Investment Commentary

THOMAS MILLER INVESTMENT

February 2018

Recent economic developments

■ On the whole, economic reports over the past month have been benign, although data releases have, on balance, been weaker than consensus forecasts. In the US, the key data point has been the advance release of GDP growth rate which showed a deceleration in real GDP growth from a previous pace of 3.2% in Q3 to 2.6% in Q4 2017. The data was notably below consensus forecast of a growth rate of 3% for the quarter.

■ In the UK, the key development from a macroeconomic standpoint was arguably the so-called 'Super Thursday', when the Bank of England's (BoE) Monetary Policy Committee voted on interest rates and released its quarterly inflation report as well as the minutes from its last meeting. Overall, the BoE flagged its expectation that strength in the global economy will drive stronger growth and higher inflation in the UK. Consequently relative to November 2017, when the BoE indicated that there could be two rate hikes of 0.25% over the next three years, it now believes that earlier and more frequent increases are needed. On the back of that, markets have brought forward expectations of further tightening by the Bank, with forecasts of three hikes in 2018 now commonplace.

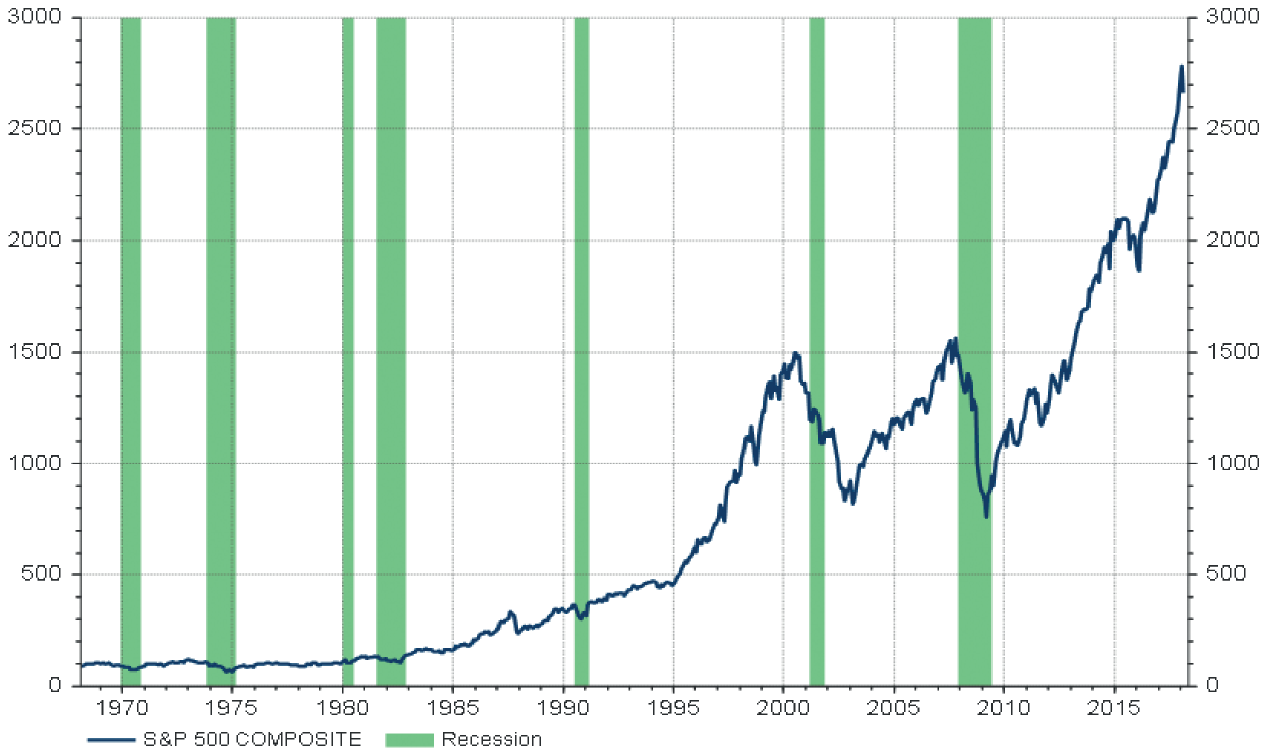
■ The BOE's latest views are currently difficult to reconcile with the available evidence. Indeed, TMI's House view is that global growth is likely to moderate in the year ahead. For this reason, we would not be surprised to see downward revisions to rate hike expectations in the UK in the months ahead. If there is an upside risk to UK interest rates in the year ahead, it is more likely to be driven by inflation rather than growth surprises.

The return of volatility

■ Equity markets entered 2018 in buoyant mood driven by expectations that the strong economic momentum enjoyed for most of 2017 would not only carry into the New Year but accelerate in the months ahead. Indeed, by the end of January, the S&P 500 index had recorded its 15th consecutive month of positive total returns. It seemed to have saved the best for the last as January recorded the strongest performance of that record-breaking run.

■ However, in late January, the remarkable two-year period of equity market rally without meaningful correction and minimal volatility finally came to an abrupt end. At the time of writing, less than two weeks into February, global equity markets are in a broad-based sell-off, with all major stock market indices having recorded peak-to-trough declines of at least 10%.

Chart 1: S&P 500 index and US Recessions, 1970–2018



Source: Thomson Reuters Datastream

■ While the timing and, for that matter, the specific trigger for any sell-off is always difficult to anticipate, it had become clear for some time that the rally across global stock markets had become very extended and markets were due a correction. When markets are rallying strongly, the challenge for benchmark-focused investors is to determine the appropriate point at which to deviate meaningfully (in asset allocation terms) from broad market indices and bear the risk of higher tracking error and potential underperformance. This is not a trivial call.

■ While a market correction is always challenging, even for long term investors, investors need to put the sell-off in appropriate context. Despite the declines of over 10% in major equity markets (so far), the majority of those markets have still delivered total returns in excess of 15% over the past 12 months. Nevertheless, it is worth assessing how bad the sell-off could get.

■ Unlike the market consensus that continues to expect an acceleration in global growth in 2018, as noted above, TMI's House view is that global growth is likely to moderate in the year ahead. However, that is not a bearish growth call in an absolute sense because while we are currently more cautious on the outlook than the market consensus, we continue to expect reasonable, albeit modest, global economic performance.

■ The important thing to note is that at this point, the available evidence suggests that a US or global recession remains a low probability outcome. To the extent that financial market history shows that equity bear markets tend to be associated with recessions (see Chart 1), the low probability of an imminent recession suggests that this latest bout of risk aversion is likely to prove temporary. For long term investors, temporary corrections of speculative excesses present opportunities to enhance long term returns.

Investment strategy summary

■ In recent months, we have noted that our more positive longer term outlook for equities means that we will view any market correction as an opportunity to add to risk assets at more attractive entry levels. Following double digit declines across major stock markets over the past couple of weeks, we now feel more comfortable with slightly higher allocation to risk assets relative to long term weightings within client portfolios.

■ Consequently, we have increased allocation to equities on a tactical basis. We also retain overweight positions in a selected range of alternative investments which exhibit lower volatility and modest correlation with mainstream asset classes. These are funded through underweight positions in cash. We maintain benchmark weighting to fixed income investments across key developed markets.

Abi Oladimeji
Chief Investment Officer

ASSET ALLOCATION

TMI ASSET ALLOCATION SCORECARD (as at 13th February 2018)

	United States	United Kingdom	Euro-Zone ex UK	Asia ex Japan	Japan	Emerging Markets
Equities (overall)	0/+					
Equity allocation by Region	0/-	0	+	0/-	+	+
Bonds (overall)	0					
Agency/ Supra	0	0	0	0	0	0
Corporate bonds	0/-	0/-	0/-	0/-	0/-	0/-
High Yield bonds	-	-	-	-	-	-
Govt guaranteed bonds	0	0	0	0	0	0
Index-linked bonds	0	0	0	0	0	0
Alternatives	+					
Cash	-					

The scorecard above represents our current tactical asset allocation position relative to portfolio benchmark. 0 = neutral, + = overweight, - = underweight.

THOMAS MILLER INVESTMENT

London
90 Fenchurch Street
London
EC3M 4ST
T: +44 (0) 207 204 2200

Birmingham
2nd Floor
Trigate Business Centre
210 - 222 Hagley Road West
Birmingham
B68 0NP
T: +44 (0) 121 222 5070

Isle of Man
Level 2 Samuel Harris House
5 - 11 St Georges Street
Douglas
Isle of Man
IM1 1AJ
T: +44 (0) 1624 645 200

Southampton
Ocean Village Innovation Centre
Ocean Way
Southampton
SO14 3JZ
+ 44 (0) 23 8038 1667

defaqto 2017 DFM Bespoke

3D 2017 THOMAS MILLER INVESTMENT AWARDED BY ARC

COLWMA CITY OF LONDON WEALTH MANAGEMENT AWARDS NOMINEE 2018

Thomas Miller Investment Limited's Despoke DFM Service has been rated 5 Star by Defaqto.

ARC's 3D Award is an independent endorsement of an investment manager's commitment to the principles of transparency, engagement and integrity.

---

tminvestment.com
