Investment Solutions

Monthly Market Commentary

July 2011

Review

The Bank of England's Monetary Policy Committee maintained an interest rate of 0.5% in July and made no adjustments to quantitative easing measures. The FTSE All Share Index fell over the month as European debt concerns played on the minds of investors.

	Index Level 31 July 11	% Change July	YtD	1 Year
FTSE All Share £	3026	-2.2%	0.7%	14.9%
FTSE 100 £	5815	-2.1%	0.5%	14.2%
MSCI World $	1306	-1.8%	3.7%	19.2%
S&P 500 $	1292	-2.0%	3.9%	19.7%
	Index Level 31 July 11	Index Level 30 June 11	Index Level 31 Dec 10	Index Level 31 July 10
UK 10 Year Gilt Yield %	2.86	3.38	3.40	3.33
GBP USD	1.64	1.61	1.56	1.57
GBP EURO	1.14	1.11	1.17	1.20
OIL - WTI $	95.7	95.4	91.4	79.0
Gold $	1628	1500	1421	1181
Wheat $	673	585	794	662

BP's chief executive, Bob Dudley, reassured shareholders that the energy company was getting back on track after last year's oil spill in the Gulf of Mexico. BP made a headline profit of $5.3 billion in the second quarter, compared with a $17 billion loss in the same period a year ago.

The euro zone interest rate was raised to 1.5%, by the European Central Bank (ECB). The sovereign debt of Greece was downgraded by Standard & Poor's, to the lowest rated country in the world during the month, suggesting that S&P expect Greece to default on its debt imminently. European leaders agreed to give Greece a second bail-out. The country will receive another €109 billion in loans from the euro zone and the IMF.

The space shuttle, Atlantis, returned safely from its final mission on July 21st, bringing an end to 30 years of NASA's space-shuttle voyages, and thus to American manned flights in space. For the moment, NASA is hoping that the private sector will pick up the slack.

Outlook

The global economy is hanging on to its recovery at the moment but there are obvious areas of volatility and key areas of concern. Our expectations for market volatility in 2011 have been amplified and we expect this to continue into the second half of 2011. Inflation remains of particular concern to us and many central bankers, as the cost of consumer staples, such as food, continues to rise. Central banks have indicated that they expect to remain with the current loose monetary policy for some time to come; this carries the risk of a policy error with inflation exceeding targets for a prolonged period of time and puts the credibility of some central banks at risk. We are also watching the unravelling of the sovereign debt situation in Europe, particularly Greece, with increasing alarm, especially as the US administration appears to place a higher priority on political point scoring rather than pulling together a coherent plan for their debt issues. The possibility of global economic recovery being derailed is still present, especially if the emerging economies revise down their expected rate of growth.

We have had a hiatus in the progress of global growth recently, with disappointing global macro news-flow, not least low GDP growth. However, we remain cautiously optimistic on the outlook for global investment markets for in the second half of 2011. In the short-term we believe the periodic setbacks and occasional weaker patches will continue as market sentiment fluctuates.

Investment Solutions Limited
Ground Floor, Abacus House, 33 Gutter Lane, London EC2V 8AS
t: 020 3465 4990 f: 020 3465 4999
enquiries@isltd.co.uk
www.isltd.co.uk

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Asset Allocation

View	Positive Points	Negative Points
UK Equity Neutral/Positive	• UK macro environment looks reasonably stable. • Earnings numbers continue to show improvement. However, the rate of increase is slowing. • Companies have strong balance sheets and reduced cost base.	• Concerns remain on the extent of government and consumer debt as well as the impact of strike action over austerity measures as we appear to be in an economic soft patch. • Global sovereign debt issues weigh on markets. • Stability of the coalition. • Inflation.
Global Equity Neutral	• The Global recovery looks stable, with reasonably strong corporate earnings figures. • Current climate benefits well capitalised businesses with more stable earnings.	• Concerns remain on the extent of Global government and consumer debt. • Optimistic earnings over the next few years may already be priced in. • Inflation - particularly from agriculture.
Emerging Market Equity Neutral	• Emerging Markets have been somewhat insulated from debt issues as governments have less debt and private savings ratios are far higher than developed economies. • Emerging Markets have experienced recent outflows of investment.	• Inflation concerns as the base effect works itself out. • EM equity is slightly expensive relative to history but more attractive than developed market equity. • Government policy responses to international capital flows are a concern e.g. Brazil. • Volatility in the short-term.
UK Fixed Interest Gilts Negative	• Defensive characteristics remain partially intact. • Government continues to demonstrate fiscal discipline. • Continues to be the safe haven investment of choice.	• Inflation continues to be above government targets and QE remains in place. • Yields are low relative to history. • Global sovereign debt issues will heighten volatility.
UK Index Linked Gilts Neutral/Negative	• Inflation continues to remain above target. • Limited supply from the DMO although demand remains strong at both the short and long ends.	• Real yields remain unattractive. • Issuance is expected to increase through 2011.
UK Corporate Bonds Neutral/Positive	• Reasonable risk return characteristics compared to cash and gilts, for Investment Grade Bonds. • Prefer industrial to financial credits due to uncertainty over effect of sovereign debt issues on banks.	• Interest rate risk remains the main concern.
UK Property Neutral	• Reasonable yields, improving rates and increased activity following large flows into the sector make this an attractive asset class only if investing in Prime Property. • There is a degree of inflation protection.	• Non-prime Commercial Property markets are likely to continue to lag as demand in this area is weak. • Government spending cuts are likely to exacerbate the perceived problem in secondary and tertiary property. • London office space is likely to go through a soft patch in rents as banks reduce costs.
UK Cash Negative	• Short-term safe haven.	• The investment value of this asset class is being eroded by current interest rates being below inflation.
Absolute Return Positive	• Following the strong run in equity and bond markets over the last year, a more defensive and diversified approach may be prudent. • Expect volatility to be elevated.	• Non trending markets can cause problems for directional strategies thus resulting in short term underperformance.

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