PPi Professional Portfolio International

momentum

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Newsflash

A new month and the 129th issue of Viewpoint from **PPI Advisory**.

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Market Commentary

So far this year, market trends have been dominated by strengthening economic activity in Europe and Japan, continuing growth in the US and Asia, and subdued inflation. Amidst this backdrop, markets have generally been benign, characterised by strong equity performance and stable bond markets. These trends continued into July, with equity markets again producing the best returns, led by emerging markets, whilst bond markets progressed with credit and high-yield bonds outperforming government bonds. Volatility remained extraordinarily low with the VIX index reaching all-time lows.

Perhaps the most notable feature of the month was the further slide in US Dollar, down 2.9% on a trade-weighted basis during the month and 9.1% year-to-date, moving to levels of early 2015. Oil was also a major mover during the month, forming a sizeable recovery with Brent Crude up 9.9% during July, reducing its year to date fall to 7.3%. The partial recovery of Brent crude was triggered by Saudi pledges to cut exports together with the first signs that the shale oil boom in the US is slowing.

Figure 1: Brent Crude Price

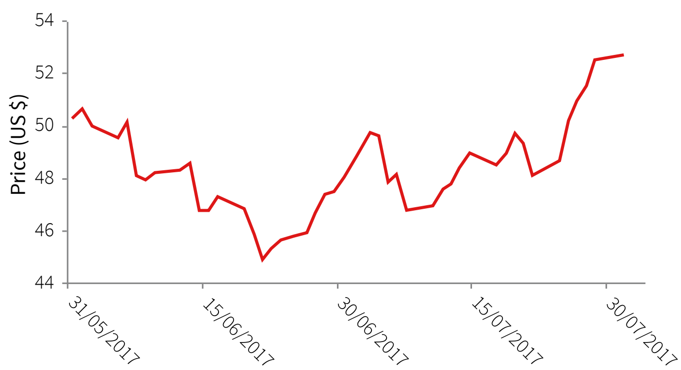
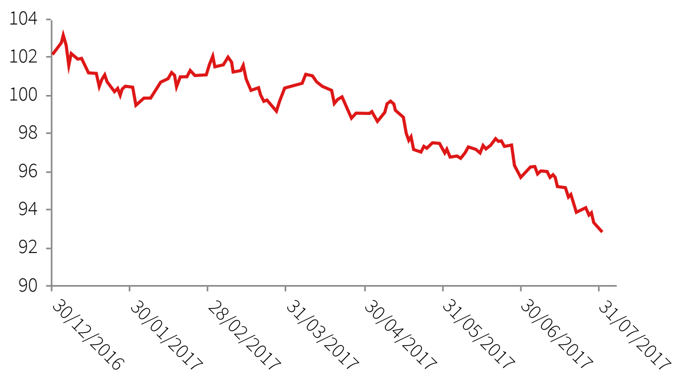
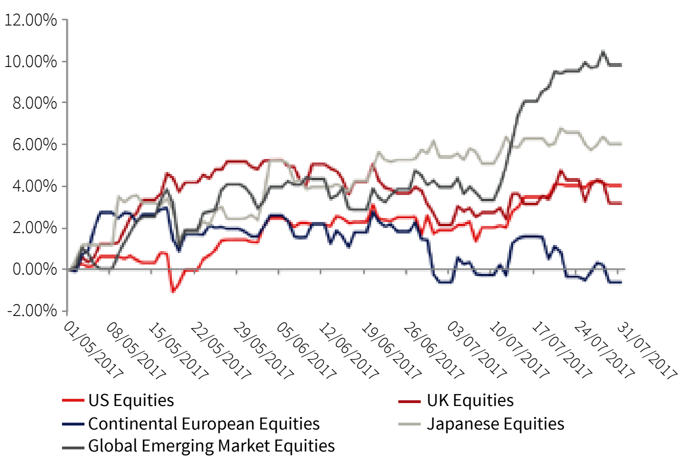


Figure 2: US Dollar Index



Currency moves had a significant impact on equity returns during the month. Emerging markets were the prime beneficiaries of a weak dollar, with all regions posting strong equity returns, amplified by the oil price recovery. Conversely, Continental European Equities continued to fall amidst the strength of the Euro and its apparent negative impact on corporate earnings growth. During July, Continental European equities fell 0.2% in local currency terms whilst the Euro rose 3.6% versus the US Dollar. UK and Japanese equities were also held back by their respective currency strength versus the US Dollar, rising 1.1% and 0.4% in local currency terms respectively.

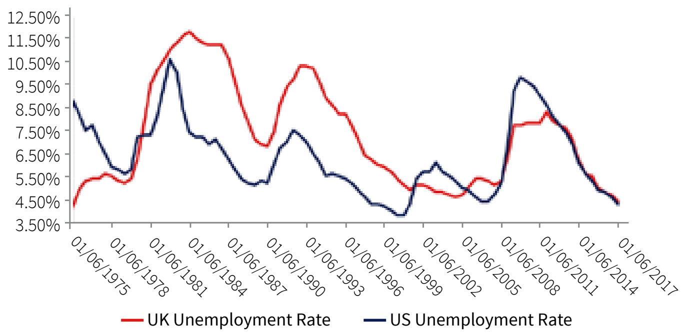
Figure 3: Major Equity Market Cumulative Returns



The global economic backdrop remained highly favourable for markets, with growth in Europe and Japan progressing at arguably the most sustainable rate since the financial crisis, whilst US growth picked up in the second quarter following a muted first quarter. Despite a turbulent political environment in the US with Donald Trump failing to achieve sufficient support for Republican healthcare plans and recent changes to key personnel, the US economy appears robust, adding 209,000 jobs in July.

With inflation remaining remarkably subdued worldwide, central banks have been able to maintain highly accommodative monetary policy. Last month the Federal Reserve, European Central Bank, Bank of England and Bank of Japan all maintained their monetary policy stance. The Federal Reserve is expected to begin its process of policy normalisation later in the year, with another rate rise accompanied by a tapering of its balance sheet. Despite this, US monetary policy is likely to remain accommodative given the underlying strength of the US economy and the indications by Federal Reserve chair Janet Yellen that the funds rate is almost at neutral policy stance level. Worldwide, core inflation has fallen almost everywhere and wage growth is low. Of particular note, wage growth in the US and UK remains low despite unemployment being at the lowest rate since 2001 in the US and 1975 in the UK.

Figure 4: US and UK unemployment rates



Bond markets have been supported by a broadly dovish central bank stance globally combined with low inflation. The encouraging growth environment and positive backdrop for the corporate sector produced favourable conditions for credit, high-yield and emerging market debt with returns generally in the 5% to 7% range this year.

After a turbulent year, the political backdrop in the UK remains uncertain. Brexit proceedings are particularly unclear and appear to be having a negative impact on spending decisions by businesses and consumers, compounded by a slowdown in the housing market and falling real wages as Sterling's weakness pushes up headline inflation. In light of this, the Bank of England has downgraded its GDP growth forecasts from 1.9% to 1.7% in 2017. Recent Brexit proceedings indicate Prime Minister Theresa May is leaning to a 'softer' approach with the prospect of a cliff edge exit in March 2019 receding. It is now likely the UK will negotiate a lengthy transitional deal with the EU that could last at least until the next scheduled general election in 2022.

Markets have performed well this year on the back of increasing economic activity with growth rates appearing to be sustainable. Although central banks remain dovish, we are entering a period of monetary policy normalisation with the Federal Reserve and the European Central Bank leading proceedings. The benign conditions so far this year have pushed valuations higher and leave markets vulnerable to a correction. In addition, the tail wind of a weak US Dollar this year could be reversed, with stronger US growth and policy tightening by the Federal Reserve acting as support to the Dollar at current levels. However, this cycle is particularly long, and it will be important to remain invested. Periodic bouts of weakness in equity markets will present buying opportunities.

Source: Bloomberg. Returns in US dollars unless otherwise stated. July 2017.

Market Performance - Global (Local returns)

Asset Class/Region	Index	To 31 July 2017		
		Currency	1 Month	Year to date
Developed markets equities				
United States	S&P 500 NR	**USD**	2.0%	11.2%
United Kingdom	MSCI UK NR	**GBP**	1.1%	5.8%
Continental Europe	MSCI Europe ex UK NR	**EUR**	-0.2%	8.4%
Japan	Topix TR	**JPY**	0.4%	7.8%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	**USD**	5.2%	26.0%
Global	MSCI World NR	**USD**	2.4%	13.3%
Emerging Market Equities				
Emerging Europe	MSCI EM Europe NR	**USD**	5.0%	9.0%
Emerging Asia	MSCI EM Asia NR	**USD**	5.6%	30.1%
Emerging Latin America	MSCI EM Latin America NR	**USD**	8.3%	19.2%
BRICs	MSCI BRIC NR	**USD**	8.6%	26.9%
Global emerging markets	MSCI EM (Emerging Markets) NR	**USD**	6.0%	25.5%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	**USD**	0.1%	2.1%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	**USD**	0.4%	1.4%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	**USD**	0.7%	4.6%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	**USD**	1.1%	6.1%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	**GBP**	0.3%	0.6%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	**GBP**	0.7%	3.0%
Euro Government Bonds	Citigroup EMU GBI TR	**EUR**	0.2%	-0.8%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	**EUR**	0.8%	1.4%
Euro High Yield	BofA Merrill Lynch Euro High Yield Constrained TR	**EUR**	1.0%	5.2%
Japanese Government	JP Morgan Japan Government Bond Index TR	**JPY**	0.0%	-0.4%
Australian Government	JP Morgan Australia GBI TR	**AUD**	0.1%	2.5%
Global Government Bonds	JP Morgan Global GBI	**USD**	1.7%	5.8%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	**USD**	1.7%	6.1%
Global Convertible Bonds	UBS Global Focus Convertible Bond	**USD**	1.9%	8.9%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	**USD**	0.4%	6.7%

Source: Bloomberg [e] *denotes estimate*

Market Performance - Global (Local returns)

Asset Class/Region	Index	To 31 July 2017		
		Currency	1 Month	Year to date
Property				
US Property Securities	MSCI US REIT NR	**USD**	1.2%	3.3%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	**AUD**	-0.1%	-6.1%
Asia Property Securities	S&P Asia Property 40 Index NR	**USD**	4.3%	20.7%
Global Property Securities	S&P Global Property USD TR	**USD**	2.8%	11.0%
Currencies				
Euro		**USD**	3.6%	12.6%
UK Pound Sterling		**USD**	1.5%	6.9%
Japanese Yen		**USD**	1.9%	6.1%
Australian Dollar		**USD**	4.1%	11.2%
South African Rand		**USD**	-0.8%	3.8%
Commodities & Alternatives				
Commodities	RICI TR	**USD**	3.1%	-2.8%
Agricultural Commodities	RICI Agriculture TR	**USD**	-0.4%	1.0%
Oil	Brent Crude Oil	**USD**	9.9%	-7.3%
Gold	Gold Spot	**USD**	2.2%	10.2%
Hedge funds	HFRX Global Hedge Fund	**USD**	0.9%*	3.5%*
Interest rates				
United States			1.25%	
United Kingdom			0.25%	
Eurozone			0.00%	
Japan			0.10%	
Australia			1.50%	
South Africa			6.75%	

Source: Bloomberg ** denotes estimate*

Market Performance - UK (All returns in GBP)

Asset Class/Region	Index	To 31 July 2017		
		Currency	1 Month	Year to date
Developed markets equities				
UK - All Cap	MSCI UK NR	**GBP**	1.1%	5.8%
UK - Large Cap	MSCI UK Large Cap NR	**GBP**	0.7%	5.1%
UK - Mid Cap	MSCI UK Mid Cap NR	**GBP**	2.2%	6.0%
UK - Small Cap	MSCI Small Cap NR	**GBP**	2.8%	12.0%
United States	S&P 500 NR	**USD**	0.6%	4.1%
Continental Europe	MSCI Europe ex UK NR	**EUR**	1.8%	13.7%
Japan	Topix TR	**JPY**	0.8%	6.6%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	**USD**	3.7%	17.9%
Global developed markets	MSCI World NR	**GBP**	1.0%	6.0%
Global emerging markets	MSCI EM (Emerging Markets) NR	**GBP**	4.5%	17.5%
Bonds				
Gilts - All	BofA Merrill Lynch Gilts TR	**GBP**	0.3%	0.6%
Gilts - Under 5 years	BofA Merrill Lynch Gilts TR under 5 years	**GBP**	0.2%	0.0%
Gilts - 5 to 15 years	BofA Merrill Lynch Gilts TR 5 to 15 years	**GBP**	0.5%	1.2%
Gilts - Over 15 years	BofA Merrill Lynch Gilts TR over 15 years	**GBP**	0.2%	0.6%
Index Linked Gilts - All	BofA Merrill Lynch Inflation-Linked Gilts TR	**GBP**	-1.3%	-1.8%
Index Linked Gilts - 5 to 15 years	BofA Merrill Lynch Inflation-Linked Gilts TR 5 to 15 years	**GBP**	0.0%	0.2%
Index Linked Gilts - Over 15 years	BofA Merrill Lynch Inflation-Linked Gilts TR over 15 years	**GBP**	-1.8%	-2.6%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	**GBP**	0.7%	3.0%
US Treasuries	JP Morgan United States Government Bond Index TR	**USD**	-1.2%	-4.4%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	**USD**	-0.7%	-2.1%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	**USD**	-0.3%	-0.7%
Euro Government Bonds	Citigroup EMU GBI TR	**EUR**	2.3%	4.0%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	**EUR**	2.9%	6.3%
Euro High Yield	BofA Merrill Lynch Euro High Yield Constrained TR	**EUR**	3.0%	10.3%
Global Government Bonds	JP Morgan Global GBI	**GBP**	0.3%	-1.0%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	**GBP**	0.3%	-0.7%
Global Convertible Bonds	UBS Global Focus Convertible Bond	**GBP**	0.5%	1.9%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	**GBP**	-1.0%	-0.1%

Source: Bloomberg [e] *denotes estimate*

Market Performance - UK (All returns in GBP)

Asset Class/Region	Index	To 31 July 2017		
		Currency	1 Month	Year to date
Property				
UK Direct Property	UK IPD All Property TR	**GBP**	0.0%	4.8%*
Global Property Securities	S&P Global Property USD TR	**GBP**	1.3%	3.9%
Currencies				
Euro		**GBP**	2.2%	5.0%
US Dollar		**GBP**	-1.4%	-6.6%
Japanese Yen		**GBP**	0.4%	-0.9%
Commodities & Alternatives				
Commodities	RICI TR	**GBP**	1.7%	-9.0%
Agricultural Commodities	RICI Agriculture TR	**GBP**	-1.8%	-5.5%
Oil	Brent Crude Oil	**GBP**	8.4%	-13.3%
Gold	Gold Spot	**GBP**	0.8%	3.1%
Interest rates				
United Kingdom			0.25%	
United States			1.25%	
Eurozone			0.00%	
Japan			0.10%	

Source: Bloomberg *estimate*

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)	Positive
Emerging market equities	Positive
Fixed Income	
Government	Neutral
Index-linked (relative to government)	Neutral
Investment grade (relative to government)	Neutral
High yield	Neutral
Loans	Neutral
Emerging market debt	Neutral
Convertible bonds	Neutral
Alternatives	
Commodities	Neutral
Property (UK)	Neutral
Currencies	
GBP	Neutral
Euro	Neutral
Yen	Neutral

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