p>Interest remains well covered and investors are well paid for the default risk.</p>	<p>In absolute terms, rather than relative, the duration component of investment grade bonds will be a headwind, should government bond yields move higher.</p> <p>While spreads are reasonably attractive, nominal yield levels are not particularly compelling compared to their history due to low reference (government) rates.</p> <p>There are market concerns over liquidity but investors are somewhat compensated for this in the current spread.</p>	<p>Investment grade debt remains a decent play against government bonds. Our positive views on corporate credit health mean investment grade is a reasonable replacement for government debt, but if taken in isolation the asset class is not particularly attractive.</p> <p>We are cognisant of debt issuance to support share buybacks, which has become more prevalent recently.</p>

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High yield	■	<p>Spreads have adjusted on the back of the fall in the oil price and the total yield is relatively attractive for investors in search of income in a low rate environment.</p> <p>Default rates remain very low and recovery rates are ahead of expectations too. Underwriting standards are looser now (non-callable periods, lighter covenants) but debt servicing remains well covered.</p>	<p>Spreads and headline yields remain low by historical standards. Spreads are at or below what we would regard as a sustainable long term level; they appear to be pricing in a continuation of the highly favourable environment we have had for corporate debt.</p> <p>The large proportion of energy related issuers could prove a risk if oil price drops are protracted.</p>	<p>A marginal amber in our colour code.</p> <p>The upside in allocating to high yield debt at present spread and yield levels is sufficient, in our view, to warrant a position to the asset class. Today this is not a fat pitch, however, so be careful on position sizing. Best valuation appeared to be at the short end of the curve today.</p> <p>If this asset class weakens we would consider increasing allocations.</p>
Loans	■	<p>Long term value remains attractive. Unlike high yield, the spread available on loans appears attractive with the additional benefit of a floating rate coupon.</p>	<p>Less liquid part of the corporate debt market with wider bid/offer spreads. Risks much the same as high yield in the sense that a significant pickup in defaults may negatively impact the asset class.</p>	<p>Hold exposure if appropriate to mandate. Very similar to high yield, with the exception that investors need to consider the less liquid nature of this market. The main advantage is the floating rate nature of the loan universe, which will help if and when interest rates rise. Seniority over unsecured bonds provides some extra security if the even defaults pick up unexpectedly.</p>
Emerging market debt (hard currency)	■	<p>Spreads today make the hard currency denominated emerging markets debt a green on our colour code. Higher coupons are attractive when considering duration and reinvestment risks.</p>	<p>In the short term, EMD remains sensitive to disappointing growth, bad economic data and 'risk aversion' trades.</p> <p>Oil price falls may disproportionately hit emerging markets issuers due to the large weight of the resources sector in their economies. Furthermore a strong US dollar makes these obligations more difficult to service, although not unmanageably so yet.</p>	<p>EMD appears sensitive to global macro news,, especially markets with current account deficits or an overreliance on oil exports. However spreads today make the hard currency parts of emerging markets debt a green on our colour code.</p> <p>Moderate allocations are justifiable, but be wary of making an oversized allocation today.</p>
Convertible bonds	■	<p>Trading at essentially fair value. Given the lack of attractive valuations in developed equity markets, the asset class provides an element of upside should the momentum in equity markets continue, with the benefit of a bond floor.</p>	<p>Significant systemic risks remain. The call optionality embedded in converts is ultimately only worth something if markets continue to increase and the particular stocks in question participate in these moves.</p>	<p>Convertible bonds have moved to fair value relative to their constituent parts. An allocation can be justified on the grounds that it retains some equity market upside with downside protection.</p>

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Alternatives		Positive	Negative	Our view
Commodities	■	<p>Global growth rates remain reasonable and may provide a baseline of demand. Asset class arguably more attractive after significant falls recently.</p> <p>Oil price falls have weighed on commodities of late and this could snap back aiding returns. Oil seems to have found some support at present levels.</p>	<p>Economic data remains unexciting. Harsh austerity plans combined with sluggish growth does not suggest inflation is a major worry.</p> <p>Strength of final demand is still questionable; China remains as murky as ever. Furthermore, China holds significant inventories already.</p>	<p>Commodities remain sensitive to negative news on growth.</p> <p>They could rally from here but volatility and ongoing economic uncertainties suggest caution.</p> <p>The recent, significant, falls in the oil price demonstrates how volatile these prices can be.</p>
Property (UK)	■	<p>Yields remain reasonably attractive. Reasonable vacancy rates still remain in certain areas.</p> <p>Active management remains key in this sector.</p>	<p>Economic data remains weak and reasonable supply is being generated in London.</p> <p>Outside London strength of final demand remains weak and the continued malaise of the high street (and other physical retail) potentially impacts a large section of the UK property bank.</p> <p>The illiquidity of direct strategies must also be borne in mind.</p>	<p>Income attractive versus gilts but limited room for capital growth. Neutral.</p>

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Currencies			
Dollar	■	Following recent strength, the dollar appears to be at or near fair value. The Fed has begun its slow unwind of extraordinary monetary policy but interest rate increases could still be pushed back as inflationary pressures subside.	Neutral
Euro	■	Sovereign issues have weighed on the euro. It is likely that the euro zone will require low interest rates for the foreseeable future and this appears to be priced in.	Neutral
Yen	■	A weak yen is good for the Japanese economy and as a result we expect to see continued downward pressure applied by the BoJ. This may serve to weaken the yen further, but at the very least it should provide significant resistance to the upside.	Underweight

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