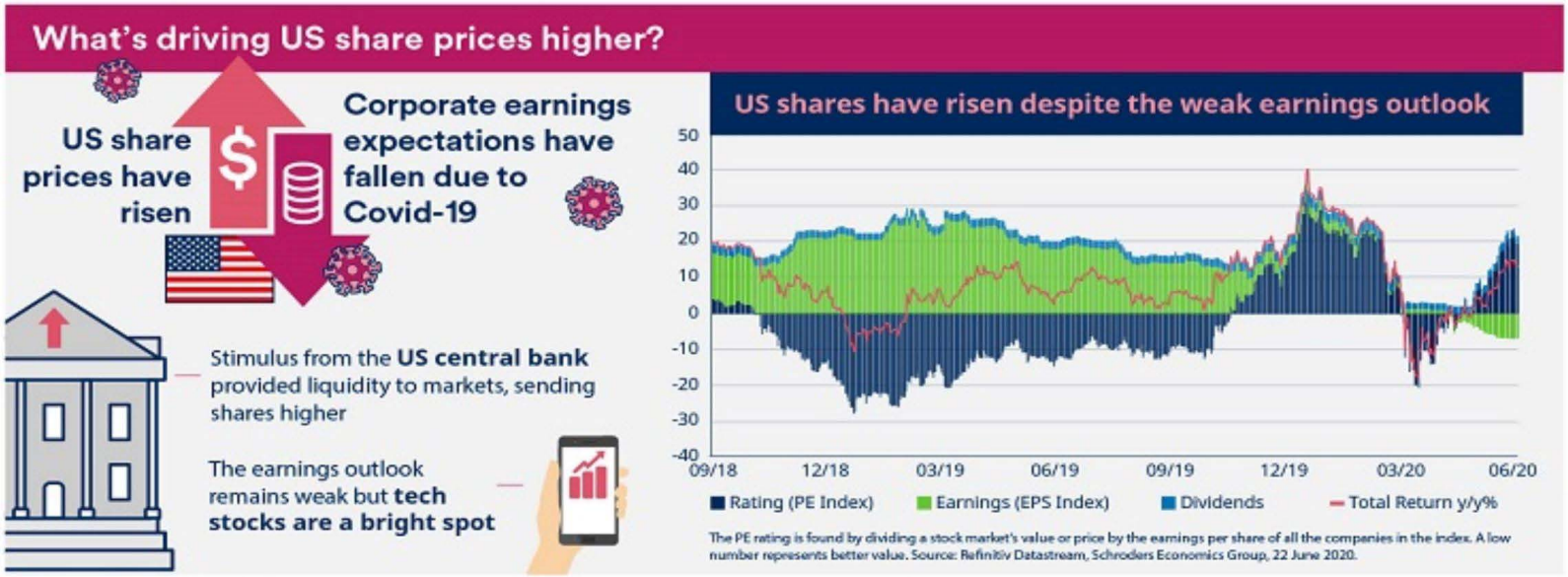
FINURA

MARKET COMMENTARY
JULY 2020

Chartered Financial Planners

Pension TRANSFER Gold Standard

INFOGRAPHIC: THE GLOBAL ECONOMY



Source: Schroders as at July 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	Neutral	We maintain our neutral view. The fundamental outlook is still weak but central bank support continues to be beneficial. The two-tier market within equities is likely to persist; this means we think we are likely to see "growth/ quality" stocks continue to outperform those classified as "value".
	Government Bonds	Neutral	We believe that the upside to bonds is limited, but it does not make sense to reduce our exposure given our holdings in riskier assets.
	Commodities	Positive/ Neutral	We remain positive on commodities as prices continue to move slowly higher as global economic activity begins to return to normal. The energy sector has been leading the price recovery.
	Credit	Positive/ Neutral	Whilst the fundamental picture remains weak, central bank support and robust investor demand will continue to support credit going forward.
Equities	US	Neutral	With levels pricing in a "V-shaped" economic recovery, valuations have little room for manoeuvre if the recovery is slower than expected. We see more attractive opportunities elsewhere.
	UK	Neutral/ Negative	With Brexit still unresolved and the lockdown continuing to hurt economic activity, we see few encouraging signs in the UK equity market.
	Europe	Positive/ Neutral	Europe remains our preferred developed market. Lockdowns are easing and we have seen a credible and coordinated response from the authorities.
	Japan	Neutral	Having done a comparatively good job in containing the spread of Covid-19 and with demand starting to pick up, there remains upside potential for Japan.
	Pacific ex-Japan	Neutral	The region has been supported by fiscal and monetary policy and has weathered the Covid-19 fallout much better.
	Emerging Markets	Neutral	We maintain our neutral view, but have upgraded China with the recovery progressing unabated and the market overlooking trade war risk.
Government Bonds	US	Neutral/ Negative	Although we are concerned that the efficacy of government bonds as a hedge is deteriorating, we believe US government bonds can still be useful in portfolios given our riskier positions elsewhere.
	UK	Negative	Yields and fiscal dynamics remain unattractive.
	Germany	Negative	We have a negative view on Germany, also due to unattractive yields and fiscal dynamics.
	Japan	Neutral/ Negative	Our view remains unchanged due to continued expansionary monetary policy from the Bank of Japan.
	US Inflation Linked	Neutral	Inflation expectations remain depressed. It is too early to be concerned about the risk of significant rises, but markets are unduly pessimistic about the medium-term outlook.
	Emerging Markets Local	Positive/ Neutral	We maintain our positive stance to benefit from looser monetary policy in the emerging world as well as taking advantage of cheap valuations in emerging currencies.

	Category	View	Comments
Investment Grade Credit	US	●	We remain positive on US investment grade (IG) credit, driven by the Federal Reserve's liquidity injections and financing programmes.
	Europe	●	We believe support measures from the European Central Bank will strengthen the European corporate bond market.
	Emerging Markets USD	●	With the recent tightening of spreads, we continue to favour local currency debt over dollar denominated, where we see better credit quality (issuing companies' ability to pay back their debt).
High Yield Bonds (Non-IG)	US	●	Our bias is for the US over Europe, as US policy initiatives continue to underpin the high yield (HY, meaning non-investment grade) market.
	Europe	●	Our view on European HY credit is unchanged due to stimulus through the expansion of the Pandemic Emergency Purchase Programme and the European Recovery Fund.
Commodities	Energy	●	As lockdowns continue to ease, demand for energy is returning. The production cuts agreed by the Organisation of the Petroleum Exporting Countries (OPEC) continue to support the recovery in energy prices.
	Gold	●	Whilst gold has performed strongly, we believe that there is the potential for further gains as gold is one of the main beneficiaries of central bank support measures.
	Industrial Metals	● ▼	The disruption to supply and the lack of scrap metal availability added to the recent rally in industrial metals. However, activity in areas such as copper are returning to pre-Covid 19 levels.
	Agriculture	●	Prices remain attractive as the agriculture market has been a laggard in the economic recovery rally this year. The US-China trade deal is also likely to provide further support.
Currencies	US $	● ▼	Downgraded as Covid-19 infection rates in the US have spiked significantly, compounding the weak growth outlook. We believe the US will underperform the rest of the world.
	UK £	●	The economic impact of Covid-19 in combination with the risk of Brexit will continue to weigh on the performance of pound sterling.
	EU €	●	We expect to see further upside following the monetary and fiscal support measures announced by the European Central Bank to boost economic recovery in the eurozone.
	JAP ¥	● ▲	The stimulus packages announced by the Bank of Japan should support the currency as the coronavirus lending programme was increased to more than $1 trillion.
	Swiss F	●	We remain neutral on the Swiss franc given its high price, whilst acknowledging its continued role as a perceived "safe haven" currency.

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, July 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 on markets in July when the US dollar declined and tech stocks posted strong quarterly earnings.

HIGHLIGHTS

- TGlobal equities gained (in dollar terms) although economic growth data confirmed the severity of Q2's downturn. Ongoing central bank and government measures continued to provide support for equities and corporate bonds.
- US equities gained, supported by robust quarterly earnings from stocks such as Amazon, Apple and Facebook. Data showed that US Q2 GDP fell sharply and the dollar weakened.
- July saw a decline for eurozone equities. Economic data confirmed the severity of the downturn in activity during the second quarter and some countries saw Covid-19 infection rates rise again.
- UK equities fell over the period as fears around a second wave of Covid-19 infections weighed on investor sentiment.
- Japanese shares fell. The yen strengthened against a generally weaker US dollar while virus infections picked up, albeit from very low levels.
- Emerging market (EM) equities enjoyed strong gains, helped by US dollar weakness. Taiwan performed well amid gains for technology stocks while progress on reforms boosted Brazilian shares.
- Government bond yields fell (i.e. prices rose) amid data confirming deep contractions in numerous large economies in Q2. The approval of the EU recovery fund provided support for Italian government bonds.
- In commodities, precious metal prices rose with US dollar weakness providing a strong tailwind.

THE US

US equities gained in July despite some unnerving economic data releases. Although it was anticipated, confirmation that Q2's quarterly contraction in GDP was the worst on record raised questions over a recovery. US GDP fell by an annualised 32.9% in Q2. Initial jobless claims also unexpectedly rose to 1.4 million, ending a 15-week run of declines. Continued jobless claims did ease lower (to 16.2 million), however, but the ending of the $600 per/week unemployment benefit muted any fanfare. In addition, US-China relations again soured, through tit-for-tat consulate closures. The US dollar weakened versus other currencies.

The Federal Reserve (Fed) left its key policy rate unchanged and Chair Jerome Powell reiterated a very cautious outlook. The Fed stated it remains ready to provide further policy accommodation as needed as it hopes for the best, but plans for the worst. Powell added that more fiscal policy support was essential given the gravity and prolonged impact of the virus-driven shock to the economy. On a brighter note, US consumer spending continued to rise in June, increasing 5.6% after a record 8.5% jump in May, as more businesses reopened. Inflation remains subdued.

Given the mixed data, it seemed likely that US stocks were swayed more by earnings releases rather than by the macro backdrop. Consumer discretionary stocks performed strongly, with index heavyweight Amazon recording a doubling of profit and better-than-expected sales. Facebook and Apple also announced strong earnings. Meanwhile, energy stocks declined, with US oil major results reflecting the oil price crash earlier in the year.

EUROZONE

July saw a decline for eurozone equities (in euro terms). The MSCI EMU (Economic & Monetary Union) Index returned -1.4%. Economic data confirmed the severity of the downturn in activity during the second quarter. Towards the end of the month, there were fears over rising numbers of Covid-19 infections in some European countries and some travel restrictions were re-imposed. The utilities and consumer staples sectors were among the main gainers while energy and financials lagged behind. The start of the Q2 corporate earnings season saw some better-than-expected numbers, particularly from technology and industrial stocks.

Second quarter growth data confirmed the severe impact of lockdowns on economic activity. Eurozone GDP contracted by 12.1% in the second quarter. Spain saw growth plunge by 18.5% while German GDP shrank by 10.1% in Q2. The eurozone unemployment rate ticked up to 7.8% in June from 7.7% in May. However, survey data pointed to an improvement in activity in July. The flash composite purchasing managers' survey (PMI) showed an increase to 54.8 from 48.5 in June. (50 is the level that separates expansion from contraction. The PMI surveys are based on responses from companies in the manufacturing and services sectors).

The EU recovery fund was approved after protracted negotiations at a mid-month leaders' summit. The fund will be made up of €390 billion of grants and €360 billion of loans to be distributed among EU member states to aid in the recovery from the coronavirus pandemic. The money will be borrowed by the European Commission and guaranteed by all EU member states.

UK

UK equities fell over the period as fears around a second wave of Covid-19 infections weighed on a number of regional stock markets. The UK was among certain European countries to report rising numbers of Covid-19 infections. In response, the government tightened lockdown measures in parts of northern England, postponed plans to re-open certain leisure venues and advised against all non-essential travel to Spain.

Despite a recovery in economic data over May and June, the rising number of infections reminded investors of the risks ahead – efforts to deal with the first wave of the virus earlier in the year had hit economic activity indiscriminately and simultaneously in all regions of the world. A number of economically sensitive areas of the market underperformed (reversing some of their gains since the market's most recent low in March) amid the general deterioration in investor sentiment

Data from the Office for National Statistics (ONS) confirmed that the UK economy had begun to recover in May as lockdown restrictions were first eased. The ONS's latest monthly estimate of GDP revealed that the economy had grown by 1.8% in May, compared to a contraction of 20.3% in April. More current data – including very strong retail sales for June – appeared to show an acceleration in growth towards the end of Q2 as further restrictions were lifted.

JAPAN

The Japanese market tracked sideways for most of July, before falling in the last few days of the month to record a total return of -4.0%. Although there were some brief reversals, strong momentum continued in a narrow range of stocks. The decline in the overall market was partly in reaction to short-term strength

of the yen against a generally weak US dollar.

For much of July, the equity market appeared resilient in the face of a strengthening yen and a pick-up in virus infections in Europe and, especially, in the US. Even Japan joined this trend with the public and government demonstrating renewed risk-aversion associated with some pick-up in the very low levels of incidence previously seen in Tokyo. This led to the suspension of several initiatives the government had put in place to stimulate consumption and could soon result in the re-imposition of a state of emergency. Overall, however, Japan continues to appear better placed than most European countries and the US to cope with a resurgence of infections. The other main concern for investors centred on the sharp deterioration in the relationship between the US and China, which was partly triggered by the imposition of a new security law in Hong Kong.

Meanwhile, the release of US GDP data confirmed the extent of the lockdown's impact in the second quarter. Japan's own quarterly GDP statistics will be released on 17 August. While the pattern will be similar, the actual decline should be less severe for Japan, in line with the lighter restrictions on mobility and economic activity. More granular economic data for Japan that was released during July has actually been slightly ahead of consensus forecasts. This includes statistics on the labour market recovery and an unexpected pick-up in the inflation rate in Tokyo. In the short-term, overall industrial production has also responded to the resumption of auto output.

ASIA (EX JAPAN)

Asia ex Japan equities generated a robust return in July, benefiting from further weakness in the US dollar. Further signs of a recovery in global economic activity and increased optimism towards the development of a Covid-19 vaccine proved supportive of sentiment. Taiwan was by far the best-performing index market, aided by a rally in technology names; Q2 earnings results were favourable for a number of companies, with third quarter management guidance also ahead of expectations in many cases. June's export orders and industrial production recovered strongly versus May's data.

Indian equities continued to rally, albeit driven by a small number of stocks, and outperforming the index. This was despite a rise in daily new cases of Covid-19 after India's lockdown was eased in June. The virus has moved to a wider number of areas and certain local lockdowns were put in place. Meanwhile, Chinese shares outperformed by a smaller margin. Manufacturing PMI data for July, which rose to 52.8, from 51.2 in June, signalled a stable recovery. In addition, Q2 GDP growth of 3.2% y/y was ahead of expectations, however, tensions with the US increased. South Korea's performed broadly in line with the index. Positive revisions to earnings estimates proved supportive. On the macroeconomic side, exports continued to steadily recover.

In contrast, Thailand, the Philippines and Hong Kong all recorded negative returns and underperformed. In Thailand, high frequency data showed minor improvement but remained relatively subdued, including official tourist arrivals still at zero in June.

EMERGING MARKETS

Emerging market (EM) equities rallied strongly in July. This was despite further acceleration in new cases of Covid-19 in certain EM countries, and an escalation in US-China tensions. US dollar weakness and continued recovery in economic data, amid ongoing monetary and fiscal support, boosted sentiment. The MSCI Emerging Markets index increased in value and outperformed the MSCI World.

Taiwan was the best-performing market in the index, led higher by technology stocks. Brazil, where currency appreciation amplified returns, outperformed amid signs of renewed progress in the government's reform agenda. India outperformed the MSCI Emerging Markets Index in spite of continued increases in the number of new Covid-19 cases. China outperformed the index by a smaller margin. Q2 GDP growth rebounded to 3.2% year-on-year (y/y), after a fall of -6.8% in Q1, and was stronger than expected. Manufacturing PMI data for July, which rose to 52.8, from 51.2 in June, also pointed to a stable recovery. However, tensions with the US escalated during the month.

By contrast, Turkish equities fell as concerns over monetary policy mounted, with foreign exchange reserves continuing to ebb. Inflation rose by more than expected to 12.6% y/y in June and remained ahead of target. The central bank held its key policy rate at 8.25%. Mexico and Russia finished in positive territory but also underperformed the index.

GLOBAL BONDS

Government bond yields fell (i.e. prices rose) amid data confirming deep contractions in numerous large economies in Q2, combined with continued friction between the US and China and further central bank policy support. At the same time, more forward-looking economic data indicated activity continued to recover well with countries emerging from Covid-19 lockdown.

The US dollar retreated sharply, following a period of strong appreciation, due to the increasing number of new coronavirus cases across many states. Aside from the positive performance of government bonds (bond yields and prices move inversely), other safe haven assets performed well with silver and gold reaching record highs, helped by the weaker dollar. Some riskier assets performed well too; credit (bonds issued by companies) outperformed government bonds, especially high yield.

The US Treasury 10-year yield fell by 13 basis points (bps) to 0.53% over the month. In Europe, Germany's 10-year yield fell by seven bps to -0.52%, France's by eight to -0.19%. The UK 10-year yield was seven points lower at 0.10%.

Europe's "periphery" performed well as the EU officially announced a €750 billion pandemic recovery fund. Italy, which stands to be among the prime beneficiaries, saw its 10-year yield continue to fall materially, down by 25bps to just over 1.0%. The announcement marked a departure for the EU since it enables the European Commission to borrow large sums in order to provide non-repayable grants to member states.

Corporate bonds saw positive returns and outperformed, led by US high yield (total return in local currency). In investment grade, the US dollar market also led. More cyclical sectors broadly performed well. Investment grade bonds are the highest quality bonds as determined by a credit rating agency; high yield bonds are more speculative, with a credit rating below investment grade.

Emerging market (EM) government and corporate bonds (hard currency) produced further good returns. Local currency bonds again saw more modest returns. EM currencies benefited from a broad decline in the US dollar, which fell 4% against a basket of currencies. The Mexican peso and Brazilian real performed well.

Turning to convertible bonds, global stock markets continued their upward trajectory in July. The Thomson Reuters Global Focus Convertible Bond Index enjoyed full participation in the gains, rising by 4.8%, in line with the MSCI World equity index. The convertible bond primary market has been incredibly

active in 2020 to date, but slowed somewhat in July during the traditional summer season lull. The main issuers continue to be in the technology space, which remains the main driver of equity returns.

COMMODITIES

The S&P GSCI (commodities index) recorded a solid gain in July, with US dollar weakness a strong tailwind. Precious metals were up sharply, with gold's 8.6% gain outstripped by a 30.0% rise in the price of silver. The industrial metals component posted a strong return, benefitting from signs of ongoing global recovery, and a pick-up in demand from China. The energy and agricultural components delivered more modest gains but still advanced.

TOTAL RETURNS (NET) % – TO END JULY 2020

	1 MONTH			12 MONTHS		
Equities	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
MSCI World	4.8	-0.5	-1.4	7.2	1.0	0.0
MSCI World Value	2.5	-2.6	-3.5	-8.9	-14.2	-15.0
MSCI World Growth	6.9	1.5	0.6	24.2	16.9	15.8
MSCI World Smaller Companies	3.9	-1.3	-2.2	-2.0	-7.8	-8.6
MSCI Emerging Markets	8.9	3.5	2.6	6.5	0.3	-0.6
MSCI AC Asia ex Japan	8.5	3.1	2.1	12.3	5.7	4.8
S&P500	5.6	0.3	-0.6	12.0	5.4	4.5
MSCI EMU	3.8	-1.4	-2.3	-1.2	-7.0	-7.9
FTSE Europe ex UK	4.7	-0.6	-1.4	4.2	-1.9	-2.8
FTSE All-Share	2.4	-2.7	-3.6	-11.8	-17.0	-17.8
TOPIX*	-2.1	-7.0	-7.8	0.7	-5.2	-6.1

	1 MONTH			12 MONTHS		
Government Bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
JPM GBI US All Mats	1.3	-3.8	-4.7	12.5	5.9	5.0
JPM GBI UK All Mats	6.7	1.3	0.4	18.2	11.3	10.2
JPM GBI Japan All Mats**	2.5	-2.7	-3.5	1.0	-4.9	-5.7
JPM GBI Germany All Traded	6.0	0.7	-0.2	7.1	0.8	-0.1
Corporate Bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global Broad Market Corporate	4.2	-1.0	-1.9	10.1	3.6	2.7
BofA ML US Corporate Master	3.2	-2.0	-2.9	12.0	5.5	4.5
BofA ML EMU Corporate ex T1 (5-10Y)	7.2	1.8	0.9	5.8	-0.4	-1.3
BofA ML £ Non-Gilts	7.9	2.5	1.6	13.6	7.0	6.0
Non-investment Grade Bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global High Yield	4.8	-0.4	-1.3	4.0	-2.1	-3.0
BofA ML Euro High Yield	7.1	1.8	0.9	5.1	-1.0	-1.9

Source: Thomson Reuters DataStream.
Local currency returns in July 2020: *-4.0%, **0.4%.
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Source: Schroders, July 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.

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