

# Asset Allocation Dashboard

■ Positive    
 ■ Neutral    
 ■ Negative

Asset class	View	Change	Comments		Our view
			Positive	Negative	
Equities					
Developed equities	■	↔	<p>Corporates continue to generate reasonable levels of profit and forward earnings per share remains robust.</p> <p>Valuations are slightly rich by historical standards but low yields warrant the higher multiple, and valuations are not stretched relative to DM sovereign bonds or credit.</p> <p>Central Bank activity continues to provide a boost to markets.</p>	<p>The global macroeconomic environment is more uncertain than risk markets might suggest and risk looks under-priced in some sectors and regions.</p> <p>Markets have continued to perform strongly and there is a risk of momentum stalling and profits being taken in the absence of improving sales or profit margins to push stocks higher.</p> <p>Geopolitical and electoral risks may not be sufficiently discounted and remain a source of volatility</p>	<p>At these valuation levels we view a broadly neutral allocation as appropriate. Valuations are not cheap but central bank policy remains supportive for risk assets and on a relative value basis vs both sovereign bonds and credit, equity returns remain attractive over the medium term, even if nominal expectations are quite low.</p> <p>Short term volatility should be expected with policy and politics central to risk pricing.</p>
UK equities Relative to developed	■	↔	<p>Valuations remain a little extended but the continued pressure on sterling will support UK businesses, more so the exporters and those that earn their revenues overseas, but the market is discounting a meaningful move higher in earnings at these levels.</p> <p>Low base rates and the continuing asset purchase program should keep risk appetite buoyed in the near term.</p>	<p>Uncertainty remains in the UK economy at this time as the Brexit process progresses following the triggering of Article 50. In the smaller cap indexes where businesses are more domestically exposed, one could argue that this risk may be under-priced today and if the earnings fail to materialise then the market looks expensive.</p> <p>The UK market remains disproportionately exposed to moves in commodity prices.</p>	<p>Following the strong rally in UK equities and weakness in sterling, return expectations have fallen back to more modest levels. With sterling at its cheapest level in decades further sustained weakness seems unlikely.</p> <p>The immediate Brexit risks have faded but have been replaced by negotiation risks.</p> <p>The market remains disproportionately sensitive to commodity prices and we are cognisant of any resurgence in oil price volatility.</p>
European equities Relative to developed	■	↔	<p>The Central Bank continues to purchase corporate debt as part of its QE program.</p> <p>Valuations remain attractive against the backdrop of generationally low yields</p> <p>Political risk has been discounted into European equities and positive electoral outcomes may boost Eurozone equities.</p> <p>European manufacturing indicators support strong growth within the region which should boost equity returns going forward</p>	<p>The ECB has now reduced the size of their monthly bond purchases and the market is expecting further reductions at the end of the year; this may cause some repricing of risk, albeit for the right reasons.</p> <p>Low rates in Europe and beyond puts pressure on the banking sector which remains under pressure.</p> <p>We are mindful of politics in Europe including elections in France and Germany this year.</p>	<p>European equity valuations have compressed in recent months but remain reasonable at current levels, especially when viewed against corporate and sovereign European bond markets.</p> <p>With European political headwinds and a growing recognition that negative rates do more harm than good, we remain cautious but optimistic today and would look to add on weakness.</p>

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US equities Relative to developed	■	↔	<p>The broad US economic outlook remains solid and arguably the region warrants a premium at a time of increasing uncertainty elsewhere. Consumer confidence remains high, jobs growth continues – albeit at a slower pace - and economic indicators suggest reasonable growth over the medium term. The new administration's expected program of fiscal spending and tax cuts will benefit certain corporates and sectors as well as the consumer, provided it is forthcoming</p> <p>Equities may be better placed over the longer term to capture any reflationary policy fallout.</p>	<p>The US remains one of the most expensive equity regions, with high investor expectations already priced in. With profit margins having peaked, US equity requires meaningful earnings growth to justify today's valuation.</p> <p>The Fed's interest rate policy will remain a source of uncertainty and an inflation surprise could see yields move higher than markets have discounted. If the dollar strengthens further that could be a headwind to earnings.</p> <p>Undefined policy objectives of the incoming Trump administration maintain uncertainty and could increase risk premia for equities.</p>	<p>Still the most expensive regional equity market in our valuation framework, but not outlandish on a relative basis and at these yields.</p> <p>Monetary policy remains a key swing factor for the US and on the political front we prefer for now to observe how the Trump administration settles and its policies unfold. There are still many unknowns.</p> <p>Recent strength in the dollar and the re-pricing of forward labor curves may serve to cool the economy and could lead earnings to disappoint versus their bullish implied levels.</p>
Japanese equities Relative to developed	■	↔	<p>Negative rates should be constructive for equities despite creating bouts of volatility in the near term.</p> <p>Valuations remain attractive in Japan and our return expectations are amongst the highest of the developed market regions.</p> <p>BoJ purchases of equity through ETF structures, as well as the continuing purchase of JGBs, should support prices.</p> <p>Any reversal in the recent bout of Yen strength would be a boost to Japanese equities.</p>	<p>A strengthening yen is a problem for exporters and leaves equities exposed to the currency.</p> <p>In real terms the currency is not expensive so there is room for this to happen, but it is likely to come in a risk off situation when the yen traditionally offers some protection as offshore capital is repatriated.</p> <p>Longer term, Japan remains in a difficult position with an ageing population, low/no inflation and little or no economic growth. This could hold domestic equities down.</p>	<p>We continue to rate this market as a green today with attractive valuations and a continuing program to increase equity allocations within pension portfolios.</p> <p>The government's pro liquidity policies are welcome but inconsistent data readings, habitual disappointment and the yen's safe haven currency status warrant some caution.</p>
Emerging market equities	■	↔	<p>Valuations remain attractive in emerging markets following several years of weak commodity prices and currency adjustments.</p> <p>Leading indicators continue to support reasonable growth expectations in isolation as well as versus DM economies.</p> <p>Global and localised policy action remains supportive towards riskier assets.</p> <p>EM currencies remain cheap in real terms which should be supportive for EM assets</p>	<p>The asset class may face near term headwinds from any additional US dollar strength and the continued moderation in Chinese growth which heavily influences the EM asset class.</p> <p>The fallout from the US election may continue to provide a headwind to certain companies and countries should trade agreements be revoked or tariffs introduced.</p> <p>Considerable political risk remains and warrant some discount, add to that increasing geopolitical tensions which may affect markets more broadly</p>	<p>Valuations are attractive in absolute and relative terms. With slowly improving fundamentals and a noticeable repositioning in risk appetite among investors, we like the prospective long term returns offered by the asset class today.</p> <p>This remains a volatile section of the equity market: care is required on position sizing.</p> <p>Caution is warranted until the path of US trade policy becomes clearer, but at current levels we see good return prospects from this asset class.</p>

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Fixed income			Positive	Negative	Our view
Government	■	↔	<p>DM policy remains broadly accommodative in aggregate across DM economies but with inflation and rates having repriced sharply higher in recent months, bond yields today are under less upward pressure.</p> <p>High quality government paper remains the ultimate haven in times of elevated risk aversion.</p> <p>Real treasury yields do not look unreasonable if growth remains muted and inflation is contained.</p>	<p>Extraordinary monetary policy has brought about artificially low bond yields and long term government bonds remain expensive in our view. Fundamentals have crept back into US bond valuations following Trump's election and may continue to re-price rate risk higher.</p> <p>There has been a reflationary theme playing out in markets and whilst it may prove to be overstated, it does have mark to market implications for rate sensitive securities including treasury debt.</p>	<p>Despite on-going supportive policy actions, on a medium term outlook the majority of government bond yields remain unattractive and the asymmetric risk of potential returns from this asset class remains elevated.</p> <p>There are some relative value opportunities for the more sophisticated investors but it is mostly the diversifying attributes of the higher quality sovereign bonds that warrant any holding today.</p>
Index-linked Relative to government	■	↔	<p>Realised levels of inflation in the developed world remain low while forward looking basis inflation expectations have started to edge higher. Inflation breakevens in aggregate look fair. Given the historical stickiness of inflation at levels above breakeven inflation rates, inflation linked bonds in select markets look better value today than fixed rate government bonds. US inflation and inflation surprise across the G4 economies has increased.</p>	<p>Linkers remain vulnerable to weak economic news flow and renewed weakness in commodity prices. Real yields in the UK are extremely negative and should be expected to rise as monetary policy normalises, causing MTM losses. It is difficult to use inflation linked bonds without accepting the higher duration risk that comes with most inflation linked bond funds. Inflation linked bonds can be more technically driven and do not always imply a true measure of future realised inflation.</p>	<p>Like their nominal counterparts, linkers are ultimately expensive. Nonetheless, compared to a conventional government bond, at these levels they do provide some protection against higher realised future inflation.</p> <p>We think inflation linked bonds are reasonably valued today, with some markets offering better value than others.</p>
Investment grade Relative to government	■	↔	<p>Investment grade spreads – a measure of relative value compared to government bonds – remain relatively attractive. At current levels we think investors are adequately paid for the fundamental risk.</p> <p>IG bonds also provide some diversification to riskier assets with their embedded rate risk.</p> <p>UK and European investment grade bonds should stay supported with their central banks as marginal buyers.</p>	<p>In absolute terms the duration component of investment grade bonds may prove to be a headwind, should government bond yields move higher than what is currently priced in. There are market concerns over liquidity but investors are somewhat compensated for this in the current spread. Financials make up a large part of the investment grade bond universe and we recognise the impact of lower sovereign rates on banks margins and profitability if base rates fall further. The US market – the largest regional allocation within the global asset class – is more progressed through the credit cycle today and leverage, whilst not at punitive levels, has been rising.</p>	<p>Investment grade debt remains a decent play against government bonds and an efficient way to earn a higher quality spread whilst retaining some underlying rate protection.</p> <p>We are cognisant of debt issuance to support share buybacks and the high aggregate debt levels.</p> <p>Asset class duration remains near the highs meaning investors are more sensitive to rate moves today than in the past.</p> <p>We retain a neutral rating today and like the balance it provides in a multi asset portfolio.</p>

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High yield	■	↑	<p>High yield spreads in both the US and Europe offer an at-best fair pick up but valuations have deteriorated as spreads have tightened. Default rates remain low in non-energy sectors. Recovery rates are below long term averages but this is a function of the market having become bifurcated between energy and non-energy sectors.</p> <p>Interest remains well covered.</p>	<p>Spreads have continued to rally hard in recent weeks and are now starting to look expensive.</p> <p>The large proportion of energy related issuers could again impact US index returns if the oil price fails to hold current levels and default rates remain high in the sector.</p> <p>Furthermore, the credit cycle is now somewhat extended in the US.</p>	<p>We prefer short duration to core high yield today as scenario analysis suggests a better risk return. The basis of expected returns we prefer US over Europe today.</p> <p>Last month we downgraded high yield after spreads in the US dipped below 350bps. This month we move the asset class back to neutral following negative total returns in March which saw spreads move back towards to the 400 level.</p>
Loans	■	↔	<p>Long term some value remains and the spread available on loans is attractive with the additional benefit of a floating rate coupon. Seniority over unsecured high yield bonds also provides additional capital security if defaults pick up unexpectedly. Loans have limited exposure to the energy sector where the risk of capital impairment is higher.</p> <p>A higher exposure to the healthcare sector could benefit from healthcare policy changes in the US.</p>	<p>Loans sit in a less liquid part of the corporate debt market with wider bid/offer spreads. Fundamental risks are much the same as for high yield in the sense that a significant pickup in defaults may negatively impact the asset class. This is less liquid than high yield and this risk should be borne in mind when considering investments. Covenant protection remains low. We are mindful of sector concentration in healthcare and technology and the use of new issue loan proceeds for acquisitive purposes.</p>	<p>We retain a modestly favourable view on the asset class and today prefer to high yield bonds in portfolios which can own the asset class. Hold exposure if appropriate to mandate. Similar to high yield, with the exception that investors need to consider the less liquid nature of this market and lack of an embedded rate component. The floating rate nature of the asset class will be accretive as interest rates rise.</p>
Emerging market debt	■	↔	<p>Spreads today on hard currency denominated emerging markets remain reasonably attractive when considering duration, reinvestment risks and opportunities in other asset classes. All in yields are also reasonable following the recent re-pricing in US rates. In aggregate the sovereign issuers that comprise the EMD universe today have higher currency reserves and more free floating currencies that should prevent a meltdown like that seen during previous EM debt crises, and aggregate rating quality is better. The worst of the EM currency depreciation looks to be behind us and this should provide some support to hard currency spreads, and will benefit from any dollar weakness.</p>	<p>In the short term, EMD remains sensitive to disappointing growth, bad economic data, a stronger dollar and 'risk aversion' trades as witnessed post-election. Oil price falls will benefit net oil importers to the detriment of EM economies that export and a strong US dollar makes these obligations more difficult to service, although not unmanageably so yet. The large weight of the resources sector in a number of EM economies leaves them exposed to the slowing of the Chinese economy. The quality of the universe remains investment grade overall but has been deteriorating.</p>	<p>EMD is sensitive to global macro news, especially markets with current account deficits or a reliance on oil exports.</p> <p>Moderate allocations are recommended at current valuations. Local EMD has optically attractive yields but dollar strength and currency risks may overwhelm the carry opportunity in the near term.</p> <p>Hard currency continues to look more attractive at the margin but both should provide reasonable real returns and a decent pick up to DM sovereigns over the longer term.</p>
Convertible bonds	■	↔	<p>Convertible valuations remain reasonably attractive today.</p> <p>We expect some pick up in volatility over the next year following several years of suppressed vol, due both to policy action/inaction and geopolitical events."</p>	<p>Systemic risks remain. The call optionality embedded in converts ultimately only has real value if markets increase and the particular stocks in question participate in these moves.</p> <p>Some equity markets look quite fully priced and convertibles will be impacted if equities come under pressure.</p>	<p>Convertible bonds are priced about fair value to their constituent parts. The asset class should always have a place in a multi asset portfolio given the upside participation and downside bond floor and the asymmetric properties they possess.</p>

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Alternatives			Positive	Negative	Our view
Commodities	■	↔	<p>Although global growth rates remain subdued commodity prices will continue to be influenced by broader risk appetite which remains buoyant at present.</p> <p>As inflation starts to surprise to the upside in some countries commodities can provide an inflation hedge in client portfolios.</p> <p>Gold can also provide a hedge against event risk in what has become a macro environment sensitive to policy error and newsflow.</p>	<p>Strength of final demand is still questionable especially with respect to China where it is clear commodity imports have slowed and growth continues to moderate.</p> <p>It is difficult to take a direct exposure to commodities and commodity curves will influence returns vehicles that invest via commodity futures, often negatively.</p> <p>The asset class more broadly remains prone to bouts of dollar strength.</p>	<p>Commodities remain sensitive to negative news on growth.</p> <p>They could rally further from here but volatility and on-going economic uncertainties suggest caution and the market still prices inflation risk at the lower end of historical levels.</p> <p>The dollar will be critical and whilst it has been on a tear of late its future direction is less clear.</p>
Property (UK)	■	↔	<p>Yields and returns remain reasonably attractive in selective regional locations and will have improved as commercial valuations have come back.</p> <p>Reasonable vacancy rates still remain in certain areas.</p> <p>Active management remains key in this sector as is the avoidance of expensive 'legacy positions' in overly mature funds.</p> <p>The weakness in sterling has revived some foreign flow into the UK property asset class and any further weakness should see support for property from the overseas buyer.</p>	<p>The UK's economic outlook remains uncertain as the Brexit negotiations evolve following the triggering of Article 50,</p> <p>The traditional British high street remains under pressure from the continuing growth of online retailing and high street chain closures are testament to this.</p> <p>We have warned in the past of the dangers of liquidity mismatch and this continues to be a risk that the sector is exposed to</p> <p>As a longer duration asset class property remains susceptible to any repricing in long terms bond yields which have moved sharply lower in recent months.</p>	<p>Income is attractive versus gilts but there is limited room for capital growth.</p> <p>On the positive side, rental growth outside of London is likely to provide a positive impetus due to a lack of new supply.</p> <p>We also recognise the 'search for yield' lends support to the asset class.</p>

Asset class	View	Change	
<b>Currencies</b>			
USDGBP	■	↔	<p>Fed pricing remains below the Fed committee's 'dot plot' but the two have converged as forward US rate expectations have moved higher. This has been constructive for the dollar but has recently fallen back.</p> <p>In the UK we continue to feel that together with extreme positioning against Sterling and a low valuation, we should see a more balanced outlook for this currency pairing but until there is a clearer picture of how Brexit is implemented it is difficult to call directionally.</p>
EURGBP	■	↔	<p>ECB policy remains accommodative – albeit-reducing - but will continue to keep rates low. Rate differentials across geographies provide little to no carry advantage so the currency will not find any support there in the near term.</p> <p>Further tapering could see the common currency find strength but financial and political newsflow in Europe will likely only serve as a near term headwind for the currency</p>
JPYGBP	■	↔	<p>In recent months the BoJ's message has lost much of its punch and they have now moved away from a target bond purchase to a yield target which may ultimately be akin to a tapering of bond purchases. Risk conditions remain favourable so any Yen strength will likely be pared. This pair remains sensitive to risk news but with both currencies looking somewhat cheap on a long term real basis, and no imminent rate events likely to upset the cross, it is difficult to take a strong directional view at this juncture.</p>



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