EQInsight

Asset Allocation: Q2 2016

Implementing a more cautious outlook

We see risks posed by accelerating levels of debt in China, the emergence of negative interest rates, anaemic global growth and the global impact of a finely balanced US rate cycle. These have led us to position our portfolios more defensively.

We have raised cash levels, tactically lightening exposure to developed market equities while maintaining full exposure to absolute return strategies and a light allocation to fixed income.

	Negative				Positive
Equities		Current	Previous		
North America		Current	Previous		
UK		Current	Previous		
Europe			Current	Previous	
Japan			Current	Previous	
Emerging Markets			Previous	Current	
Fixed income		Current			
Commodities		Previous	Current		
Property			Current		
Absolute return				Current	
Cash			Previous	Current	

Current outlook: Q2 2016 Previous outlook (Q1, if different)

Equities

We are taking advantage of a rebound in equities to reduce our overall allocations. Valuations paint a mixed picture globally; developed markets appear fully valued while developing markets are of more interest.

Within equity allocation

Developed market valuations appear expensive and we are reducing our positions. Lacklustre global growth will struggle to drive corporate earnings further to support ever higher prices.

Within emerging markets we are starting to view certain valuations more favourably, despite the general malaise affecting the sector. In Latin America we note that political reform and developing domestic economies could lead to improved conditions for investors.

Fixed Income

Our outlook remains negative and we continue to hold low allocations. There are no imminent signs of a return to inflation. We are watching the slight uptick in some US measures and stabilisation of commodity prices closely, but these factors are yet to spur further rises in US interest rates and have done little to dampen record high bond prices. In addition, we are concerned about reduced liquidity in certain areas of the fixed income market.

Within fixed income allocation

Our positioning remains defensive towards interest rate risk. With bond prices so high, markets are more sensitive to changes in the interest rates that investors demand.

We are picking up yield through corporate bonds. Corporate earnings show no signs of stellar growth but balance sheets remain healthy and cash flows are unlikely to present risks to bond holders. Therefore, significant defaults (outside of the energy sector) are unlikely.

Alternatives

We continue to reduce UK commercial property. This provides a healthy yield but faces headwinds from high valuations and international concerns over the looming EU referendum.

Lack of outstanding value in traditional equity and fixed income markets keep us overweight absolute return strategies.

We have returned to a neutral view on commodities as prices appear to be stabilising.

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