

Viewpoint

Monthly market update

March 2016



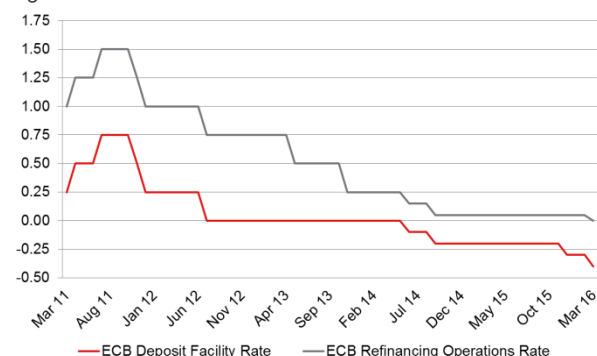
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1. Market commentary

The recovery in markets, which started in February, continued into March and by month-end many equity markets had recovered much of the ground lost in the big sell-off at the start of the year. A rally of 12.6% in the MSCI World index from the February lows to the end of March left the year-to-date return at -0.3%. Emerging markets led the way, with a return of 13.2% in March alone, taking the year to date return to 5.7%. Among the major developed equity markets the US produced the best return, 6.7% in March, bringing the S&P 500 index to within a whisker of its all-time high. Europe and Japan also rallied, but less strongly in local currency terms: continental Europe up 1.9% in euro terms in March; the UK up 1.7% (sterling terms) and Japan up 4.8% in yen terms. Credit participated fully in the rally in risk assets, with investment grade bonds up 2.8% in March, high yield up 4.4% and EM debt up 3.2%.

Figure 1. ECB interest rates



Several factors lay behind the recovery, aside from the fact that markets have oversold at the start of the year. First, the oil price bottomed in late January and rallied over 50% at time of writing, to above USD 40 per barrel. This eased the pressure on the oil sector and related companies, as well as on several important emerging economies. Second, signs that the key US, European and Chinese economies were showing stability after a soft patch, with a series of data releases which on balance pointed to continuing, albeit relatively subdued, growth added to the performance of risk assets. Third, once again the central banks provided big support, with the European Central Bank over-delivering on its long anticipated round of further monetary easing. The bank cut interest rates further into negative territory, extended the size and extent of its asset purchase programme,

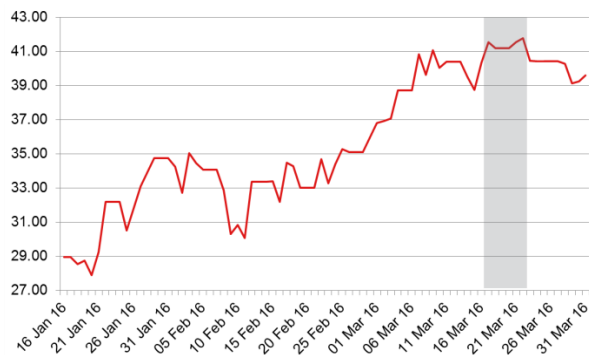
and provided a new financing facility for Eurozone banks to help offset the problem of negative interest rates on profitability. The US Federal Reserve then delivered a series of more dovish statements, including changing its expectations for interest rate rises this year from four to two, and lowering its longer term expectations for interest rates by some 0.25 percentage points. Finally the weakness in the US dollar provided much needed relief to commodities and emerging markets, with several emerging currencies enjoying double digit gains. The greenback's trade-weighted index fell by 3.7% in March.

Figure 2. USD over 3 years



Notably the rally in emerging market equities started on the same day that the oil price bottomed; risk assets have in the short-term become highly sensitive to movements in the oil price. Despite record high crude inventories, evidence of significant falls in US oil production together with rising demand for oil provided support for the price, but arguably the most important factor was discussions among OPEC, and certain non OPEC members, of a production freeze at current levels. The April 17th meeting to discuss this is becoming a key focal point for markets. Whatever the outcome of this meeting, the prospect of a better balance between supply and demand is drawing closer, and by early 2017 the current oversupply in the oil market is likely to be at or close to an end. There are therefore improving prospects that the bottom of the market has been reached, and a modest recovery underway, towards the USD 50 level that many forecasters see as the new equilibrium price.

Figure 3. Oil price over Q1



Having experienced a strong rally, and against a background of subdued growth, corporate profitability under pressure, continuing debt problems especially in Europe, and question marks over extraordinary monetary policy, markets are due a period of consolidation. On the positive side, the worst fears and consequences of the crash in oil and commodity markets are now fully priced in and discounted, and we may already have seen the bottom in these markets; additionally economies continue to grow, albeit modestly, while emerging markets are 5 years

through the down cycle and offer recovery prospects from these levels. Finally, a damaging surge in inflation seems a distant prospect, and with USD 7 trillion of government debt, or about one third of the total in issue globally, trading with negative yields, risk assets are likely to see continuing support. However, with these competing forces on markets, it is likely that the volatility we have witnessed in the first quarter of this year will be a feature in the months if not years ahead. In these conditions we believe it is important to stay invested, broadly diversified, and patient. Alongside risk assets, safe havens such as investment grade bonds and gold or gold producers, offer good diversification and some protection from periods of market dislocation. Finally the big shift from growth to value stocks in the past quarter illustrates the benefit of diversification across equity styles, and with value still trading at relatively low levels, widespread opportunities still exist in the value sector globally.

Source: Bloomberg. Returns in US dollars unless otherwise stated. March 2016.

2. Market performance

		To 31 March 2016		
Asset class/region	Index	Currency	1 month	Year-to-date
Developed markets equities				
United States	S&P 500 NR	USD	6.7%	1.2%
United Kingdom	MSCI UK NR	GBP	1.7%	0.2%
Continental Europe	MSCI Europe ex UK NR	EUR	1.9%	-7.1%
Japan	Topix TR	JPY	4.8%	-12.0% ^e
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	11.6%	1.9%
Global	MSCI World NR	USD	6.8%	-0.3%
Emerging markets equities				
Emerging Europe	MSCI EM Europe NR	USD	16.1%	14.3%
Emerging Asia	MSCI EM Asia NR	USD	11.4%	1.9%
Emerging Latin America	MSCI EM Latin America NR	USD	20.4%	19.1%
BRICs	MSCI BRIC NR	USD	14.9%	1.3%
Global emerging markets	MSCI EM (Emerging Markets) NR	USD	13.2%	5.7%
Bonds				
US Treasuries	JP Morgan United States Government Bond Index TR	USD	0.1%	3.4%
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	1.9%	4.7%
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	2.8%	4.0%
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	4.4%	3.4%
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	-0.2%	5.2%
UK Corporate (investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	2.1%	3.0%
Euro Government Bonds	Citigroup EMU GBI TR	EUR	0.5%	3.4%
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	1.4%	2.5%
Euro High Yield	BofA Merrill Lynch Euro High Yield Constrained TR	EUR	3.8%	2.0%
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	1.1%	4.6%
Australian Government	JP Morgan Australia GBI TR	AUD	-0.4%	2.5%
Global Government Bonds	JP Morgan Global GBI	USD	2.2%	6.7%
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	USD	2.6%	5.8%
Global Convertible Bonds	UBS Global Focus Convertible Bond	USD	4.6%	-0.1%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	3.2%	5.9%

Source: Bloomberg. ^e denotes estimate

		To 31 March 2016		
Asset class/region	Index	Currency	1 month	Year-to-date
Property				
US Property Securities	MSCI US REIT NR	USD	10.1%	5.9%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	2.4%	5.5%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	8.3%	0.9%
Global Property Securities	S&P Global Property USD TR	USD	9.8%	5.1%
Currencies				
Euro		USD	4.7%	4.8%
UK Pound Sterling		USD	3.2%	-2.6%
Japanese Yen		USD	0.1%	6.8%
Australian Dollar		USD	7.2%	5.1%
South African Rand		USD	7.5%	4.8%
Commodities & Alternatives				
Commodities	RICI TR	USD	5.0%	-0.9%
Agricultural Commodities	RICI Agriculture TR	USD	4.5%	-0.2%
Oil	Brent Crude Oil	USD	10.1%	6.2%
Gold	Gold Spot	USD	-0.5%	16.1%
Hedge funds	HFRX Global Hedge Fund	USD	1.3% ^e	-1.8% ^e
Interest rates		Current rate		
United States		0.50%		
United Kingdom		0.50%		
Eurozone		0.05%		
Japan		-0.10%		
Australia		2.00%		
South Africa		7.00%		

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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