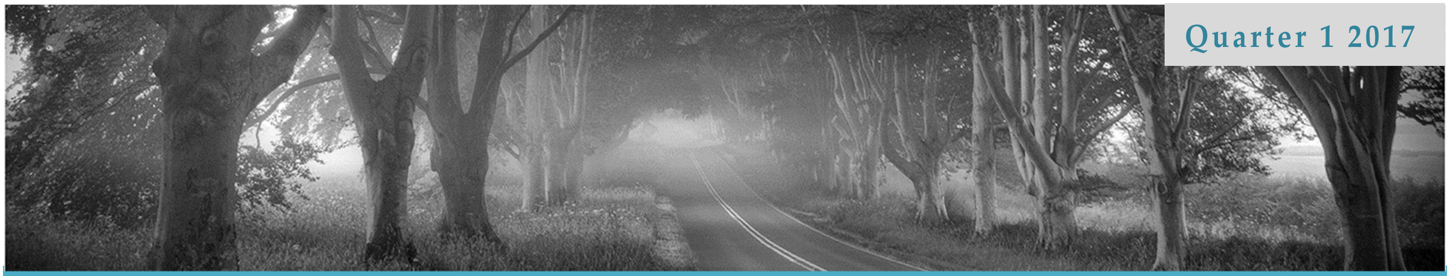

Quarter 1 2017

Tactical Asset Allocation Views & Commentary

Tactical positions are relative to the long term strategic allocations for our five proprietary risk rated portfolio benchmarks which are at the core of our investment process. They are expressed as seen in the key below.

- -	-	N	+	+ +
Strong Underweight	Underweight	Neutral	Overweight	Strong Overweight

Please contact us if you require further information.

Asset Class	Tactical Position	Commentary
Global Government Bond	-	We have reduced to underweight as the US increase in rates and the move to fiscal stimulus makes rate rises more likely. We still think the pace of rises in 2017 will be less than the market has priced. This asset still hedges any "risk-off" scenarios
Investment Grade Bond	N	Stronger growth favours credit over government bonds. We believe fixed income investors are being paid to take some risk. Credit markets have a larger safety cushion than government bonds vs the risk of further rises in interest rates.
High Yield Bond	+ +	A supportive policy environment, continuing low default risk and a strong positive carry over other fixed interest means we move to strong overweight. Lower interest rate sensitivity and yield spread compensates for any default risk
Emerging Market Sovereign Bonds	- -	Rising USD and prospect of trade protectionism increases risks for EM debt. Some of this is in the price - yields rising since the US election. EM local and hard currency bonds still offer yield premium but we maintain strong underweight
UK Equity	+ +	Continued sterling weakness and loose monetary policy are supportive to UK companies and favour exporters. We expect some volatility as Brexit fears remain but there are still opportunities to buy good companies at reasonable valuations
Developed Market Equity	+ +	The US shift toward fiscal expansion and deregulation are supportive, but uncertainties remain and valuations are elevated. We shift some allocation towards Europe on early signs of growth and cheap valuation compared to US
Emerging Market Equity	-	Threats to emerging markets are reducing, but still remain. USD strength and Chinese debt malaise is a concern in the coming months. Although EM growth seems to be improving our overweight positions elsewhere mean we stay cautious
Commodities	- -	We have seen strong returns in this asset class as OPEC cut production and stronger global growth drove markets. Oil may struggle to move higher if Trump is supportive of the US energy sector. Trade protectionism is a concern here
UK Commercial Property	+	The post Brexit panic in commercial property seems to be over as most funds are open again. Investors knee jerk negative reaction was overplayed as we thought. We remain long term holders of the asset class for yield and long term growth
Absolute Return	+ +	We stay strong overweight and expect this basket's balancing effect and low correlation help maintain portfolio diversification and dampen volatility which may occur as equity markets adapt to the US led changes in economic policy
Cash	+ +	We maintain high cash allocations as bond exposure is as high as we can justify as we approach the end of a 30-year bond bull market. We expect equity market volatility and chances to add to current risk exposures in the coming months

Looking Back

The final quarter of 2016 was dominated by Donald Trump and the Federal Reserve. US government bond yields rose post-election expecting higher inflation. Equity markets gained, with financial stocks in focus as higher yields were seen as supportive. Trump's fiscally expansive policies moved the global policy discussion away from the obsession with monetary stimulus spurring inflation expectations that was already buoyed by the modestly improved global growth outlook since the summer.

The S&P 500 advanced 3.8% as the market ignored the possible negative implications of the new government, including the risk of protectionist trade policies. Trump's plans to cut taxes and regulation whilst boosting infrastructure spending were seen as positive for domestic growth with small and mid-cap equities performing particularly well post-election.

The UK FTSE All-Share index rose 3.9% supported by financials (as above) and resources stocks after OPEC agreed to cut oil production. The Chancellor abandoned the pledge to run a balanced budget suggesting a move towards fiscal stimulus. Brexit fears receded as the UK economy grew at a better-than-expected 0.6% over the third quarter. Consumer spending remained resilient, despite the prospect of real wages falling in 2017, as well as higher energy prices and risks of imported inflation due to sterling weakness.

Europe made gains with the MSCI EMU index +8.1%. Financials again performed well. The ECB extended its quantitative easing programme to December 2017, but reduced the monthly bond purchase amount from €80bn to €60bn. The eurozone economy continued its slow recovery, with GDP growth +0.3% in Q3. Inflation edged up to 0.6% in November from 0.5% in October.

Japanese stocks were strong, drawing support from the currency as the yen weakened in November and December. Asia ex Japan equities fell as Donald Trump's surprise victory created heightened expectations of a faster pace in interest rate rises.

Emerging market equities underperformed, posting a negative return with uncertainty over US trade and foreign policy, as well as the prospect of tighter US dollar liquidity.

Government bond yields moved higher and yield curves steepened. The 10-year US Treasury yield rose from 1.59% to 2.44%, while the German 10-year Bund yield at last climbed out of negative territory, moving from -0.12% to 0.21%.

Global investment grade credit fell (BofA Merrill Lynch Global Corporate index -2.4% in local currency), while High Yield corporate bonds shone. All three major high yield markets - USD, euro and sterling – generated positive total returns. The BofA Merrill Lynch Global High Yield index rose 1.6% (local currency) beating government bonds by 3.7%.

Looking Forward

"I'll be the greatest president for jobs that God ever created."
President-Elect **Donald Trump**

Post Trump's victory, there has been a remarkable 'pop' in many sentiment indices and the equity market, however this is not really supported by the economic numbers such as CAPEX or industrial production which are soft. Retail spending has improved but households are still not seeing any real income increase. This is a factor which helped Trump to be elected but which he may struggle to change.

Trump's fiscal plans could deliver a boost to the US economy, but the magnitude and potential side effects are uncertain. He has pledged to slash taxes and boost infrastructure spending but uncertainties remain over the details of the plans as well as the fiscal multiplier – how much each dollar of fiscal expansion boosts GDP. The drivers of the US economy are productivity growth and increasing worker numbers both of which sit at historical low. If we consider the subdued capital expenditure and high debt levels in the US corporate sector along with a President who has vowed to control immigration, it suggests that throwing more money into the economy may not be the panacea markets clearly believe.

As the world's second largest economy, China's stabilising growth has eased some of the investor anxiety of early 2016. But it is not surprising given continued credit growth and significant lending to national and local state-owned enterprises (SOEs). China's private debt-to-GDP ratio has surged to more than 200%. Never has a big economy piled up so much debt so quickly. Chinese households are massively underweight foreign assets leading to large capital outflows which has led to the authorities imposing capital controls. It is rumoured that the inflated transfer activity related to the Chinese Super league is a manifestation of wealthy Chinese trying to get money out of the country. Paying well over the odds, they are using footballers and their agents to do this.

But having created so much domestic liquidity, shutting the stable door now may simply create higher domestic inflation. If handled badly, China faces stagflation or worse in 2017. Over recent months, credit growth has slowed, this tightening intended to protect the value of the Remnimbi. China's economy will need to slow over the first half of 2017 or inflation may become rife – which could affect us all.

The extraordinary monetary easing since 2008 created a rising tide which lifted all boats. We feel other markets are likely to mirror the US trend as major central banks approach the limits of monetary easing. The likely change to fiscal stimulus and regulatory changes, is likely to favour some sectors over others and asset price dispersion creates opportunities for the active manager who can be nimble while staying focused on long-term goals. We feel that 2017 will favour an active approach to investing as rising dispersion creates opportunities to identify security and asset class winners and losers.