

# Viewpoint

## Monthly market update

*March 2018*



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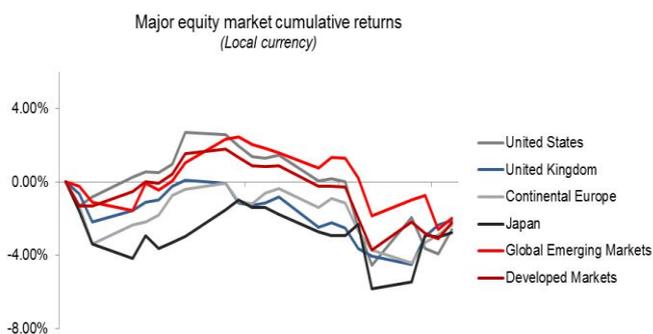
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# 1. Market commentary

After a broad sell off across many asset classes in February, volatility continued into March, with equity markets declining and government bonds rallying. Risk markets were impacted by the prospects of a US-China trade war with President Trump continuing to push his 'America First' philosophy. Emerging market and developed market equities fell, with emerging markets marginally outperforming.

US equities fell 2.6% during the month, taking Q1 2018 returns to -0.9%. A key contributing factor seemed to be President Trump's imposition of tariffs on imports of Chinese steel and aluminium and proposals for further tariffs on a wide range of goods. China immediately responded, imposing tariffs on several US imports, including wine. This led to worldwide concerns of a potential trade war, which could have implications for global growth. In addition to this, tech stocks, among the strongest performers in 2017, suffered sharp share price declines. This followed a serious data breach at Facebook which led to a series of governments seeking to tighten the loose regulation of companies in the sector, while tax authorities are seeking to impose more effective taxes.

Figure 1: Equities decline in every major region

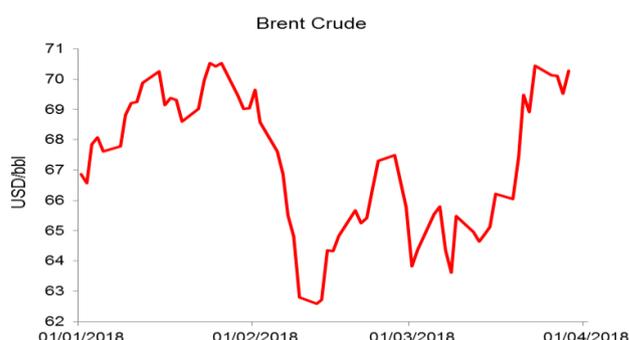


Source: Bloomberg, Momentum GIM

The concerns in the US were felt worldwide, with every major equity market falling. UK equities fell 2.1% in Sterling terms, with additional concerns regarding the path of UK interest rates, which are likely to rise more aggressively than previously anticipated. Asian equities also declined on the trade war concerns, with Japanese equities declining 2.7% and Asia Pacific (ex-Japan) equities falling 2.4%.

Global developed market equities fell 2.2%, a sharper fall than the 2.0% decline in global emerging market equities. Despite the fall, emerging market equities still posted positive returns over the quarter, advancing 1.3% in US Dollar terms versus a 1.3% decline in developed market equities.

Figure 2: After hitting year-to-date lows in February, Brent crude recovered in March



Source: Bloomberg, Momentum GIM

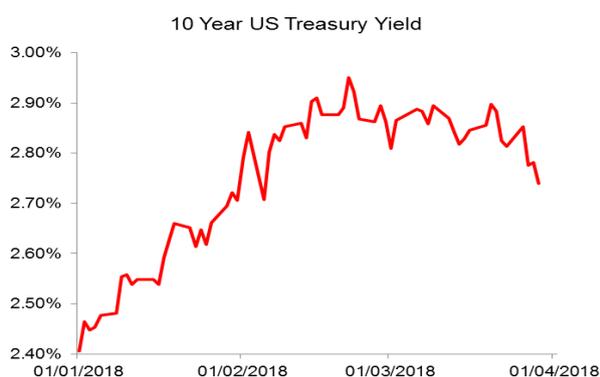
The US Dollar continued to weaken, falling 0.7% on a trade weighted basis in light of a mixed domestic economic and political sentiment. Sterling performed particularly strong versus the US Dollar, rising 1.9%. As previously mentioned, this follows an increased likelihood that UK interest rates would rise faster than previously anticipated, driven by strong labour market data including wage growth accelerating to 2.6%, the fastest rate in two and a half years. In commodities, oil was a major mover, with Brent crude advancing 6.8% amid rising confidence that OPEC would maintain its production cuts throughout 2018.

In fixed income, US Treasuries returned 1.0% in March, with 10 year yields falling 12.2 basis points to 2.74%. High yield credit and global convertibles were impacted by equity market concerns, with US high yield falling 0.6%, Euro high yield falling 0.2% and global convertibles falling 0.6%.

At this still favourable stage of the economic cycle the vast majority of threats to bond markets are inflation and interest rate related rather than credit risk. Perhaps the most notable recent development in bond markets is the continual flattening of the US treasury yield curve. The yield on 2 year Treasuries has risen

over 100 basis points in the past 12 months, narrowing the gap with 10 year Treasuries to 47 basis points, the lowest since before the financial crisis. While this is typically seen as a precursor to worsening economic conditions, the move largely reflects the abnormally low yields on longer dated bonds, supported by post-crisis central bank asset purchases.

Figure 3: Ten year Treasury yields decline in March



Source: Bloomberg, Momentum GIM

There were several positive developments in geopolitics. The UK and EU agreed terms for a 21 month transition period following the agreed exit date of March 2019. This is an important breakthrough and gives the UK more time to negotiate its future with the EU and for businesses to prepare for Brexit. While economic uncertainty still overhangs the UK as it progresses through the Brexit process, the sharp underperformance of UK equities in the past 18 months leaves them undervalued and offers opportunities as the uncertainties dissipate. Of greater importance on the global stage has been the cooling of tensions on the Korean peninsula, with the world awaiting President Trump's meeting with Kim Jong-Un. A successful meeting could herald a meaningful reduction to this particular tail risk in markets, with the potential for all out conflict greatly reduced.

Despite this, the direction of markets in the coming months is most likely to be determined by central bank policy action rather than geopolitics. While there is risk Trump's imposition of tariffs could lead to broader protectionism and trade wars, the actions taken so far have been limited and are unlikely to

derail the benign economic conditions globally. Although growth momentum has eased in the past three months, forward indicators are still suggesting strong growth in 2018. Any signs of acceleration in inflation will be the greatest concern for markets, as this would certainly be a catalyst for more aggressive monetary tightening.

On the current trajectory of growth and inflation, the Federal Reserve will continue as planned with its asset reductions and will raise interest rates twice more this year, following its 25 basis point increase in March. At the same time, the European Central Bank, still engaged in its asset purchase programme, will likely reduce its asset purchases to zero by year-end and will begin to raise interest rates by mid-2019. The Bank of England is also expected to raise rates this year, possibly as soon as May, with the UK economy performing stronger in the lead up to Brexit than previously anticipated. The net effect is that by year-end central banks in aggregate will be withdrawing liquidity, rather than contributing. Led by the US, interest rates are likely to follow an upward path towards normalisation. This is likely to keep bond markets under pressure with yields rising further, and with that, the valuation hurdle for equity markets.

The combination of tightening policy and heightened uncertainty means that markets are likely to be more vulnerable to setbacks and greater volatility than in 2017, and may be held back by rising interest rates. Despite this, the underlying strength of the global economy remains, and the pace of monetary stimulus withdrawal will be cautious. Policy will still remain loose by historical standards and is highly unlikely to derail the currently favourable economic conditions. We therefore believe this cycle has further to run and view the current setback in markets as a healthy correction after a long unbroken run in asset prices. Equities remain our preferred asset class, and further setbacks in markets will present buying opportunities, while in fixed income we continue to believe that shorter duration exposure is appropriate at this still early stage of the global monetary tightening cycle.

Source: Bloomberg. Returns in US dollars unless otherwise stated. March 2018.

**Past performance is not indicative of future returns.**

## 2. Market performance – Global (local returns)

| Asset class/region                  | Index  | To 29 March 2018 (local returns) |         |          |
|-------------------------------------|--|----------------------------------|---------|----------|
|                                     |  | Local currency                   | 1 month | 3 months |
| <b>Developed markets equities</b>   |  |                                  |         |          |
| United States                       | S&P 500 NR   | USD                              | -2.6%   | -0.9%    |
| United Kingdom                      | MSCI UK NR   | GBP                              | -2.1%   | -7.3%    |
| Continental Europe                  | MSCI Europe ex UK NR                                 | EUR                              | -2.3%   | -3.6%    |
| Japan                               | Topix TR   | JPY                              | -2.7%   | -5.4%    |
| Asia Pacific (ex Japan)             | MSCI AC Asia Pacific ex Japan NR                     | USD                              | -2.4%   | -0.7%    |
| Global                              | MSCI World NR  | USD                              | -2.2%   | -1.3%    |
| <b>Emerging markets equities</b>    |  |                                  |         |          |
| Emerging Europe                     | MSCI EM Europe NR                                    | USD                              | -4.7%   | 2.1%     |
| Emerging Asia                       | MSCI EM Asia NR                                      | USD                              | -1.6%   | 0.6%     |
| Emerging Latin America              | MSCI EM Latin America NR                             | USD                              | -1.0%   | 8.0%     |
| BRICs                               | MSCI BRIC NR   | USD                              | -3.1%   | 2.2%     |
| Global emerging markets             | MSCI EM (Emerging Markets) NR                        | USD                              | -2.0%   | 1.3%     |
| <b>Bonds</b>                        |  |                                  |         |          |
| US Treasuries                       | JP Morgan United States Government Bond Index TR     | USD                              | 1.0%    | -1.2%    |
| US Treasuries (inflation protected) | Barclays Capital U.S. Government Inflation Linked TR | USD                              | 1.1%    | -0.9%    |
| US Corporate (investment grade)     | Barclays Capital U.S. Corporate Investment Grade TR  | USD                              | 0.3%    | -2.3%    |
| US High Yield                       | Barclays Capital U.S. High Yield 2% Issuer Cap TR    | USD                              | -0.6%   | -0.9%    |
| UK Gilts                            | JP Morgan United Kingdom Government Bond Index TR    | GBP                              | 2.1%    | 0.3%     |
| UK Corporate (investment grade)     | BofA Merrill Lynch Sterling Non Gilts TR             | GBP                              | 0.6%    | -1.2%    |
| Euro Government Bonds               | Citigroup EMU GBI TR                                 | EUR                              | 1.6%    | 1.4%     |
| Euro Corporate (investment grade)   | Barclays Capital Euro Aggregate Corporate TR         | EUR                              | -0.1%   | -0.4%    |
| Euro High Yield                     | BofA Merrill Lynch Euro High Yield Constrained TR    | EUR                              | -0.2%   | -0.5%    |
| Japanese Government                 | JP Morgan Japan Government Bond Index TR             | JPY                              | 0.2%    | 0.5%     |
| Australian Government               | JP Morgan Australia GBI TR                           | AUD                              | 1.3%    | 1.1%     |
| Global Government Bonds             | JP Morgan Global GBI                                 | USD                              | 1.6%    | 2.2%     |
| Global Bonds                        | Citigroup World Broad Investment Grade (WBIG) TR     | USD                              | 1.2%    | 1.2%     |
| Global Convertible Bonds            | UBS Global Focus Convertible Bond                    | USD                              | -0.6%   | 1.7%     |
| Emerging Market Bonds               | JP Morgan EMBI+ (Hard currency)                      | USD                              | 0.7%    | -2.0%    |

Source: Bloomberg.

**Past performance is not indicative of future returns.**

|                                       |                               | To 29 March 2018 (local returns) |         |          |
|---------------------------------------|-------------------------------|----------------------------------|---------|----------|
| Asset class/region                    | Index                         | Local currency                   | 1 month | 3 months |
| <b>Property</b>                       |                               |                                  |         |          |
| US Property Securities                | MSCI US REIT NR               | USD                              | 3.7%    | -8.4%    |
| Australian Property Securities        | S&P/ASX 200 A-REIT Index TR   | AUD                              | 0.0%    | -7.3%    |
| Asia Property Securities              | S&P Asia Property 40 Index NR | USD                              | -0.2%   | 0.1%     |
| Global Property Securities            | S&P Global Property USD TR    | USD                              | 2.1%    | -3.6%    |
| <b>Currencies</b>                     |                               |                                  |         |          |
| Euro                                  |                               | USD                              | 0.9%    | 2.5%     |
| UK Pound Sterling                     |                               | USD                              | 1.9%    | 3.7%     |
| Japanese Yen                          |                               | USD                              | 0.2%    | 5.9%     |
| Australian Dollar                     |                               | USD                              | -1.1%   | -1.7%    |
| South African Rand                    |                               | USD                              | -0.4%   | 4.9%     |
| <b>Commodities &amp; Alternatives</b> |                               |                                  |         |          |
| Commodities                           | RICI TR                       | USD                              | 0.6%    | 2.1%     |
| Agricultural Commodities              | RICI Agriculture TR           | USD                              | -2.6%   | 2.8%     |
| Oil                                   | Brent Crude Oil               | USD                              | 6.8%    | 5.1%     |
| Gold                                  | Gold Spot                     | USD                              | 0.5%    | 1.7%     |
| Hedge funds                           | HFRX Global Hedge Fund        | USD                              | -1.0%   | -1.0%    |
| <b>Interest rates</b>                 |                               | <b>Current rate</b>              |         |          |
| United States                         |                               | 1.75%                            |         |          |
| United Kingdom                        |                               | 0.50%                            |         |          |
| Eurozone                              |                               | 0.00%                            |         |          |
| Japan                                 |                               | 0.10%                            |         |          |
| Australia                             |                               | 1.50%                            |         |          |
| South Africa                          |                               | 6.50%                            |         |          |

Source: Bloomberg.

**Past performance is not indicative of future returns.**

### 3. Market performance – UK (all returns in GBP)

| Asset class/region                 | Index  | To 29 March 2018 (all returns in GBP) |         |          |
|------------------------------------|--|---------------------------------------|---------|----------|
|                                    |  | Local currency                        | 1 month | 3 months |
| <b>Equities</b>                    |  |                                       |         |          |
| UK - All Cap                       | MSCI UK NR   | GBP                                   | -2.1%   | -7.3%    |
| UK - Large Cap                     | MSCI UK Large Cap NR                                       | GBP                                   | -1.9%   | -7.6%    |
| UK - Mid Cap                       | MSCI UK Mid Cap NR   | GBP                                   | -3.1%   | -6.7%    |
| UK - Small Cap                     | MSCI Small Cap NR  | GBP                                   | -0.7%   | -5.0%    |
| United States                      | S&P 500 NR   | USD                                   | -4.2%   | -4.4%    |
| Continental Europe                 | MSCI Europe ex UK NR                                       | EUR                                   | -3.3%   | -4.9%    |
| Japan                              | Topix TR   | JPY                                   | -4.1%   | -3.4%    |
| Asia Pacific (ex Japan)            | MSCI AC Asia Pacific ex Japan NR                           | USD                                   | -4.0%   | -4.2%    |
| Global developed markets           | MSCI World NR  | GBP                                   | -3.9%   | -4.8%    |
| Global emerging markets            | MSCI EM (Emerging Markets) NR                              | GBP                                   | -3.6%   | -2.3%    |
| <b>Bonds</b>                       |  |                                       |         |          |
| Gilts - All                        | BofA Merrill Lynch Gilts TR                                | GBP                                   | 2.1%    | 0.2%     |
| Gilts - Under 5 years              | BofA Merrill Lynch Gilts TR under 5 years                  | GBP                                   | 0.0%    | -0.5%    |
| Gilts - 5 to 15 years              | BofA Merrill Lynch Gilts TR 5 to 15 years                  | GBP                                   | 1.2%    | -1.0%    |
| Gilts - Over 15 years              | BofA Merrill Lynch Gilts TR over 15 years                  | GBP                                   | 4.0%    | 1.5%     |
| Index Linked Gilts - All           | BofA Merrill Lynch Inflation-Linked Gilts TR               | GBP                                   | 2.4%    | 0.1%     |
| Index Linked Gilts - 5 to 15 years | BofA Merrill Lynch Inflation-Linked Gilts TR 5 to 15 years | GBP                                   | 0.5%    | -1.2%    |
| Index Linked Gilts - Over 15 years | BofA Merrill Lynch Inflation-Linked Gilts TR over 15 years | GBP                                   | 3.4%    | 0.6%     |
| UK Corporate (investment grade)    | BofA Merrill Lynch Sterling Non Gilts TR                   | GBP                                   | 0.6%    | -1.2%    |
| US Treasuries                      | JP Morgan United States Government Bond Index TR           | USD                                   | -0.7%   | -4.7%    |
| US Corporate (investment grade)    | Barclays Capital U.S. Corporate Investment Grade TR        | USD                                   | -1.4%   | -5.8%    |
| US High Yield                      | Barclays Capital U.S. High Yield 2% Issuer Cap TR          | USD                                   | -2.2%   | -4.3%    |
| Euro Government Bonds              | Citigroup EMU GBI TR                                       | EUR                                   | 0.6%    | 0.0%     |
| Euro Corporate (investment grade)  | Barclays Capital Euro Aggregate Corporate TR               | EUR                                   | -1.1%   | -1.7%    |
| Euro High Yield                    | BofA Merrill Lynch Euro High Yield Constrained TR          | EUR                                   | -1.2%   | -1.9%    |
| Global Government Bonds            | JP Morgan Global GBI                                       | GBP                                   | -0.1%   | -1.4%    |
| Global Bonds                       | Citigroup World Broad Investment Grade (WBIG) TR           | GBP                                   | -0.5%   | -2.3%    |
| Global Convertible Bonds           | UBS Global Focus Convertible Bond                          | GBP                                   | -2.3%   | -1.9%    |
| Emerging Market Bonds              | JP Morgan EMBI+ (Hard currency)                            | GBP                                   | -1.0%   | -5.5%    |

Source: Bloomberg.

**Past performance is not indicative of future returns.**

|                                       |                            | To 29 March 2018 (all returns in GBP) |                     |          |
|---------------------------------------|----------------------------|---------------------------------------|---------------------|----------|
| Asset class/region                    | Index                      | Local currency                        | 1 month             | 3 months |
| <b>Property</b>                       |                            |                                       |                     |          |
| Global Property Securities            | S&P Global Property USD TR | GBP                                   | 0.4%                | -7.0%    |
| <b>Currencies</b>                     |                            |                                       |                     |          |
| Euro                                  |                            | GBP                                   | -1.0%               | -1.2%    |
| US Dollar                             |                            | GBP                                   | -1.9%               | -3.6%    |
| Japanese Yen                          |                            | GBP                                   | -1.6%               | 2.0%     |
| <b>Commodities &amp; Alternatives</b> |                            |                                       |                     |          |
| Commodities                           | RICI TR                    | GBP                                   | -1.1%               | -1.5%    |
| Agricultural Commodities              | RICI Agriculture TR        | GBP                                   | -4.2%               | -0.8%    |
| Oil                                   | Brent Crude Oil            | GBP                                   | 5.1%                | 1.4%     |
| Gold                                  | Gold Spot                  | GBP                                   | -1.1%               | -1.9%    |
| <b>Interest rates</b>                 |                            |                                       | <b>Current rate</b> |          |
| United Kingdom                        |                            |                                       | 0.50%               |          |
| United States                         |                            |                                       | 1.75%               |          |
| Eurozone                              |                            |                                       | 0.00%               |          |
| Japan                                 |                            |                                       | 0.10%               |          |

Source: Bloomberg.

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## 4. Asset allocation dashboard

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