momentum
global investment management

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GLOBAL MATTERS
MONTHLY MARKET UPDATE

December 2020

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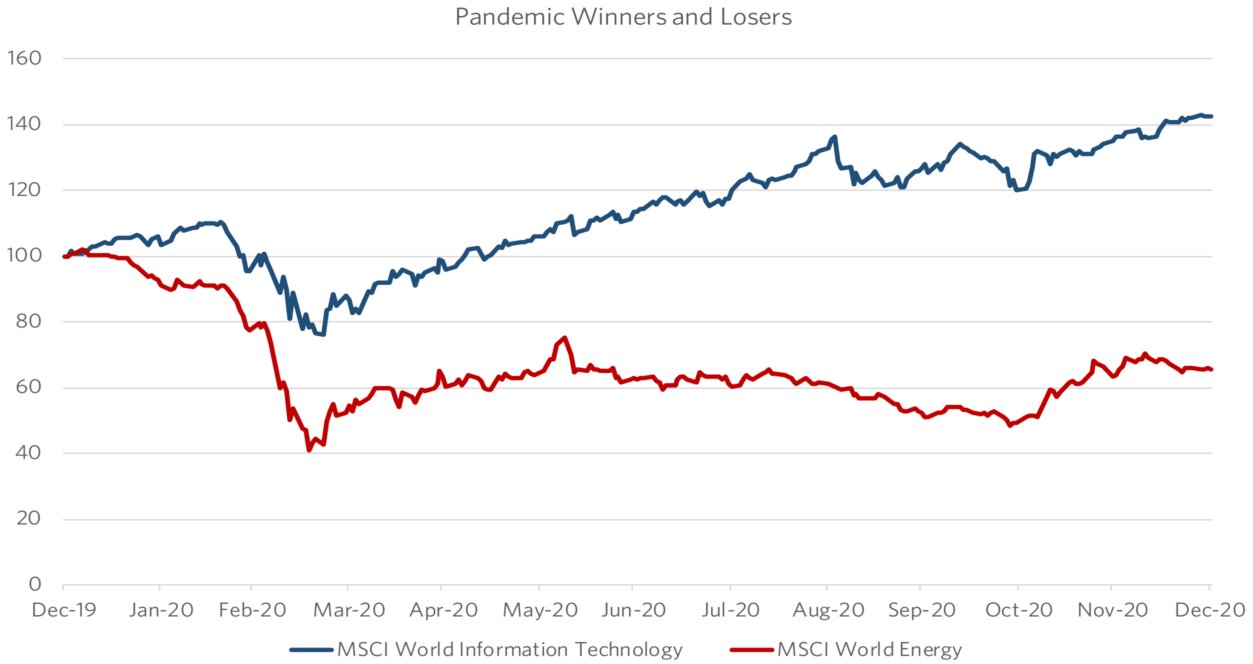
Market Commentary - December 2020

2020 Review

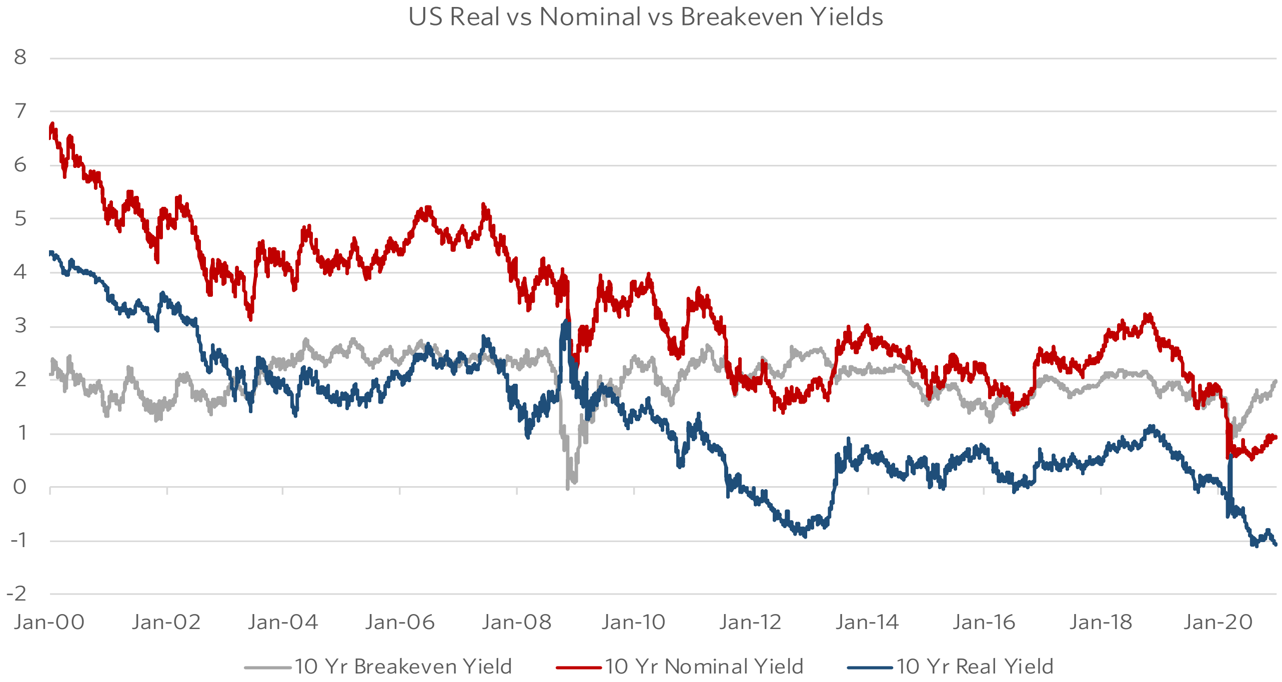
Returns in 2020 of 16% from global developed world equities, 18% from emerging markets, and 10% from global government bonds (all in USD terms) mask the enormous turmoil wrought by the coronavirus pandemic and the scale of its economic, financial and human damage: an exogenous shock with global reach, not on radar screens a year ago and matched in the past 100 years only by world war. Behind the headline figures is a year of extraordinary volatility, with a sudden and dramatic collapse of markets as the pandemic spread rapidly beyond China (at 33 days, the fastest and shortest bear market in the past century), and an equally sudden recovery triggered by fiscal and monetary support on a scale never before seen.

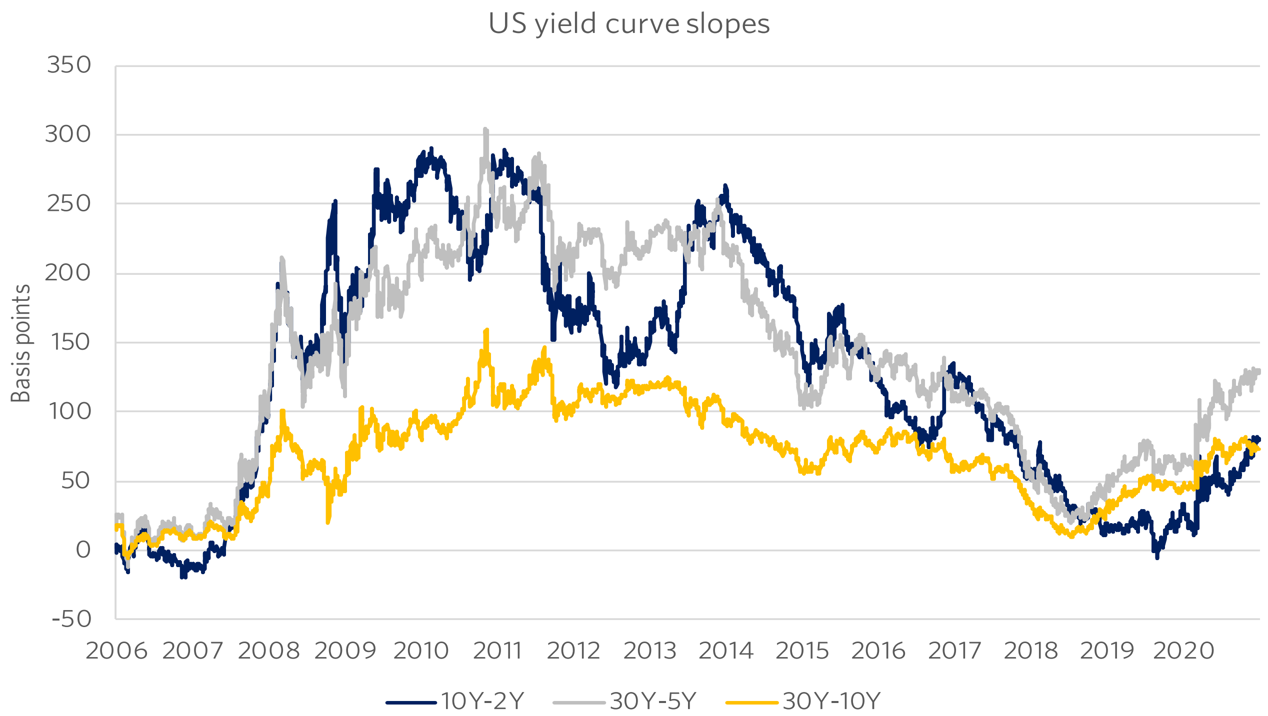
There was huge volatility between and within markets too; without the phenomenal performance of the digital winners from the pandemic and the behavioural changes triggered, aggregate equity market returns would be very different: value stocks, largely reflecting the pandemic losers such as energy, financials, real estate, hospitality and tourism, were down over the year, despite a rally of 19% in the final 2 months following the news of vaccine success and, to a lesser extent, Biden's election as US President. At a regional level the differing extent of the economic damage from COVID-19 together with the proportion of pandemic winners in stock markets produced substantial differences in performance. The US returned 18% in the year, dominated by the so-called FAANGs and other tech stocks, and east Asian markets also performed well as they were seen to bring the pandemic under control more effectively than elsewhere, whereas Europe struggled with more damaging economic impacts from the pandemic, and a worrying second wave later in the year, as well as higher exposure to value stocks. Europe ex UK managed only a marginal gain in euro terms in the year while the UK market was down 13%, negatively impacted too by the intense uncertainty, at least until Christmas Eve, surrounding the shape of the future trading relationship with the EU. In emerging markets the bulk of returns came from China, up 30%, which recovered from the pandemic more rapidly and successfully than elsewhere; emerging markets in SE Asia, Europe and Latin America suffered double digit falls.



Source: Bloomberg, Momentum Global Investment Management

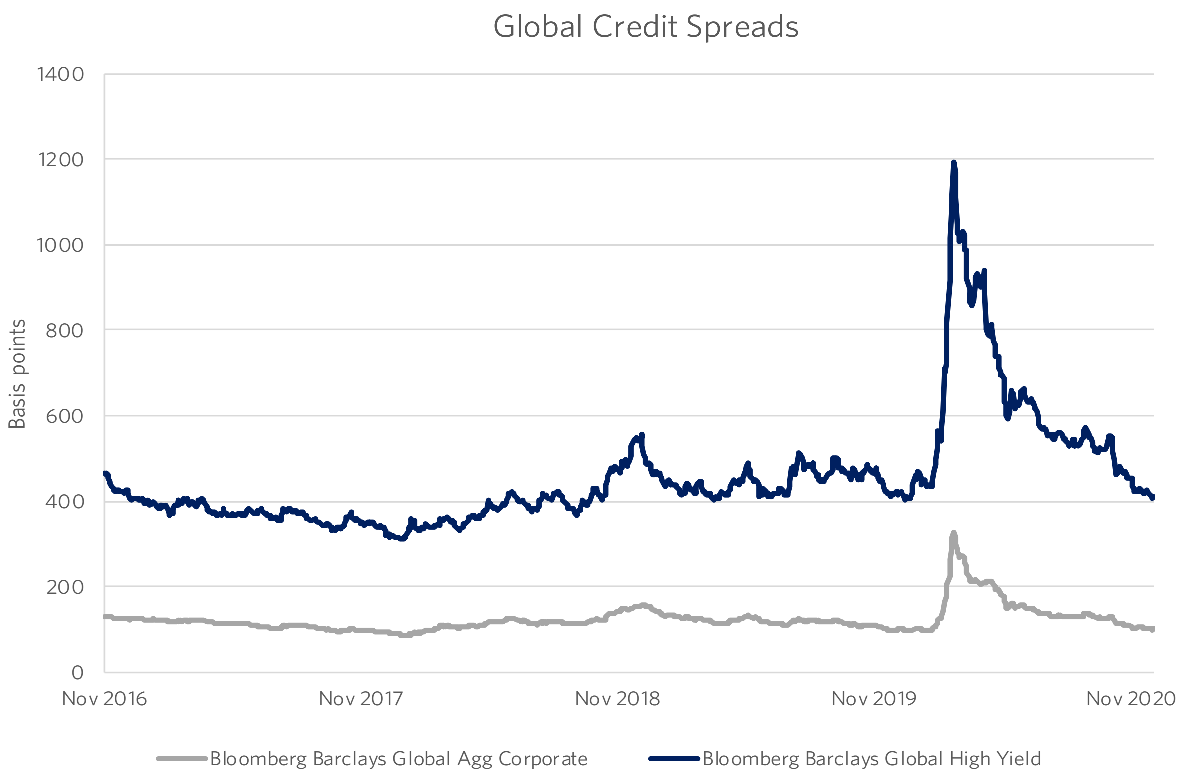
Bond markets were driven by a substantial fall in both nominal and real yields as policy rates were cut to near or below zero across the developed world and real rates fell to new lows, well into negative territory. Returns for the year were led by the higher yielding bond markets, with the US and UK +8-9%, while in the euro area the peripheral markets significantly outperformed German bonds as spreads tightened in the face of substantial ECB buying. However, most of the returns on government bonds came in the first half of the year when economies slumped into deep recession. As recovery took hold and positive news of vaccine developments emerged, along with increased prospects for a substantial fiscal spending programme in the US as a result of Biden's win, the yield on 10 year US Treasuries rose from a low of 0.5% in early August to 0.9% by year end, having started 2020 just shy of 2%.





Source: Bloomberg, Momentum Global Investment Management

Credit markets fell sharply as the pandemic took hold in Q1 but recovered rapidly in the face of massive injections of liquidity, falling interest rates and a hunt for yield. As the 'reflation trade' emerged later in the year credit spreads narrowed to near historic lows, and investment grade, high yield and emerging market bonds outperformed government bonds, recovering most of their underperformance earlier in the year. However, the stand-out performance in the year in the fixed income sector was a 23% return from convertible bonds, a highly risk-efficient asset to own in multi-asset portfolios, providing participation in equity market upside along with downside protection from the bond component.



Source: Bloomberg, Momentum Global Investment Management

Inflation expectations, having fallen sharply as economies collapsed during the first wave of the pandemic, picked up during the second half of the year as prospects for economic recovery improved while central banks continued to pursue an aggressive monetary easing programme across the world, fuelling concerns among investors that inflation could pick up in the medium term.

A combination of intense uncertainty, zero interest rates, a weak dollar, down 13% on a trade weighted basis from its March peak to the year end, and historically low rates on other defensive assets, led to the gold price moving to all-time highs of over $2000 by August. Growing confidence in recovery and vaccine development saw a period of consolidation in gold, which ended the year at $1900, still one of the best asset class returns in 2020 of 25%, proving its mettle as an excellent portfolio diversifier.

Globally and across asset classes, ESG investing moved into a new phase in 2020 and is now fully mainstream in portfolio construction. While the outperformance of sustainability factors was mostly due to the economic collapse triggered by the pandemic and resultant underperformance of the least 'green' sectors, rather than by ESG factors alone, the shift to ESG investing is an irreversible trend.

2021 Outlook

As we enter the new year the deep uncertainties which beset 2020 have lifted. Back in March, the end of the pandemic was nowhere in sight, few had expectations of a vaccine for several years or indeed ever, many expected a chaotic end to the UK's transition period with the EU, and fears about the outcome of the US Presidential election were surfacing. Although second waves and mutations of coronavirus are ravaging many parts of the world, particularly the developed economies of the northern hemisphere, the extraordinary achievements of scientists in developing effective vaccines in record time have been a game changer. There is now not just light at the end of the tunnel, but the exit is in full sight.

Risks remain, notably around the effectiveness of vaccines against the new emerging strains of the virus and the logistical challenges of mass vaccination programmes, but there is now a clear path to exiting the restrictions which have inflicted immense damage on economies and especially certain sectors, on business and consumer confidence, and on employment. The first quarter of the year will be very tough and could well result in double-dip recessions in parts of Europe and North America, but thereafter the beginnings of a return to near-normality should be underway and the conditions are set for a strong recovery: release of pent-up consumer demand, renewed business investment, refocus of fiscal spending on stimulus and growth rather than support for businesses and people most damaged by the pandemic, and continuing ultra-loose monetary policy.

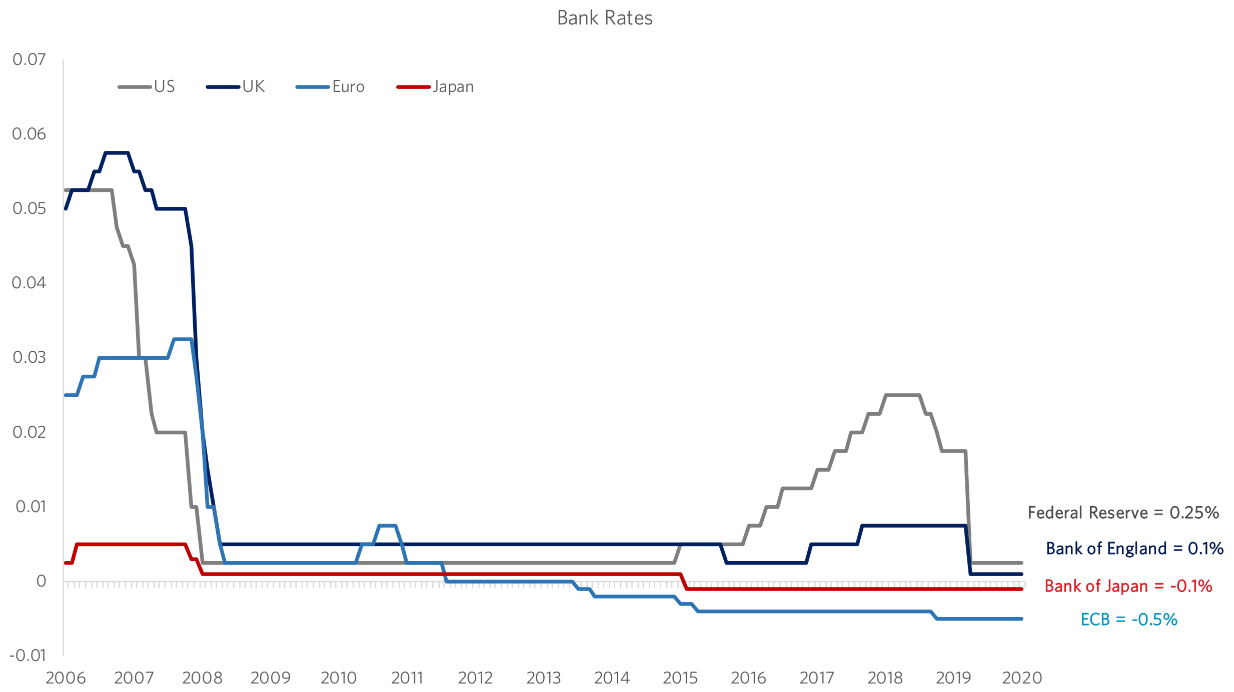
While the pandemic has rightly dominated the narrative in the past year, and the vaccine success was by far the most important development in Q4, the news on the US election and the UK-EU Brexit deal were also very significant and lift heavy clouds that have been holding back confidence. The end of the chaotic Trump era and return of stability, predictability and reliability in US leadership have been widely welcomed, and the much-feared contested election and break down of law and order have been largely avoided: the constitution has prevailed. Biden's success is likely to result in larger fiscal packages to promote growth, along with some tax rises, but the more extreme elements of the Democrat's policy agenda are unlikely to be implemented given the narrowness of the result, especially in the Senate. Stricter regulations for 'big tech' are now more likely but there will be a thawing of international relationships, especially with US allies, a return to the post WWII international order, and renewed focus on multi-lateralism. Trade related uncertainty will be much reduced, although relations with China will be one of Biden's greatest challenges beyond the pandemic, with a return to the pre-Trump status quo ante highly unlikely given the bi-partisan support for a more hawkish approach to China; Sino-US tensions are likely to continue to play out through trade and tariff controls, security, human rights and more subversively through Hong Kong.

In classic EU style, the Brexit negotiations came down to the wire, but in the event PM Johnson confounded the doomsayers by delivering a trade deal free of tariffs and quotas while restoring sovereignty and taking the UK out of the jurisdiction of the European Court of Justice. His manifesto commitment of 'getting Brexit done' has been fulfilled and has given the UK much-needed good news and a boost to confidence after four and a half years of post-referendum uncertainty. In the PM's own words 'the old and vexed question of Britain's political relations with Europe' have been resolved; aside from a small minority of hard core 'rejoiners' the country has moved on. There are challenges ahead as the UK adjusts to its new trading arrangements with its biggest partner, and there is much to be resolved around service industries, most importantly the key finance sector, but there is no question that the deal removes intense uncertainty and brings new opportunities globally. Already the UK has agreed trade deals with 62 countries and is in advanced discussions with the biggest prize, the US. Together with the UK's early approval and roll-out of vaccines, the Brexit deal brings much greater optimism, the foundation for a robust recovery, and is likely to herald the end of the long period of underperformance of the UK equity market.

Conclusion

Despite the human and economic distress being inflicted by the pandemic on large parts of the world, we enter 2021 with considerable optimism. The vaccines will facilitate a gradual lifting of social mobility and other economically damaging restrictions, and in time will restore near-normality. The first quarter of the year will be challenging but beyond that there are grounds for expecting a very strong rebound in activity. Much of 2021 and into 2022 should be an unusually strong period for global growth, underpinning a huge recovery in corporate earnings. Beyond the pandemic, the biggest of the immediate worries, Brexit and the US Presidency, have been removed and political issues should feature much less among investor concerns.

At the same time, policy measures will be supportive. Central banks across the world are committed to maintaining substantial asset purchases and interest rates at or very close to the lower effective bound, close to or below zero. There is no prospect of increases in policy rates in 2021, and probably for a considerable time beyond. The importance of the Fed's decision in late 2020 to move to average inflation targeting should not be under-estimated; it means the Fed is prepared to let the economy 'run hot' for a period to achieve its inflation target and underpins the case for 'lower-for-longer'. The ECB is currently reviewing its own policy and is likely to move to a similar approach during 2021.



Source: Bloomberg, Momentum Global Investment Management

The enormous emergency fiscal support provided by many governments to offset the damage wrought by the pandemic will taper off during the year as the virus retreats, but we see no appetite for, or return to, fiscal austerity. With borrowing rates at or close to all-time lows and negative in real terms, the case for increased levels of capital spending is difficult to deny.

Spending will shift to growth enhancing measures, covering infrastructure, communications and green energy/climate change initiatives. The time to focus on paying down the debt mountains built up during the pandemic will come, but not yet as recovery has yet to take firm hold and the global economy is too fragile. During this period an increasing alignment between fiscal and monetary policies is likely, whether by design or otherwise. The test for its durability will surely come if inflation begins to pick up; although this is highly unlikely in the year ahead given the current state of the global economy and over-capacity, it is a risk not to be dismissed.

Against this background, we believe that equities will make further progress and provide the bulk of returns in 2021. We are mindful of the strong gains made in recent weeks and high valuations in some parts of the market but see a rotation into undervalued sectors with the largest recovery potential: value stocks should perform well. Growth stocks play an important part in portfolio construction but high valuations and risks of big tech coming under greater regulatory scrutiny are likely to hold back returns after a stellar period of performance. Generally, we see corporate earnings rather than higher valuations driving markets in 2021.

We believe it is unlikely that bond yields will fall from current levels; more likely we see some steepening of yield curves as the year progresses and economies recover strongly. Other than in their role as the ultimate defensive investment, there are therefore few opportunities in safe haven government bonds; we continue to focus our fixed income investments on credit and emerging market debt to take advantage of their higher yields and the potential for modest spread tightening during the strong recovery phase ahead.

Finally, we believe it is important to retain protection against the risks and uncertainties that inevitably lie ahead. Gold continues to play a role and while it is unlikely to repeat its performance of 2020 it is a proven store of value during both deflationary and inflationary periods - risks which might presently seem remote, but which would have substantial impact.

Our optimism should be tempered by those risks and uncertainties. The roll-out and efficacy of the vaccines, the duration of protection and their impact on transmission; the risk of policy errors, which could be particularly damaging given the extent to which economies and markets have come to rely on central banks and governments for support during the pandemic; the huge public debt overhang which could be disruptive in funding markets; the risks of long term scarring from the pandemic; longer term inflationary concerns; the uncertain evolution of the key US-China relationship; all point to the likelihood of bumps along the way as we navigate through what we hope and expect to be the final stages of the pandemic. As ever, true portfolio diversification, including defensive assets and a range of equity styles, will be the best way to mitigate these risks and enhance returns, and most importantly it will be vital to stay invested; the highly promising prospects for 2021 should reward investors and we see any setbacks in the weeks ahead as a good opportunity to add to portfolio risk.

Market Performance - Global (local returns)

			To 31 December 2020			
Asset Class / Region	**Index**	**Currency**	**1 month**	**3 months**	**YTD**	**12 months**
Developed Markets Equities						
United States	S&P 500 NR	USD	3.8%	12.0%	17.8%	17.8%
United Kingdom	MSCI UK NR	GBP	3.2%	10.6%	-13.0%	-13.0%
Continental Europe	MSCI Europe ex UK NR	EUR	2.2%	10.5%	1.7%	1.7%
Japan	Topix TR	JPY	3.0% e	11.2% e	7.4% e	7.4% e
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	6.6%	19.1%	22.4%	22.4%
Global	MSCI World NR	USD	4.2%	14.0%	15.9%	15.9%
Emerging Markets Equities						
Emerging Europe	MSCI EM Europe NR	USD	10.6%	22.5%	-12.5%	-12.5%
Emerging Asia	MSCI EM Asia NR	USD	7.1%	18.9%	28.4%	28.4%
Emerging Latin America	MSCI EM Latin America NR	USD	11.9%	34.8%	-13.8%	-13.8%
China	MSCI EM China NR	USD	5.2%	15.3%	17.6%	17.6%
BRICs	MSCI BRIC NR	USD	2.8%	11.2%	29.5%	29.5%
Global emerging markets	MSCI Emerging Markets NR	USD	7.4%	19.7%	18.3%	18.3%
Bonds						
US Treasuries	JP Morgan United States Government Bond TR	USD	-0.3%	-0.9%	8.4%	8.4%
US Treasuries (inflation protected)	BBgBarc US Government Inflation Linked TR	USD	1.1%	1.6%	11.5%	11.5%
US Corporate (investment grade)	BBgBarc US Corporate Investment Grade TR	USD	0.4%	3.0%	9.9%	9.9%
US High Yield	BBgBarc US High Yield 2% Issuer Cap TR	USD	1.9%	6.4%	7.0%	7.0%
UK Gilts	JP Morgan UK Government Bond TR	GBP	1.6%	0.6%	9.0%	9.0%
UK Corporate (investment grade)	ICE BofAML Sterling Non-Gilt TR	GBP	1.5%	3.2%	8.0%	8.0%
Euro Government Bonds	ICE BofAML Euro Government TR	EUR	0.1%	1.2%	4.9%	4.9%
Euro Corporate (investment grade)	BBgBarc Euro Aggregate Corporate TR	EUR	0.2%	2.0%	2.8%	2.8%
Euro High Yield	BBgBarc European High Yield 3% Constrained TR	EUR	0.8%	5.2%	2.3%	2.3%
Japanese Government	JP Morgan Japan Government Bond TR	JPY	0.0%	0.0%	-1.0%	-1.0%
Australian Government	JP Morgan Australia GBI TR	AUD	-0.4%	-0.6%	4.4%	4.4%
Global Government Bonds	JP Morgan Global GBI	USD	1.2%	2.3%	9.7%	9.7%
Global Bonds	ICE BofAML Global Broad Market	USD	1.2%	2.7%	8.9%	8.9%
Global Convertible Bonds	ICE BofAML Global Convertibles	USD	6.5%	18.9%	39.2%	39.2%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	2.0%	5.6%	7.1%	7.1%

Source: Bloomberg, Momentum GIM. Past performance is not indicative of future returns. e= estimate

			To 31 December 2020			
Asset Class / Region	**Index**	**Currency**	**1 month**	**3 months**	**YTD**	**12 months**
Property						
US Property Securities	MSCI US REIT NR	USD	3.2%	11.2%	-8.7%	-8.7%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	-0.9%	11.8%	-8.0%	-8.0%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	-0.6%	7.7%	-11.6%	-11.6%
Global Property Securities	S&P Global Property USD TR	USD	3.3%	12.5%	-7.2%	-7.2%
Currencies						
Euro		USD	2.4%	4.2%	8.9%	8.9%
UK Pound Sterling		USD	2.6%	5.8%	3.1%	3.1%
Japanese Yen		USD	1.0%	2.1%	5.1%	5.1%
Australian Dollar		USD	4.8%	7.4%	9.6%	9.6%
South African Rand		USD	5.3%	14.0%	-4.7%	-4.7%
Commodities & Alternatives						
Commodities	RICI TR	USD	5.7%	14.5%	-7.7%	-7.7%
Agricultural Commodities	RICI Agriculture TR	USD	7.6%	17.2%	16.8%	16.8%
Oil	Brent Crude Oil	USD	8.8%	26.5%	-21.5%	-21.5%
Gold	Gold Spot	USD	6.8%	0.7%	25.1%	25.1%
Hedge funds	HFRX Global Hedge Fund	USD	2.4%	5.1%	6.8%	6.8%
Interest Rates				**Current Rate**		
United States				0.25%		
United Kingdom				0.10%		
Eurozone				0.00%		
Japan				-0.10%		
Australia				0.10%		
South Africa				3.50%		

Source: Bloomberg, Momentum GIM. Past performance is not indicative of future returns. e=estimate

Market Performance - UK (all returns in GBP)

			To 31 December 2020			
Asset Class / Region	**Index**	**Local Currency**	**1 month**	**3 months**	**YTD**	**12 months**
Equities						
UK - All Cap	MSCI UK NR	GBP	3.0%	10.6%	-13.2%	-13.2%
UK - Large Cap	MSCI UK Large Cap NR	GBP	2.4%	9.9%	-15.9%	-15.9%
UK - Mid Cap	MSCI UK Mid Cap NR	GBP	4.7%	12.3%	-5.9%	-5.9%
UK - Small Cap	MSCI Small Cap NR	GBP	7.1%	19.8%	-4.9%	-4.9%
United States	S&P 500 NR	USD	1.5%	5.9%	14.4%	14.4%
Continental Europe	MSCI Europe ex UK NR	EUR	2.2%	8.9%	7.6%	7.6%
Japan	Topix TR	JPY	2.1%e	7.9%e	9.3%e	9.3%e
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	4.3%	12.7%	19.0%	19.0%
Global developed markets	MSCI World NR	USD	2.0%	7.8%	12.6%	12.6%
Global emerging markets	MSCI Emerging Markets NR	USD	5.0%	13.2%	14.9%	14.9%
Bonds						
Gilts - All	ICE BofAML UK Gilt TR	GBP	1.7%	0.6%	8.8%	8.8%
Gilts - Under 5 years	ICE BofAML UK Gilt TR 0-5 years	GBP	0.2%	0.1%	1.5%	1.5%
Gilts - 5 to 15 years	ICE BofAML UK Gilt TR 5-15 years	GBP	1.0%	0.4%	5.6%	5.6%
Gilts - Over 15 years	ICE BofAML UK Gilt TR 15+ years	GBP	2.8%	1.1%	13.8%	13.8%
Index Linked Gilts - All	ICE BofAML UK Gilt Inflation-Linked TR	GBP	0.5%	1.2%	11.3%	11.3%
Index Linked Gilts - 5 to 15 years	ICE BofAML UK Gilt Inflation-Linked TR 5-15 years	GBP	0.2%	-0.8%	4.6%	4.6%
Index Linked Gilts - Over 15 years	ICE BofAML UK Gilt Inflation-Linked TR 15+ years	GBP	0.7%	2.2%	15.3%	15.3%
UK Corporate (investment grade)	ICE BofAML Sterling Non-Gilt TR	GBP	1.5%	3.2%	8.0%	8.0%
US Treasuries	JP Morgan US Government Bond TR	USD	-2.6%	-6.3%	5.1%	5.1%
US Corporate (investment grade)	BBgBarc US Corporate Investment Grade TR	USD	0.4%	3.0%	9.9%	9.9%
US High Yield	BBgBarc US High Yield 2% Issuer Cap TR	USD	1.9%	6.4%	7.0%	7.0%
Euro Government Bonds	ICE BofAML Euro Government TR	EUR	0.1%	1.2%	4.9%	4.9%
Euro Corporate (investment grade)	BBgBarc Euro Aggregate Corporate TR	EUR	0.2%	2.0%	2.8%	2.8%
Euro High Yield	BBgBarc European High Yield 3% Constrained TR	EUR	0.8%	5.2%	2.3%	2.3%
Global Government Bonds	JP Morgan Global GBI	GBP	-1.0%	-3.3%	6.6%	6.6%
Global Bonds	ICE BofAML Global Broad Market	GBP	1.2%	2.7%	8.9%	8.9%
Global Convertible Bonds	ICE BofAML Global Convertibles	GBP	6.5%	18.9%	39.2%	39.2%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	GBP	-0.3%	-0.1%	4.0%	4.0%

Source: Bloomberg, Momentum GIM. Past performance is not indicative of future returns.

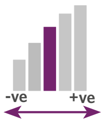
			To 31 December 2020			
Asset Class / Region	**Index**	**Local Currency**	**1 month**	**3 months**	**YTD**	**12 months**
Property						
Global Property Securities	S&P Global Property TR	GBP	1.0%	6.4%	-9.8%	-9.8%
Currencies						
Euro		GBP	-0.2%	-1.5%	5.7%	5.7%
US Dollar		GBP	-2.5%	-5.4%	-3.0%	-3.0%
Japanese Yen		GBP	-1.6%	-3.5%	2.0%	2.0%
Commodities & Alternatives						
Commodities	RICI TR	GBP	3.4%	8.3%	-10.3%	-10.3%
Agricultural Commodities	RICI Agriculture TR	GBP	5.2%	10.8%	13.4%	13.4%
Oil	Brent Crude Oil	GBP	6.5%	19.6%	-23.7%	-23.7%
Gold	Gold Spot	GBP	4.5%	-4.8%	21.6%	21.6%
Interest Rates				**Current Rate**		
United Kingdom				0.10%		
United States				0.25%		
Eurozone				0.00%		
Japan				-0.10%		

Source: Bloomberg, Momentum GIM. Past performance is not indicative of future returns.

Asset Allocation

Equities

Developed Equities



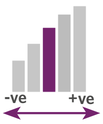
» Sentiment has changed markedly in recent weeks in the wake of the US election and following the announcement of a safe and highly effective vaccine. Undoubtedly risks remain to the global economy but recent newsflow has been a tailwind for risk assets into the end of last year, and to a lesser extent the start of 2021

» Policy measures remain accommodative and are likely to remain so for some time

+ Despite lofty index valuations in some markets and sectors, global equities still offer selective regional and sectoral value

– Earnings will continue to be impacted, or fail to recover, if vaccine development proves less effective or more difficult to roll out than currently thought

UK Equities



» Brexit and Covid 19 continue to drive risk appetite in the UK today. UK equities rallied into the end of the year as a Brexit deal was agreed and the run has pleasingly continued through the start of 2021

» The UK market's larger cap constituents are more globally focused than they are UK, and have earnings shielded in large part from FX swings, which makes them less sensitive when/if those issues resurface. Thus the UK is not unattractive when thinking beyond 2020, and the recent style rotation could help UK equities edge higher

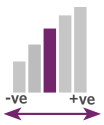
+ Most UK assets remain at a multi decade discount to the global index. Long term investors can buy into some great UK businesses at today's levels

+ The UK has lagged the recovery and offers some scope for a cyclically led catch up should the vaccine rollout - now well underway - prove effective

– UK Plc is having to deal with a painful resurgence of Covid-19 infections. The UK high street is already under extreme pressure and lockdown 3.0 does not help

– The banks and energy heavy UK index may continue to struggle if the recent rotation loses momentum

European Equities

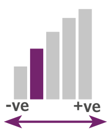


» Europe was hard hit by the first lockdown and is now dealing with secondary lockdowns as cases re-emerge. The European Recovery Fund and continued support from the ECB should help support European risk assets through into 2021

+ Continued ECB asset purchases and policy stimulus will provide support to risk assets in the region

– The ECB has little room to manouvre with rates at current levels; more devolved fiscal action and helicopter money may be needed longer term

US Equities



» With the election behind us, and the vaccine program underway, two major risks have been mitigated. We still view the US market in aggregate as somewhat expensive, but active stockpickers have opportunities today. Headline valuation however keeps the US view in check for now

+ The US remains one of the higher quality markets, and the Dollar something of a haven should the recent positive sentiment wane. It is a natural home for those looking to add to their equity allocations, and that could keep US equities supported despite froth in some places

+ The Fed stimulus is constructive for credit, risk assets and by extension should be constructive for equities

– US equity valuations remain elevated vs other regions today, despite some froth coming out of the stay at home stocks in recent weeks

– The US now has by far the highest rate of reported infections and vaccine complacency is a risk

– Trade and geopolitical risks remain, even with Biden soon to be in the White House; domestic cicil flare ups - like that seen recently in Washington - may continue to cause headlines

Japanese Equities

» At a high level, and considering demographics and locality, Japan has probably had a better outcome from the virus to date than many might have expected. Prospects look reasonable on a sustained pick up in business activity into 2021 should economic activity continue to rebound

+ BoJ ETF buying remains supportive for Japanese risk assets. Asia has stayed ahead of other global regions in the global Corona-cycle which may help Japan be on the front foot for a more sustained rebound in activity, should it prove to have legs

– In a protracted risk off scenario Yen strength resulting from its safe haven status would hurt Japanese equities

Emerging Market Equities

» On a longer term view we remain in favour of EM assets more generally over DM but recognise the continuing risks to developing economies from the Coronavirus, not least in securing and distributing vaccines, and the pressure on local health infrastructure and government budgets

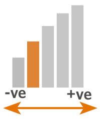
» EM equities have continued to gain alongside global equities in recent months, proving quite resilient on market weakness, and stand to gain further if a sustained rebound materialises

+ EM currencies remain lower in aggregate than a year ago, but have recovered meaningfully as the panic subsided, recovery gathered pace and the Dollar fell. At a lower level, for businesses that earn foreign income this translates into better earnings that helps in some way to offset weaker revenues that will likely eventuate through 2020

– Emerging markets remain prone to bouts of volatility and flow reversal at times of heightened perceived risk. Negative newsflow and any reversal in the recent pick up in sentiment, would likely crimp returns

Fixed Income

Government



» DM government bond prices remain high/yields low despite the more recent back up in yields. They provide some diversification still but cash may prove a better diversifier until a higher level of yields and steeper curves are reached. Nonetheless, given the back up recently seen, and the increasingly consensus view on a reflationary recovery, government bonds offer a modicum of tactical value today

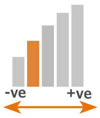
+ Quality government bonds remain one of the better diversifiers, over the long term, in a multi asset portfolio, even when they are optically expensive. For that reason we advocate having some exposure depsite extreme valuations

– Liquidity in the treasury market has been tested several times over the last year, both in the cash treasury market and repo. This causes some concern, but can be allayed with unlimited Fed firepower, which has been provided

– Any spike in inflationary expectations, increasingly a concern among investors albeit still small, could see 'risk free' bonds sell off sharply, more so now that the Fed has explicitly acknowledged a move to target average inflation over time

Index-linked

Relative to government



» Inflation linked bonds cheapened in the Covid induced sell off but have rebounded meaningfully in the interim, but still offer some value. Whilst near term inflation risk looks limited, over 5 to 10 years we take a more constructive view and view breakevens more favourably, preferring over pure rate risk in select markets

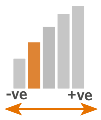
+ Index linked bonds are one of the few ways to meaningfully protect against inflation risk, and with the amount of money pumped into the system, and more scope for helicopter style money, it is a more meaningful concern down the line

+ The Fed's inflation stance has changed, and is likely to mean periods of higher inflation will be tolerated

– Inflationary forces remain muted today, and the reflation trade is becoming an increasingly consensus view

Investment Grade Corporate

Relative to government



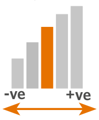
» Investment grade bond spreads have largely normalised after the recent tightening, but are likely to remain supported. With yields now near new lows though, longer term real returns are threatened

+ Central bank buying of IG bonds provides a tailwind for the asset class; there may still be some upside on the table

– "Liquidity remains a concern, and IG is starting to look rich again. We have taken further profit on recent trades The IG universe remains at greater risk of BBB downgrades "

–

High Yield Corporate



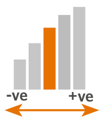
» Like their investment grade corporate cousins, high yield spreads have tightened meaningfully, but still offer some value and a reasonable yield. We are mindful of the more equity like characteristics of the asset class, and continued sensitivity of the (US) index to energy

+ Maturity profiles have been extended in the recent good years, and rates policy and stimulus measures will be directed to keep credit markets functioning, as evidenced by the Fed stepping in to buy HY ETFs - largely to support 'fallen angels'

– Any further weakness in equity markets, for which there is a real possibility at this time, will likely hit HY bonds more than IG

– There is still a meaningful amount of energy exposure in US high yield markets which remains sensitive to any renewed pressure on oil prices

Emerging Market Debt

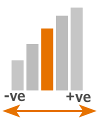


» The asset class continues to look optically attractive, yields well, and we continue to rate favourably. Risks clearly remain and some EM countries still have concerningly high and growing Covid infection rates, and new variants appearing in Brazil and other countries, so as with EM equity some caution recommended

+ Despite recent strength we believe EM bonds continue to offer some of the best longer term real return opportunities in bond markets today, and implied default rates look excessive

– Any renewed Dollar strength may weigh on EM assets, with local bonds and FX likely bearing the brunt EM governments will come under more pressure if Corona related expenditure and support continues to rise

Convertible Bonds



» Convertible bonds had a stellar 2020. The perfect outcome for the asset class

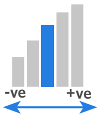
» We continue to favour an allocation to convertibles in a multi asset portfolio for the convexity the asset class brings, but continue to take profit and pare back allocations to at most a neutral level. This reflects a more tempered view towards growth names which are well represented by the convertible universe

+ The natural convexity provided by convertibles should continue to provide reasonable protection against any renewed equity weakness

– Any sustained dampening of implied and realised vols to more normal levels may crimp future returns

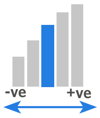
Real Asset / Alternatives

Commodities



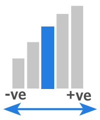
- » The price of commodities moved markedly through most of 2020, and oil's dip into negative territory and subsequent rebound demonstrates the extremes this go to. As the recovery in economic activity continues we would expect some upside but clearly the asset class and individual commodiites are highly sensitive to the economic backdrop
- » Commodity prices are primarily supply and demand driven (Coronavirus and oil a prime example) and idiosyncratic factors can be as important as the global economic cycle
- \+ Gold remains a reasonable hedge against risk off outcomes, and both deflationary and inflationary sentiment, as witnessed more recently through the downward pressure on real yields as inflation expectations have ticked higher. Any cyclical upside and a post vaccine ramp up in industrial production should help industrial commodity prices move higher
- − Coronavirus weighed on the industrials commodities sector through the first half of 2020, and supply chains may remain challenged, until vaccines are rolled out more widely
- − Gold is sensitive to real rates and susceptible to pricing lower on any meaningful move higher in rates, albeit unlikely in the near future

Property



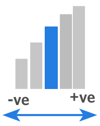
- » Property remains an attractive asset class for investors requiring yield. Rental collections are improving and dividends being reinstated, and the vaccine news is a strong positive for the asset class
- » When viewed against high quality, longer duration Sterling assets and inflation linked bonds, UK property holds appeal, with selective industrial, data centres and residential having more attractive fundamentals than certain under pressure retail and office sectors
- \+ Premium yields and quality assets should attract capital and provide some floor to prices, notwithstanding recent market turbulence
- \+ The longer duration qualities of the asset class make it a good diversifier over the long term within multi asset portfolios
- − As a long duration asset class property remains susceptible to any repricing in long term bond yields
  The retail & office sectors remain under pressure as a result of COVID-19
- − Rent holidays and tenants being unable or unwilling to pay pressures cashflow and ability to pay out income, should lockdowns be prolonged

Infrastructure



- » As a long duration asset class property remains susceptible to any repricing in long term bond yields
  The retail & office sectors remain under pressure as a result of COVID-19
- » Rent holidays and tenants being unable or unwilling to pay pressures cashflow and ability to pay out income, should lockdowns be prolonged
- \+ In a multi asset portfolio the usually more defensive nature of the asset class and a degree of inflation protection make the asset class appealing
- \+ The asset class offers a decent yield at a reasonable valuation today - both equity and debt flavours
- − As a long duration asset class infrastructure remains susceptible to any repricing higher in long term bond yields
- − Regulation can work both for and against the underlying investments, and underlying infrastructure stocks remain exposed to these risks

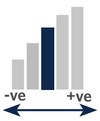
Liquid Alternatives



- » We define this section as less/non-directional, absolute return type strategies that seek to capture long term risk premia or market mispricings, and includes hedge fund alternatives/systematic strategies in predominantly UCITS vehicles
- » We favour owning an allocation to a basket of liquid strategies today to provide additional diversification with high quality bonds remaining expensive
- \+ These strategies provide additional diversification with reasonable return potential, at a time when other traditional diversifiers, such as treasuries, remain expensive
- − The sector is relatively young and growing. Thorough due diligence is vital, and blend is recommended, as idiosyncratic performance can be unpredictable

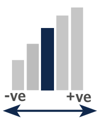
Currencies*

GBP



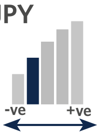
- » Cable' can look forward now that a Brexit deal has been agreed in an eleventh hour deal. We would probably upgrade our view were it not for a still weak economic backdrop, possibility of negative rates and third lockdown. The downward bias to base rates is unlikely to lift the currency higher anytime soon, but it remains cheap on long term valuation measures

EUR



- » The Euro has shown itself to be the favoured carry currency in recent years and 'Covid covering' has helped support it through the tough times. We maintain the more neutral view going forward
- » In real terms the common currency looks about fair value today but there is no obvious and imminent catalyst for an uplift, and on balance the local fundamental backdrop appears weak which makes the currency largely unattractive today

JPY



- » Rate differentials continue to offer little reason to buy the Yen. However, in real terms the Yen remains cheap today. What sets the Yen apart from Sterling and the Euro is the currency's diversifying qualities at times of risk. However, with the Yen's recent strength in a risk on market, and following positive vaccine news, we pare back the view

*Currencies views are expressed versus the US Dollar

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