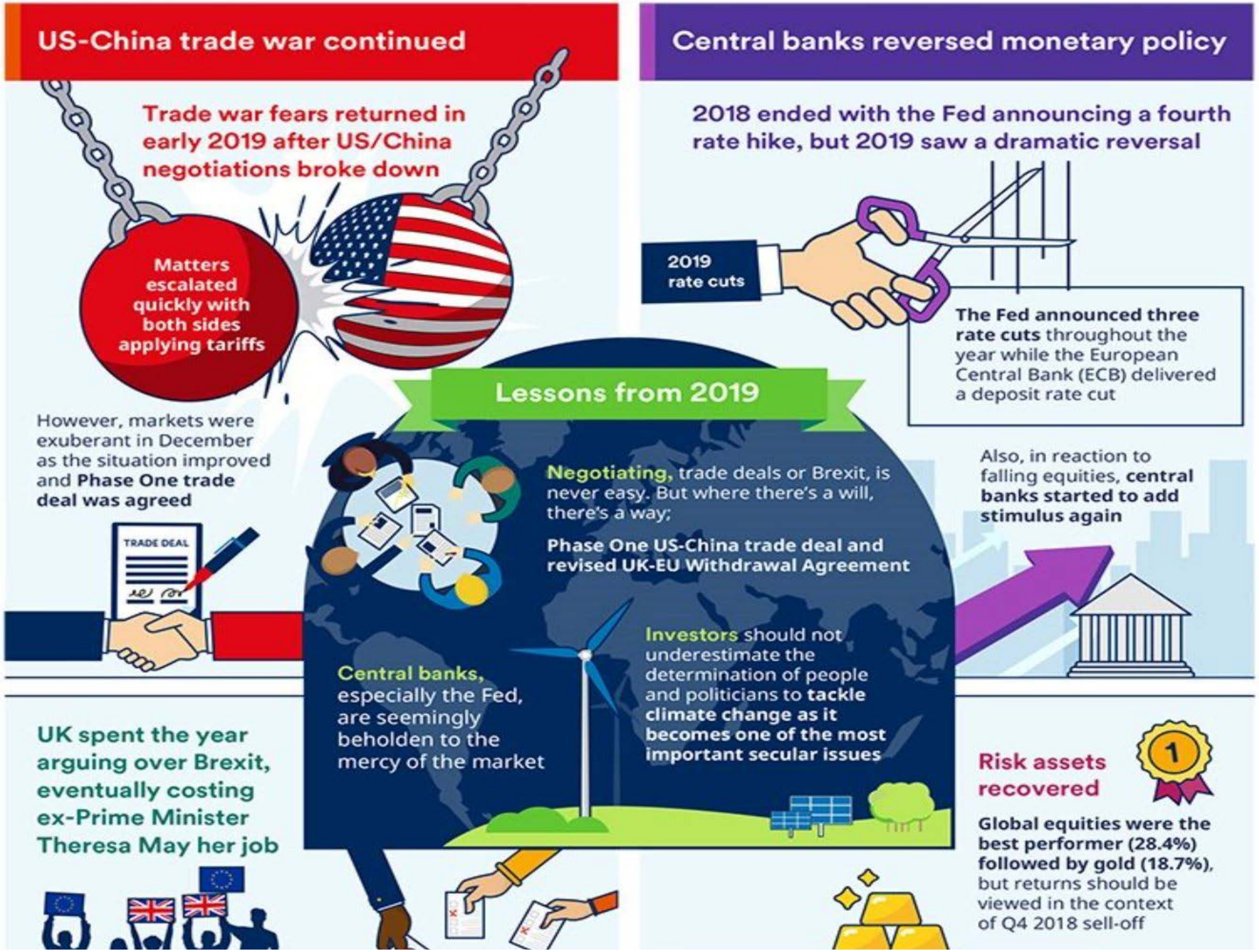
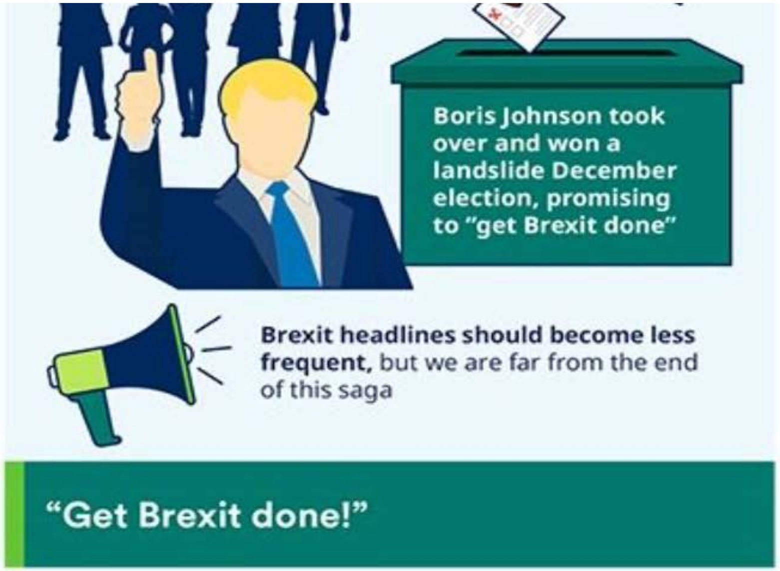
FINURA

MARKET COMMENTARY
JANUARY 2020

INFOGRAPHIC: THE GLOBAL ECONOMY





Source: [Schroders as at January 2020.]

MULTI-ASSET INVESTMENT VIEWS

KEY

▲ Up from last month ▼ Down from last month

● Positive ● Positive/Neutral ● Neutral ● Neutral/Negative ● Negative

	Category	View	Comments
Main Asset Classes	Equities	Positive/Neutral	Although valuations are beginning to turn expensive, equities (shares) still appear attractive relative to both bonds and cash.
Main Asset Classes	Government Bonds	Positive/Neutral ▲	We favour bonds with longer maturities, especially those that are inflation-linked. This is because there is ample liquidity (ie readily available funds) globally and yield-hunting investors are likely to keep demand high.
Main Asset Classes	Commodities	Positive/Neutral	Global liquidity conditions, as discussed above, remain supportive, but unless there is an increase in demand and a slowdown in supply, prices are likely to remain constrained.
Main Asset Classes	Credit	Positive/Neutral	Looking at valuations, the recent rise in prices (fall in yields) puts pressure on our overall positive view. However, because demand for corporate bonds remains strong due to central bank policy, we maintain our positive stance.
Equities	US	Positive/Neutral ▲	Upgraded this month, as economic activity indicators continue to suggest the economy is stabilising. Plus, the recent signing of the US-China trade deal should support company profits.
Equities	UK	Neutral	The recent election result provided some confidence to markets. Nevertheless, little has actually been solved in trade negotiations with the EU.
Equities	Europe	Positive/Neutral	Economic indicators in Europe continue to show signs of a mild recovery. The US-China trade deal should also support European corporate profits going into 2020.
Equities	Japan	Positive/Neutral	Despite the recent strong performance which has seen valuations rise, we remain positive on Japanese equities. This is because the country's growth outlook continues to improve and valuations remain attractive relative to history.
Equities	Pacific ex-Japan	Neutral	Economic indicators are stabilising for both domestic and export areas, and monetary policy support continues to come through.
Equities	Emerging Markets	Positive/Neutral	While developed market earnings remain fairly stable, emerging market earnings are seeing signs of improvement. At the same time, valuations continue to look attractive relative to their developed market counterparts.
Government Bonds	US	Neutral ▲	Although bond yields are yet to reflect the improvement in economic data, , their long-term returns are still better than cash.
Government Bonds	UK	Neutral/Negative ▲	Despite upgrading slightly, we still remain negative. This is because our economists expect UK growth to pick up in 2020 (which would be negative for bonds) due to the clear parliamentary majority and less business uncertainty.
Government Bonds	Germany	Neutral/Negative ▲	Economic indicators point to a turnaround in European economic data and we expect real yields to rise (bond prices fall when yields rise).
Government Bonds	Japan	Neutral/Negative ▲	Sentiment is lifting after the VAT hike, and with an improvement in trade data, together with Bank of Japan sounding less dovish, we expect growth will likely improve.
Government Bonds	US Inflation Linked	Positive/Neutral	We remain positive due to an improving global growth outlook and potential for inflation to be higher than expected.
Government Bonds	Emerging Markets Local	Neutral	The growth outlook in emerging markets looks to be improving, causing yields to rise (prices to fall).

	Category	View	Comments
Investment Grade Corporate Bonds	US	●	The US is still our preferred corporate bond market. However, we remain aware that valuations are becoming more expensive.
	Europe	●	The gap between Europe and US corporate bond quality appears to be narrowing, as more leveraged and foreign issuers tap the European market.
	Emerging Markets USD	● ▼	We downgrade EM sovereign bonds, although remain positive on corporate EM bonds.
High Yield Bonds	US	●	We continue to favour US high yield (those deemed by rating agencies to be below investment grade in quality) with the strong demand and liquidity backdrop supporting prices.
	Europe	●	While there remain lingering concerns about deteriorating fundamentals, low interest rates continue to support demand for the asset class given the yields on offer.
Commodities	Energy	● ▼	Additional shale gas supply from the US combined with non-US/OPEC supply increases will continue to spur a supply glut, putting downward pressure on prices.
	Gold	●	Gold is a potentially attractive hedge at the late stage of the economic cycle, as it is seen as an asset that may be able to protect against inflation and a slowing economy.
	Industrial Metals	●	We remain neutral on industrial metals as our more optimistic shift on the underlying macro-economic landscape for 2020 is offset by increased supply in response.
	Agriculture	●	The phase one trade deal between the US and China should benefit agricultural prices, but record South American harvests remain a concern due to a possible glut in supply.
Currencies	US $	●	USD valuation has fallen to its lowest level since Jun 2018, but it remains on the boundary between expensive and fair value.
	UK £	●	We remain negative as recent weaker data is leading to speculation that the Bank of England will now cut interest rates, which would be negative for sterling.
	EU €	●	Stabilisation of European data, and some trade resolution between the US and China, should improve sentiment towards Europe.
	JAP ¥	●	Reduced recession and geopolitical risk, combined with a stable Federal Reserve, warrants a neutral score on this perceived safe haven currency.
	Swiss F	●	Recent inflation numbers were worse than expected opening Switzerland to risk of relapsing into deflation. The Swiss National Bank has lowered its inflation forecast.

Past performance is not a guide to future performance and may not be repeated. The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.

Source: Schroders, January 2020. The views for equities, government bonds and commodities are based on return relative to cash in local currency. The views for corporate bonds and high yield are based on credit spreads (i.e. duration-hedged). The views for currencies are relative to US dollar, apart from US dollar which is relative to a trade-weighted basket.

MARKETS REVIEW

A look back at markets in January when the spread of coronavirus saw investors favour “safe haven” assets like government bonds.

HIGHLIGHTS

- Global equities, as measured by the MSCI World index, declined in January as the spread of coronavirus reduced investors’ appetite for risk. Assets perceived as safe havens, such as government bonds, performed well.
- US shares were flat overall. They carried strong momentum into the new year but mounting fears over the spread of the coronavirus erased the early gains. Energy stocks were especially hard-hit.
- Coronavirus concerns led to a lower start to the year for eurozone equities. The weakest sectors included energy, materials and consumer discretionary. Companies with significant exposure to China underperformed.
- UK equities fell in January. The end of the month marked the UK’s official departure from the EU and its entry into a transition period. Sterling was volatile, gaining sharply after the Bank of England kept interest rates unchanged.
- Japanese shares fell as news coverage emphasised the spread of coronavirus. The yen was slightly more volatile against the US dollar than in recent months although the actual yen/dollar rate ended January almost unchanged.
- Emerging markets (EM) equities also lost value. Commodity price falls weighed on sentiment towards a number of countries, notably Brazil, Chile, Colombia and South Africa.
- Government bond yields fell significantly over the month (meaning prices rose) amid investor caution and central banks reaffirming accommodative stances.

THE US

US equities rallied strongly in the first half of January before giving up the gains to end the month flat. Strong momentum from the end of 2019 continued into January, with the S&P 500 hitting a new record high in the middle of the month. Trade tensions that dogged markets for much of 2019 eased with the phase one US-China trade deal, signed as expected on 15 January.

US economic data remained broadly stable. The unemployment rate remains at a 50-year low of 3.5%, but muted wage growth has kept inflation under control. This gave the Federal Reserve the flexibility to leave monetary policy unchanged, although it adjusted its description of household spending growth to “moderate” rather than “strong”. Q4 GDP was in line with expectations, growing at 2.1% quarter-on-quarter (annualised).

In the second half of the month, however, mounting fears over the spread of coronavirus, in China and beyond, erased the early stock market progress. The Trump administration has imposed a temporary travel ban upon non-US citizens travelling to the US from China. Investor concerns over disrupted supply chains and weakened demand led to fears that growth could slow.

Energy stocks were especially hard-hit. The oil price fell steeply as the virus outbreak led to expectations of lower Chinese demand, adding to already cautious guidance from major oil producers. More defensive areas such as utilities performed better, with IT also holding up well in light of the trade war ceasefire.

EUROZONE

Eurozone equities had a weak start to the year amid fears over the potential impact of the coronavirus on global economic activity. The MSCI EMU, an index of large eurozone companies, returned -1.7% in January. The weakest sectors during the month included energy, materials and consumer discretionary. Industries with significant exposure to China – such as luxury goods – underperformed.

The top performing sector during the month was utilities. Utilities is seen as a safe haven sector that tends to perform well in times of uncertainty. Additionally, the sector drew support from news that the German government will pay €2.6 billion compensation to RWE as part of the country's move to switch from coal to renewable energy sources. Meanwhile, EDF benefited from reports that the French government may introduce new price regulation for the wholesale nuclear power market.

The flash GDP estimate for Q4 2019 showed growth of just 0.1% quarter-on-quarter in the eurozone, down from 0.3% growth in the previous quarter. Annual inflation ticked up to 1.4% in January from 1.3% in December – still well below the European Central Bank's target. Jobs data remained encouraging with the unemployment rate down to 7.4% in December, the lowest rate since May 2008.

Forward-looking data showed stabilisation at low levels, with the flash composite purchasing managers' index (PMI) for January steady at 50.9. (50 is the level that separates expansion from contraction. The PMI surveys are based on responses from companies in the manufacturing and services sectors).

UK

UK equities fell over the period. The end of January marked the UK's official departure from the EU and its entry into a transition period. Sterling was volatile, recovering sharply towards month-end after the Bank of England (BoE) kept interest rates unchanged, confounding market expectations which had predicted a cut. The Monetary Policy Committee voted to hold rates steady as indicators of future activity started to recover following the decisive general election outcome in December.

Data released in January covering the end of 2019 was mixed. Latest growth numbers from the Office for National Statistics (ONS) showed that UK GDP rose 0.1% in the three months to the end of November, but shrank by 0.3% in November itself. Meanwhile, the ONS also reported that retail sales volumes fell 0.6% in December month-on-month. The data prompted speculation the BoE would cut rates, pressuring sterling, which initially gave back some the strong gains it had made at the end of 2019.

However, forward-looking indicators suggested there has been a sharp recovery in the confidence of the UK consumers and corporates since the election. IHS Markit/CIPS confirmed that its composite purchasing managers' index (PMI) had recovered above the 50 mark which separates expansion from contraction. Meanwhile, the CBI's quarterly industrial trends survey found that the proportion of manufacturers expecting business conditions to improve was 23% larger than the share predicting them to worsen.

JAPAN

The Japanese market fell 2.1% in January as news coverage emphasised the spread of coronavirus. Sentiment in early January was also hit by the sudden escalation of tension over Iran. The yen was slightly more volatile against the US dollar than in recent months as a generally weaker trend was punctuated by the buying of yen as a perceived safe haven. Nevertheless, the actual yen/dollar rate ended January almost unchanged.

Japanese consumer confidence has picked up in the last two months, following the consumption tax increase on 1 October. However, the recovery appears somewhat muted compared to previous tax rises. Some of this may be the result of one-off impacts from warm winter weather and natural disasters, but the data completes the picture of a greater-than-expected economic impact from the tax rise.

The reporting season for the October to December period has started, but the overall picture will not emerge until early February when the bulk of companies report. The potential for the current heightened global uncertainty to be transmitted through a stronger yen may lead to continued caution in companies' outlooks.

At the individual stock level, there were further examples of ground breaking Japanese corporate activity in January. The battle for control of components of the Toshiba Group, which began with Nuflare Technology in December, escalated in January. An activist investor launched a tender offer for Toshiba Machine. Later in the month, a seemingly straightforward move by Maeda Construction to acquire 100% of Maeda Road was rebuffed by the subsidiary company. Maeda Road is now looking at a potential third-party or "white knight" to help it escape from its parent company.

ASIA (EX JAPAN)

Asia ex Japan equities declined in January amid concerns over the impact of the coronavirus outbreak in China on economic growth. This was despite an initial improvement in sentiment mid-month, as the US and China signed a phase one trade deal as expected.

Thailand and the Philippines were the weakest markets in the MSCI Asia ex Japan index, with tourism expected to be impacted by reduced visitors from China. South Korea lagged as the prospect of weaker global growth, and the risk of component shortages from China weighed on the outlook. China and Taiwan underperformed by a more modest margin. In Taiwan, President Tsai-Ing-Wen was re-elected for a second term.

By contrast, Pakistan posted a small gain and was the only index market to finish in positive territory. India recorded a small negative return but outperformed the index. The economy is less open than other regional markets and less exposed to global growth. Hong Kong performed broadly in line with the index.

EMERGING MARKETS

Emerging market (EM) equities lost value in January, as the outbreak of the coronavirus in China increased concerns over global growth. The Chinese authorities responded by imposing travel restrictions and cancelling Lunar New Year events. As the outbreak escalated, the re-opening of factories after the new year holiday was delayed.

Given the negative implications for Chinese economic growth, global commodity prices came under pressure. Against this backdrop, Brazil, Chile, Colombia and South Africa all underperformed, with currency weakness amplifying negative returns. In South Africa, the central bank unexpectedly cut its headline interest rate by 25bps, amid ongoing weakness in economic growth.

China slightly underperformed the broader EM index, although the mainland markets were closed for the new year holiday from 24 January to month end. A number of Asian EM, including South Korea, Thailand and the Philippines, also underperformed.

By contrast, Turkey recorded a positive return and outperformed as the central bank cut its headline interest rate by 75bps, more than expected, to 11.25%. Egypt was the best-performing market in the index, supported in part by currency strength. The central bank left its key interest rate unchanged, against expectations for a 50bps cut. Mexico posted a small gain, as trade-related uncertainty eased following President Trump's signing of the US-Mexico-Canada-Agreement (USMCA).

GLOBAL BONDS

Government yields declined in January (meaning prices rose) as investors sought lower risk assets amid an outbreak of coronavirus in China and uncertainty as to the potential economic impact. The Federal Reserve (Fed) and Bank of England (BoE) left policy rates unchanged with their accompanying comments taken as dovish.

The Fed changed its description of household spending growth to "moderate" from "strong". The BoE dropped forward guidance for "limited and gradual tightening", cut growth forecasts and said it expects inflation to remain below target until the end of 2021.

The US 10-year Treasury yield fell from 1.92% to 1.51%, while the two-year yield fell from 1.57% to 1.31%. As expected, developments in impeachment proceedings against President Trump indicated the case would most likely be thrown out by the Senate. US economic data remained healthy overall.

In Europe, the German 10-year yield fell from -0.19% to -0.43% with France's falling from 0.12% to -0.18% and Spain's from 0.47% to 0.24%. Italian bonds outperformed as the populist Lega party lost a regional election. The country's 10-year yield fell 47 basis points (bps) to 0.94%. The UK 10-year yield declined from 0.82% to 0.52%. The eurozone economy showed further stabilisation at low levels, with the flash composite purchasing managers' index for January at 50.9.

Corporate bonds produced positive overall returns (in local currency), led by investment grade, as global yields declined, but underperformed government bonds. US energy lagged after strong performance the previous month. UK investment grade corporate bonds proved an exception, outperforming government bonds, led by capital goods. Investment grade bonds are the highest quality bonds as determined by a credit ratings agency; high yield bonds are more speculative, with a credit rating below investment grade. In high yield, certain sectors in the UK and Europe performed well.

Emerging market hard currency government and corporate bonds produced positive total returns, although EM currencies fell overall. Latin American currencies broadly weakened given the renewed uncertainty around Chinese growth.

While the overall MSCI World equity index lost 0.6% in January, convertible bonds as measured by the Thomson Reuters Global Focus index gained 1.8% in US dollar terms. Convertibles in the US and Europe became cheaper in January while Asian and Japanese convertibles continue to trade below our estimate of fair value.

COMMODITIES

The S&P GSCI Spot Index saw a double digit fall in January, as global growth concerns weighed on the demand outlook for commodities. Energy was the weakest index component. Crude oil prices fell sharply on expectations of weaker demand, especially from China given the likelihood that the spread of coronavirus and measures to contain it will weigh on economic activity. Industrial metals also fell on weaker demand expectations. Agricultural commodities recorded a small negative return, led lower by coffee and soybeans. Conversely, precious metals generated a positive return, with gold and silver both moving higher.

TOTAL RETURNS (NET) % – TO END JANUARY 2020

	1 MONTH			12 MONTHS		
Equities	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
MSCI World	-0.6	0.7	-0.1	17.7	21.9	17.5
MSCI World Value	-2.9	-1.7	-2.4	10.3	14.2	10.0
MSCI World Growth	1.7	3.0	2.2	25.4	29.9	25.2
MSCI World Smaller Companies	-2.8	-1.5	-2.3	11.2	15.2	11.0
MSCI Emerging Markets	-4.7	-3.4	-4.2	3.8	7.5	3.6
MSCI AC Asia ex Japan	-4.4	-3.2	-4.0	5.2	8.9	5.0
S&P500	-0.0	1.3	0.5	21.7	26.0	21.4
MSCI EMU	-3.0	-1.7	-2.5	12.0	16.0	11.8
FTSE Europe ex UK	-2.0	-0.8	-1.6	15.2	19.3	15.0
FTSE All-Share	-3.7	-2.5	-3.3	10.9	14.8	10.7
TOPIX*	-1.9	-0.6	-1.4	10.6	14.5	10.4

	1 MONTH			12 MONTHS		
Government Bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
JPM GBI US All Mats	2.6	3.9	3.1	9.4	13.3	9.2
JPM GBI UK All Mats	3.4	4.8	3.9	10.6	14.5	10.4
JPM GBI Japan All Mats**	0.8	2.1	1.3	2.5	6.1	2.3
JPM GBI Germany All Traded	0.6	1.9	1.1	0.8	4.4	0.6
Corporate Bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global Broad Market Corporate	1.6	2.9	2.1	10.8	14.8	10.6
BofA ML US Corporate Master	2.4	3.7	2.9	14.6	18.6	14.3
BofA ML EMU Corporate ex T1 (5-10Y)	0.2	1.5	0.7	5.4	9.1	5.2
BofA ML £ Non-Gilts	2.3	3.6	2.8	10.8	14.8	10.6
Non-investment Grade Bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global High Yield	0.1	1.4	0.6	9.4	13.3	9.2
BofA ML Euro High Yield	-0.1	0.2	-0.6	5.3	9.0	5.0

Source: Thomson Reuters DataStream.
Local currency returns in January 2020: *-2.1%, **0.5%.
Past performance is not a guide to future performance and may not be repeated.

Source: Schroders, January 2020: The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested. Past performance mentioned is not a guide to future performance and may not be repeated. The sectors, securities, regions and countries shown are for illustrative purposes only and are not to be considered a recommendation to buy or sell.

Important Information: This communication is marketing material. The views and opinions contained herein are those of the named author(s) on this page, and may not necessarily represent views expressed or reflected in other Schroders communications, strategies or funds. This document is intended to be for information purposes only and it is not intended as promotional material in any respect. The material is not intended as an offer or solicitation for the purchase or sale of any financial instrument. The material is not intended to provide, and should not be relied on for, accounting, legal or tax advice, or investment recommendations. Information herein is believed to be reliable but Schroder Investment Management Ltd (Schroders) does not warrant its completeness or accuracy. The data has been sourced by Schroders and should be independently verified before further publication or use. No responsibility can be accepted for error of fact or opinion. This does not exclude or restrict any duty or liability that Schroders has to its customers under the Financial Services and Markets Act 2000 (as amended from time to time) or any other regulatory system. Reliance should not be placed on the views and information in the document when taking individual investment and/or strategic decisions. Past Performance is not a guide to future performance. The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested. Exchange rate changes may cause the value of any overseas investments to rise or fall. Any sectors, securities, regions or countries shown above are for illustrative purposes only and are not to be considered a recommendation to buy or sell. The forecasts included should not be relied upon, are not guaranteed and are provided only as at the date of issue. Our forecasts are based on our own assumptions which may change. Forecasts and assumptions may be affected by external economic or other factors. Issued by Schroder Unit Trusts Limited, 31 Gresham Street, London, EC2V 7QA. Registered Number 4191730 England. Authorised and regulated by the Financial Conduct Authority.

FINURA

Level 2, Juxon House, 100 St Paul's Churchyard, London, EC4M 8BU
T: +44 (0)20 3102 7730   E: enquiries@finurapartners.com   W: finurapartners.com