Macro Roundup

QUOTEDDATA

November 2014

A collation of recent insights on markets and economies taken from the comments made by Chairmen and investment managers of investment companies – have a read and make your own mind up. Please remember that nothing in this note is designed to encourage you to buy or sell any of the companies mentioned.

In this month's roundup

Global economy *(compare Global funds here)*

Looking to our new financial year, the outlook for the US economy remains favourable, the UK economy is improving more strongly than many economists had expected, while Japan is seeing signs of recovery in the domestic economy. In Europe however, economic growth remains very weak and assistance from the ECB is probably needed to accelerate growth. Therefore, while significant geo-political risks remain and there is still too much leverage in the world's economic system, we are cautiously optimistic about the longer term outlook for global equity markets. *From Tom H Bartlam, Chairman, Jupiter Primadona*

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It is perhaps fair to say that the year so far has been one of rotation within markets, where, as ever, the unexpected has confounded the consensus. Early on, growth-orientated assets continued their market leadership until March when there was a marked turnaround, seeing smaller-cap companies and previously in-vogue sectors catching a chill, allowing larger, more defensive or income-producing assets to come to the fore. Coincidentally, previously underperforming Asian and emerging market equities also rebounded from oversold conditions. In the middle of May, the trend briefly reverted once more with growth and smaller companies catching up some of the lost ground before ending the first half of the year with a more mixed picture. These market rotations have made trend-following strategies and macro-based investing even more challenging than usual.

Looking ahead, we think the immediate concern for investors is Europe, where Mario Draghi, the President of the ECB, has intimated his readiness for greater market intervention in order to counteract the potential for deflation and to stimulate the region's stagnating economic growth. Exceptional measures have already been implemented, including a negative interest rate. Paying money to leave cash on deposit would appear like an extreme step to stimulate the economy but it is a stark reminder that we live in exceptional times and that the "normality" of the pre-crisis world remains but a distant hope. *From Richard Curling and Derek Pound, Jupiter Asset Management Limited*

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UK *(compare UK funds here)*

The best of the bull market has passed. But the bear market won't be back quite yet - whilst there are more worries than there ever were for financial markets (including hair raising debt levels and structural stagnation issues) the forces of continuing accommodative interest rates from the Fed, the global savings glut in countries that have no further material room to invest it internally and more quantitative easing from Japan and the ECB mean that we may see stock markets grinding higher.

Share buy backs may be replaced by M&A - shareholders may well turn against CEOs continuing to enhance their remuneration through the escalating value of option packages via the enhancement of earnings from share buy backs, and hence the next tactic they may try is to enhance earnings via M&A synergies.

The Dollar continues to appreciate - this may result in Dollar earners performing better than Pound earners so UK centric small capitalisation stocks may not repeat their returns of the last two financial years. The developing markets will slow but should still grow faster than developed markets - so we continue to favour global companies with exposure to these markets. Demographics in the developed world may make growth structurally slower. *From Mark Sheppard, Investment Manager, Manchester & London*

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Despite the inevitability of monetary tightening at some stage, as economic growth gathers momentum in both the USA and UK, short dated bond yields have, unexpectedly, continued to fall.

Although consumer confidence in the USA has improved, the Federal Reserve continues to have concerns about the strength of US manufacturing and has confirmed that it is ready to introduce further stimulatory measures should growth falter. Geopolitical tensions in the Ukraine and Syria/Iraq have increased the probability of decisions over raising interest rates being pushed into the future. The oil price has been unexpectedly weak, given the possible disruption to supplies and confounding many investors. The service and house building sectors of the UK economy have produced positive surprises but manufacturing (motor cars apart) has been hit by continuing stagnation in Continental Europe. Business investment is, however, finally starting to recover.

European policy, in particular, remains well behind the curve. M. Draghi gave advance warning of his intentions during the Jackson Hole conference and then acted decisively to announce more accommodative moves in an effort to avert deflation, but it remains to be seen how far the Germans will permit the ECB to go down the QE path. The Japanese deflationary malaise of recent years is now stalking Continental Europe.

Asian economies have continued, as forecast, to deliver superior rates of growth. India and Indonesia, both populous nations, have started to accelerate their economies following recent elections. Notwithstanding this and the strong balance of payments position of China and most Asian (India excepted) economies their stock-markets have remained out of favour. The Chinese economy continues to slow and is not moving fast enough to a more sustainable economic balance with increased emphasis on consumption. Investors continue to be concerned about the level of potential bad debts, particularly in the Chinese local authority sector.

Looking ahead, the point at which the very significant monetary stimulus of recent years is withdrawn is likely to commence in the UK, followed by the US, but the issue remains when. In so far as economic recovery is not derailed in the process, stock markets should benefit in what will remain by historical standards a low interest rate environment. *From Lord Flight, Chairman, Aurora Investment Trust*

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There is considerable uncertainty as to how markets will perform over the next few months. The Eurozone economy remains weak and there are continuing concerns about the possible consequences of events in the Middle East, Eastern Europe and West Africa. The apparent willingness of governments to counter recessionary pressures with quantitative easing and other monetary measures to support growth provides some assurance, together with more positive recent economic data in the USA and UK, that an overweight position in equities remains appropriate. *From Sir Laurence Magnus Bt, Chairman, JPMorgan Income & Capital*

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The UK macroeconomic picture is likely to maintain its improvement over the coming months as consumption and business investment continue to pick up speed, although the deteriorating economic outlook in the Eurozone could weigh on the UK's economic progress. Also domestically, an interest rate rise is looming on the horizon as the Bank of England begins to exit a six-year period of unorthodox monetary policy.

Although interest rates rises are likely to be limited and gradual over the coming 12 months, the market currently expects interest rates to rise before the May 2015 election. This is likely to take some of the froth out of the buoyant housing market, which increased 11% year on year in July, driven mainly by rocketing London prices.

Interest rate rises are also likely to cause some market volatility. The outlook for corporate earnings growth will depend on the progress of the global economy. 75% of UK blue-chip companies source their revenues from overseas, therefore global economic growth should be a positive for UK companies. UK corporate earnings have been hampered over the last two quarters by the strength of sterling, but the currency has shown signs of weakening and this may also be helpful to export--driven stocks. Although there are significant international macro and geo--political uncertainties in the short term, we believe that the UK equity market continues to offer opportunities for both income and capital growth for medium term investors. *From John Baker and Sarah Emly, Investment Managers, JPMorgan Income & Capital*

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UK Property *(compare UK property funds here)*

The overall business environment in which we operate has turned positive, notwithstanding ongoing concerns relating to weak economic fundamentals in the Eurozone, deflationary expectations and the interest rate cycle. Activity in the retail and commercial sectors has improved on the back of these improving economic conditions. Occupational trends across all the sectors in which we operate are showing positive fundamentals, albeit to varying degrees.

Hotel properties benefited from a stronger UK economy. Sentiment in the UK hotel sector remains buoyant, with expectations of growth continuing for the remainder of 2014 and into 2015. The market has been driven by better than expected UK GDP growth and a pick-up in both corporate travel and tourism. According to the latest PwC hotel industry report, these factors have pushed rates in favour of owners.

London is expected to see average RevPars reach an all-time high by the end of 2014, driven largely by growth of over 3.0% in average daily room rates. Regional hotels have also performed ahead of expectations, in strong locations including Aberdeen and Edinburgh.

Supply of new rooms in London is expected to have risen approximately 5% by the end of 2014 and a further 5% is anticipated in 2015. In strong locations, new supply is being taken up by additional demand.

Investment markets remain competitive and assets with sound fundamentals have typically transacted at prices well above asking levels. As an increased number of sellers enter the market to take advantage of recent yield compression, opportunities to acquire good quality assets may improve in 2015. *From Redefine International*

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Europe *(compare European funds here)*

Despite disappointing macroeconomic news during the second quarter, our Portfolio Managers remain broadly positive on European equities. Valuations are reasonable relative to other asset classes and to U.S. equities. European earnings expectations for 2014 are also now more realistic and the weakening of the Euro should support revised growth forecasts.

In late August, Mario Draghi, president of the European Central Bank (ECB), indicated that he is willing to see some economic stimulus and this should increase interest in European stocks in the coming months. Draghi's clear objective is to protect the Euro while promoting nominal growth in Europe and recent measures announced by the ECB are designed to provide a boost in liquidity with the ultimate aim of reducing the cost of corporate debt. Developments are not expected to be rapid, but more [*accomodating*] central bank policy should help to support any European economic recovery which has faltered in recent months and provide a positive catalyst for markets. *From Carol Ferguson, Chairman BlackRock Greater European*

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The economic recovery in Europe has faltered in recent months and this has exacerbated the problems faced by Europe's cyclical businesses following a difficult second quarter. Whilst the recovery in Europe is more muted than initially expected, we believe that we are unlikely to see a 'triple-dip' recession in the region, given that economic momentum in the U.S. continues to be strong and the ECB package of measures should have a positive impact on growth over the next 12 months. While the ECB measures directly address the supply of credit, many investors remain worried about the lack of demand at both company and household levels. In our view, after a muted five years, there is some pent up demand in corporate spending, with companies' investment intentions improving. Demand for credit has also been encouraged by current lower business loan rates.

European valuations have re-rated over the last year and look to be in line with their long term average. However, European equities are still under-priced versus the U.S. and are at extremely cheap valuations on longer term metrics. Consensus earnings estimates have been cut this year but they now are beginning to be adjusted upwards from a low base, and the Euro weakness is likely to provide support to earnings with over 50% of European listed companies' turnover coming from outside Europe. On balance, the European recovery is in our view intact, albeit the pace remains sluggish. *From Vincent Devlin and Sam Vecht, BlackRock Investment Management (UK) Limited as managers of BlackRock Greater European*

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It seems to be a feature of August each year (when I start to write this report) that there is a long list of worries. Coinciding with the commemorations of the start of the First World War, Europe's structure and level of integration are facing extreme challenge. The Russia-Ukraine conflict may lead to significant unrest, while the Middle East is also in a highly problematic state. The USA and UK are preparing to tighten monetary policy in response to better growth, while most of the Euro area continues to struggle with low growth and low inflation. Earnings have failed to come through as expected so far. Some globally active fund managers with shorter term investment horizons have become frustrated with Europe's lack of progress and have started to withdraw funds from the region. This latter development is, in my view, quite good news. The impatience of short term investors could provide a good opportunity for those with greater reserves of perseverance. From our many meetings with companies, I actually feel they are in better health in most cases than has been the case for years. Valuations of European markets look quite high - the price earnings ratio on average for the Europe (excluding UK) markets has risen from a low of 8.4x in 2011 to a recent level of 13.8x prospective earnings. But I do believe those earnings will start to come through, and the recent weakness of the Euro against the US Dollar will also help. Furthermore, the average price earnings ratio of the higher growth companies has actually declined over the last twelve months. Since their growth is now accelerating again, their valuation has swung more firmly in our favour. *From Tim Stevenson, Fund Manager, Henderson Eurotrust*

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The rally driven by the market's relief at the European Central Bank's "whatever it takes" reassurance has come to something of a standstill in recent months. Persistently low inflation and fears of deflation have combined with inaction with regards to structural reforms in countries such as France and Italy to undermine the stock market's confidence in the recovery. Notwithstanding these real concerns, the underlying economy in Europe is healing and there are a number of good stocks that offer attractive upside for the Company to invest in. Europe is blessed with a large number of world beating smaller companies that are at the forefront of the changes occurring in the world with technology and globalisation. *From Audley Twiston-Davies, Chairman, TR European Growth*

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The onset of summer has seen global investors become more pessimistic about European equity markets, as the region's economic recovery has paused. Investors have also recently turned their attention once more to more exotic emerging markets. Our central scenario remains largely unchanged from a year ago; that we are in the mid-cycle of a long, drawn out and muted recovery in European economies.

European equity markets have stalled following a two-year sentiment rally, driven by receding fears of a Eurozone breakup. Corporate earnings growth has continued to disappoint, in line with European gross domestic product ("GDP") forecasts being lowered. It is not difficult to find reasons/excuses to run away from European equity markets in general, and more economically sensitive smaller companies in particular. The geopolitical backdrop is uncertain, with the Ukraine crisis impacting confidence in even Europe's economic powerhouse, Germany. We have seen no great impact from Prime Minister Matteo Renzi's reforms in Italy. The less said about France and its ever-increasing debt levels the better. Finally Mr Draghi, head of the ECB, has done a lot of talking, but where are the benefits? Deflation fears abound. Elsewhere, the US is moving towards higher interest rates.

Yet, despite these uncertainties, we believe there a lot of grounds for optimism. Draghi's Targeted Longer-Term Refinancing Operations ("TLTRO") measures will enable European banks to borrow at 0.25%, if they expand their loan book. Positive credit growth could have a huge effect in the coming months. This was always going to have a lagged effect, as banks have to go through the ECB's Asset Quality Review. By October, the review will be finalised and lending will no longer be suppressed. In Italy, Mr Renzi has a popular mandate for reform and has announced a series of reforms to increase labour flexibility and reduce corporate taxation. Italy, alongside Greece, Ireland and Portugal, is among the top economic reformers of the Organisation for Economic Co-operation and Development ("OECD").

We must not forget that Europe has come a long way in the last couple of years. Even Mr Hollande, the least popular French President ever, seems to have woken up and is at least trying to stimulate the property market with new incentives (though we still hear nothing of much-needed economic reforms).

The US may be moving to credit tightening, which should surprise no one and reflects an ever-improving US economy. Data out of China is getting better. Closer to home, the UK's economy has an upward trajectory. We believe that we are heading for a global synchronised economic recovery, which should provide a very supportive backdrop to the European smaller company space.

At a stock market level, after a long period where markets seem to have been running on vapour we finally believe we are approaching the point where earnings downgrades are coming to an end. This is necessary after a period of equity markets re-rating. Within European markets we continue to believe that the greatest value lies at the low end of the market capitalisation range, below GBP1 billion.

We are also expecting to see a pick-up in M&A, which would be supportive. After little activity since 2007, corporates are once again seeking supplementary inorganic growth. This should benefit European smaller companies disproportionately, as they become targets for bolt-on acquisitions for larger firms.

We do not think the European recovery is over and, while it may be subdued, the recovery has only just begun. *From Ollie Beckett, Fund Manager, TR European Growth*

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German property *(compare European property funds here)*

Recent reports from German retail companies indicate year on year real sales growth of 1.2% and while unemployment remains low and stable at around 6.5%, consumer sentiment is expected to remain positive.

Prime rents increased on average 2.5% for the 12 months to June 2014, slightly ahead of the rate of growth seen on the same period last year. Rental growth in the 10 biggest retail locations increased 3.5% in the same period, with Berlin and Hamburg showing the biggest absolute rises to levels of EUR300 and EUR275 per sqm per month respectively.

Consumer spending will remain a key driver of Germany's economic and retail performance and a positive differentiator from the balance of the Eurozone.

Prime yields in the key German markets have compressed by 20bps to 30bps in the 12 months to June 2014 (Colliers) and are now back to historically low levels. The pricing of prime assets has resulted in a noticeable increase in risk appetite with institutional investors moving into secondary assets and a general increase in the number of transactions focused on more asset management intensive portfolios.

The availability of capital to invest in real estate from both German and international investors is expected to remain strong and currently outweighs existing available supply. Likewise, liquidity in the banking market remains robust and given the current interest rate environment, borrowing costs are likely to stay at exceptionally low levels. Recent investment activity suggests increased risk appetite and demand for assets outside of Germany's top 10 cities or assets that are more management intensive. This is expected to have a positive impact on the value of good quality secondary assets. We continue to find value in the German investment market, which combined with the historically low interest rate environment and attractive borrowing costs, is providing an opportunity to generate attractive cash-on-cash returns. *From Redefine International*

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USA *(compare US funds here)*

Attempting to forecast the stock market is a largely futile exercise because markets are phenomena that move to their own beat. For those determined nevertheless to attempt to examine the auguries, the three key drivers of the equity market are rising profits, easy money and investor psychology: with all three working in the correct direction, the market will rise but with only one, it is likely to fall. An expanding US economy appears to support the first and the Fed's reluctance to raise rates helps the second. Investor scepticism, after fading over summer (a bad sign) appears to be reappearing more recently (a good sign as a bull market needs a pool of sceptics to provide fresh buying potential).

The real concern for the market in the next couple of years is the timing and pace of an interest rate rise. This is difficult to predict and for now weakness in the housing market and overseas economies helps to put off the evil day.

What can be said with more certainty is that the long term outlook for America - and by extension, domestically focused stocks, such as, smaller companies - is relatively bright, helped by the triple tailwinds of shale reserves, superior demographics and revitalised manufacturing competitiveness. *From Robert Siddles, Fund Manager, Jupiter US Smaller Companies*

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Asia *(compare Asian funds here)*

Despite geopolitical risks, stock markets appear on a firmer footing compared to conditions in early 2014. Major central banks are committed to expansionary monetary policy, given the mixed global outlook. While the US economy is improving, Europe remains fragile. There are, however, some headwinds that could trigger renewed volatility. The end of US quantitative easing in October comes to mind. That said, Asia has sturdier fundamentals that should reinforce its resilience in tough times. Its favourable demographics also offer long-term opportunities to smaller companies, which are more exposed to domestic consumption. *From Nigel Cayzer, Chairman, Aberdeen Asian Smaller Companies*

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Encouragingly, there has been renewed enthusiasm towards smaller Asian companies. Meanwhile, our fundamental outlook for companies in the asset class remains unchanged. Consumer-oriented companies have been doing well and should continue to benefit from the region's relatively favourable demographics and domestic consumption trends. In particular, companies in the sector are seeing improved margins, aided by cost cuts. Conversely, earnings forecasts for exporters appear mixed and very much dependent on the macroeconomic health of their export destinations. The trend of normalising monetary policy in the developed world could result in lower consumption in the short term, though that should gradually pick up over the longer term. *From Aberdeen Asset Management Asia Limited, as managers of Aberdeen Asian Smaller Companies*

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Japan *(compare Japanese funds here)*

Over the past year there has been a significant improvement in attitudes towards corporate governance in Japan; one of the many aspects of Mr Abe's third arrow is one where carrots and sticks are being wielded enthusiastically. Along with longer term trends such as the detailed publication of voting at Japanese AGMs there has also been much more emphasis on the appointment of independent external directors to Boards, increasing dividends and a greater exposition by the authorities about the need for all companies to make more in profits than their capital costs. 74% of companies listed on the Tokyo market now have at least one independent director and if they don't, now need to comply or explain why not. We believe that shortly an explanation will not be enough and it will become mandatory to have an outsider on the Board.

Dividends are rising and companies are showing a lessening tendency to hoard cash. For the half year to September 2014 it is likely that pay-outs will be at a record level in Yen terms. There is scope for continued growth as the percentage of profits paid out is still low by international standards. Share buy backs are also at the highest level since the Lehman's shock and show a willingness by companies to raise returns.

The new JPX 400 index which is likely to be adopted by GPIF, the Japanese government pension fund which is the world's largest, includes qualitative criteria such as Return on Equity as part of the selection process. Venerable but unprofitable companies which have been left off the list are now feeling excluded. One has taken direct action to improve in order to be considered and was rewarded with a sharply rising share price. Japan has also published a stewardship code and this has been adopted by roughly 150 institutional investors, both domestic and foreign. This encourages investors to have substantive dialogue with companies and to exercise their voting rights, thus increasing pressure on managements to behave more in the interests of shareholders.

These changes, taken together, are a very positive background to be investing in Japanese companies as managements focus more on shareholders. We also don't believe that this is to the detriment of the internal stakeholders in companies, as the status quo becomes increasingly less tenable and dangerous. Change is also driven by rising Asian competition and the labour shortage in Japan. Economy and Profits

The past year has seen divergence between certain parts of the economy where the recovery is clear and becoming stronger, notably the labour market and the property market and those where there has been considerable weakness since the increase in the consumption tax in April 2014, such as industrial production. Mr Abe has passed thirty bills as part of his Third Arrow deregulation reform programme, including the formation of special economic zones where regulation will be substantially relaxed. Mr Kuroda, at the Bank of Japan, has also continued to expand the monetary base in Japan aggressively. However the negative effect of the tax rise seems to have had more impact in the short term. Despite this, reported profits for the three months after the rise were still growing; partly as an increasing proportion originate from overseas whether via exports or foreign subsidiaries.

The government still has its strong position in the Diet and Mr Abe is remarkably popular for this stage in a premiership. Further legislation for reform is likely to be passed, whilst Mr Kuroda has pledged to 'do what it takes' to get inflation to 2%. The government are currently debating the next consumption tax increase from 8% to 10% which is scheduled to happen in September 2015. Further weak data will make this difficult.

Although there remains widespread scepticism about any positive effects from Abenomics there are certain areas which have been boosted. Unemployment is now extremely low and labour shortages are becoming more widespread, whilst visa regulations for foreign workers have been eased. More women have returned to the workforce and there is increasing recognition of the practical measures, such as improved childcare, that are needed for employment equality. The property market is rising and vacancy rates and rents improving. Inbound tourism is booming and some of our retail holdings are direct beneficiaries. Duty free shopping will be deregulated further in the autumn. However it seems unlikely that growth in the economy overall is going to be particularly rapid but the link between GDP growth and profits is lessening as shown in the most recent quarter.

Although Japan has been reporting inflation rather than deflation for a year, the national mind-set has not yet shifted towards investment in riskier assets. Personal financial assets, which are approximately two and a half times the value of GDP, are still being invested predominantly in cash and companies have record amounts of cash on their balance sheets. If Abenomics achieves the sustained inflation rate that is one of the targets this is likely to change, which should benefit equities. The government are leading the way with the reform of the GPIF which is likely to sell its bond holdings and reinvest in equities which have much higher yields.

However, even without such a shift, profits are rising and valuations remain attractive. Japanese companies are now more globally minded and more globally competitive in the manufacturing arena and there is increased confidence in the non-manufacturing sector. Global trends, such as the increase in e-commerce, are reflected within Japan and provide opportunities for investment. *From Sarah Whitley, investment manager, Baillie Gifford Japan*

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Japan is not the only part of the investment world at the moment where there is a divergence between what is happening in the economy and what is happening in the stock market. Take home pay is still falling in real terms and companies are not seeing much volume growth domestically, but the stock market is up by more than a half in local currency terms since the end of 2012.

The factor pulling the two together is of course Abenomics, and the hope that the Prime Minister's policies will reinvigorate Japan. The policies have certainly changed stock market sentiment, but 20 months after the policy changes started it is still too early to say how much they will change the economic environment. *From Jonathan Taylor, Chairman, Schroder Japan Growth*

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Whilst concerns remain that the impact of the consumption tax increase in April may be deeper and more prolonged than originally envisaged, it remains probable that the economy is past the point of maximum strain. In addition, it seems more likely than not that the Bank of Japan will embark on additional easing. Together with attractive valuations and greater incentives to improve corporate governance, this represents a generally supportive backdrop for the stock market. *From Schroder Investment Management Limited as managers of Schroder Japan Growth*

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Vietnam *(compare country specialists – Asia here)*

Successful investment in Vietnam requires conditions both inside and outside the country to be on an even keel or trending up. The headwinds which accompanied tapering this time last year have petered out and on balance demand from the developed world appears to be picking up, albeit modestly. In China, which is of course a global economic heavyweight in its own right, growth seems to be recovering following a slowdown last year on the back of tightened credit conditions. Whatever the geopolitical concerns, and they are many, a healthy Chinese economy is likely to be key to Vietnamese economic prospects.

Longer term trends support the continuation of foreign direct investment ("FDI") into Vietnam. Outsourcing of manufacturing across the technological spectrum and rapidly rising wage rates in north Asia all point to greater FDI.

Inside the country, economic conditions are fairly stable, with growth running above 5 per cent and inflation under control. The Government is keen to accelerate the equitisation process and will need supportive capital markets to achieve its goals. There remain question marks about the recapitalisation needed in the banking sector, but a revival of property values would work wonders there.

In the meantime, the Vietnamese equity market trades at about 14 times 2014 earnings, a rating below the regional average of 16 times but reflecting a significant increase over the last year, according to Bloomberg. *From Steven Bates, Chairman, VinaCapital Vietnam Opportunity Fund*

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Emerging Markets *(compare global emerging markets funds here)*

The outlook is far from clear. The operating environment in emerging market economies is tough. The confluence of prospectively tighter US monetary policy, political developments and economic slowdown make it harder for companies to grow and even to maintain profits and dividends. *From Andrew Hutton, Chairman, JPMorgan Global Emerging Markets Income.*

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Emerging markets have had a troubled time but the situation seems to have stabilised. On a valuation basis, they are generally regarded as looking attractive despite the risks compared to developed markets. We are not out of the woods yet with regard to volatility in emerging markets but we appear to be moving in the right direction. *From Alan Saunders, Chairman, JPMorgan Emerging Markets*

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Notwithstanding the subdued stock market returns of the last few years, the long term prospects for making money in emerging markets remain huge: how can there not be great investment opportunities in an asset class which covers most of the world's population and a large and rising share of the world economy? If one wanted to look for a reason to be cautious, one could ask: how can immature economies produce companies to compete with the world's best? Will that opportunity not be taken by companies from the developed world, rather than by indigenous firms? And yet this clearly can happen. The best firms in emerging markets are highly competitive in any context. This is evidently true of export-oriented businesses, which would not exist otherwise; but in domestic industries the same competitiveness can also be found. There are few businesses more localised than beer; and today, the two largest companies in the world in that industry, AB Inbev and SAB Miller, both grew from beginnings in emerging markets. *From Austin Forey, Investment Manager, JPMorgan Emerging Markets*

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Private equity *(compare private equity funds here)*

Although the pace of economic recovery across the regions and markets in which the Company operates is mixed, the general outlook for continued economic recovery in some major markets is helpful in underpinning the rates of underlying corporate earnings growth in our portfolio. Risks of a reversal in market sentiment, however, remain. As recovery takes hold and quantitative easing slows, some factors such as labour costs and interest rates, which have been subdued for some time, may begin putting a brake on the pace of corporate profit growth. Additionally, while the recent events in Ukraine and the Middle East have to date had little impact on public markets, these remain a potential threat to stability. Within the private equity market, easy availability of credit and buoyant equity markets have created a positive environment for realisations but can also lead to an increase in leverage risk.

Secondary pricing has tightened as public markets have risen and conditions for exits have remained benign, giving buyers greater confidence in valuations. However, this has also had the effect of increasing the number of secondary market sellers, with 2014 transaction volumes on track to exceed those of 2013, which in itself was a record year. *From Tom Bartlam, Chairman, Pantheon International*

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The economic recovery has continued over the last year with many developed economies experiencing GDP growth, albeit at a low rate. Despite a slowdown in the first quarter of 2014 due to the severe winter, the US recovery seems to be on track. In Europe, recovery limps on and the risks to growth remain high. With public markets seeming fully valued, particularly in the US, and given the easy availability of credit, we believe investors must exercise vigilance in selecting assets and be prepared for any setbacks to recovery.

Although the public market rallies experienced in the second half of 2013 lost steam in the US and Europe during the first half of 2014, they have remained relatively stable. US markets in particular have pushed on to a record high, while volatility, as measured by the VIX, remains low. Credit is easily available and debt pricing has continued to fall. These conditions have proved supportive for exits by private equity managers both in the US and Europe.

Elsewhere, despite growth rates remaining lower, emerging markets continue to grow at a faster rate than developed economies. While markets in the region have been volatile, there is an increased possibility that GDP growth in China may stabilise and rise in 2015 as the government introduces measures to support the economy. Market confidence has also begun to return to India, anticipating positive economic developments following the recent change of government.

USA

The US recovery is now well underway, despite a slowdown in the first quarter of 2014 related to the unusually severe winter. US GDP grew 1.9% in 2013 and is forecasted to grow 1.7% and 2.3%, respectively, in 2014 and 2015. Housing starts are on an upward trend, household debt has fallen, and property prices have recovered. The USA continues to benefit from increasingly competitive labour costs (relative to China) and inexpensive energy created by an abundant supply of natural gas, both of which have contributed to a re-shoring of manufacturing.

Private equity firms invested $89bn of capital during the first half of 2014, a 16% decrease over the first half of 2013. A slowdown in the number of large deals completed contributed to this decline, as readily available and inexpensive debt financing have increased median purchase price multiples to pre-crisis levels. In contrast, deal activity by number increased by 8% during the first half of 2014, driven by growth and add-on transactions that are more conservatively valued and often have limited or no competition. The industrial and information technology sectors were the most active during the first half of 2014, representing 30% and 15% of deals completed, respectively. We expect healthy deal activity in the second half of 2014 due to significant dry powder remaining in the market and investors' desire to put capital to work.

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Exit activity has remained strong in 2014, despite the record $586bn distributed to investors by private equity managers in 2013. During the first half of 2014, private equity investors exited 435 companies valued at $127bn, a 57% increase over 2013. IPOs continue to be an attractive exit route, comprising 7% of all exits in 2014 to date. Private equity firms raised $15.6bn in 36 IPOs during the first half of 2014, a 44% year-over-year increase. Secondary buyouts and trade sales remain the most popular exit routes as both sponsors and strategics are seeking to acquire high quality companies.

Venture capital ("VC") investment continued to increase during the first half of 2014, while financing activity slightly declined. VC funds invested $28.9bn in US start-ups, driven by large rounds for later stage companies, including Uber ($1.2bn), Airbnb ($519.7m), Lyft ($250m) and Pinterest ($200m). High valuations resulted in fewer seed stage financings, which also contributed to the 22% year-on-year volume decline. Exit activity remained steady, with investors selling $25.1bn of investments through 369 liquidity events), and is expected to end 2014 on a high note with the completion of Facebook's $19bn acquisition of WhatsApp. IPOs remain a popular exit route for investors, with 68 VC-backed IPOs completed in the first half of 2014. Strong LP distributions in 2012 and 2013 fuelled a rebound in the VC fundraising market in 2014. Through the first half of the year, 105 US VC funds have been raised totalling $17.4bn in capital commitments, compared to the $18.2bn raised in all of 2013.

US fundraising remains strong with continued investor demand for private equity, in part due to robust distributions. In 2013, private equity funds raised $167bn, a post-crisis record, driven by 11 funds that closed on more than $5bn of commitments. Fundraising momentum continued in the first half of 2014, with private equity firms raising more than $87bn. High-quality managers continue to benefit from scarcity value, resulting in quick fundraises often with a single close. Despite a strong first half, 2014 fundraising will likely not exceed that of 2013 as there are fewer large funds in the market and LPs have shifted their focus to small and middle market funds.

Europe

The picture in Europe remains mixed with overall GDP growth sluggish. Estimates of Q2 2014 GDP growth suggest this was flat in the Eurozone and +0.2% across the EU. Consumer recovery remains slow, particularly in Southern Europe. Evidence of an improvement in either industry or exports is light, with a particular divergence between France and Germany. Unemployment is lower but was still 11.5% in the Eurozone in June 2014, however, encouragingly, Spain and Portugal did see falls in unemployment and generally youth unemployment is creeping lower. There has been no significant pick-up in exports but prospects are brighter given the weakening of the euro and potential for growth amongst the principal export markets such as China and the US. The ECB's decision in September 2014 to cut interest rates and signal future purchases of asset-backed securities is supportive. Despite this relatively weak backdrop, as seen in our own portfolio, with careful selection of high quality assets. Europe can be an attractive investment prospect.

Investment activity has slowed slightly as valuations have increased but purchase price multiples for companies with enterprise values below $250m where many of our managers are active, have not experienced the same increases. Private equity managers are favouring smaller add-on acquisitions to platform buyouts. Just as in the US, credit is easily available on attractive terms.

The exit environment has been strong during the first half of 2014. While trade sales and secondary buyouts have remained viable exit routes, there was a significant jump in IPO activity in the period, particularly in the UK, with numerous portfolio companies successfully listing on the London Stock Exchange. 2014 is on track to record one of the most active periods for larger exits since the pre-crisis boom, with a number of EUR1bn+ transactions closing in the first half of the year.

Rising equity markets and an increasing rate of distributions have encouraged investors to replenish their commitments to European private equity. New capital has been concentrated towards an ever-smaller group of high-quality funds, with investors continuing to favour the most experienced private equity managers with proven performance track records.

Asia

Emerging markets appear to have avoided a hard landing, with GDP growth in China expected to stabilise this year at around 7.4%. Debt remains high but we are seeing steps from the Chinese government to control this. Investor confidence in India has improved with better exit conditions but uncertainty remains around regulatory issues.

The first half of 2014 saw a significant increase in the value of deals completed. Many Asian company owners are finding traditional sources of capital restricted and they are becoming more familiar with private equity as a constructive source of capital. These improving perceptions are giving rise to a greater supply of investment opportunities, where private equity managers are taking significantly influential shareholdings, enabling their active involvement throughout the ownership period.

Investor confidence and optimism for the second half of 2014 remains high. Asia is an attractive diversification option for investors, and private equity managers continue to unlock opportunities from the large stock of private companies. Improving market conditions should provide the encouragement required for investment transactions throughout the remainder of 2014. Equally, robust credit markets have made capital more accessible and potentially facilitate increased deal-making going forward.

Secondary market activity reached a historical high, with $16bn of deal volume in the first half of 2014 versus $12bn in the same period last year. Sellers came from a broad spectrum, with banks, public pension funds and asset managers among the most active participants in the market. Regulatory change, capital adequacy testing and portfolio management typically dominate sellers' motivations; this year, they were also enhanced by higher secondary market pricing levels.

The overall market saw $36.5bn of secondary deals transacted during the past year, significantly higher than the prior period due to a very busy second half of 2013. Matching the broader increase in activity, Pantheon saw an increase in deal flow, reviewing over $50bn of transactions across approximately 280 sellers during the year to 30th June 2014.

During the year, secondary market pricing continued to recover towards pre-crisis ranges, with many funds trading at par, or even at premium pricing, to most recent net asset values. This has been partly caused by rising public market valuations, but also by the expectation of further increases in public market valuations and continued strong realisation activity.

Despite the potential for a delay in the implementation of the Volker rule compliance deadline beyond June 2015, banks that continue to hold private equity assets are expected to engage in more selling activity by the end of the year. In addition, if pricing levels persist at current levels, sellers are likely to continue to opportunistically access the secondary market. Given the likely deal flow in the second half of the year, there is a real prospect of secondary deal volume reaching record volumes of over $30bn in 2014. *From Pantheon International Participations*

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Debt *(compare debt funds here)*

Global economic recovery appears to be solidly entrenched, except perhaps in the Eurozone, with the United States and the United Kingdom amongst those showing good progress. Quantitative easing may be giving way to the prospect of interest rate rises in the latter, but it seems that the Eurozone can be relied upon to keep monetary policy slack. *From James G West, Chairman, New City High Yield*

The growth in the USA economy will be key going forward. We still expect the first rate rise to come at the end of quarter one 2015, if anything can be drawn from history then the fact that more companies go into default when the economy is in early/mid recovery phase, then this is a flag worth looking for in the coming months.

In China GDP growth is now officially forecast below the "Magic" 7% level although this is still a large number, we would expect this to have a negative effect on both global growth and commodity prices.

Europe is still trying hard to get some growth into the economy, but this continues to be an uphill struggle.

The UK, post the 'No' vote in the independence vote for Scotland, will still be in political stress with the forthcoming general election in May 2015, and "what about England?" calls from various factions. Away from this uncertainty the underlying economy is still recovering well and given the forward guidance from the Bank of England we would expect a rate rise around about the same time as the USA at the end of Quarter one. *From Ian Francis, New City Investment Managers, manager of New City High Yield*

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