THOMAS
MILLER
INVESTMENT

Investment Commentary

MARCH 2015

Economic & Financial Market Commentary

In a continuation of the trend since the last quarter of 2014, economic data released over the past month have been quite mixed.

Although there have been some notable bright spots (e.g. labour markets in the US and UK), on balance, the data from both sides of the Atlantic have typically undershot expectations. However, while the data covering the recent past have been lacklustre, the outlook, as measured by key economic leading indicators, remains positive. Specifically, OECD Composite Leading Indicators, designed to anticipate turning points in economic activity relative to trend, point to positive change in growth momentum in the euro area and stable growth momentum in most other major economies. In the key emerging markets, the outlook for growth remains strong in India while remaining stable in China and Brazil. However, the indicators continue to flag weakening growth momentum in Russia.

> **"The case for monetary policy caution is arguably stronger in the UK. As a result, we do not expect interest rates to rise in the UK in 2015."**

The strength in the US labour market and recent comments by some officials of the US central bank (Fed) have resulted in widespread expectations of a June 2015 start to the US rate tightening cycle. Nevertheless, we continue to believe that the risks of a delay to the start of Fed tightening relative to consensus expectations of a June start are high. This is because concerns about ongoing disinflationary pressures from lower oil prices and stronger US Dollar could counter the effects of stronger labour market data. The case for monetary policy caution is arguably stronger in the UK. As a result, we do not expect interest rates to rise in the UK in 2015. Finally, it is important to note that, from a global standpoint, monetary policy remains accommodative. The ECB has now joined the Bank of Japan as a second major central bank that is currently implementing QE and several other central banks have eased policy in recent weeks.

The behaviour of financial markets so far this year has again confirmed the enduring dominance of monetary policy over fundamentals/valuations as the primary driver of market direction. Specifically, the ongoing divergence in the outlook for monetary policy across the major developed economies is driving significant dispersion in financial market performance. So, while the US Federal Reserve is widely expected to start raising rates later this year, the ECB and the Bank of Japan are implementing Quantitative Easing; and the Bank of England sits in the middle—being widely expected to remain on hold for the rest of 2015.

The result has been a sharp increase in the value of the US Dollar across the board against other currencies, notably the Euro; a broad-based decline in government bond yields across the developed economies; and strong rallies in European and Japanese equity markets.

In light of current valuations, it is clear that neither equities nor bonds are "cheap" or "undervalued" in an absolute sense. Indeed, some longer term valuation metrics suggest that both are quite stretched at current levels. Nevertheless, from a longer term perspective, relative valuation favours equities over bonds. But as Keynes famously noted, the "long run is a misleading guide to current affairs".

Looking out to the rest of the year, it seems likely that the combination of QE, low (and falling) inflation, and various geo-political concerns would ensure that government bond yields remain atypically low. Likewise, the global backdrop of accommodative monetary policy and resulting surplus liquidity could drive equity prices notably higher in the months ahead. But we expect the uncertainty surrounding the outlook for US interest rates to drive volatility higher too.

In the shorter term, momentum and sentiment indicators are now approaching elevated readings for equities. This suggests a higher risk of some price correction (or range-bound trading) in the near term. However, our positive longer term outlook for equities relative to other asset classes means that we would seek to add to equity positions in the event of a meaningful correction. In the currency markets, it is worth noting that investors' bullishness on the US Dollar has now risen to levels that have historically heralded a temporary bout of reversal. Overall, considering the balance of risks and outlook for returns across various asset classes, we retain an asset allocation positioning that is broadly in line with client benchmarks.

Abi Oladimeji
Head of Investment Strategy

ASSET ALLOCATION

TMI ASSET ALLOCATION SCORECARD

	United States	Euro-Zone ex Germany	Germany	United Kingdom	Japan	Emerging Markets
Equities (overall)	0 /+					
Equity allocation by region	0	0	0	0	0	0
Bonds (overall)	0					
Corporate bonds	0	0	0	0	0	0
High Yield bonds	0	0	0	0	0	0
Govt guaranteed bonds	+	0	0	+	0	0
Index-linked bonds	+	0	0	0	0	0
Alternatives	0					

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

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