Investment Solutions

Monthly Market Commentary

November 2011

Review

The Bank of England's Monetary Policy Committee maintained the Base Rate at 0.5% in November and increased quantitative easing measures to £275billion.

The FTSE All Share Index fell marginally after a volatile month as global sovereign debt concerns continued in spite of all the efforts of European leaders to produce a credible solution. The FTSE All Stocks Gilt Index had another good month, from a performance perspective, as investors continued to seek safe haven assets.

Global Markets ended flat over the month while uncertainty surrounding global sovereign debt continues to hit investor confidence, triggered by the continuing political wrangling around debt reduction and the debt ceiling.

	Index Level 30 Nov 11	% Change Nov	YtD	1 Year
FTSE All Share £	2836	-0.4%	-4.3%	2.6%
FTSE 100 £	5505	-0.2%	-3.4%	3.2%
MSCI World $	1185	-2.4%	-5.0%	2.0%
S&P 500 $	1247	-0.2%	1.1%	7.8%
	Index Level 30 Nov 11	**Index Level 31 Oct 11**	**Index Level 31 Dec 10**	**Index Level 30 Nov 10**
UK 10 Year Gilt Yield %	2.31	2.44	3.40	3.23
GBP USD	1.57	1.61	1.56	1.56
GBP EURO	1.17	1.16	1.17	1.20
OIL - WTI $	100.4	93.2	91.4	84.1
Gold $	1746	1715	1421	1386
Wheat $	596	628	794	650

The European Central Bank (ECB) appointed a new governor, Mario Draghi, from 1st November and he cut the interest rate for the euro zone to 1.25% on 3rd November. The significant sovereign debt of many member states particularly Italy was a huge concern for markets and contributed significantly to the market sentiment. European leaders Merkel and Sarkosy held a series of meeting throughout the month and agreed several measures to try to put a floor into markets. As ever, politics seemed to interfere with the plan.

The Emerging Markets were not immune from market volatility, although performance was in line with developed markets. China cut the capital adequacy requirements for banks on the last day of the month as concerns began to shift from fighting inflation to ensuring growth.

Outlook

The global economy is experiencing a particularly weak patch in economic growth at the moment with elevated volatility and key areas of concern such as inflation and global sovereign debt. Our expectations for market volatility in 2011 have exceeded our hypothesis and we believe this will continue whilst markets remain uncertain. 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. However, central bankers see the risk of a slowdown as being greater than high inflation.

We are watching the unravelling of the sovereign debt situation in Europe, particularly Greece, Portugal and Italy with increasing alarm. The possibility of the global economic recovery being derailed is a realistic threat with the current uncertainty, especially with several of the larger emerging economies revising down their expected rates of growth. We are also concerned about the US debt management plans.

We have had a general lull in the advancement of global growth recently with disappointing global macro news-flow, not least poor employment growth. In the short-term we believe the periodic setbacks and occasional weaker patches will continue as market sentiment fluctuates and policy makers struggle to innovate solutions. In the long-term, it is our view that markets and the global economy will move forward and grow, albeit below trend.

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Asset Allocation

View	Positive Points	Negative Points
UK Equity Neutral	• Companies have strong balance sheets and reduced cost base. • Corporate earnings and margins are proving resilient.	• Concerns remain on the extent of government and consumer debt as well as the impact of remedial measures as we appear to be in an economic soft patch. • Global sovereign debt issues weigh on markets. • Stability of the coalition and the global political environment. • Earnings expectations are starting to slow.
Global Equity Neutral	• The Global recovery is broadly intact with strong corporate earnings figures, through earnings growth slowing. • 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. • Economic growth favourable demographics • Emerging Markets have experienced recent outflows of investment and a sensible retrenchment in market levels.	• Inflation concerns as the base effect works itself out. Particularly wage inflation in India/China. • EM equity is slightly expensive relative to history • Monetary policy and spill over from euro crisis. • Government policy responses to international capital flows are a concern e.g. Brazil. • Volatility in the short-term compounded by currency volatility.
UK Fixed Interest Gilts Neutral/Negative	• Defensive characteristics remain partially intact. • Government continues to promote fiscal discipline. • Continues to be the safe haven investment of choice.	• Inflation continues to be above government targets and QE remains in place and possibly extended. • Global sovereign debt problems will heighten volatility. • Real yields remain unattractive.
UK Index Linked Gilts Neutral/Negative	• Inflation continues to remain above target. • Limited supply from the DMO and demand remains strong at both the short and long ends.	• Real yields remain unattractive. • Issuance is expected to increase through 2011.
UK Corporate Bonds Positive	• Spreads are widening – increasing the 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 a concern. • Economic weakness in Europe may lead to spreads widening further.
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. • Growth fears lead to shorter term leases. • Government spending cuts are likely to exacerbate the perceived problem in secondary and tertiary property.
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.