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Monthly summary | Investment Companies

9 November 2015

Economic & Political Roundup

November 2015

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 minds up. Please remember that nothing in this note is designed to encourage you to buy or sell any of the companies mentioned.

Global equities

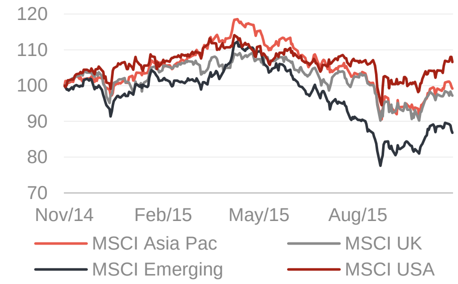
At the latter stages of the current market cycle with Chinese Growth and the prospect of US interest rate rises key risk factors.

Richard Hills, Chairman of Henderson Global, says that, whilst they're constructive on equities they're aware that we are probably in the latter stages of a market cycle and are mindful not to take undue risk. Wouter Volackaert, the manager, cautions that, whilst growth is positive, the absolute level of growth is low and it will not take much to move it back into negative territory. The main risks currently being the Chinese economy and the impact of rising US interest rates. Ben Lofthouse, manager of Henderson International Income, observes that economic policy remains accommodative and suggests that the fact that some Central Banks are considering when to raise rates is a sign that economic growth is on the right path. Angus Macpherson, Chairman of JPMorgan Elect, believes we should be prepared for recent volatility to continue. Katy Thorneycroft, the manager says they are generally positive on developed economies but expect emerging economies to continue to drag on global growth without stalling it.

Exchange Rate	31/10/15	Chg. on month
USD / GBP	1.5427	+2.0%
USD / EUR	1.1006	-1.5%
USD / JPY	120.6	+0.6%
USD / CHF	0.9876	+1.4%

MSCI Indices rebased to 100

Time period 01/11/14 to 31/10/15



Source: Bloomberg and Marten & Co

	31/10/15	Chg. on month
Oil (Brent)	$49.41	+2.1%
Gold	$1141.5	+2.4%
US Tsy 10 yr yield	2.142%	+5.2%
UK Gilt 10 yr yield	1.922%	+9.1%
Bund 10 yr yield	0.517%	-11.9%

UK

Equity market facing strong headwinds from rising interest rates and Chinese growth expectations. EU referendum a concern.

Sir Laurence Magnus, Chairman of JPMorgan Income & Capital, thinks that the equity market is facing some strong headwinds but central bank support makes it hard to form a definite view. John Baker and Sarah Emly, managers of that fund, make the case that, despite low CPI levels, the UK's large current account deficit and low productivity growth could mean inflationary tendencies remain strong but they believe rate rises will be modest and gradual. Sir David Thomson, Chairman of The Investment Company, believes the abrupt fall in commodity prices indicates the extent to which world growth expectations have deteriorated. However, he says that the UK has a stable business-friendly Government in place, which may give it something of a safe haven status. Gervais Williams and Martin Turner, managers of that fund, say when long-term bond yields fall to very low levels, it suggests that forthcoming returns on many mainstream assets could be sub-normal. Georgina Brittain and Katen Patel, Managers of JPMorgan Smaller Companies see three key risks: the EU Referendum, interest rate rises in the US and UK and the increase in the National Living Wage. Nicholas Fry, Chairman of BlackRock Smaller Companies says that UK smaller companies are no longer conspicuously cheap compared to their larger counterparts. Lord Flight, Chairman of Aurora, comments that against a background of inflation remaining very low and the possibility of further stimulation of the Chinese economy, investor sentiment could improve rapidly, leading to a bounce in equity valuations.

Europe

Some are concerned about current market levels but many believe valuations are reasonable and that the trajectory for growth remains positive. Sanditon somewhat positive on commodities which they see as uncorrelated to other assets.

The managers of Sanditon Investment Trust, say they are not expecting commodity prices to recover quickly. They like their low correlation to other assets, which they now see as far more vulnerable to a general market correction. Nicola Ralston, Chairman of Henderson Eurotrust, expects short term interest rates to remain lower for longer and thinks European valuations look reasonable in a longer term context. Tim Stevenson, manager of Henderson Eurotrust, has a slight fear that European markets are trading at high levels just at a time when perhaps we are close to being at the point where it is "as good as it gets". Carol Ferguson, Chairman of BlackRock Greater Europe, thinks European equities remain attractive and the likely path is one of continuing growth, helped by lower energy costs and a favourable exchange rate. Vincent Devlin and Sam Vecht, Managers of that fund, believe European economic growth should continue to improve over the next year. They say that macroeconomic momentum remains positive and monetary policies remain supportive.

Asia

Value in the smallest companies. Slow down in US and Europe may lead to further downward pressure given export dependency.

James Ferguson, Chairman of Scottish Oriental Smaller Companies, believes that the best value in Asia can be found in the smallest companies but that their liquidity makes them difficult to access. Wee-Li Hee, Martin Lau and Scott McNab, Managers of Scottish Oriental Smaller Companies, are not particularly optimistic at present. They say that increasing evidence of a slowdown in the US and Europe indicates that market expectations may still have further to fall given much of Asia's dependency on exports, which is feeding into currency depreciation.

Japan

Key changes in corporate governance, tight labour market and inbound tourism.

Baillie Gifford, Manager of Baillie Gifford Japan, believe there are three key forces driving changes in Japan at the moment: a fundamental sea-change in corporate governance, a tightening labour shortage and an increase in inbound tourism. They would not claim that all the many aims of Abenomics will be a success, but there is enough forward progress for them to be encouraged.

Emerging markets

Valuation levels becoming attractive but there are still many real risks

Andrew Hutton, Chairman of JPMorgan Global Emerging Markets Income, says that low growth in China, abrupt currency adjustments, political tensions, weak commodity prices, capital outflows and the risks of policy error are all real hazards with the spectres of weak growth and deflation especially worrisome. Richard Titherington and Omar Negyal, Managers of that fund, say that emerging markets may finally be approaching valuation levels that compel long-term investors to reallocate to the asset class and that these equities appear to be pricing in a much more negative outlook for growth and corporate profits than is perhaps justified.

Private Equity

High equity prices are supportive of disposals but may hamper new investment. Benign credit markets supportive of follow on transactions

Tom Bartlam, Chairman of Pantheon International Participations, says that easing credit market conditions are keeping M&A markets active. However, high equity prices create a hurdle to achieving good investment performance when making new investments. Nonetheless, benign credit markets allows companies to reduce their cost of capital which is supportive of follow on transactions. Pantheon Ventures say that the fall in commodity prices and continued competitive devaluation amongst a major currency blocs have added further to investors' difficulties. Economic growth has strengthened in developed markets but asset valuations look increasingly stretched and may be vulnerable to likely rises in interest rates in the US and beyond.

Debt

Potential for sector rotation in sectors that are more exposed to interest rate risk

Antony Vallee, Natalia Bucci and Robin Dunmall, Managers of JPMorgan Global Convertibles Income, say they see the potential for opportunities to emerge in sectors disproportionately exposed to changes in interest rates, such as utilities and other non-cyclical industries. Their analysis suggests that equity markets have tended to perform positively in periods in which interest rates rise from low levels.

Property

Care sector facing headwinds from living wage, funding uncertainty and regulation. Student accommodation market expected to continue to be tight

Malcolm Naish, chairman of Target Healthcare REIT, expects economic uncertainty to continue to impact sentiment and pricing in the investment market. The care sector is also facing headwinds from: introduction of the living wage, uncertainty over government funding of care, and; a stronger regulatory regime. Robert Peto, Chairman of GCP Student Living, expects the shortage of purpose–built, modern student residential accommodation in and around London to continue for the 2015/16 academic year and beyond. He expects planning reforms and land values to make it difficult to bring on stream new developments and limit the number of operators.

Renewable energy

Uncertainty over support for new installations

John Rennocks, Chairman of Bluefield Solar Income, says that there are uncertainties regarding support for new installations in 2016 and low power prices are also an issue.

Contents

Global

(compare Global funds **here**)

Richard Hills

Richard Hills (Chairman of Henderson Global). Six years into the market recovery that started in 2009, we remain constructive on equities and are fully invested. However, we do recognise that we are probably in the latter stages of a market cycle and are mindful not to take undue risk.

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Wouter Volckaert (Manager of Henderson Global). With liquidity-driven multiple expansion becoming less of a tailwind, economic and corporate earnings growth need to take over as the key driver for equity markets. The good news is that the global economy is improving gradually. The bad news is that the absolute level of growth is low and it will not take much to move it back into negative territory, with the main risks currently being the Chinese economy and the impact of rising US interest rates. The fragility of the global economy and the fickleness of investor expectations explain why earnings growth should continue to be a more volatile driver of stock markets compared to excess-liquidity driven multiple expansion.

All things considered we remain cautiously optimistic and the portfolio is fully invested. However, we are cognisant that we are well into the market rally that started in 2009 and that market volatility will rise going forward. Therefore, we have no desire to use leverage at this point in time.

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Christopher Jonas, CBE (Chairman of Henderson International Income). Economic growth in developed economies remains stable and interest rates remain at very low levels. Major countries are more aligned politically on policies to deal with the remainder of the 2007 induced recession, even if the rise in strongly left or right wing groupings within them presents a new challenge. Public debate about whether or when Central Banks should raise interest rates discloses a general belief in growth continuing for the near term, even if this growth may be patchy. Against this background, we judge that well positioned, cash generating companies with good dividend yields will remain attractive to investors looking for growing income streams and the potential for capital growth.

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Ben Lofthouse (Manager of Henderson International Income). The economic recovery since the financial crisis several years ago has been slower than expected but unemployment is generally falling in most developed markets, which is an important measure of progress. Economic policy remains accommodative, with even the European Central Bank acting to stimulate credit growth, and the fact that some Central Banks are considering when to raise rates is a sign that economic growth is on the right path. Whilst there are significant risks to economic growth that we remain vigilant about we are optimistic and will take advantage of volatility in markets.

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Angus Macpherson (Chairman of JPMorgan Elect) Global equities have experienced considerable volatility, fuelled in part by concerns over the strength of the Chinese growth story. We should be prepared for this volatility to continue, at least while the nature and strength of global growth remain unclear. The policy initiatives that successfully stimulated the global economy in 2008 were new and have ushered in an economic environment with which we are mostly unfamiliar. Against this background, it seems inappropriate to speculate too much about the outlook for the next 12 months. However, I am confident in predicting that it will be interesting.

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Katy Thorneycroft (Manager of JPMorgan Elect). We maintain a moderately pro-risk stance, reflecting our generally positive outlook for developed economies. While the economic challenges in emerging economies are likely to continue their drag on global growth, we do not believe these forces will be enough to stall domestic recoveries in the US and Europe.

China will continue to divide opinion. While China has accounted for around one-third of world nominal GDP growth since the crisis, International Monetary Fund (IMF) projections have this falling to around one-fifth in 2016. The US and increasingly, Europe drive global growth and we remain optimistic that the domestic recoveries in both regions are robust. However, EM weakness will constrain global growth rates overall.

We therefore remain cautiously optimistic on risk assets, with a preference for developed markets; but questions over growth and policy lead us to moderate portfolio risk. On balance, we maintain our view that the gradual healing of developed economies will more than offset weakness across emerging markets, leading to a steady maturing of the mid-cycle phase in which the US economy currently sits.

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UK

(compare UK funds **here**)

Sir Laurence Magnus Bt (Chairman of JPMorgan Income & Capital). Given the sharp market correction in August (and continuing turbulence in September) combined with increasing concerns about a slowdown in world growth, it is clear that the equity bull run witnessed since 2009 is facing some strong headwinds. It is difficult, however, to reach a definite view given the extent to which central banks appear to be willing to provide support to faltering economies and markets by way of low interest rates and liquidity injections.

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John Baker and Sarah Emly (Managers of JPMorgan Income & Capital). As we head towards the end of 2015, attention is turning to monetary policy and the timing of the first UK interest rate rise. Although the consumer price index remains at very low levels, the UK's large current account deficit and low productivity growth could suggest that inflationary tendencies in the economy remain strong. As a result, the recent strength of UK economic data - particularly a pick-up in wage growth and a post-election surge in house prices - reinforces the prospect of eventual interest rate rises.

Rising interest rates would be expected to cause headwinds for domestically focused companies, which have generally outperformed over the last 12 months. Nevertheless, interest rate rises, when they are eventually introduced, are likely to be modest and gradual, which may ease the pressure on stocks. The UK market also remains reasonably attractive from a valuation perspective, trading on a lower forward price-to-earnings ratio than many other developed markets and offering a high dividend yield compared to the low income available from government bonds. Corporate earnings' expectations have fallen in the last year, so any further rebound in European growth and a stabilisation in commodity prices could lead to upgrades and provide further support to valuations.

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Sir David Thomson (Chairman of The Investment Company). The abrupt fall in commodity prices underlines just how profoundly world growth expectations have deteriorated. Fortunately, the UK has a stable business-friendly Government in place for the coming five years, which may give it something of a safe haven status in an unsettled world.

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Gervais Williams

Gervais Williams and Martin Turner (Miton Asset Management Limited, managers of The Investment Company). When long-term bond yields fall to very low levels, it suggests that forthcoming returns on many mainstream assets could be sub-normal over the coming years. In this context, the fact that the yield on the 10 year UK Government Bonds has fallen to 2.0% or so at the end of June 2015 is sobering. In short, there is a greater challenge on all active funds to ensure their strategies have plenty of scope to generate an attractive return for their investors without taking unreasonable risks.

It is widely recognised that smaller quoted companies tend to have more growth potential than larger companies. This differential has not been especially distinctive during a long credit boom when world growth has been plentiful. However, the huge setback in commodity prices underlines just how much expectations for world growth have reduced. In spite of many years of remarkably low interest rates, and the adoption of novel policies such as Quantitative Easing, world growth has progressively decelerated. Therefore, there may be great advantage for those funds that can invest in both larger and smaller companies to buck the wider trend in the future. Such a portfolio has greater opportunity to deliver premium returns through investing in those stocks that can sustain growth even at a time when economic conditions are more challenging. In addition, smaller companies have the added advantage that many stand on less demanding investment valuations currently, plus there is greater scope for extra return through investing in those with mispriced valuations versus the sub-normal average.

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Michael Quicke OBE (Chairman of JPMorgan Smaller Companies). There are a wide range of economic and political uncertainties that continue to worry markets. Internationally, these include the timing and pace of US interest rate increases, the slowdown of the Chinese economy and political deadlock in Europe. Domestically, the outcome of the forthcoming EU referendum is uncomfortably uncertain.

However, against this background, the UK economy is making good progress. For the time being, domestic politics provide a reasonable environment for smaller companies to prosper, although after a long period of stability, we expect wage inflation to become a greater concern in the future.

A good flow of companies coming to the market is providing our managers with new opportunities, and the recent increase in merger and acquisition activity reinforces our view that smaller companies currently represent relatively good value.

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Georgina Brittain and Katen Patel (Managers of JPMorgan Smaller Companies). Both the US and the UK continue to grow, with the UK currently enjoying 2.6% GDP growth year-on-year. Inflation remains very low, benefiting from the on-going low oil price, the recent fall in commodity prices, and declining food prices. In addition, wage increases are occurring well ahead of inflation; real wages are now predicted to rise by 3.5% this year, unemployment is down to 5.6% and we have now seen 20 consecutive months of year-on-year increase in consumer spending power. Unsurprisingly, this has led to UK consumer confidence being at a 15 year high.

In Europe, a key trading partner for the UK, Greece has secured a bailout extension with its creditors, and new data points from the Eurozone on business and consumer confidence demonstrate that the recent Greek crisis caused little damage to the broader Eurozone countries. We also expect the European economies to continue to benefit from the on-going stimulus plan. Stock market concerns have now focused on China, but it is our view that the perceived risks from recent Chinese stock market turbulence are being over-played. The Chinese economy has clearly slowed from the heady days of 8% GDP growth per annum, but this slowdown is well-known and is also less relevant for smaller companies.

There are three relevant risks on the horizon; the EU Referendum, interest rate rises in the US and UK and the increase in the National Living Wage. On the former, current surveys appear to show little risk of the UK leaving the EU. Regarding rate rises, it remains our view that any rises in interest rates (possibly in the second quarter of 2016 in the UK) will be small and controlled, and reflect the improving health of both the US and UK economies. More recently, post the Summer Budget, the Chancellor's significant increases in the minimum wage - the National Living Wage - have already started to have an impact. It is currently our view that the beneficial impact on the consumer, as wages rise, should approximately balance out the cost to certain companies of significant wage increases, but we are keeping a weather eye on the outcome of this policy change.

Overall, we believe that smaller companies will remain strong beneficiaries of the on-going economic recovery. While bouts of stock market volatility have become the norm, we continue to use them to add to our favoured holdings, and we continue to believe that the domestic bias of the majority of our holdings shelters them from many global concerns. Valuations remain extremely attractive in smaller companies, as evidenced by the wave of M&A we have seen. This, plus the increasing number of exciting new growth companies that we have seen coming to the market, provides us with confidence for the year ahead.

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Nicholas Fry (Chairman of BlackRock Smaller Companies). With the uncertainty surrounding the outcome of the UK General Election now removed, investors now have a clearer idea of the likely domestic political and economic policy landscape over the next couple of years. For the first time in many years the UK working population is also now experiencing real earnings growth, which should support domestic consumption.

Abroad, the slowdown in China’s economy and resulting decline in demand for commodities has had a knock-on impact on many of the emerging markets, and has also had a powerful disinflationary effect, allowing central banks to sustain low interest rates for much longer than previously expected.

In the context of equity valuations generally, and following strong relative performance, UK smaller companies are no longer conspicuously cheap compared to their larger counterparts.

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Mike Prentis (Manager of BlackRock Smaller Companies). The economic growth slowdown in China, and the steps taken by the Chinese authorities to stimulate their economy, have unsettled global stock markets. Markets also remain worried by the likelihood that interest rates could rise in the US and UK, and by the volatility in the oil price. At the company level we have seen generally good results from our portfolio, and outlooks which suggest that this is likely to continue. We believe that it is safest to stick with our predominant exposure to developed markets demand, especially from the consumer sector.

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Lord Flight (Chairman of Aurora). In the UK, post the unexpected overall victory by the Conservative Party in May, the economy has remained robust, led by the services industries. The confidence of a further five years of domestic political certainty has resulted in a spurt of increased levels of investment by the private sector. Meanwhile in Continental Europe, despite the adverse effects of economic sanctions against Russia, there has been definite evidence of improvement in certain economies, notably Germany, Spain and Ireland, resulting from the belated introduction of Q.E., together with the dramatic falls in commodity prices in general.

Against such a global background of inflation remaining very low in most territories and the possibility of further stimulation of the Chinese economy, investor sentiment could improve rapidly. With deployment by both institutions and corporates of the high current levels of liquidity a sharp bounce in equity valuations would be a logical result.

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MJ Barstow (Manager of Aurora). At a time when the majority of Developed Economies appear to be strengthening and when the prospects for interest rates to remain low are set fair, the level of investor sentiment is unduly negative against a background of high institutional liquidity. Accordingly, a sudden rebound in equity markets could easily occur in the near term, with a likely catalyst being the faintest glimpse of improved economic statistics emanating from China, where some are already of the firm opinion that the leading indicators have turned upwards.

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M & L Capital Management Limited (Managers of Manchester & London). Our five best guesses for 2016 are set out below:

- Another low growth = low returns year
- China to be the big worry
- Consolidation through M&A will pick up
- The Dollar continues to appreciate
- The developing markets will slow but ASEAN should still grow faster than developed markets

Our concerns rest around the potential for a dramatic slowdown for China which drags the world down into a deflationary cycle where debts become overwhelming. Our best guess is that this won’t happen and we are in line for another low economic growth and low market returns year where the dollar continues to appreciate. We are also hopeful of a pick-up in M&A activity.

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Europe

(compare European funds **here**)

Sanditon Asset Management Limited (Managers of Sanditon Investment Trust). One area we have become more interested in as the year has progressed has been the commodity space. We do not pretend to have any ability to predict any commodity price but after close to a five year bear market for commodities, it strikes us that they are starting to become a more interesting 'long' investment. The days of the China commodity boom are long gone; capex which mushroomed during the boom is now being slashed and although we are quite sure that falling commodity prices are warning us and all investors of the likely future trajectory of global growth, we like the fact that they have, almost without exception, been terrible investments for five years. A commodity bull has gone the way of the dodo. We are not saying we expect commodity prices to recover quickly, although it is possible as we suspect financial players have become as vigorous chasing commodities down as they chased them up in the boom. It may be unfair to single out Goldman Sachs who a few years ago forecast oil would hit $200 a barrel but are now trumpeting their bearishness. Our point is, this is classic behaviour for a very cyclical sector. Increased capex leading to increased supply nearly always leads to falling prices and then falling capex as the cycle continues. Commodity companies are price takers and we do not like them as long term investments but we do currently like their low correlation to other assets, which we see as far more vulnerable now to a general market correction.

Policy makers around the world have spent their time since 2008 with their foot on the monetary accelerator. We cannot remember a time when asset markets have been so vigorously manipulated by authorities be it through QE programmes or more flagrant interventions like the Chinese. We will soon find out how even a modest application of the brakes will affect financial markets.

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Nicola Ralston

Nicola Ralston (Chairman of Henderson Eurotrust). With the marked slowdown in China in the summer of 2015, it now looks as though short interest rates will remain lower for longer in the major economies. This is particularly the case in Europe where, earlier in the year, the European Central Bank made a commitment to buy government bonds (known as "Quantitative Easing") in an attempt to boost the rate of inflation towards a 2% level. In this uncertain environment equities, including European equities, have been weak in recent months. Yet European valuations are still reasonable in a historical context; and, boosted to some extent by the weaker currency, earnings growth remains strong.

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Tim Stevenson (Manager of Henderson Eurotrust). The menu of "worries" mentioned in last year's Annual Report included Ukraine, the Middle East, and the prospect of tighter monetary policy in the USA and the UK. A year on, and the list is the same, and now Greece can be added, and also the uncertainty that may be caused by a sharper slowdown in the Chinese Economy. In addition there is a further pressure on the "Emerging Markets" which are struggling due to the strength in the US Dollar. There is a slight fear in the back of my mind that European markets are trading at high levels just at a time when perhaps we are close to being at the point where it is "as good as it gets". If there has been an element of "faute de mieux" behind the flows to European markets, then the flows which have avoided bonds might just swing back to ten year bonds when yields rise back towards a level of say 2.5% to 3% as inflation returns to a level of closer to 2% as expected by the ECB.

It could herald a more difficult twelve months ahead. In spite of that word of caution, the facts are clear that European economies are recovering, which is a result of the huge stimulus from the ECB's Quantitative Easing (QE) programme. This may have started later than some had wanted, but the fact that it was launched at a time when some were arguing that recovery had already started might mean that Europe is experiencing QE on steroids. Lower raw material prices - especially oil - has meant that the significant decline in the Euro has not translated into inflationary pressures, but that a weaker Euro has boosted the translation impact of overseas sales and profits. With these earnings coming through, companies are continuing the trend of paying a greater proportion of earnings to shareholders and I am confident that we will see increasing dividends for our holdings again this year. There will almost certainly be stress within the Euro area again, but at last, after many years of hesitancy, global investors are beginning to understand that there are some outstanding companies listed on the European markets.

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Carol Ferguson (Chairman of BlackRock Greater Europe). Stock markets globally remain caught between concerns about a Chinese economic slowdown on the one hand, and fears about the path of US interest rates on the other. Our Managers do not believe, however, that the current slowdown in China will prompt the start of a global economic recession and the resulting onset of a bear market.

European equities remain attractive in a global context, given the competitive position of many exporters after the weakness of the Euro in recent years. Shares are more reasonably rated than their U.S. counterparts and the ECB's policy remains accommodating. Whilst numerous challenges remain, not least the political and economic strains of coping with growing numbers of refugees, the likely path of the region's economy overall remains one of continuing growth, helped by lower energy costs and the favourable exchange rate.

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Vincent Devlin and Sam Vecht (Managers of BlackRock Greater Europe). Despite recent market volatility, we remain positive on the prospects for the broader European equity market given that the macroeconomic momentum remains positive and monetary policies remain supportive. The recent correction has made investors somewhat fearful of global growth prospects, but for companies with more domestic exposure, European equity earnings momentum remains robust. The ECB's programme of Quantitative Easing remains in place and is having a positive impact on the credit cycle and European GDP growth. After five years in crisis, economic growth is recovering across the European region and, with supportive monetary policy, should continue to improve over the next twelve months in our view. Over the long term we continue to believe that the corporate earnings and cash generation of companies are the key drivers of equity returns.

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Asia

(compare Asian funds **here**)

James Ferguson (Chairman of Scottish Oriental Smaller Companies). The long-term arguments for investment in smaller companies in Asia remain persuasive. The immediate outlook is much more challenging. We are in the midst of a period of unusual economic circumstances and it is difficult to guess how long it will take to return to more normal conditions. Our managers are not particularly optimistic at the moment. At present, the smallest companies provide the best value, but these are difficult to buy as they tend to be illiquid.

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(Wee-Li Hee, Martin Lau and Scott McNab Managers of Scottish Oriental Smaller Companies). The outlook for Asian equity markets remains uncertain. Although forecasts for economic growth and corporate earnings have fallen, increasing evidence of a slowdown in the US and Europe indicates that market expectations may still have further to fall given much of Asia's dependency on exports. It is probably no coincidence that, as weakening export conditions became more apparent, the speed of currency depreciations accelerated. It is not possible for a single nation, let alone an entire continent, to achieve wealth by debasing its currency. Competitive devaluations merely lead to increased competition for market share in the export sector and reduced purchasing power at home. The likely outcome will not be the creation of sustainable growth.

In China, the government looks set to continue its attempts to boost both the real economy and the stock market but this will remain akin to pushing on a string, given the various challenges that economy faces. Policies aimed at reducing corruption and increasing the quality of growth need to be endured for China to prosper in the longer-term. Many of the measures that the government is taking are sensible but others are short-term in nature and will not address the issues of overcapacity in certain industries and overvaluation in certain sectors of the stock market.

The outlook for India and South East Asia is slightly brighter given the greater number of quality companies. However, political discord and social tension are both risks to these regions and although valuations are cheaper than a year ago there are few bargains. Accordingly, the Trust will remain conservatively positioned and endeavour to seek out sustainably run businesses at reasonable valuations. The longer-term case for investing in Asia remains unchanged with the region's attractive demographics and expanding middle class providing structural growth that is missing in the developed world. Pockets of value have been found in Taiwan and China recently but we would need further market falls for us to feel enthusiastic about the medium-term prospects.

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Japan

(compare Japanese funds **here**)

Jonathan Taylor

Jonathan Taylor (Chairman of Schroder Japan Growth). One judgment for investors, following the Chinese stock markets' collapse, is whether this is just a reaction to market events in China (which have little direct impact on the Company's portfolio), or indicative of a more fundamental change in the outlook for global growth. Resolution of this is not made any easier by concern that Abenomics may be running out of steam.

One obvious hangover from the market correction, however, is that day-to-day volatility in share prices remains high. While this is always threatening to investor confidence, one benefit is that this is likely to be an environment with considerable opportunities for a stock-picker looking for long term value.

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Schroder Investment Management Limited (Manager of Schroder Japan Growth) The current economic environment is less supportive of the equity market than it was during most of the last year, as evidenced by a sharp correction and increased volatility immediately after the Company's July year end. Whilst the external environment remains uncertain, especially in relation to China, we are more confident that the domestic economy will emerge from its recent soft patch.

The fall in the market has brought stock market valuations back to lower levels. Corporate profit trends bear watching but so far the revisions index overall remains positive, even if it is weaker for manufacturing. Despite specific problems at one leading Japanese company, Toshiba, nothing has happened to undermine the more positive underlying developments in corporate governance, capital efficiency and shareholder returns. On balance we expect market volatility to continue, but remain cautiously optimistic from current levels given these developments at the corporate level.

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Nick Bannerman (Chairman of Baillie Gifford Japan). The Board visited Japan in May this year, meeting with a variety of companies of interest to the Managers and we returned with a more positive outlook on the investment opportunities within Japan as a whole. Prime Minister Abe strengthened his mandate for political and economic reforms by calling and winning a snap election last December. We also saw much evidence of the encouraging improvements in corporate governance across Japan which the Manager continues to press for with all our holdings.

There has been significant volatility across world markets since our August year end with Japan no exception; however, we continue to believe there are significant opportunities for investment growth.

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Baillie Gifford (Manager of Baillie Gifford Japan). We believe that there are three key forces driving changes in Japan at the moment. The first is the fundamental sea-change in corporate governance, encouraged by the advent of Abenomics but also by the demographic changes and the increase in international competition.

Last year Japan introduced a new stewardship code encouraging institutional investors to constructively engage with the companies they invest in and this year a new Corporate Governance code was introduced in June. This encourages companies to change their boards and already the number of independent Directors has risen further and now 94% of companies have outsiders on the board. Companies also have to issue a statement about their attitude to issues like cross-shareholdings by the end of this year. This push is also coming at a time when the importance of some other stakeholder groups is lessening. We believe that there will be fundamental change over a five year period and that this will lead to lower cash holdings on balance sheets and increasing dividends along with investment for growth. The retirement of the baby-boomer generation, with their corporate pensions and the increasing labour shortage, means that managements no longer have to run companies to maintain employment in Japan.

The second development driving change is therefore the tightening labour shortage. Again related to the aims of the Abe government more women have been working in Japan but the unemployment rate is now extremely low and surveys show employment conditions extremely tight. There are suggestions that most new jobs in Japan in the past few years have been created by companies younger than five years, whilst the older companies are reducing employment. This is a very welcome rebalancing and one that has very positive implications for productivity. It goes alongside the change in corporate governance and the rise in entrepreneurship in Japan. In 1992, after the bubble burst, the major cause of bankruptcy in Japan was a labour shortage for small companies artificially created by large corporations continuing to recruit whilst the economy turned down. Now the situation is different and the very strong confidence being reported by the non-manufacturing sector, which is the majority of employment in the economy. In terms of significant formal immigration that remains some years away, although the number of foreign residents of Japan continues to rise and there are many anecdotal reports of informal employment.

Thirdly, increased inbound tourism is arguably one of the most successful outcomes of the original aims of Abenomics. The easing of visa restrictions alongside the improvement in access provided by more low cost airlines flying into Japan, mainly from Asia have contributed to inbound tourism. For example, there is now a new terminal at Narita, Tokyo’s main international airport, dedicated to such airlines offering cheaper landing fees as historically the punitive rates for the main airport have been a deterrent to travel. Last year the total number of foreign tourists reached 13.4m and the likely outcome for 2015 is now very likely to exceed 18m. Originally the target had been 20m in 2020, when Japan is hosting the summer Olympics in Tokyo, but this is likely to be comfortably exceeded. This new source of demand is helping certain retailers and manufacturers as well as increasing the occupancy rates of hotels, but it is also beginning to have social impacts. As travellers come on return trips they are travelling outside the main cities and many traditional Japanese attractions, from temples to ryokan, are adapting and becoming more welcoming. Made in Japan is viewed increasingly as a badge of quality, particularly by Chinese tourists.

Whilst global stock markets have been experiencing turbulence in recent weeks we think that the long term positive changes for Japanese companies will be more important over the next year. This is not to deny that weakness in the Chinese economy will see demand fall for some products but rather that the longer term shifts in behaviour will outweigh shorter term difficulties. This is also not to claim that all the many aims of Abenomics will be a success, but that there is enough forward progress to be encouraged. Prime Minister Abe was re-elected with a strong majority in December 2014, and having achieved his aims of changing the security laws in Japan is now refocused on improving the economy. There is much negative commentary on Japan's outstanding levels of debt and very little on the overall level of assets, which makes Japan the world's largest ever net creditor nation. In November Japan Post Holdings, Bank and Insurance will all be privatised which will move very significant businesses from the public to the private sector. Against this background and with the belief that valuations are not too high the trust has increased its levels of gearing after the year end.

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Thailand

(compare Country Specialist – Asian funds **here**)

Nicholas Smith

Nicholas Smith (Chairman of Aberdeen New Thai). The prevailing environment is unlikely to rouse Thai markets significantly in the short term. The global economy looks to be teetering between a stalled recovery and a full-blown slowdown, neither of which bode well for Thailand's export-dependent economy. China's deepening malaise and sustained weakness in commodity markets will continue to dampen risk appetites. Meanwhile, the US Federal Reserve's decision to delay a much-anticipated interest rate hike seemed broadly positive for emerging markets. However, it is likely to merely prolong the uncertainty, potentially stoking further market volatility.

Domestically, Thailand continues to grapple with its own economic challenges. Deflation is a looming threat, exports have taken a battering from lacklustre offshore markets, while confidence and spending remain depressed. That said, there is hope of an imminent pick-up in consumption as the impact of 2012's first-car buyers scheme, which suppressed up to four years of future demand, finally dissipates. Increased public spending should also be broadly supportive. Elsewhere, tourism appears to have held up in the wake of the bomb blast and should remain a cornerstone of the economy; the healthcare and hospitality industries stand to benefit in particular.

Outwardly the junta appears to be laying the groundwork for a return to democratic rule, yet it also seems loath to relinquish its hold on power. Nevertheless, for now the country has much to gain from stable government and the leadership has, at least, made some headway in tackling economic deficiencies.

Thailand may be down, but it is far from out. At the corporate level, there are plenty of fundamentally-sound, well-managed and resilient businesses.

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Emerging Markets

(compare Global Emerging Market funds **here**)

Andrew Hutton (Chairman of JPMorgan Global Emerging Markets Income). Investors will be concerned by the continuing stream of bad news associated with the emerging markets. The hazards are real and not to be underestimated or downplayed. Low growth in China, abrupt currency adjustments, political tensions, weak commodity prices, capital outflows and the risks of policy error - all these are current and they are ugly. The spectres of weak growth and deflation are especially worrisome. An extended period of low growth - or no growth - in these economies would weigh heavily, but not just on developing markets: developed markets would also suffer.

In the Board's view, however, the prospects are actually improving. If we look through the negative narrative we see a number of positive factors:-

- We have been here before. No two cycles are quite the same but in emerging markets they tend to follow patterns. These markets are volatile - never for the faint-hearted - and have proven time and time again that they can recover after a beating.
- Weaker currencies improve economic competitiveness in the medium term and are of real benefit to certain exporting businesses.
- These markets now look undervalued. On the basis of the ratio of price to book value, the valuation of these markets is now in the cheapest decile of its historical range. History also suggests that from these levels, subsequent returns have been strongly positive. This is not to say these markets cannot get cheaper. They can. But it does suggest that the upside is interesting.
- This is becoming a "target-rich" environment. The Managers are now seeing plenty of stocks that trade at attractive valuations with healthy balance sheets and reasonable long term growth prospects.

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Richard Titherington and Omar Negyal (Managers of JPMorgan Emerging Markets Income). Emerging markets may finally be approaching valuation levels that compel long-term investors to reallocate to the asset class. On several measures, emerging market equities appear to be pricing in a much more negative outlook for growth and corporate profits than is perhaps justified. Although emerging markets are slowing, these economies overall are still growing, while today's much more flexible exchange rate regimes should provide greater support.

Nevertheless, the outlook for emerging market profits has become cloudier, and this continues to provide a challenging backdrop for income-seeking investors. In particular, the recent declines in currencies across emerging markets are putting near-term pressure on profit and dividend streams from emerging market companies, from a sterling viewpoint. Even in this environment, we are still finding many opportunities in stocks with attractive dividend yields.

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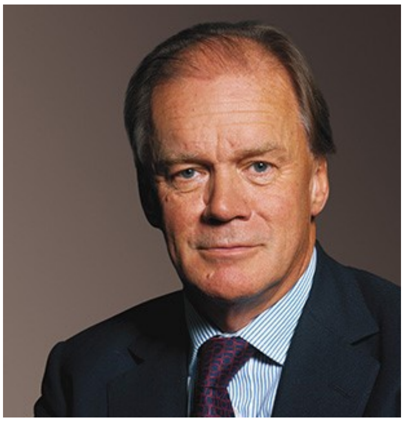
Private Equity

(compare Private Equity funds **here**)



Tom Bartlam

Tom Bartlam (Chairman of Pantheon International Participations). While stock markets have reached levels that may make them more vulnerable to the unexpected, we expect that M&A activity will continue apace as both corporate and financial buyers are holding such high levels of financial resources. The credit markets have eased even further and this factor is also helpful in keeping M&A markets active. The IPO markets, while still a less common route for portfolio company exits, have provided further useful liquidity opportunities in our portfolio. Equity prices are high relative to historic norms and this creates an added hurdle to achieving good investment performance when making new investments. With the advantages of a longer time frame, private equity investors are well positioned to weather cycles and to use the benign credit markets to reduce the cost of capital within portfolio companies. Consequently we have seen the pace of refinancing within the private equity market increase as managers take full advantage of these conditions. This is also supportive of the many managers within our portfolio who create efficiencies and bring down the effective pricing of investments through add-on acquisitions using cost effective financing.

While some of our energy assets experienced valuation pressure associated with the oil price decline, we view this downturn in the oil related energy markets as an opportunity to invest further in the sector and we intend to maintain our current weighting within our special situations portfolio at up to approximately 10% of the portfolio.

Assets in the year have been more fully priced on the secondary market, reflecting an increase in the supply of capital targeted at secondaries particularly within the large 2006-2008 vintage pool as those funds become more mature and cash generative. We expect that the vintage 2006 - 2008 vintage pool will continue to represent the largest opportunity for us in the secondary market.

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Pantheon Ventures (UK) LLP (Manager of Pantheon International Participations). During and after the financial year, stock markets around the world have registered uneven progress as they have responded to the factors affecting global liquidity including the Eurozone's attempt to resolve the latest Greek solvency crisis, the effects of quantitative easing in Japan and Europe and the dramatic falls in the oil price and more recently, the Chinese public equity markets. The fall in commodity prices and continued competitive devaluation amongst a number of the world's major currency blocs have added further to investors' difficulties.

However, economic growth around the world has been steadier. Amongst the developed markets, the US and UK have continued to demonstrate growth albeit after a dip in the US in Q1 caused by the unusually cold weather. While economic growth has strengthened in these markets, it has not been without setbacks and with asset valuations that look increasingly stretched there remains a question mark over the vulnerability of asset prices to the likely rises in interest rates in the US and beyond. Greece notwithstanding, recovery in the Eurozone has been unsurprisingly slow and economic indicators are not much brighter for the foreseeable future. Asian economies still lead world GDP growth but at lower levels and as seen most acutely in China, these economies remain vulnerable to policy missteps and wider liquidity flows that almost guarantee a bumpy ride in public share markets.

US

The US appears to be escaping lower global growth and recession. US GDP grew 2.4% in 2014, the best full year growth since 2010 and is forecasted to grow 2.3% and 2.8%, respectively, in 2015 and 2016 (Capital Economics, Global Economic Outlook Q3 2014). Public markets are generally at all-time highs, while bond yields are at some of their lowest levels, notwithstanding an expected interest rate increase in 2H 2015. The US continues to benefit from cheaper energy and rising labour costs in China, both of which provide support for consumer spending and US-based manufacturing. However the increase in the value of the US dollar has pressured exports for many businesses, mitigating these tailwinds to some extent.

Elevated valuations in public and private markets over the past year and stiff competition from corporate acquirers have combined to subdue the pace of private equity capital deployment. Private equity firms invested $215.9bn of capital during the first half of 2015, a 22% decrease over the first half of 2014 and on pace to be the slowest year since early 2013 (Preqin). Furthermore, GPs have increasingly pursued buy-and-build strategies, favouring smaller platforms that can be built up through add-on acquisitions to help mitigate higher initial entry multiples. Unlike the 2007-2008 market peak where deals over $1bn comprised a large portion of new deal activity, since the recovery, deals under $1bn have accounted for the vast majority (over 75%) of capital deployed in 2014 and 1H 2015. Add-on investments have increased significantly during this time period as well, accounting for over 60% of the deals completed in the last year (Prequin).

Exit activity remained on a steady upward trajectory, with exit proceeds reaching record levels in 2014 and surpassing the elevated levels observed in 2012 when tax rates were set to change. While elevated levels of exit activity are necessarily correlated with the spike in investment activity during the 2006-2008 period, robust capital markets are facilitating the volume and magnitude of favourable outcomes. During the first half of 2015, private equity investors exited 478 companies valued at $185bn, a 39% capital increase year-over-year (Prequin). Secondary buyouts and strategic sales to corporations have been the most popular exit routes. Sales to corporate buyers have totalled $160bn in the first half of 2015 alone (Prequin), nearly the full-year amount of 2014, as companies look to M&A to find new segments and synergies that support their core businesses. However, one area that in the first half of 2015 lost momentum was IPOs with only 17 completed private equity-backed IPOs, a 56% year-over-year decline (Prequin). This could be explained partly by the fall-off in energy-related IPOs that were prominent in early 2014 as well as the trend for VC-backed companies to stay private with large private financings.

Driven by large rounds for later stage companies, capital invested in VC-backed companies reached $59bn in 2014, and $37bn through 1H 2015, the highest levels since the dot-com era (2015 Annual US Venture Industry Report). This elevated level of investment activity reflects the convergence of two related trends; many VC-backed companies opting to delay IPOs in favour of large private rounds as well as an increase in participation by non-traditional investors, including corporate VC arms, hedge funds, mutual funds, and some private equity firms. The big story has been the prevalence of large financing rounds, with over 40 financings exceeding $100m in 2014 (2015 Annual US Venture Industry Report). Uber's two $1bn+ rounds and Airbnb's $475m round are notable not only for their scale but also for the extent to which these tech companies are disrupting traditional industries. Exits for venture capital in 2014 was the highest in the past decade, with 845 VC-backed exits totalling $78.4bn (2015 Annual US Venture Industry Report). Notably 6 out of the 12 consumer tech M&A deals over $1bn were completed in 2014, including WhatsApp, Nest Labs, and Oculus VR. Strategic acquirers were the dominant source of liquidity for VC-backed companies, although IPO markets remained strong throughout 2014 and were a popular exit route for biotech companies in particular. In the first half of 2015, exit activity has slowed somewhat, although this is in part due to companies opting to delay IPOs in favour of private rounds.

2014 and 2015 have been strong years for fundraising, characterised by a robust fundraising environment for established GPs and an increased volume of first-time fundraisings. The past few years are typified by the growing prevalence of access-constrained top-performing funds reaching their caps swiftly, with managers turning away many interested investors. In 2015, private equity fundraising has been slightly off-pace from that of 2013 and 2014. 2013 and 2014 each recorded at least $200bn of capital raised, while the first half of 2015 has raised $75.6 bn (Prequin). The largest funds of over $5bn have accounted for only 22% of total capital raised, compared to 45% and 29% in 2013 and 2014, respectively (Prequin). The majority of capital raised in the first half of 2015, or 53%, went to funds in the $1bn to $5bn range, reflective of the post-recession preference for middle market funds (Prequin).

Value creation has benefited over the past year from the robust exit environment and continued relative strength of the US economy. Across most sectors, strategic buyers have been increasingly willing to pay full prices for maturing portfolio companies in order to achieve their growth and diversification goals. The healthy IPO and credit markets have provided valuation support and optionality for exiting companies, further lifting valuations. Technology companies in particular have enjoyed a vibrant market for valuation increases as new technologies have created high growth opportunities across the US economy, notably in healthcare and manufacturing. Biotech has been another area of strength, with new therapeutics and other healthcare advancements receiving interest from both strategic and public markets. The energy sector has been a notable area of concern, as 2014 saw extensive falls in oil prices that continue to reshape the industry. To this point, capital markets have provided financial support and we have not seen many situations of distress.

Looking forward, we believe the US private equity market is well positioned to navigate the current market, characterised by high valuations and resulting low real interest rates. We expect that top quartile managers will continue to take advantage of strong exit markets to return capital to investors and to engage with portfolio companies to achieve higher than market rates of return.

Europe

Economic growth in Europe has remained sluggish with the EU-28 recording GDP growth of 1.6% in the 12 months to June 2015 (Prequin). Consumer confidence has at various times shown an improvement but remains vulnerable. Industrial production is benefiting from a tailwind from the depreciation of the Euro which has fallen by 18% against the dollar in the 18 months to June 2015 (and 14% against sterling in the same period). Nevertheless, demand remains subdued and the region remains vulnerable to economic shocks. There remains a continued question mark over Greece's longer-term membership of the EU which has cast a cloud over markets with uncertainty affecting the Euro and public markets (the MSCI Europe returning -7.2% in the year to June 2015).

Quantitative easing (more recently from the ECB) as a policy response to sluggish demand and deflationary pressures has impacted European private equity as it has all other asset classes. Liquid markets have ensured that competition for new deals remains strong and entry pricing remains high, most marked in sectors such as healthcare and technology where long-term secular trends provide an attractive backdrop for investment. Private equity firms have responded to high pricing with caution and the deployment pace for active funds remains subdued, €90bn (Prequin) was deployed in completed deals in the year to 30th June 2015. The flip side is that exit markets have remained buoyant with private equity firms able to see exits from all main routes, trade sale, secondary buyouts and IPOs being viable options. In many cases the competitive tension between trade, private equity and the listed markets has facilitated rapid exit processes and higher exit prices. Overall, the response of the European private equity industry has been to recognise the advantages of the current environment as a time to sell rather than to buy, a marked difference to the last time that market prices peaked in 2007. Underlying value increases in private equity portfolios have continued to be strong with double digit valuation increases being typical in the last 12 months.

Investor appetite for European-focused private equity funds has remained steady. There continues to be strong demand for mid-market buyout funds but interest in large buyout funds has remained healthy as global capital seeks exposure to Europe.

The outlook for investors is largely dependent on wider macroeconomic concerns. Specifically the depreciation of the Euro in the last 12-18 months has wiped out most if not all of the gains made by dollar and sterling investors in the period. Resolution of the Greek crisis (if only temporarily) and improved prospects for European growth would be supportive of a stronger Euro and recovery of value for investors. Within this context, our portfolio emphasises companies in the mid-market, operating at a scale that makes them less constrained by anaemic rates of overall GDP growth which meant that, prior to any foreign exchange effects, our overall level of investment returns in Europe during the year have been consistent with what we have experienced in other regions.

Asia

Since June, attention in the Asian region has been focused on dramatic falls in the Chinese public equity markets, the successive devaluations of the renminbi and the implications of these factors for the Chinese economy. However, the relationship between China's public equity market and the real economy is at least as symbolic as it is real because it represents only a very small part of the capital raised by Chinese corporations. Although growth has slowed, with China's 2015 GDP forecast to be 7.0%, falling to 6.5% in 2016 and 2017 (Weathering the Storms Q3 2015, Capital Economics), it is expected China will continue to lead world growth. Chinese authorities have been mindful of the need to remain broadly focused on measures to support growth through structural and fiscal reforms.

The positive political mood in India anticipated signs of recovery in the economy but it is too early to say whether the Modi-led government will tackle as successfully as anticipated the economic reforms required for accelerated economic growth.

Consistent with the experience elsewhere in the world, private equity investment activity in Asia decreased over the 12 months ended 30th June 2015 compared to the prior period both by number of deals and by capital deployed (Prequin). Capital deployed in select markets like India, however, has actually picked up, in part due to a handful of larger deals but also reflecting a general trend of increasing investment activity in these markets.

As in the more developed markets, high levels of exits were also seen in Asia. Private equity exit activity overall in Asia increased by value to 30th June 2015 compared to the previous period. This increase was particularly strong in China and India, followed by Japan. In the first half of 2015, it was driven by several large transactions completed by trade and other private equity buyers. Examples include the sale of listed shares in Shriram City Union by TPG Asia to Apax Partners of the sale of listed shares in Energy Developments by Pacific Equity Partners to DUET Group, whereas exits from smaller investors were less prevalent.

The market generally has witnessed upward pricing pressure. Valuations on a mark-to-market basis remained high in 2014, buoyed by public markets, but have since softened as markets were affected by volatility in the Chinese domestic market. Private equity managers are selected by Pantheon in part for their ability to exercise pricing discipline so as to take advantage of softer market conditions when they arise.

Co-investment

Co-investment deal flow continues apace due to an active buyout market and a continued recognition on the part of private equity managers of the importance of offering co-investment opportunities to further cement their relationships with their investors. Sourcing and securing allocations to co-investments, however, continues to be very competitive as an increasing number of investors are trying to access these opportunities given that co-investments typically have no or low fees or carried interest associated with them. Therefore, investors must differentiate themselves on their ability to efficiently execute co-investment opportunities and pro-actively originate such opportunities from their base of manager relationships.

Secondary Market

Secondary transaction volume for the first half of 2015 reached $12bn (excluding real estate transactions) (Greenhill Cogent Secondary Market Trends & Outlook, July 2015). Public pension plans, particularly in North America, have built very large, often unwieldy portfolios, and have taken advantage of these conditions to trim their positions. Pension funds were active sellers in the period comprising 35% (Greenhill Cogent Secondary Market Trends & Outlook, July 2015) of overall deal flow within the market. The reduction in selling activity by financial institutions such as banks was almost fully offset by a combination of higher selling activity by public pension plans, and a greater diversity of seller types.

Pricing in the market remained strong, with an average high bid of 92% of NAV for transactions in the first half of the year, versus 91% of NAV for transactions in the first half of 2014 (Greenhill Cogent Secondary Market Trends & Outlook, July 2015). Moreover, as in 2014, large deals have continued to be an important feature of the market in 2015, with six secondary transactions of more than $1bn.

Despite delays in the Volcker Rule potentially deferring banks' sale decisions, the greater diversity of seller types and increasing use of the secondary market for portfolio management purposes are expected to help sustain secondary market deal volume at around current levels. In addition, activity is expected to be weighted towards the second half of the year, with intermediaries projecting this year's deal flow to be only slightly behind last year's record $38bn in secondary deal flow (Greenhill Cogent Secondary Market Trends & Outlook, September 2015).

Roger Yates (Chairman of Electra Private Equity). Competition for and pricing of private equity investments are at historically high levels. Against this backdrop, Electra Partners has been active in realising value from some of the more mature assets in the portfolio. Realisations during the year were at a high level.

Electra Partners (Manager of Electra Private Equity). New investment has been slower this year. Our customary discipline has led us to focus on the relative value offered by portfolio company add-ons compared to new standalone investments this year. The former often take just as much time to complete as the latter. Nonetheless we continue to see opportunities to deploy capital.

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Debt

(compare Debt funds **here**)

James G West (Chairman of CQS New City High Yield Fund). Our portfolio manager continues to find value in the bond markets and is placing a particular emphasis on providing additional protection by increasing diversity. The recent rout in Chinese equity markets has made stock markets everywhere jittery, and provided the latest exercise to delay tightening global monetary policy.

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Ian Francis

Ian Francis (Manager of CQS New City High Yield). The year ahead holds a new phase for markets as we enter into rate rises in the US and UK with continued QE in Europe, with China and the Far East trying to rekindle their growth. This undoubtedly will add volatility to the market and we believe will provide opportunities in the forthcoming year.

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Antony Vallee, Natalia Bucci and Robin Dunmall, (Managers of JPMorgan Global Convertibles Income). We believe the asset class has the potential to perform well relative to traditional fixed income markets in an environment in which supportive central bank policies are slowly withdrawn. A structurally low average maturity for convertibles helps to limit the natural sensitivity to interest rates, while the embedded equity sensitivity can support returns if the equity backdrop remains supportive, as in the Taper Tantrum of 2013.

An increase in interest rates could stimulate convertible issuance by improving the relative attractiveness of convertibles for issuers relative to non-convertible debt. This would increase our opportunity set and provide investment opportunities with incrementally more attractive coupons. We also see the potential for some sector rotation as more opportunities present themselves in sectors disproportionately exposed to changes in interest rates, such as utilities and other non-cyclical industries.

While any policy mistake from central banks could lead to negative equity performance and mark-to-market risks for the portfolio, our analysis suggests that equity markets have tended to perform positively in periods in which interest rates rise from low levels. If interest rates rise for benign reasons, such as continued economic growth, this could indicate a conducive environment for credit spread tightening - although the fact that spreads are currently tight relative to recent history makes this far from assured.

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James Gilligan (Chairman of Volta Finance). Recent weakness exhibited by the Chinese economy, the significant decline in the prices of most of the major commodities and volatility in global equity and currency markets show that global investors are increasingly alert to the risks to economies and markets. That said, our Investment Manager does not believe that these worries present a material threat. Indeed, the manager believes that periods of volatility such as those observed in September 2014 or August 2015 are likely to recur in coming years and represent an opportunity, given the generally benign environment in the US and the improving picture in Europe. One outcome from these periods of volatility has been to curb the tightening of credit spreads that has been seen for years in most structured finance markets. In the medium to long term, this will be positive for returns. For the current financial year our investment manager remains confident of being able to source assets in the 8% to 11% projected IRR range, in line with recent acquisitions. This target range is a few percent below what could be reasonably expected on a long-term basis. This is a direct consequence of a prolonged low interest rate environment but equally remains a highly attractive total return when weighed against the embedded risk profile of the portfolio.

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AXA Investment Managers Paris (Manager of Volta Finance). Our view is that we will continue for some time to live under a period of moderate economic growth, but with significant involvement and control from governments and central banks in order to limit economic and financial volatility (commonly referred to as the "new normal" regime) due to the significant amount of debt that had been accumulated during the previous decade. The QE from the ECB and the termination of QE from the US Federal Reserve mean that Europe is now more active in this "new normal" regime than the US.

Economic agents that accumulated significant amounts of debt are typically households, governments and local state entities. Corporate entities in the US and in Europe, despite a recent and modest increase, still have amounts of debt in line with or below the last ten to 20 years' most common measures (relative to EBITDA or enterprise value).

In our opinion, the significant appreciation of the US dollar and the significant decline in oil prices and other commodity prices are likely to bring some uncertainties to overall economic activity. We do recognise that the decline in prices of commodities is positive for US and European consumers, but it may imply some significant rebalancing in the relative situation of some economic sectors and raise some concerns on commodity producing countries. Our view is that such a situation should not significantly damage the economic pattern for US and European economies, but that it opens the door for slightly more frequent occurrences of sudden volatility. Regarding corporate credit, it is reasonable to expect an increase in the number of defaults, especially in the US, from a below historical average pace. Taking this into account, together with the support provided by the ECB QE programme and the relative weakness of the euro, we believe that some rebalancing in favour of Europe should continue to be considered.

We recognise a number of existing known risk factors, including excessive bank balance sheets in China, geopolitical issues in the Middle East and Eastern Europe as well as the Greek situation, but we do not expect these uncertainties to impact the way developed economies are managed under the present regime.

Regarding structured finance markets it is our view, for the coming year, that:

- The CLO market, in the US and in Europe, will continue to be very active, both in terms of new issuances and in terms of secondary trading. Thanks to various regulations, CLO Debt yields are still at attractive levels relative to historical levels and fundamental risks. This makes CLO 2.0 Equity tranches less attractive than the CLO 1.0 Equity tranches from the 2006/2007 vintages; however, we think that selecting the appropriate CLO manager and the appropriate structure can permit achieving returns in the 9% to 12% range for some new CLO Equity tranches;

- When considering current housing prices and mortgage standards in the US, it seems to us that US mortgages constitute a compelling asset for securitisation, yet there are few issuances in this area that permit a direct investment for Volta. This view materialised through the investment in a fund that we co-manage with Ellington in the US (St Bernard Opportunity Fund). We hope to see at some point a resumption of opportunities (in the primary market) in this area; and
- Bank Balance Sheet transactions will continue to be a sizeable and interesting market, especially in Europe, for investors looking for returns in the area of 10%.

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Property

(compare UK Property funds **here**)

Malcolm Naish (Chairman of Target Healthcare REIT). Economic uncertainty over interest rates and Chinese growth will continue to impact sentiment and pricing in the investment market. Additionally, the care sector in the UK is facing headwinds from: introduction of the living wage, which will increase the cost of providing care; uncertainty over government funding of care, and; a stronger regulatory regime. That said, the underlying fundamentals of population demographics and supply/demand imbalance of quality UK care home stock are compelling. Our primary challenge is in responding to the competitive acquisition landscape this has created to continue to acquire attractive assets into a portfolio balanced by region, operator and size

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Target Advisers LLP (Manager of Target Healthcare REIT). The combination of an ageing population and paucity of quality care home stock continues to present a compelling investment opportunity. Strong levels of investment activity across the UK's elderly care sector have continued during the year, resulting in some investment yield compression and providing a competitive landscape which remains particularly congested for transactions offering scale and /or access to specific geographic locations such as the South East of England. A wide range of participants remain in the market, including generalist commercial property investors, continuing the trend noted in the prior year, though we may currently be witness to a collective "pause for breath" as a reaction to the sector-specific headwinds (mentioned by the Chairman – see above).

Whilst yields for the most hotly-contested assets reflect the desirability of these assets, with some very keen yields having been paid for the perceived strongest quality covenants, we continue to believe the best value can be found within regional mid-market: single asset and smaller portfolios of homes; likely involving regional operators; who deliver robust trading performance often as a result of a strong care culture.

In his Summer Budget on 8 July 2015, the Chancellor announced a new living wage which will commence in April 2016 and by 2020 will reach 60 per cent of UK median earnings.

Typically, 50-60 per cent of the costs of a care home are staff costs and approximately two thirds of these staff costs are paid at minimum wage levels. We welcome the announcement that care workers, who undertake what is a critical and often demanding role, will receive fair remuneration for their efforts.

That said, the government needs to ensure this is properly and adequately funded. In recent years, the fees local authorities have paid care providers have risen below cost inflation. If this trend continues, care home operators face the combined effect of wage cost inflation and Local Authority austerity.

Due to this, as in previous years, the cost of care homes will almost certainly increase disproportionately for self-funded residents. It was announced on 17 July 2015 in a written ministerial statement that the £72,000 lifetime cap on care costs will be delayed until 2020, rather than starting in April 2016 as previously expected. The official line from the government is that it remains firmly committed to the cap – and it was included as a manifesto promise at the recent general election – but notwithstanding this there are those who predict the cap will not now be introduced. For operators themselves, the care cap was something of a mixed blessing and many will be relieved that at least another tier of bureaucracy has been deferred.

Feedback from our tenants, and from operators generally, would appear to indicate that the English regulator is applying a particularly zealous approach to home inspections at present. Required responses to an adverse inspection will likely be increased costs and potentially a restriction on the ability to house new residents, which may even be the case for apparently good homes in such an environment. Time will tell if this is a temporary change in approach or the new normal, but it will impact performance of many homes within the sector.

We believe maintaining a diversified investment portfolio which draws on income from both local authority and self-funded residents provides a good investment strategy as tenants face these uncertain times.

Additionally, modern homes [should benefit defensively] as the pressure from these headwinds hastens the retiral from the market of the many aged and inadequate homes.

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Robert Peto

Robert Peto (Chairman of GCP Student Living). The student accommodation sector has seen unprecedented transaction volumes, with c.£4.6 billion of assets traded in the first six months of 2015. The expectation is for a similar trend to persist throughout 2015/16 as prime yields continue to tighten across the market, fuelled by a combination of historically low interest rates and an increasing number and range of investors seeking exposure to the sector.

With student numbers at an all–time high, the ongoing supply and demand imbalance for purpose–built, modern student residential accommodation in and around London is expected to continue for the 2015/16 academic year and future years. The removal of the student cap for 2015/16 on the number of places that can be offered to UK students has led to a record number of acceptances, a 3% rise on the prior academic year.

On the supply side, the Directors (as advised by the Investment Manager) do not expect to see substantial volumes of new accommodation arising in the Company's core markets in the near term, as planning reforms and inflated land values make it ever more difficult to bring on stream new developments and limit the entry of new operators into the market.

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Gravis Capital Partners LLP (Manager of GCP Student Living). It is expected that the long-term impact of higher domestic tuition fees will increase the competitiveness of the best HEIs in the country, particularly the Russell Group, as domestic students become more selective over where they will study as they take on higher levels of debt. London has five of the 24 Russell Group Universities in the UK and two of the top ten universities in the world for the 2015/16 academic year. .

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European Property

(compare European Property funds **here**)

Charles Hunter (Chairman of AXA Property Trust). Conditions in the European property markets have been improving but the wider economic and markets background continues to be uncertain.

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AXA Real Estate Investment Managers UK Limited (Manager of AXA Property Trust). With regards to German Retail, the performance of monthly retail sales support the view that consumption remains a strong pillar of the German economy as they continued to increase in May 2015 by 0.5%. One of the main reasons behind the recent rise in retail sales had been the positive effect of falling oil prices, leading to enhanced spending on other items. As oil prices are likely to firm over the coming months, this effect could weaken.

In the first half of 2015, investments in German retail soared up to €9.8bn. Volumes have more than doubled in comparison to H1 2014. Portfolio sales contributed strongly to the overall investment volume and were responsible for 65% of all sales. Also regional centres and second-tier cities have gained in popularity which reflects the higher risk affinity of investors. High street investment volumes were boosted by the takeover of 43 Galeria Kaufhof department stores by Canada based Hudson's Bay Company.

Prime yields have remained flat in all markets with the exception of Munich and Hamburg, where yields fell by 10bps and 9bps respectively. Yields in all German markets are at their lowest level on record. Prime rents have been flat over the last quarter in all markets.

For Italian Industrial, the take-up of industrial spaces in Italy in Q2 2015 reached 204,650 sq m, an increase of almost 250% on the previous quarter and a 1% decrease on same period of 2014. Quarterly take-up involved existing buildings and no pre-let transactions have been recorded. With 27% of quarterly take-up, 3PL operators were once again the most active occupiers, followed by retailers which are increasingly gaining influence as a driver of demand. Milan and its clusters continued to be the regions with the strongest letting activity. Overall, prime rents increased in the first quarter to €50/sq m/year in Milan, up from €48/sq m/year of the previous quarter, according to CBRE. In the second quarter of 2015, no significant investment transactions have been recorded in the Logistics sector. Half-yearly volume remained slightly below € 90m.

In terms of Netherlands Logistics, the industrial market is continuing to benefit most from the country's economic recovery, due to its central location along the European logistics corridor. The Central and East Brabant and Limburg regions, which are focused on European distribution and high-tech sectors, continue to benefit from cheaper rents and good accessibility to the rest of Europe. Occupiers are actively looking to relocate to more modern facilities with good accessibility but overall demand growth looks set to remain weak over the next few quarters, given the current uncertainty in the Eurozone. Following strong growth along the European corridor (up 4.2% in Rotterdam) in the first quarter, prime rents have remained stable in the second quarter of 2015 at €75/sq m/year. The investment market has, however, been revived in the second quarter, with €408m invested into industrial property, which represents a 8% year-on-year increase. While anticipated improvement in demand had pushed prime yields down in Q1 2015, prime yields remained stable in Q2 2015. In Amsterdam and Rotterdam, they now stand at 6%.

Renewable Energy

(compare Renewable Infrastructure funds **here**)

John Rennocks

John Rennocks (Chairman of Bluefield Solar Income). There are challenges ahead in 2016 when the shape of future pipelines is uncertain and the levels of support for new installations remains unclear. Despite the market facing considerable headwinds in the form of lower power prices and regulatory uncertainty, the company has delivered a strong set of returns.

Further to this, there remains an immediate and compelling opportunity to invest into a competitively priced energy market achieving attractive infrastructure level returns with low levels of leverage, and contracted into long dated, largely regulated and indexed revenues. We strongly believe that the UK remains an attractive place for infrastructure investors and that the market continues to offer appealing risk adjusted returns.

Resources

(compare Commodity & Natural Resources funds **here**)

David Hutchins and Kjeld Thygesen (Managers of Global Resources). While some stability has returned to the mining market, the economic outlook remains clouded. The Fed guessing game on US interest rates continues, and the much anticipated increase will be determined by a combination of US and Chinese economic data in the coming months, with any increase being construed as positive.

QuotedData

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