momentum

Viewpoint

Monthly market update

January 2015

global investment management

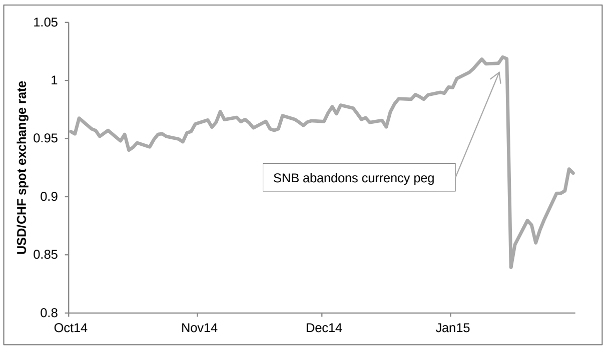
Contents

1. Market commentary

January was another extraordinary month in markets. Volatility continued to rise in most markets while yields on many government bonds across Europe and Japan fell into negative territory. Longer dated bond yields fell almost everywhere, including in the world's two fastest growing economies – the UK and US – where yields fell to all-time lows.

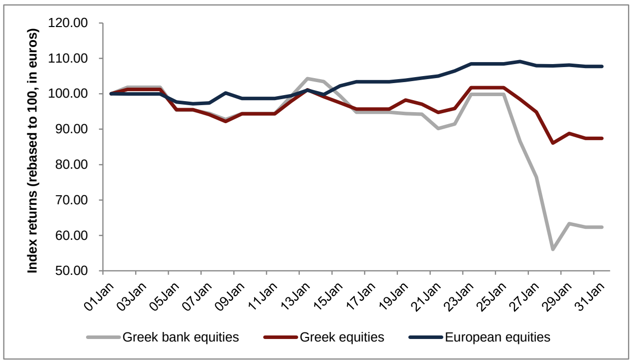
Europe dominated the news last month. First the Swiss National Bank (SNB) shocked markets by abandoning its currency peg to the euro, introduced in 2011. The Swiss franc immediately appreciated by 30% against the US dollar, before settling down to a gain of circa 20%. The move by the SNB occurred ahead of the long anticipated move by the European Central Bank (ECB) to introduce a programme of full scale Quantitative Easing (QE). With a series of well-orchestrated leaks ahead of the formal announcement, ECB President Mario Draghi managed to surprise markets by announcing a larger than expected programme totalling €60 billion per month. The programme is set to start in March 2015 and will run until September 2016, but with an open-ended commitment to extend the programme if there is not a resultant pickup in inflation. At a minimum therefore, the ECB will buy assets worth €1.1 trillion, or circa 11% of euro area GDP.

Figure 1: SNB abandons euro peg



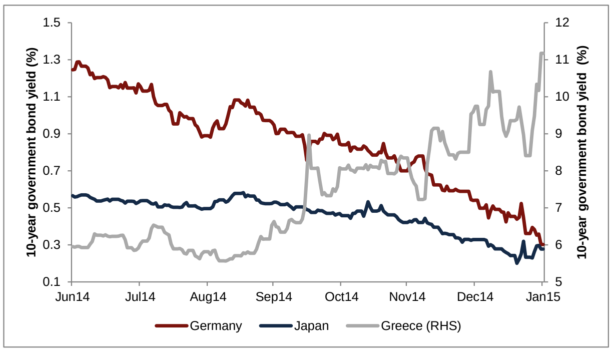
In Greece, the leftist Syriza party won the general election and moved quickly to form a government with the right wing Independent Greeks, who share a strong objection to Greece's bailout conditions. Syriza's aggressive anti-austerity rhetoric unnerved markets in the immediate aftermath of the election, causing Greek bonds and equities to sell off. Greece's banking sector suffered in particular, halving in value. As Syriza toned down its rhetoric in the following days, equities recovered some of the losses, but the situation remains highly unpredictable.

Figure 2: European equities versus Greek equities and banks



The immediate impact of these events was to push the euro materially lower against all major currencies, falling by 6.7% versus the dollar, 3.5% versus sterling and 8.4% versus the Japanese yen (the yen actually rose by 1.8% versus the greenback over the month). This pushed European bond yields lower and equities higher. Although 10-year Greek bond yields spiked to over 10%, and the Greek equity market fell substantially (-12.5% in euro terms), there was very little impact on other peripheral markets, with yields on Spanish, Portuguese and Italian bonds all lower over the month. Yields on the safe European sovereign credits continued to grind lower. German bunds traded in negative yield territory as far out along the curve as five years, and 10-year yields fell below 0.4%.

Figure 3: Government bond yields in Greece, Germany and Japan



In these unprecedented times, with the fear of deflation spreading across many developed regions, central banks embarked on further monetary easing, with ten major central banks easing policy in January. The most notable was the ECB but central banks in Australia, Canada and India also cut rates. The People's Bank of China reduced banks' reserve requirements as it continues to try to combat China's slowing growth. Despite being the fastest growing economy in the developed world last year, there are still no signs of an inflationary pick up in the UK, even though jobs growth remains remarkably strong. The US Federal Reserve is also maintaining a cautious approach to interest rate policy, continuing to state that they will be "patient" in regards to their first hike.

Equity markets fell in the first half of January as the continuing sharp fall in the oil price unnerved investors and led to further falls in the price of energy shares. Markets rebounded, however, post the ECB's announcement. Europe led the way with gains of 7.7% in euro terms. Germany, arguably the biggest beneficiary of the weak euro, outperformed adding 9.1% in euro terms. The UK returned 2.8% in sterling terms and Japan 0.5% in yen terms. Notably, the US underperformed, falling by 3.0% as the strong dollar (which reached its seventh consecutive month of rises versus a basket of major global currencies in January) started to weigh on US corporate profits. Overall global equities returned -1.8%, mostly due to the underperformance of the US.

In the short term, the Greek situation is likely to have a disproportionate impact on markets. The current bailout programme of loans ends on the 28th of February and requires renegotiation to be extended. The most likely outcome to these negotiations is a further period of 'muddling through'. Nevertheless, some nervousness in markets is inevitable as talks progress. Beyond this, however, markets look set for further gains. The economic recovery is picking up, albeit slowly, and the scale of monetary easing via global QE is the biggest since the crisis started in 2008. The oil price recovered some of its recent losses to end January at circa $50 per barrel. This will ease investor fears while still leaving consumers with a windfall, some of which should translate into spending and growth.

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

2. Market performance

Asset class/region	Index	Currency	Month	Year to date
		To 30 January 2015		
Developed markets equities				
United States	S&P 500 NR	USD	-3.0%	-3.0%
United Kingdom	MSCI UK NR	GBP	2.8%	2.8%
Continental Europe	MSCI Europe ex UK NR	EUR	7.7%	7.7%
Japan	Topix TR	JPY	0.5%	0.5%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	1.5%	1.5%
Global	MSCI World NR	USD	-1.8%	-1.8%
Emerging markets equities				
Emerging Europe	MSCI EM Europe NR	USD	-3.5%	-3.5%
Emerging Asia	MSCI EM Asia NR	USD	2.4%	2.4%
Emerging Latin America	MSCI EM Latin America NR	USD	-6.2%	-6.2%
BRICs	MSCI BRIC NR	USD	1.1%	1.1%
Global emerging markets	MSCI EM (Emerging Markets) NR	USD	0.6%	0.6%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	USD	2.9%	2.9%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	3.3%	3.3%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	3.0%	3.0%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	0.7%	0.7%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	5.5%	5.5%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	4.7%	4.7%
Euro Government Bonds	Citigroup EMU GBI TR	EUR	2.3%	2.3%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	0.9%	0.9%
Euro High Yield	Barclays European HY 3% Issuer Constraint Total Return Index Value	EUR	1.0%	1.0%
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	0.0%	0.0%
Australian Government	JP Morgan Australia GBI TR	AUD	2.1%	2.1%
Global Government Bonds	JP Morgan Global GBI	USD	0.3%	0.3%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	USD	-0.4%	-0.4%
Global Convertible Bonds	UBS Global Focus Convertible Bond	USD	-0.9%	-0.9%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	0.6%	0.6%

Source: Bloomberg. e denotes estimate

		To 30 January 2015		
Asset class/region	Index	Currency	Month	Year to date
Property				
US Property Securities	MSCI US REIT NR	USD	6.7%	6.7%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	7.7%	7.7%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	1.9%	1.9%
Global Property Securities	S&P Global Property USD TR	USD	5.5%	5.5%
Currencies				
Euro		USD	-6.7%	-6.7%
UK Pound Sterling		USD	-3.3%	-3.3%
Japanese Yen		USD	2.4%	2.4%
Australian Dollar		USD	-5.0%	-5.0%
South African Rand		USD	-0.7%	-0.7%
Commodities & Alternatives				
Commodities	RICI TR	USD	-5.4%	-5.4%
Agricultural Commodities	RICI Agriculture TR	USD	-6.7%	-6.7%
Oil	Brent Crude	USD	-7.6%	-7.6%
Gold	Gold Spot	USD	8.3%	8.3%
Hedge funds	HFRX Global Hedge Fund	USD	-0.2%	-0.2%
Interest rate			**Current rate**	**Change at meeting**
United States	12 February 2015	USD	0.25%	-
United Kingdom	12 February 2015	GBP	0.50%	-
Eurozone	12 February 2015	EUR	0.05%	-
Japan	21 January 2015	JPY	0.10%	-
Australia	03 February 2015	AUD	2.25%	-
South Africa	12 February 2015	ZAR	5.75%	-

Source: Bloomberg. e denotes estimate

3. 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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