Economic & Political Roundup

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.

Roundup

Brexit rumbled on and the Democrats won control of the House of Representatives in November. The big move though was the collapse in the oil price. The Federal Reserve's chairman, Jerome Powell, made a speech at the end of the month in which he hinted that US interest rates would not need to rise much further. US Treasury yields fell as a result.

Global

Increased market volatility was, perhaps, inevitable and seems likely to persist into 2019. This may create opportunities for those able to take advantage.

Susan Noble, chairman of British Empire, suggests that it was perhaps inevitable that we would enter a period of greater uncertainty given market complacency about the risks in the global economy. Alan Hodson, chairman of JPMorgan Elect, thinks that market volatility may persist but says corporate earnings and dividends have been robust. Katy Thorneycroft, manager of that fund's growth portfolio, thinks US monetary policy will still be supportive for risky assets into early 2019. Rachel Beagles, chairman of Securities Trust of Scotland, says that the threat of overly aggressive monetary tightening by the US Federal Reserve or an escalation of China/US trade tensions should not be ignored. The manager of that fund expects to see further spikes on volatility and sharp sell-offs in equities. Fiona McBain, chairman of Scottish Mortgage, quotes Jack Ma "monumental challenges give rise to monumental opportunities". The team behind Personal Assets believe after decades of falling yields, fixed income will not provide the portfolio protection it has in the past but says that, for those with liquidity, bargain hunting may not be too far away.

Exchange Rate	30/11/18	Change on month %
GBP / USD	1.2749	(0.1)
USD / EUR	0.8835	(0.1)
USD / JPY	113.57	0.6
USD / CHF	0.9979	(1.1)
USD / CNY	6.9605	(0.2)

Source: Bloomberg, Marten & Co

MSCI Indices rebased to 100

Time period 31/10/2017 to 31/10/2018

Source: Bloomberg, Marten & Co

	30/11/18	Change on month %
Oil (Brent)	58.71	(22.2)
Gold	1220.52	0.5
US Tsy 10 yr yield	2.9879	(4.9)
UK Gilt 10 yr yield	1.364	(5.1)
Bund 10 yr yield	0.312	(18.8)

Source: Bloomberg, Marten & Co

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United Kingdom

It is Brexit, Brexit, Brexit as our commentators highlight the opportunities thrown up by the de-rating of the UK market and the uncertainty facing the UK

James Goldstone, manager of Keystone, notes that the wild card that Brexit represents has become the dominant factor in the UK stock market and with negotiations heading for a perhaps predictably late and fraught conclusion, this has weighed heavily on domestically focused shares. The managers of Troy Income & Growth say this backdrop may also create investment opportunities. Richard Burns, chairman of Aberdeen Standard Equity Income, thinks it is probable that the 35-year period of falling British interest rates is over. Thomas Moore, that fund's manager, believes that any Brexit outcome that is less extreme than no-deal offers the prospect of material valuation re-rating. This sentiment echoed was by others including Ian Barby, chairman of Schroder Income Growth and the managers of that fund. John Baker and Katen Patel, managers of the income portfolio of JPMorgan Elect, highlight the attractive yield offered by the UK market. While Katy Thorneycroft, speaking in her capacity as manager of that fund's cash portfolio, is cautious. She sees an elevated risk of poor outcomes for the UK, even assuming Brexit negotiations conclude more or less successfully. Alex Wright, manager of Fidelity Special Values, espouses a contrarian view (in this select group of investors in UK companies) that large cap UK companies look more attractive than smaller domestically-focused ones. Mark Barnett, manager of Perpetual Income & Growth, hopes that momentum-based investing will remain out of favour allowing fundamentals to shine through. Montanaro UK Smaller's manager says it has been unwise to invest on the basis of politics and thinks, long-term, investors in UK small caps will be rewarded. However, Odyssean's manager thinks many higher growth AIM momentum stocks still appear to trade on considerable premia to potential takeout multiples.

Europe

Notable challenges to European markets include Italy, Brexit and US trade wars but there is some optimism

Michael MacPhee, chairman of The European Investment Trust, puts the case for a slow and steady approach to investing. Craig Armour, manager of that fund, highlights the particular threats that Italy, Brexit and US trade policy pose to European markets. The managers of JPMorgan European Smaller Companies agree but think heightened volatility represents a market correction rather than the start of a more prolonged downturn. The managers of JPMorgan's European large cap trust think above-trend growth in Europe in 2019 could support consumer confidence.

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Asia ex Japan

Asian markets look cheap. Headwinds, notably the trade war, exist but may be priced into markets

The managers of Schroder Oriental Income note that Asian markets are close to the valuation lows seen in late 2015/early 2016, suggesting that investor caution is already elevated. Hugh Young, manager of Aberdeen Standard Asian Focus, is cautious but expects to use market weakness as a buying opportunity. John Russell, chairman of Henderson Far East Income, believes China's leaders are determined to raise Chinese living standards to western levels and will not deviate from that path. Michael Kerley, manager of that fund, is cautiously optimistic. As manager of an Asian income fund, it is encouraging that he believes Asian companies have low levels of debt, a pragmatic view on capital expenditure and strong cash flow generation which should allow dividend pay-out ratios to rise in the years ahead. Allan McKenzie, chairman of Edinburgh Dragon, suggests that Trump is following a predictable path of bluster and then compromise on the trade war front. The managers of that fund say some companies are shelving investment plans which could dampen economic growth in the short term. Harry Wells, chairman of Martin Currie Asia Unconstrained, points out that

exports, especially to the US, are less important to Asian economies than they were. The managers of Establishment Trust think many headwinds are priced into markets.

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Japan

Japan is vulnerable to a global economic slowdown but its companies are innovating and recent market falls may provide opportunities

Andrew Fleming, the chairman of JP Morgan Japanese, highlights the support that the Bank of Japan has provided to both the Japanese bond and equity markets. The managers note that Japan is more cyclical than other developed markets and therefore sensitive to global economic developments. Baillie Gifford Japan's chairman, Nick Bannerman, points out that Shinzo Abe is on course to be Japan's longest-serving Prime Minister. The managers of JPMorgan Japan Smaller Companies draw attention to the innovation they see coming from many Japanese companies and the improvements in corporate governance. Aberdeen Japan's managers think the market's fall may provide longer-term investors the opportunity to take advantage of more attractive valuations.

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Property

While Brexit overshadows mainstream UK property funds, alternatives property plays, such as social housing and medical centres, have different drivers

Brian Bickell, chief executive of Shaftesbury, discusses the strengths of an investment in property in London's West End. Brexit is a worry for Nicholas Thompson, chairman of Picton Property Income, and Mark Burton, chairman of AEW UK REIT. The managers of the latter fund expand on the prospects for individual sectors of the UK property market. Allan Lockhart, chief executive of NewRiver REIT, goes into the changes that are taking place in the UK property market and how they might affect his company. Hugh Seaborn, chairman of TR Property, thinks the ECB may be forced to defer interest rate increases and the reversal of its quantitative easing programme – such a scenario would help underpin property valuations. As usual, Marcus Phayre-Mudge, manager of TR Property, provides an in-depth look at the property market; this is always worth a read. The teams behind Residential Secure Income and Civitas Social Housing talk us through the social housing market in the UK and the shortage of suitable accommodation. While Assura discusses NHS capital investment.

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Other

We also have comments on global emerging markets from Templeton Emerging; China, from Dale Nicholls, manager of Fidelity China Special Situations; India, from Aberdeen New India; a detailed look at Eastern Europe from Baring Emerging Europe; Debt, from TwentyFour Income and Alcentra European Floating Rate Income; a comprehensive look at the healthcare market from the team managing Worldwide Healthcare; HICL's chairman discusses the Infrastructure market. NextEnergy Solar and John Laing Environmental Assets outline the prospects for electricity prices. Lastly, Andre Liebenberg, chief executive officer of Yellowcake, explains the likely drivers of the uranium price.

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Global

(compare Global funds **here**)

Susan Noble, chairman, British Empire: After a long period where markets have been resilient or even complacent about the risks which abound in the global economy, it was perhaps inevitable that we would enter a period of greater uncertainty.

Equity and bond markets have experienced a bout of heightened market volatility which has been driven by, among other things, the threat of a global trade war, the effects of rising interest rates as quantitative easing is slowly removed, and uncertainty over Brexit.

The potential effect of these major issues is very difficult to predict. [*A*] focus on company fundamentals should provide both strong returns over the long term and a degree of protection against the vagaries of markets.

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Alan Hodson, chairman, JPMorgan Elect: For several years it has been easy to highlight heightened investment risks but markets have generally continued to perform well. 2018 has seen increased volatility, with material falls in the Spring, followed by all-time highs for the UK market in May and the US in September. More recently, we have seen further significant declines. This volatility may continue as markets struggle with political and economic uncertainty but corporate earnings and dividends have been robust and markets are generally not expensive. Our managers still see value in equities and remain cautiously optimistic.

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Katy Thorneycroft, manager, JPMorgan Managed Growth: After the very strong start to the year, we have seen a divergence in global equity returns. The US has continued to outperform versus the rest of the world and the gap between the most expensive and cheapest stocks in the market, within both sectors and countries, is reaching historical extremes. However, the economic momentum has certainly slowed from the highs witnessed in 2017, especially outside the US. Our view is that global growth is set to remain above trend, but changes to US trade policy and the impact of higher US rates have increased the risks in our outlook. We expect US policy rates to continue steadily tightening over coming quarters, but even then monetary policy will remain accommodative and supportive for risky assets into early 2019

We would note that investment trust discounts to net asset value have continued to narrow, and this warrants some caution. However, valuations of equities are not at extreme levels, and economic growth should be sustained despite tightening monetary policy.

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Fiona McBain, chairman, Scottish Mortgage: The Managers believe in the benefits of listening to and learning from those who are cleverer than they are. Jack Ma, in his last letter to shareholders as chairman of Alibaba, made the following observations: "Recently, the global economy has found itself in a state of turmoil. Uncertainties abound in trade relations, consumer trends, stock markets and the manufacturing industry. US-China trade tensions create increased risk of instability….our past experience tells us there are huge opportunities behind the anxiety and friction. The only question is how we should pivot. Monumental challenges give rise to monumental

opportunities..." The Managers agree. In the long run, only businesses which retain this flexibility to change direction thrive.

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Will Wyatt, chairman, Caledonia: An increase in volatility in October 2018 has reminded investors that stock markets are not an upward only escalator. The recent rise in US interest rates led to significant movements in both equity and bond markets. The return of a real cost of capital is bound to be reflected at some stage in the pricing of assets and a reduction in liquidity. The outcome of the current Brexit negotiations, particularly if they result in a 'no-deal' exit, could also have significant further impact on equity and bond markets.

Caledonia has recently made two significant investments in the UK manufacturing sector, underlining our belief that well-managed companies, selling high quality and competitively priced products into global markets, should be able to thrive even in the current period of economic uncertainty.

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Rachel Beagles, chairman, Securities Trust of Scotland: Global equity markets, driven by the US, have been good to investors for nearly 10 years now, driven to a large extent by low interest rates. Whilst the US economy continues to surprise on the upside, the threat of overly aggressive monetary tightening by the US Federal Reserve or an escalation of China/US trade tensions should not be ignored. Valuations in Europe are lower, but the market is right to be concerned over the fiscal path to be taken by the new Italian government, and Brexit related risks cast a shadow over the prospects for the UK and to a lesser extent Europe. Heightened volatility, such as that experienced since the period end, is likely to be a feature for equity markets as a result.

Despite this uncertain backdrop, these market moves and this increased volatility present fertile territory for a globally unconstrained stock picker.

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Mark Whitehead, manager, Securities Trust of Scotland: Recent economic data points toward a reacceleration in US activity, while Europe and the rest of the world have decoupled to varying extents. The US purchasing managers' index (PMI), a gauge of the economic health of the manufacturing sector, rose to 55.6 at the end of September 2018, which denotes a fast pace of expansion and could lead to upgrades of GDP estimates for 2018/2019. Consumer spending in the US remains robust as the tax windfall drives activity. Corporate spending is still rising, led by investment in intellectual property products and equipment, with corporate capex for the S&P 500 growing by 20% yoy in the second quarter - this should bode well for future growth. Strong corporate sales and higher margins are fuelling strong earnings and although the rate of earnings growth may slow for the second half of 2018 and into 2019, it should still be decent. Added to this, the S&P 500 has de-rated over the past nine months, as earnings growth has been so strong, while the market has fallen since the peak in late January. With all this in mind, the set-up for late 2018 is positive for the US market, unless it is knocked off course by an external influence or shock.

We believe we will continue to see spikes in volatility and sharp sell-offs in equities. There is an expectation of further fiscal and monetary tightening well into 2019, which could well be enforced to slow the US economy down and keep inflation in check. This poses a major conundrum, as too much monetary tightening could choke off activity too quickly, plunging the economy into recession; while this is not our central forecast, it is a risk we remain acutely aware of.

US and China trade wars are not helping calm volatility either and the Chinese equity market has fallen sharply, also affecting other emerging market countries. Should tensions escalate further, it could precipitate a sharp devaluation of the Chinese currency, effectively exporting deflation westwards, causing western exports heading east to slow markedly. It is likely corporates would also look to pass on higher tariffs to consumers should this happen, effectively stalling growth, either due to a response from consumers by spending less, or from central bankers, as they act to raise interest rates to quell cost- push inflation.

The outlook for Europe is, of course, more troublesome. Economic activity is rebounding a little since the sharp falls earlier in the year, but business and consumer sentiment is unlikely to improve dramatically until the UK's exit from the EU is agreed and some sort of trade accord ratified. Here, the mood music has improved a little recently, but we should expect sentiment to oscillate. If an agreement is reached, it is reasonable to expect a rebound in European equities which have struggled over the recent months. Italy also continues to be a hotbed for political altercation, with frequent disruptions likely, as new fiscal budgets and key policies are debated, impacting asset prices through a gradual degradation of confidence.

As trade wars, geopolitical tensions and market volatility escalate, we remind ourselves that high-quality, structural dividend growth stocks should offer protection and opportunity as a style, during the last stages of expansion in the economic cycle. Dividend growth has been strong year to date and many out of favour stocks not only offer defensive attributes but also look better value than they did earlier in the year.

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Sebastian Lyon, manager, and Robin Angus, executive director, Personal Assets: The American economist Hyman Minsky famously identified the 'Minsky Moment' when 'Stability breeds instability', and 2017 was a year of remarkable stability. Stock market volatility was at record lows, sentiment was positive and smooth sailing was anticipated. But high equity market valuations were flashing danger, and in retrospect 2017's stability was indeed a warning signal. In 2018 stock markets have stumbled twice, once in February and again in October. The October dip confirmed that we were entering a period of turbulence for risk assets. From the 'New Normal' of permanently low interest rates and quantitative easing we have been witnessing the attempt by central bankers to return to an earlier 'normality' of tighter monetary conditions. How this will work after almost a decade of monetary munificence is unpredictable, such an exit never having been attempted before.

To date this tightening has exhibited a classic pattern, the fringe being affected first but the effects slowly shifting towards the centre. This time it began with the collapse of Bitcoin and other cryptocurrencies in December (the dotcoms of today?). Emerging markets topped out long ago, hindered by a resurgent US dollar, while developed markets (with the exception of the United States) peaked in January. The Chinese stock market has fallen sharply this year on the threat of rising trade tensions and weaker economic data. In the US, value-insensitive buying was becoming increasingly concentrated in a short list of technology-related growth stocks. The concentration of performance in a small number of large cap stocks often occurs close to the peak of stock market cycles, and October's precipitous falls in these stocks suggest that we may have seen the peak of this cycle.

After benefiting from record profit margins and gorging on cheap debt, companies face the rising costs of labour that come with record low unemployment and a rising cost of money while vulnerabilities are now being exposed. Our concern is that after decades of falling yields, fixed income will not provide the portfolio protection it has in the past. (Interestingly, bonds failed to rally during the recent equity market falls.) However,

liquidity, in the form of cash, short-dated index linked bonds and gold, offers some protection, while currencies offer little opportunity with the exception of a resurgent US dollar.

Looking into 2019, monetary conditions are only likely to get tighter with the European Central Bank, following the Federal Reserve, committed to retreating from quantitative easing. Earnings momentum from tax cuts will begin to dissipate while GDP growth is likely to taper. However, barring a material deterioration in conditions, central bankers will be reluctant to step in and rescue markets. For those with liquidity, bargain hunting may not be too far away.

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United Kingdom

(compare UK funds **here**)

James Goldstone, manager, Keystone: The assumptions I made and wrote about a year ago were that:

- UK disposable income would move into growth territory as CPI fell and wage inflation accelerated. That would be a tailwind for domestic consumption. This has now happened and provides a powerful impetus to UK consumption growth.
- The risk to UK base rates and market rates of interest was clearly to the upside. The MPC has since raised rates twice and the 10 year gilt yield is 0.3% higher than a year ago.
- Geopolitical uncertainty was at an uncomfortable level and presented risks both to global markets and to the global economy. This has certainly worsened as trade relations have deteriorated. In theory this provides a headwind to exports and to the earnings of businesses in export or trade-dependent sectors.
- Valuation disparities were at extreme levels with US technology company shares looking particularly over-valued. Should those valuations compress, there was a risk of contagion into elevated share prices of growth companies in unrelated sectors in all regions. A number of these US shares have now de-rated and at the time of writing some of the most highly valued UK listed growth stocks are also coming under pressure.
- After years of monetary largesse, the withdrawal of stimulus via interest rate rises and quantitative tightening (QT) posed risks to the global economy and to stock markets. With the US Federal Reserve still pushing rates higher and global central banks now implementing a net reversal of quantitative easing, there is an increasing sense of unease that monetary policy may now pose a risk to global growth and therefore to stock market valuations.
- Brexit negotiations would bring volatility to UK equities, but in time this would be seen to have presented unusually attractive investment opportunities.

The global and domestic macro environment therefore looks broadly in line with my expectations. Unfortunately, the wild card that Brexit represents has become the dominant factor in the UK stock market and with negotiations heading for a perhaps predictably late and fraught conclusion, this has weighed heavily on domestically focused shares. Many of the stocks I had already considered to be attractively valued, especially financials, have therefore remained under pressure, shunned by international and domestic investors alike despite a constructive if unspectacular economy. In this process of falling out of favour, these shares have exhibited the

negative price momentum that sees them excluded from or shorted by quantitative strategies whose flows have increasingly defined the shape of markets in recent years. This somewhat circular phenomenon is still in full effect.

At the time of writing (in November) in advance of the supposed late November deadline for a Brexit deal to have been settled, and four months before Brexit itself, it is too early to judge whether this volatility brought about by Brexit has indeed presented “unusually attractive investment opportunities”.

The fundamentals of the vast majority of domestic holdings remain intact. For now at least the UK consumer still appears robust and on the basis that Brexit does not bring about the recession that is widely priced in, the opportunity to own these companies at or close to post-financial crisis valuation lows still looks extremely attractive. At the same time, to reflect the totality of the risks the wider market faces (trade frictions escalating, Italy, Iran, US fiscal weakness, risk to the US dollar’s reserve currency status, Chinese credit to name but a few), I have increased the weighting in gold equities.

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Troy Asset Management, manager, Troy Income & Growth: As we look towards the final quarter of the calendar year, 'Brexit' continues to resound through the collective British conscience. While a deal is now on the table, the initial cautious optimism and signs of support from business leaders proved to be short-lived. We find ourselves with a government divided on (i) the deal itself, (ii) leadership of the Tory party, and (iii) even the elementary question of whether Brexit should happen at all. Such uncertainty rightly breeds concern over the UK economy, but may also create investment opportunities.

US tariffs likewise have the potential to cast uncertainty wherever President Trump decides to focus his attention. There is as yet no obvious resolution to the ongoing US-China trade war, with Trump's additional $200bn of tariffs on Chinese imports sparking retaliation of $60bn in tariffs on US imports to China. The continuing crisis in Turkey, catalysed partially by US sanctions, is a sharp reminder that complacency borne of the preceding years of calm should not go unchecked. And Turkey is not the only economy witnessing dislocation; in August the Argentine peso depreciated sharply following President Macri's request that the IMF try to expedite its $50bn bailout, while Indian markets witnessed a sell-off in September due to a confluence of factors including inflation fears, widening trade deficit and a liquidity squeeze in the non-banking financials sector. Rising rates signal what was inevitable; that central banks cannot indefinitely pour money into markets to stabilise economies. This is not likely to be the end of instability in global markets.

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Richard Burns, chairman, Aberdeen Standard Equity Income: The last year has seen reasonable economic growth around the world, with the United States being the best of the developed economies, which has led to a significant rise in interest rates there, both at short and long maturities. This has not happened to any great extent in either Europe or the UK, no doubt because growth has been much less strong, but it does seem probable that the 35 year period of falling British interest rates, which saw long gilt yields decline from 16% to below 3% and was one of the main drivers of the equity market, is over. Brexit is due in little more than four months and it is still not clear if an exit deal approved by Parliament can be struck.

All this means that the investment outlook is at least as uncertain as it was twelve months ago. Careful and skilful stock selection remains the key to investment success.

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Thomas Moore, manager, Aberdeen Standard Equity Income: The recent market sell-off is a reminder of the importance of remaining disciplined on valuation. An exciting growth story does not always make a good investment if the valuation is excessive. Conversely some of the best investments can be found within unloved sectors by identifying inexpensive stocks with the potential to deliver better fundamentals than the rest of the market expects. We see many such stocks within unloved sectors such as Financials, Consumer and Resources. It is partly as a result of the uncertain economic and political outlook that these opportunities exist. We remain mindful of "event risk", in particular the potential of a no-deal Brexit. This risk of a no-deal Brexit needs to be seen in the context of very low valuations among UK stocks that have a domestic bias, reflecting a consensual bearish view on these stocks. Markets move on news that is unexpected hence the next market crisis is rarely the one that people are already worrying most intensely about. Any Brexit outcome that is less extreme than no-deal offers the prospect of material valuation re-rating.

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Ian Barby, chairman, Schroder Income Growth: Surveys suggest that the UK stock market has rarely been so unpopular with international investors as it is now. It is easy to see why - it is equally rare for the political backdrop to be as unclear - nevertheless the market has continued to provide opportunities.

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Managers, Schroder Income Growth: The global economy remains relatively robust. However, more recently there has been a slight tempering in growth expectations. This largely reflects concerns over an escalation of the trade war between the US and China. The US Federal Reserve has hiked rates another 0.25% based on strong US economic data boosted by the government's loose fiscal policy. Similarly, the Bank of England has raised rates against the backdrop of a relatively strong summer of growth and inflation data, driven by a pick-up in household spending. In Europe, quantitative easing should be over by the end of 2018, and it is expected that the European Central Bank will raise rates twice in 2019. Therefore, on aggregate, whilst the world economy remains in expansion mode, leading indicators have weakened and a more difficult period of slowing growth and rising inflation may lie ahead.

Turning to focus on the domestic economy, the UK has recovered from the slowdown seen in the first quarter of 2018, with GDP growth in the second quarter rising to 0.4% quarter-on-quarter. This pick-up came from a combination of household spending and investment. Real incomes in the UK have been positive since January 2018, in marked contrast to last year. The UK also saw an increase in employment in the first half. This has led the Bank of England to increase interest rates to 0.75%, its highest level since March 2009. It restated its intention for slow and limited interest rate rises, with three rate hikes in three years broadly expected. These market expectations are contingent on a Brexit deal being agreed. However, headline improvement has masked concerns over weak domestic demand and poor external performance, in addition to uncertainty over Brexit negotiations.

The most obvious impact of this uncertainty on UK assets will be on sterling, which may continue to be volatile as news flow swings back and forth. Sterling has been an effective mechanism for either expressing confidence or fear in Brexit and the fate of the UK economy. This is well-illustrated by a poll conducted by our economists of a mixture of investment banks and economic consultancies, asking where they thought sterling would trade against the US dollar when it became apparent which scenario the UK was heading for: no deal Brexit or a withdrawal agreement. The majority of those surveyed expect significant downside in a no deal scenario, the average estimate being around $1.10 to the pound - equating to downside of approximately 15%. In the event

of a withdrawal agreement, the average estimate is for the pound to appreciate to approximately $1.40, equalling to upside of approximately 8% from current levels of around $1.30.

The uncertainty clearly also affects sentiment towards the UK stock market, with many international investors remaining nervous about investing in UK companies. Accordingly, the UK remains one of the most out-of-favour asset classes. However, therein lies the opportunity. Despite the UK equity market being widely ignored by the investment community, corporate activity has been strong. This suggests that there are considerable opportunities in the UK equity market at present.

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John Baker and Katen Patel, managers, JPMorgan Managed Income: The domestic economic and political outlook remains unclear and is not helped by the uncertainty around the Brexit negotiations. Underlying momentum in the domestic economy remains subdued, whilst the threat of continued global trade tensions adds to the negative risks.

However, whilst UK economic growth is subdued, it is still positive. Additionally, growth in the rest of Europe has stabilised following a period of slower momentum earlier in the year and the US economy continues to do well, fuelled by fiscal stimulus.

The UK equity market continues to offer an attractive dividend yield of 3.9%. This provides some cushion, even in the event of a negative outcome to the Brexit negotiations. The floating exchange rate could take the strain if there is a no-deal outcome. Given the proportion of UK dividends earned overseas, a weak exchange rate would boost dividend-paying capacity.

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Katy Thorneycroft, manager, JPMorgan Managed Cash: The UK faces a unique set of secular and shorter-term uncertainties. The UK's impending departure from the European Union (EU) already seems to be affecting the country's medium-term prospects. Immigration from the rest of the EU has slowed sharply, a direct hit to the economy's potential growth rate. Persistent weakness in capital expenditure may also partly reflect Brexit uncertainty. Meanwhile, since the referendum the economy appears to have moved further into late-cycle territory, with the unemployment rate at its lowest level since the 1970s and inflation running close to the BoE's target. Continued growth has come at the expense of the private sector's financial position, now the most stretched in several decades, largely reflecting a very low household saving rate. The UK economy thus looks vulnerable to retrenchment in the face of shocks. This set of circumstances sets up a tricky challenge for the BoE. Purely cyclical considerations argue for steady monetary tightening even as the economy prepares for a leap into the unknown. We see an elevated risk of poor outcomes for the UK, even assuming Brexit negotiations conclude more or less successfully, and think a weakening of the currency will help the economy re-adjust in the new world.

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Andy Irvine, chairman, Fidelity Special Values: The outlook for the global economy appears to have moderated slightly and financial conditions have tightened somewhat. However, growth is expected to remain relatively robust. The outlook for investment in the UK is more subdued than this time last year due to the persistent economic and political uncertainty. We have seen financial conditions in the UK tightening as well, albeit slightly, but it remains encouragingly accommodative. Given this environment, a more discriminating approach will be required to separate the best opportunities from those that could disappoint.

Alex Wright, manager, Fidelity Special Values: The uncertainty surrounding Brexit continues. A recurring question I have been asked recently has been whether I am finding opportunities among apparently unloved UK small and medium sized companies, particularly post Brexit. This reflects a strong consensus belief, reinforced by fund manager surveys and press coverage, that UK small and medium sized companies are deeply out of favour and under-owned compared to their larger and more international cousins in the FTSE 100. Looking at performance and valuation data since Brexit (June 2016), we see a different perspective on this one-sided narrative. In reality, small and medium sized companies have outperformed the FTSE 100 since June 2016, continuing the trend of previous years.

Although all of the market has de-rated, the FTSE 100 is now much cheaper on forward earnings estimates than the more domestic FTSE 250 and I have incrementally been finding more interesting new ideas in large sized companies.

In the 6 years I have been managing the portfolio, the UK market has delivered returns of almost 10% per year on an annualised basis. This is well above very long term historical averages, and it would probably not be wise to expect such unusually high returns to continue indefinitely.

However, I am feeling increasingly positive on the performance outlook for the UK market – particularly relative to other markets. The reasons I am positive chiefly relate to how negative everybody else seems to be. Most investors I meet are underweight in UK stocks, and many global investors avoid holding UK stocks at all if they can help it. The Brexit narrative has meant UK assets have become deeply unloved, and therefore interesting from a contrarian point of view. One thing I have learnt from investing in unloved companies is that you shouldn't necessarily wait for the good news to become obvious before investing. By investing when all the bad news is 'in the price' and no good news is expected at all, then you put the odds in your favour. I believe that whatever the outcome of the negotiations with the EU, any improvement in clarity could result in a period of stronger performance for the UK market. Investors will use any sort of agreement as a catalyst to revisit the UK market, and find that it contains many good quality undervalued companies, particularly compared to other developed markets, such as the US, where valuations are much higher.

That said, I still believe that a selective approach remains important. Not all stocks are equally attractive, and although many domestic businesses are being unfairly ignored, others are structurally compromised, financially unsound and therefore best avoided. Attractive valuations are now to be found in more defensive and large-cap parts of the market, although the financials sector remains a fertile source of ideas. There is certainly a plentiful supply of unloved companies in the UK market today.

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Hugh Aldous, chairman, Downing Strategic Micro Cap: Markets decide, from time to time, that a correction, a 'reset' is needed. Such a view has now triggered a correction coupled with a more sober view of global growth. Nothing catastrophic has happened - yet, although Janet Yellen has pointed out an increase in doubtful lending. At times like these it is even more important that stock selection should be value driven and should grip sound earnings and long-term value.

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Mark Barnett, manager, Perpetual Income and Growth: Over the course of 2018 the UK stock market has been range bound, effectively fluctuating within a 10% range. This pattern is likely to continue for the foreseeable future until the market has clarity over two key issues, namely the extent and duration of rising US interest rates and Brexit. The political uncertainty has been especially damaging and has resulted in a wide

degree of polarisation within the market. Companies with substantial overseas revenues have benefitted from the devaluation of sterling and by contrast, UK domestic orientated stocks have generally performed poorly and remain undervalued relative to the broader market.

The extent of this relative cheapness is substantial and although the overall market is not expensive at present the most glaring opportunities rest within domestic sectors. Many are valued at multi-year lows both in absolute terms and relative to the wider market and are discounting a sharp deterioration in profits and a slowdown in the UK economy, both of which look overly pessimistic. Recently published economic indicators point to continued steady, if unspectacular, economic growth in the UK. The level of GDP growth can reasonably be expected to be higher over the remainder of the year, supported by robust employment growth and a recovery in real wages, which in turn should help to strengthen consumption growth. Given the forecast increase in government spending next year and the Treasury's flexibility to provide further injections after the Brexit date, it is reasonable to expect the UK economy to be more resilient than most forecasts assume.

The drawn out Brussels negotiation has exacerbated a pessimistic consensus towards the UK. Oil and Tobacco remain attractively valued in a market driven by short-termism and an emphasis on new disruptive business models in all industries.

In recent weeks the return of more volatile markets has suggested a breakdown in momentum style investing which has been such a powerful characteristic of the multi-year bull market. It is to be hoped that this change will herald a return to valuation based investing with an emphasis on fundamental company analysis.

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Robert Talbut, chairman, Shires Income: Since the end of the period, there has been increased volatility in markets, with a combination of rising interest rates and global geopolitical concerns causing some material sector and stock moves. However, with economic growth globally still positive and earnings growth remaining strong, the manager remains reasonably confident on the potential for equities to deliver positive returns.

While the UK economy continues to move at a slower pace than many developed economies, there are clear attractions to UK equities and the manager recently upgraded the UK to be its preferred equity market. Brexit worries have driven international investors away from the UK and the market is relatively inexpensive. While the shape of Brexit remains uncertain, many companies are insulated by their overseas earnings and dividends paid by UK companies are a significant contributor to total return.

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Manager, Montanaro UK Smaller: UK SmallCap has once again become attractively valued, sitting below its long-term average Price-to-Earnings ratio and looking cheap compared to European and US markets. Brexit may well explain much of investors' lack of appetite for the asset class. However, investing on the basis of politics has proven unwise in recent times. Those who remain in - or choose to return to - UK SmallCap, may find themselves well rewarded in the years ahead.

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Jane Tufnell, chairman, Odyssean: The long-term investment case for smaller companies is well documented and accepted - namely, that patient long-term investors are rewarded with superior returns. It is an imperfect market and the board shares the

view of the portfolio manager that recently introduced legislation is and will continue to exacerbate some of the market imperfections.

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Stuart Widdowson and Ed Wielechowski, managers, Odyssean: Volatility has dominated the period since the end of September 2018. Highly valued companies have appeared to be first in line to bear the brunt of the sell-off. We anticipate that this volatility will continue to create opportunities.

For the first time in four years, there is obvious value in UK markets, which appear to be shunned by international investors. Anecdotal evidence suggests that MiFID II is leading to less communication between buy-side and sell-side market participants. We believe that this could be contributing to what we perceive to be increased share price volatility and polarised valuations.

However, value is not ubiquitous, and despite a de-rating of expensive, higher growth AIM momentum stocks, many still appear to trade on considerable premia to takeout multiples. Buying shares in these companies seems to us to offer a limited margin of safety.

Where we are finding pockets of value, the key judgement call is whether companies' earnings projections are realistic. To help mitigate this, we remain focused on finding companies which are generating margins below their peak and potential, but where we believe there is limited downside. These companies should be able to grow profits through management actions, even in circumstances where sales growth may prove challenging.

Liquidity remains patchy, bid offer spreads remain wide and individual share price volatility remains high. There is no evidence to date of material outflows from open-ended funds.

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Europe

(compare European funds **here**)

Michael MacPhee, chairman, The European Investment Trust: This has been a challenging period for European investment and Europe in general. Slightly improved economic growth does not tell the story very well. Tectonic plates appear to be shifting. Underlying stresses within the European Union and the populations comprising it have come increasingly to the surface, as has been the case elsewhere. Diverging economic outcomes between nations and within them remain quite extreme. Trends within stock markets have been equally marked and every bit as apparent. Lowly valued companies have been swept aside by fervour for more clearly rapidly growing businesses. The combination of low interest rates, low discount rates and high assumed future revenue and profits growth has dominated other factors. Mean reversion in both interest rates and stock markets has not entirely disappeared, slow and steady does it over time, and banks, oil companies, telecommunications and pharmaceuticals businesses, for example, are still capable of generating worthwhile absolute long-term returns for their shareholders from a position of some competitive strength and undemanding initial valuations.

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Craig Armour, manager, The European Investment Trust: Economic fundamentals remain positive in Europe. Employment is growing and wage inflation is in evidence. The European Central Bank has confirmed the end of monetary easing with asset purchases to cease in December 2018 and that interest rates are likely to rise in the second half of 2019. However, there are a number of threats to this positive growth outlook. In Italy, an unusual alliance of the political left and right is proposing to increase government spending and reverse some of the structural reforms of the previous government. These policies put Italy at odds with the European Commission and could lead to renewed sovereign debt fears. The unresolved Brexit process represents another threat, particularly to countries and sectors with substantial trading links with the UK. However, the most significant risk comes from US trade policy, where the imposition of protectionist trade tariffs is bound up with an aggressive approach to China, which is adversely impacting industrial stocks and companies with emerging market exposures.

Our central investment case is for ongoing recovery and modest economic growth in Europe, supporting a rise in the cost of money. This should lead to a reduction in the valuations of highly rated growth stocks and an improvement in the performance of stocks with lower growth expectations and starting valuations. However, with growing threats to the growth outlook, it is essential to maintain a focus on risk as well as reward.

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Francesco Conte and Edward Greaves, managers, JPMorgan European Smaller Companies: The recent rise in the US 10 year bond, at one point to above a 3.2% yield, reduced the appetite for stocks across all geographies, including Europe. On this side of the Atlantic, fears about the Italian budget and continued uncertainty around Brexit added to the general malaise. The US mid-term elections in the US resulted in a split Congress, meaning the recent loosening of fiscal policy, through tax cuts, is unlikely to be repeated. This has been a driver of higher US interest rates, and therefore we see a standstill here as a positive. In Europe, with Italian 2 year yields close to 1%, bond markets are signalling that political risks are manageable. In summary, we believe the volatility in October was a long overdue correction, rather than start of a more prolonged downturn in markets.

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Stephen Macklow-Smith, Alexander Fitzalan Howard, Michael Barakos and Thomas Buckingham, managers, JPMorgan European: European growth is expected to be above trend once again in 2019, and this should bring a further fall in unemployment, which will support consumer confidence. Government spending across Europe is anticipated to expand, and increased tightness in the labour market should encourage companies to invest more in capital equipment. The construction sector looks in good health, and with the rest of the world continuing to grow exports should hold up. In theory this should make for a bright future for corporate earnings, but political clouds are likely to remain. There is uncertainty regarding the extent to which the US will apply trade tariffs, particularly whether they will extend to include car manufacturing and component industries. The UK's future trade relationship with the EU has not started to be negotiated formally, although a withdrawal of the type currently being proposed by the UK government would leave the situation very much unchanged for the transition period that would start in April of next year. The Italian government is likely to keep pushing for a budgetary target that exceeds the EU's rules, although here the bond market could temper their ambitions if spreads (and therefore interest costs) continue to rise.

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Asia ex Japan

(compare Asian funds **here**)

Schroder Oriental Income: Arguably all purely financial forecasts and considerations are trumped (pardon the pun) by major, and by their nature unpredictable, political considerations. The most prominent surrounds the current poor relations between the US and China, which go far beyond mere trade considerations. However, other imponderables include whether Italy will ever have the political will to do what it takes to create a competitive economy (rather than muddle through), Brexit, and, most critically, whether the Chinese leadership holds the line accepting lower trend growth as the price for long-term financial sustainability.

Some or all of these issues may be amenable to at least short-term outcomes that are better than the consensus would suggest. However, the global economic and financial fundamentals are troubling, namely an unbalanced growth picture between the US and the rest, tightening liquidity, and the rising risk of more systemic financial shocks resulting from mis-priced risk eg loan funds, peer-to-peer lending, ETFs, remarkably low spreads in the high yield market, and multi-layered "risk free" infrastructure funds.

A stronger dollar, rising interest rates, trade tariff pressure from the biggest bilateral trade partner, and related faltering in investor and corporate confidence are not a great combination for the relatively trade-dependent and open economies of Asia. In general, the vulnerability to external financial shocks is lower across the region, certainly when compared with the 1997/98 crisis, and with 2013 during the "Taper Tantrum".

Of greater concern are the prospects or otherwise for a smooth transition to a lower, but more sustainable, growth model for China. Our central view remains that the authorities can manage a soft landing consistent with its desire for a less credit intensive growth model. Attacks from Washington are certainly not making the process any easier. However, it is also being made more complicated by less favourable country-specific factors including a shift towards a current account deficit, elevated levels of domestic credit, and increasing vulnerability to capital flight. Combinations of marginal credit loosening, modest rise in spending and a gradual depreciation of the Renminbi accompanied by discouragement of capital outflows may still do the trick, but in our opinion scope for a more marked stimulus package looks limited.

Having said all that, regional markets are within a few per cent of the valuation lows seen in late 2015/early 2016, suggesting that investor caution is already elevated. A destabilising event in China remains a possibility rather than an imminent likelihood, and some progress on US/China relations is not out of the question.

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Hugh Young, manager, Aberdeen Standard Asia Focus: I have to say that I'm more cautious than optimistic over the short term, given the current macro climate. Will share prices go down further from here? Yes. Should I be worried? No, because it's an opportunity for me to buy more. If we do thorough research and keep our heads on straight, our chances of long-term success are good. Looking back at some stage in the future, I suspect we'll see this period as being yet another market pull-back that provided an excellent buying opportunity.

I think Asia remains as exciting as it was when I first landed in Singapore in 1992 to set up Aberdeen Standard's local office. The region has so much to offer, so much to change and so much more in terms of growth and prospects for companies and

investors. It is still the world's fastest-growing region, and I think it will remain dynamic for many more years to come. I think Asia is a fertile hunting ground.

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John Russell, chairman, Henderson Far East Income: The outlook for the world we know best, the post WW2 liberal democracy, which created the elevated standard of living we enjoy, is under threat. It is not possible to conjecture how this might unfold and what the consequences might be.

By contrast, the Asian world we invest in seems to be on track to continue to deliver strong economic outcomes and rising standards of living. China has a plan and is very unlikely to be blown off course by events in the west. It appears that China concluded in the summer that President Trump's tariff play is mostly about halting or at least slowing the rise of China as a global power. This is unfortunate as China will do whatever it takes to stay on track and it does raise the prospect of a much more aggressive response to US imposed tariffs. There are two milestones the Chinese leadership are determined to meet. The first is to build a "moderately prosperous society" by 2020, the 100th anniversary of the creation of the communist party in China and the second is to become "a great modern socialist country" with living standards similar to European standards by 2049, the 100th anniversary of the creation of the People's Republic of China. It is very difficult to foresee what events would force China to deviate from their plan.

Of course, coming months will be very testing for China if the US continues with current policies. Will the leadership be up to the task? The success of the past 30 years suggests they will at least be able to limit the damage and continue to follow their objectives.

China's response to the tariff increases thus far has been restrained and proportionate. Policy makers are signalling clear easing in monetary and fiscal conditions to compensate for the impact on growth the tariffs are likely to make. Current estimates suggest nominal GDP growth could be dragged down by 0.3% to 0.5% over 2018/19 to a number closer to 6.0%.

A further concern is whether tariff changes will encourage businesses to move production out of China to other Asian countries notably, Indonesia, Vietnam or Cambodia. This is a risk but modern business requires high quality transport and communication infrastructure and access to a highly trained workforce. This is available in China but much less so elsewhere.

On top of these developments for investors to absorb came the highly negative western press response to the removal of the Presidential term limits almost universally dubbed as "president for life" and a "personal power grab" by President Xi.

While concerns are understandable the reality is somewhat different. The real power in China lies with the General Secretary of the Chinese Communist Party, a role already held by Xi, and this post has never had term limits. The role of President was restored in the 1982 Chinese constitution and its main function is purely to enact the decisions of the National People's Congress. Deng Xiaoping pushed a policy of administrative separation between Government and Party, a necessary reform at the time. Since that time the Party has developed into a highly effective governing institution as the developments of the last 30 years demonstrate and all the leading functions of Government are now centred within the CCP. Fusing together the head of state and the Party is making the system of Government more transparent and reflective of political reality. On the available evidence concerns seem somewhat misplaced.

As US global engagement declines, China will become more dominant in the region with other Asian countries becoming more closely aligned to the Chinese economic development model. The impact on the region and the cross border trade it will encourage will further cushion China from adverse policies emanating from the west.

All this adds up to a strong investment case for the region. Valuations in the region are quite low by comparison with the west and dividend growth is strong. As analysis shows dividend flows play a very important part in long term investment performance. As a recent Janus Henderson report demonstrated, dividends from Asia Pacific companies rose by 12.7% in the year to May 2018 and have tripled since 2009 substantially ahead of the rest of the world and streets ahead of returns from money market funds over the period.

In a troubled world, portfolio diversification is even more important than normal. Despite the risks, the Asia Pacific region remains an attractive investment destination particularly for savers taking a medium to long term view and seeking growing levels of income.

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Michael Kerley, manager, Henderson Far East Income: We remain cautiously optimistic on the outlook for Asia Pacific in the medium to long term. Forecast earnings growth is off its highs but still expected to be double digit while valuations have corrected as market volatility has increased. There are obvious risks from rising US interest rates, a stronger US dollar, which would tighten liquidity, increased trade and geo-political tensions and contagion from emerging markets but we feel, at current levels, these are reflected in prices.

Our focus remains on domestic orientated areas which are exposed to the improving spending power of the consumer across the region and away from the export orientated sectors which are exposed to a slowdown in global growth and an increase in protectionism. In our opinion China offers the best combination of value, growth and dividends in the region and remains the largest part of the portfolio. At the sector level we are positive on financials, energy and materials and cautious on high priced technology.

The outlook for dividends in Asia Pacific is still the most compelling story. Asian companies have low levels of debt, a pragmatic view on capital expenditure and strong cash flow generation which should allow dividend pay-out ratios to rise in the years ahead.

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Allan McKenzie, chairman, Edinburgh Dragon: Like the rest of the emerging markets, the situation in Asia appears bleak at first glance, especially in view of the US dollar liquidity crunch, the US induced trade war, the tensions in the South China Sea and the Fed's planned interest-rate hikes.

Deeper analysis suggests that Asia does not face the same challenges as those emerging economies currently under such close scrutiny. This is because none of the Asian countries is in the same boat as those in the other troubled regions, having learnt well the lessons from the 1997 financial crisis. Inflation is relatively low, economic growth is still resilient and central banks have been uncompromising in their approach. Indonesia, which was identified lately as being vulnerable to the emerging markets contagion, saw its central bank raise interest rates successively to quell inflation and staunch the rupiah's decline.

Fears over China's moderating growth rate and elevated debt levels appear overdone as well, chiefly because its financial system is a closed one, with little likelihood of spill-over impact if the situation goes awry. In addition, Beijing has been responsive and shown a steady hand during difficult spells. It could also bring to bear its massive arsenal of foreign exchange reserves that stand at more than 1.5 times that of Japan, the next nearest country on the World Bank's top five list.

On the US-China trade war front, while shots have been fired and tariffs imposed, both sides have nevertheless shown restraint in not pushing for the maximum amount flaunted in the rhetoric. This supports the view that all the sound and fury has merely been posturing so far and both countries have left ample room for future negotiations. President Trump's "Art of the Deal" approach to trade relations is starting to become somewhat predictable, with his opening gambit giving way to a subsequent more composed compromise, as was the case with the recently concluded NAFTA deal, now known as the United States-Mexico-Canada Agreement.

With these factors in mind, the outlook for Asia seems relatively positive.

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Aberdeen Standard Investments (Asia), manager, Edinburgh Dragon: Given prevailing trade tensions, investor sentiment has turned more wary, and politics and policy will likely continue to hold sway over Asian markets. Many companies are shelving investment plans, which could dampen near term economic growth in the region. There are also other market specific issues that could present challenges to the portfolio's underlying holdings. In India and Indonesia, political risk may feature more prominently given upcoming elections. Beijing's delicate tightrope between reducing risks in the financial system and sustaining growth could have wide reaching implications. More broadly, central banks in the region also have to grapple with defending their currencies and maintaining price stability, while contending with rising commodity prices, tightening US monetary policy and a strengthening US dollar.

However, many Asian economies are in better shape, with healthy external balances and foreign currency reserves. Corporate fundamentals remain resilient too.

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Harry Wells, chairman, Martin Currie Asia Unconstrained: Since the end of September, there have been sharp falls in global markets, especially in Asia and emerging markets, on fears of slowing global growth and, in particular, speculation of pronounced weakening in China's domestic economy. In response, the Chinese have reduced banking reserve requirements and they have the arsenal to implement domestic stimulus programmes, if they so wish. A weakening Renminbi may partially offset the cost of tariffs to American consumers. However, exports now represent only a fifth of China's GDP and growth in inter- regional trade is a sustainable trend. India has always been driven by the domestic economy and South Korea is heading that way, a far cry from the export model of 30 years ago. These "power houses" should continue to reap the benefits of the rise of aspiring middle-class consumption on the back of steadily increasing per capita income growth.

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Manager, Establishment: The Asian region continues to face particular headwinds. The Federal Reserve continues to tighten monetary policy with four interest rate increases of 25bps in the past twelve months and to shrink its balance sheet. Further tightening is forecast as a corollary of a strong American economy. This has placed pressure on most Asian currencies with the Bloomberg-JPMorgan Asian Dollar Index declining 7% since March 2018. The index is approaching the lows seen in early 2009

and 2016. Within Asia, it is those countries with weaker balance of payment positions that have felt the most pressure on their currencies, notably the Philippines, Indonesia and India.

The imposition by the United States of 10% tariffs on $250 billion of Chinese exports, which may increase to 25% in January 2019, along with the threat of tariffs on a further $270 billion of exports, continues to weigh on sentiment not only in China but across the entire trade orientated Asian region.

The imposition of sanctions on Iran by the United States has led to heightened concerns on the potential supply and demand imbalance in the oil markets. These sanctions come into place at a time of limited exploration activity by global oil majors and production issues in Venezuela and Libya. Brent Oil prices rose by 25% to over $80 per barrel during the period under review. Asia is energy deficient and rising oil prices place stress on the trade accounts and inflation profiles of the regional economies.

Forthcoming national elections in India, Indonesia and Thailand pose some a degree of political uncertainty.

As always, the question is how many of these 'headwinds' are now priced into markets. Your manager believes that the majority of the bad news is now 'in the price' with regional equities trading on circa 11x 2018 earnings and at 1.3x 2018 book value. Economic growth across the region may slow somewhat but the strong secular drivers of growth remain in place and we remain optimistic.

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Japan

(compare Japanese funds **here**)

Andrew Fleming, chairman, JPMorgan Japanese: There are three particularly important developments that are likely to impact the outlook for Japanese quoted companies: the first is the continuing general improvement in Japanese corporate return on equity; the second is the scale of the Bank of Japan's quantitative easing ('QE') programme which now stands out globally in scale and reach and the third is Japan's exposure to global trade in general and the Chinese economy and supply chain in particular.

Japanese quoted company operating margins and returns on equity are now on average the highest for 30 years with the latter, for example, having risen in aggregate to over 10%. Similarly, the ratio of current profits to sales is the highest for 30 years. Foreign investors, fixated as they have been by returns from US companies in recent years, have been very large sellers of Japanese equities so there is the real potential for these flows to reverse if these improvements in performance can be maintained. The second important positive for Japanese equities has been the Bank of Japan's (BoJ) bond and asset-purchase programme. The bond-purchase programme has been adjusted to maintain long-term interest rates effectively at zero, and the equity purchases continue on a huge scale albeit to buy into market falls rather than the earlier more indiscriminate buying programme. The BoJ now owns approximately half the government bond market, and nearly three quarters of equity ETFs and is now a top ten shareholder in over 40% of TSE-listed companies.

The big risk for Japanese equities is the potential for a slowdown in global growth and /or the dislocation of global trade flows through greater protectionism. In both respects

it is worth noting that Japanese companies now trade more with China then they do with the United States.

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Nicolas Weindling and Shoichi Mizusawa, managers, JPMorgan Japanese: The Japanese market is more cyclical than other developed markets and can be impacted by global economic developments, both positively and negatively. Currently there are concerns about a potential trade war between the United States and China. In addition, Chinese macro data is weaker than recent years and negotiations for a new trade deal between the United States and Japan are at an early stage. However, we continue to see robust corporate earnings growth, progress on corporate governance reform and good economic activity in Japan.

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Nick AC Bannerman, chairman, Baillie Gifford Japan: It is worth reflecting on [*macro issues*] given that Prime Minister Shinzo Abe recently won the leadership contest in the ruling Liberal Democratic Party by a wide margin. This prospectively leaves him in office until 2021 as Japan's longest serving Prime Minister. Debate about his likely legacy focuses on an expansionist economic strategy (known as Abenomics) and on constitutional reform covering the role of the Self-Defence Forces. The Prime Minister has expressed his firm intention to go ahead with the previously delayed increase in the sales tax from 8% to 10%, in October 2019. A further notable event is set for May with the Imperial succession when Crown Prince Naruhito takes over on the abdication of His Majesty Emperor Akihito.

Against the background of an ageing population and low birthrate, the labour market is extremely tight thus stimulating labour market related innovation among companies.

Corporate governance remains an important pillar of the Government's economic programme. Under the revised Stewardship Code, disclosure, fiduciary responsibility, increased return on equity and reform of cross-shareholding are all highlighted and we have been pleased to see something of a watershed in corporate leaders' prioritisation of shareholder interests.

The economy has grown for six successive years and, despite some distressing and damaging natural disasters this year, the signs are encouraging for 2019. There also remain some political tensions in the region, especially over US-China trade relations.

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Eiji Saito, Shoichi Mizusawa, Naohiro Ozawa and Michiko Sakai, managers, JPMorgan Japan Smaller Companies: There are structural and long-term trends, or themes, that underlie much of our stock selection. These trends include changing demographics, technological innovations and international trade, including tourism. Japan faces slower economic growth due to changing demographics, but some Japanese companies are working to improve the quality of life for an ageing population. Technological innovation is now happening everywhere in Japan. Although Japanese companies are often by nature very conservative, due to the tight labour market caused by a shrinking workforce, many old-fashioned Japanese companies are having to pursue innovation. Moreover, Japan is in a good position to capture the benefits of high economic growth across Asia, as this creates new customers for Japanese goods, services and brands.

Another important change that has taken place in Japan over the past five years has been the improvement in corporate governance, which began with the adoption of a stewardship code and was followed by a corporate governance code.

This has resulted in steady increases in both dividends and share buybacks, a rise in the number of outside directors sitting on company boards, and more companies specifying returns on equity and/or asset targets. Although the pace of change is moderate, we believe this trend will endure.

The outlook for Japanese equities remains positive. We believe that global economic growth will continue at a healthy rate, though this may slow due to the US-China trade war. The lack of inflationary pressure suggests that the risk of aggressive tightening in monetary policies around the world is low. Although the Japanese equity market has performed well in the last three to five years, this is largely attributable to earnings growth rather than increasing valuation measures and so the market remains attractively priced.

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Manager, Aberdeen Japan: Japan's stock market has tumbled significantly after the close of the review period. China's moderating economic growth as well as the escalating US-China trade war are casting a shadow over the country's growth prospects, and both the US and China are major buyers of Japanese goods.

In light of these uncertainties, Japanese corporates remain cautious as ever: expansion plans are being slowed, whilst production is gradually shifted elsewhere in light of potentially heavier tariffs on exports from China. At this juncture, we believe it is important to distinguish between shorter-term cyclical issues and the prospects of medium- to longer-term structural growth. Factory automation stocks have fallen on the back of weaker orders, but the needs of an aging demographic and of improved manufacturing quality in China and elsewhere aren't going away. Similarly, the rise of China's middle class puts Japanese products in a favourable position.

This period of volatility, driven by macro concerns, may provide longer-term investors the opportunity to take advantage of more attractive valuations.

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Global emerging markets

(compare global emerging markets funds **here**)

Paul Manduca, chairman, Templeton Emerging Markets: It is unlikely that the trade dispute between the USA and China will dissipate quickly and there are headline-grabbing issues in some emerging markets such as Turkey, Pakistan and Argentina, all of which are serving to unsettle markets. Nevertheless, there are many reasons to be positive about the long-term outlook. Emerging markets are diverse with different economic and political drivers. As a general comment, and notwithstanding the market volatility in October and November, your Board believes that emerging markets are in good health and issues in countries such as Turkey, Pakistan and Argentina do not reflect the asset class as a whole, and furthermore those countries are small in comparison with the rest of the emerging markets universe.

Investment in emerging markets is no longer based on the availability of commodities or cheap labour to supply developed markets. Growing GDPs and individual wealth have led to growth in intra-regional trade, while technology and high-quality manufacturing have become key drivers of economic growth and hence investment opportunities.

Chetan Sehgal, manager, Templeton Emerging Markets: While investor sentiment and markets continued to be volatile after the reporting period, with further declines in October and into November, our view is that valuations reflect a more pessimistic scenario than we currently envisage for emerging markets over the medium-term. We remain positive on emerging markets, even as challenges in some countries dominate the headlines. The asset class is broad and diverse, comprising countries with differing economic drivers and levels of political risk. We believe that weaknesses in markets such as Turkey and Argentina are not likely to result in macroeconomic contagion, and we think that contagion fears should be seen in the perspective of the overall health of emerging markets.

Collectively, emerging markets show stable fundamentals. They are still widely expected to achieve faster economic growth than developed markets in the years ahead, extending a trend that has been evident for some time. Within emerging markets, new areas of growth are driving economies.

The much-vaunted demographics of emerging countries are at play too. Numerous companies are poised to benefit from increased market penetration as a young and growing middle class spends more on goods and services. Rising affluence should also continue to drive the "premiumisation" trend that is spurring demand for high-end products.

We still see many investment opportunities in Asia, including China. US trade tariffs on China have come at a challenging time, when its labour-cost advantage is fading, and it is embarking on the process of reducing debt. However, we believe reducing debt and supply-side reforms could help to ease structural risks. Meanwhile, China's shift towards innovation, technology and consumption as new drivers of growth supports more sustainable corporate earnings.

In the last decade, China has outgrown the United States to become a more important export market for most large emerging economies-not least due to its burgeoning consumer market-and, accordingly, trade growth now predominantly comes from rising demand from other emerging markets. Rising protectionism in the West may further pivot the focus towards regional agreements.

Latin America also offers interesting investment opportunities. We believe that Brazil's new president is likely to press on with reforms, and this should bolster the country's long-term prospects. Corporate earnings have also been resilient, as many companies underwent adjustments and reduced costs to weather the previous recession. In Mexico, if the new administration can deliver on its promises and preserve solid economic fundamentals, we could see healthy growth this year and in 2019.

Meanwhile, Russia remains home to companies that have fared well despite macroeconomic and geopolitical challenges. The country's energy producers are some of the largest in the world and enjoy cost advantages in an environment of robust oil prices. Rapid growth in e-commerce and other internet services has turned local internet firms into global leaders. We are also seeing signs of an increased focus on corporate governance in the country.

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China

(compare Asian single country funds **here**)

Dale Nicholls, manager, Fidelity China Special Situations: Chinese stock markets [*have been*] volatile. Additionally, October saw one of the sharpest monthly falls since the global financial crisis of 2008.

The prospect of much higher trade tariffs is clearly a concern: there are no winners in a trade war. Chinese exporters will see higher import duties on their products sold in the US and the US consumer is likely to see higher prices and increased inflation as a result. While Chinese exports to the US as a proportion of their total exports globally has been falling for years as China has expanded its global reach and trading partners, increased tariffs will impact the export sector. Of greater concern is the broader impact on general sentiment and the prospect of delayed investment by Chinese companies in general.

There has been a slowdown in the rate of growth of consumption, particularly in larger durable goods such as cars. This has not been helped by falling markets and the sense that house prices have peaked. Whilst there has been a tapering-off in consumption growth, I do not see signs that we are entering a major adjustment: growth rates in China remain the envy of most economies. Retail sales are still showing year-on-year growth of 9% despite the decline in car sales. The vast majority of the companies we focus on continue to deliver solid earnings growth.

China is a volatile market so there are always such risks. I take comfort from much lower valuations following the recent falls and the fact that negative factors overhanging the market have been well publicised. Even with a general economic slowdown, the medium term prospects for earnings growth remain strong. The current level of the stock market may or may not be the bottom of the market, but I am confident of long-term growth from these levels.

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India

(compare Asian single country funds **here**)

Hasan Askari, chairman, Aberdeen New India: A more testing period awaits India. Moderating credit growth, due to the troubles in the financial sector, could have wide reaching implications across the economy, including the incipient consumption recovery. It could also dampen industrial activity, which has remained stubbornly sluggish despite robust headline growth. The outlook for corporate earnings has also diminished. Companies are turning more cautious as higher energy prices add to cost pressures. Politics is another concern, and not just due to uncertainty over the 2019 general election outcome. Prevailing global worries, including an intensifying trade war, strengthening US dollar and tighter monetary conditions, will also sway sentiment.

India [*has*] continuing structural advantages, including a growing middle class and expanding infrastructure development. Thus, while there will be bumps along the way, the Board remains cautiously optimistic.

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Managers, Aberdeen New India: In the near term, geopolitical and trade tensions will continue to test both Indian equities and the currency, which has depreciated significantly on global and domestic concerns. At home, tighter liquidity conditions, a weaker rupee and higher oil prices could hamper capital investment and growth. In such an environment, companies with pricing power and solid balance sheets should emerge stronger.

Meanwhile, growth in this large domestic focused economy should help buffer it against external shocks. Rural growth remains healthy and a consolidation in the financial sector should help the economy in the longer term. In addition, the weaker currency has helped the export oriented sectors and earnings upgrades are gradually broadening out across most industries.

Looking ahead, we are more cautious in light of the emergent political concerns and we may see market volatility in the run up to the election. While the current ruling party BJP is expected to stay, a reduced majority could force the government into a coalition. However, this should not derail reform agendas.

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Emerging Europe

(compare Emerging European funds **here**)

Frances Daley, chairman, Baring Emerging Europe: Emerging Europe provides a highly uncorrelated investment universe which is prone to examples of both stellar performance and pronounced weakness from different parts of the region within one reporting period. For this reason, it is hard to generalise about the region without dividing it up into its component parts, noting the importance of both asset allocation and stock selection to performance:

Whilst one should not underestimate the effects of US sanctions, particularly if these are tightened in the future, Russian economic progress continues, which should benefit domestically focused companies. The fall in the Ruble helps exporters, especially in the energy sector where they benefit from lower Ruble costs whilst reporting income in US Dollars. With valuations low despite rising earnings and dividends, it is clear, that the market currently prices in significant further deterioration in the overall political situation with a knock-on effect on the Russian economy. Whether this is justified remains to be seen.

We are cautious about Turkey. Nevertheless, current valuation levels are very attractive following government monetary policy measures to stabilise the Lira.

We are used to geopolitical concerns affecting performance in Emerging Europe but, as I write this, global markets are also showing volatility over a lengthening list of investor worries including the possibility of a US trade war with China, Italy’s budget wrangles and fears of a disorderly Brexit. Inevitably our investment universe will be drawn into this, so the important thing is to focus on the investment fundamentals over the medium term and try to look beyond the noise from short-term elements we cannot control.

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Manager, Baring Emerging Europe:

Russia

While Russia hosted the Football World Championship to widespread acclaim, geopolitics remained centre stage and provided the backdrop for Vladimir Putin's presidential election victory in March. It is fair to say Russia's relationship with the US and the UK has reached a low point amidst continued allegations of US election interference and the Skripal case in the UK. This led to the eventual imposition of US sanctions on individuals and companies in Russia. The Kremlin's relationship with the EU, Turkey and China, however, subject to a higher degree of Realpolitik, saw signs of renewed engagement. Examples include French President Macron's visit to the St Petersburg Economic Forum, where a multi-billion dollar investment of the French energy supermajor Total in Russia's multi-billion USD Arctic Liquified Natural Gas project was unveiled; Germany's grand coalition's agreement to adhere to the extension plan of NorthStream, the gas pipeline in the Baltic Sea. Further examples were evident in Turkey where President Erdogan toyed with the idea of equipping NATO's second largest army with Russia's state-of-the-art S-400 missile defence system or the Chinese e-commerce giant Alibaba's announcement at the Vladivostok Eurasia Summit to pursue a multi-million USD joint venture with Russian internet firm Mail.Ru.

Over the period, the Russian economy benefitted from rising oil production, a direct result of the OPEC+ Russia agreement which has supported industrial production, while overall household consumption and investment remained muted, which we believe to be a direct consequence of sanctions. Elsewhere, the increase of the pension age and the planned rise in VAT served to support ambitious plans for infrastructure investment and increased spending on education and health. Widespread public condemnation of the pension reform eventually lead to a dilution of the original plans, showing that implementing unpopular reforms remains difficult everywhere, regardless of the political system. The Russian government's plan to lower the economy's oil dependency, lowering the Ruble's sensitivity to global oil dynamics, started to take form through the introduction of a budgetary fiscal rule. This fiscal rule aims to feed surplus energy sector-related revenues from the budget to the National Wealth Fund, which is intended to be released to the budget in times of falling oil revenues, i.e. counter-cyclically. The effect of this policy on the Russian Ruble can already be felt as it has rendered the currency less susceptive to oil price swings, a development we welcome as it allows for a more balanced long term development of the economy.

Turkey

Turkish financial markets have transitioned through a period of extreme stress this Summer as an indecisive monetary framework combined with political interference and rising inflationary pressures undermined the Turkish Lira's credibility, pushing the country's financial system to the limit. This was brought about by a number of events beginning with a lax fiscal attitude in the run-up to early presidential and parliamentary elections in June, while the continued erosion of the country's institutional framework, exacerbated further by a sharp deterioration in bilateral relationship with the US served to portray a narrative that undermined the credibility of Turkey. This led to a crisis of trust that manifested itself into a situation where the Turkish Lira declined considerably shedding more than 1/3 of its value within a concentrated period of time. While the Turkish economy had shown signs of overheating prior to these events, market participants had priced in the expectation that Erdogan would instigate a more realistic approach to economic and foreign policies once he was able to fulfil his grand ambition to become Turkey's first president under the recently established US-style presidential system. This perception was supported by the belated but determined action of the Turkish Central Bank to increase interest rates in the run-up to elections,

counterbalancing rising inflationary pressure on the back of rising energy prices and generous fiscal handouts during the election campaign. Amidst rising inflationary pressures, the Central Bank seemed to abandon orthodox policy leaving rates unchanged and markets reeling. The eruption of a dispute between Turkey and the US regarding the detainment of an American pastor, led the Trump administration to impose sanctions on government officials in Ankara. This served to add further pressure on the Lira at a time when concerns are mounting on the health of the Turkish economy. Crucially, Turkish policy makers and politicians have begun to recognise that the successful stabilisation of the Lira will enable Turkey to re-build trust with markets and curb inflation from spiralling out of control. This renewed stance was shown in a clear synchronised monetary and fiscal response via drastic rate hikes in September, a departure from previous growth orientated, fiscally expansive plans.

Poland

Poland's economic development continued to benefit from robust export performance and rising confidence across all sectors of the economy. Poland's multi-year economic expansion success story has provided households with substantial real wage increases, bolstering domestic activity, consumer confidence and investment. Ongoing investment in human capital, infrastructure and R&D has enabled the economy to continue to improve productivity, preserving its status as an attractive and sustainable investment destination in the ultra-competitive environment of industrial manufacturing and software services. Poland has also benefitted from knowledge transfer, finding itself as a much sought-after immigration destination in its own right, notably a hub for many Ukrainians. Citizens of the neighbouring former Soviet Republic have become an integral component of the Polish labour market, providing a flexible and responsive pool of workers benefitting from the high demand in sectors such as Agriculture or Construction. Polish officials have formalised this process by establishing a work-visa based employment system, which has successfully married flexibility with key social benefits such as social insurance. Notably, looking through the sphere of Brexit, Poland is expected to be impacted in different ways. The projected fall of immigration to the UK is predicted to stem the outflow of skilled labour from Poland, the number one country of origin of EU-citizens working in the United Kingdom, which may function to counterbalance wage inflation. Moreover, Brexit also implies that there will be a sizable reduction in contributions to the EU budget. As one of the consequences, we believe that the EU cohesion funds' contribution to infrastructure investments in its main target area, the new EU member states will be affected negatively.

Other Economies

The European Parliament voted on 12 September 2018 to initiate disciplinary action against Hungary over alleged breaches of the EU's core values, including the rule of law, freedom of the media, and an insufficient fight again corruption. With more than two-thirds of MEPs backing the vote, the European Union sent a clear message in defense of the institutional and legal framework across all member states but placed a spotlight on Emerging European nations such as Hungary, Poland and Romania. Our belief is that this will highlight that European Union membership is not confined to economic implications but also a clear commitment to the development of the rule of law and investment into institutional oversight. A welcome development, initial discussions on the next European Commission multi-annual financial framework 2021-2027, proposed the introduction of a new cohesion policy conditionality related to the rule of law, thereby attaching a monetary incentive in the form of structural fund grants to compliance with EU core values. An advancement, which we view to be beneficial in fostering corporate governance and friendly shareholder practices.

Greece exited the last of its three bail out packages in August as its creditors, predominantly the European Union, and its member governments, believe the country's

finances have improved sufficiently to access public markets again. Overall, we observe economic growth to remain lackluster, and primarily confined to the tourism sector. We believe the key to increasing investment lies in unlocking the availability of credit within the banking sector. The successful monetisation of collateral, mainly re-possessed real estate, would release liquidity that could support economic activity by way of credit extension.

Outlook

2018 was a testing year for Global Emerging market investors as markets had to grapple with challenges old and new. Emerging European stock markets in particular were confronted with rising political and policy risks, such as the impact of the US sanctions on the Russian economy and stock market, concerns over adequate monetary policy in Turkey, or the increasing concern of EU institutions over independence of the legal system and the overall rule of law in Emerging European member states. Against this backdrop, investors could be forgiven for not registering any of the various positive developments on the corporate but also political level that can impact earnings growth potential and stock market performance going forward.

Aided by excellent Russian earnings performance, profit margins for Emerging European companies have continued to improve and we see potential for this trend to remain intact in the future as the sectors such as finance, retailing, telecommunication, utilities are positioned to be supported by the ongoing investment into growth and efficiency as well as a more supportive political and fiscal backdrop in many countries.

As Emerging European countries find themselves at different stages of the economic cycle, we consider a synchronised growth downturn as relatively unlikely. This should also allow investors to benefit from diversification effects. This was exhibited in 2018 where we saw Russian oil stocks deliver substantial outperformance over global peers.

On a similar note, dividend generation has increased driven by increasing earnings, thereby supporting internally generated resources to fund future growth. Dividend yields on Emerging European markets are substantially higher than in other geographies mostly owing to the attractive valuation levels of stock indices in Russia, Turkey and the new EU member states.

In terms of growth, we note the substantial opportunities we see in the consumer space, export industries and social media/the internet. Rising household income levels, a well-educated, highly efficient workforce and investment into infrastructure lay the foundation for sustainable growth and the attraction of foreign investment.

We acknowledge the potential challenges posed by the prevailing economic policy and political risks. However, we are encouraged by the fact that Emerging European economies remain deeply committed to free market economics. Going forward, we believe that preserving a favourable investment climate, a prerequisite to rising growth potential, remains an important priority to all governments within the region.

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Debt

(compare debt funds **here**)

TwentyFour Income Fund: Sentiment in the ABS market is relatively balanced, with recent fears of a material supply glut largely set aside; however, the Portfolio

Management team do continue to view the timing of new issue supply as a driver of market performance. In particular the expectation is that CLO issuance will be relatively low, as the economics of new issue transactions is not as favourable for equity investors given the relative cost of funding versus the yield on senior secured loans. This should help valuations as demand outweighs supply. In addition, while ABS issuance has been higher in 2018 than initially expected, a number of UK issuers have sought to capitalise on the relatively attractive spreads they can issue at in the USD market, taking further supply away from European investors.

Loan pools continue to perform well in fundamental terms with arrears and defaults remaining at historically low levels. This means that market pricing has tended to focus more on the technical balance of supply versus demand, with one eye on external risks such as the continuing rise of populist politics, monetary policy and Brexit, to name a few. While these events are largely less important from a fundamental point of view, the impact of market risk sentiment can spill over from more directly affected financial instruments as risk sentiment changes.

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Alcentra European Floating Rate Income: With demand remaining strong due to growth in CLO formation and continued inflows into unleveraged funds, we continue to remain constructive in our outlook for the market. While short term there has been some pressure on existing tighter margin loans in secondary, in the medium term the growth in well priced new loan issuance is a positive for the market.

European Loan issuance has been strong year to date, with volumes through Q1 2018 standing at €62.2 billion, c 6.5% higher than at this point in the prior year. Significantly, M&A volumes are up +97% year to date versus the prior year while re-financings are down -51%, resulting in material net new issuance growth.

New issue spreads were better in Europe than the US over the last 3 months. The high level of loan net-issuance has allowed investors to be more selective on new investments, driving new issue spreads wider.

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Healthcare

(compare biotech and healthcare funds **here**)

Sven Borho and Trevor M Polischuk, managers, Worldwide Healthcare: The political backdrop in healthcare has certainly been a critical macro factor over the past 10 plus years, from U.S. healthcare reform, the passage of "Obamacare", U.S. Presidential elections, the "Repeal and Replace" debate, and of course, the current and ongoing debate over drug pricing in the United States. 2018 was expected to be different, but the Republican administration kept drug pricing at the forefront of their mandate this year. Comments from key players throughout the year, from FDA Commissioner Scott Gottlieb, to Secretary of Health and Human Services Alex Azar, to President Trump himself, the message was clear and consistent: they were going to be tough on drug prices. With that said, the evidence was mostly to the contrary.

Whilst numerous proposals were put forward including President Trump's "blueprint", nothing of significance has yet to come into law. President Trump's highly anticipated signature speech in May 2018, where he detailed his plans in the legislation entitled "American Patients First", was mostly benign. The speech was bombastic yet very

short. He articulated a focus on lowering out-of-pocket expenses for patients and targeting "the middle man" (e.g. pharmacy benefit managers) in the drug chain. However, most notably, there was nothing in the speech on implementing direct drug price negotiations with drug companies, nor the allowance of the re-importation of drugs across the border, nor the rationing of the utilisation of drugs by patients.

Rather, the President focused on continued motivation to increase competition to lower drug prices via market forces, through innovation (a positive surprise) and more drug approvals. Much of the focus of the President's speech, of course, pandered to the public, promising to lower the out-of-pocket burden for patients by getting the drug plans to share rebates and discounts with said customers. Whilst some of the proposals could have a tangible impact, none were industry changing. Overall, President Trump's message was consistent with his administrational mandate: solving America's problems with pro-business and free market solutions.

Other political developments were also positive for the healthcare industry. This included President Trump's signature legislation thus far, the Tax Cuts and Jobs Act (TCJA). This plan was proposed in November 2017, passed in December 2017, and became effective for the fiscal year 2018. The positive effects were immediately noticeable: lowered corporate tax rates and lowered repatriation tax rates resulting in increased earnings power for large capitalisation corporates and more cash for debt servicing, increased dividends, share buy-backs, and business development.

Finally, the FDA is on the verge of another record year for drug approvals in 2018. Current commissioner Scott Gottlieb, a Trump-appointee, continued the enactment of his "Drug Competition Action Plan" and it has yielded impressive results. The FDA approved a record 46 novel drugs in 2017. Moreover, by 17 October 2018, the FDA approved 45 more, but with another 11 applications pending approval, each with an action date before the end of 2018, a new record is imminent. Additionally, 2017 saw a record number of generic approvals by the FDA, over 1,000 approvals. The pace for 2018 is only slightly behind that mark.

A continued hallmark in healthcare has been mergers & acquisition (M&A), particularly in the therapeutics space. The pace of M&A got off to a strong start in 2018 with a flurry of high-profile takeovers in the biotechnology sector, in hot areas like gene therapy and cell therapy. That said, the pace slowed somewhat in the second half of the year, somewhat disappointingly given the increased cash flows stemming from the Tax Cuts and Jobs Act.

Part of the reason has been the historic initial public offering (IPO) market in the U.S. The pace of the number of new biotechnology IPOs in 2018 is expected to be the second highest in history at approximately 70. Moreover, the average gross proceeds per IPO was at or near record highs. The impact? Easy access to capital may have blunted M&A. As one industry executive recently opined, "I think as you've seen, there's also been generally a dearth of M&A across the industry recently. There has been significant funding flowing into small biotechs including via IPOs, which are at multiyear highs. So as a result, biotechs have access to ample capital and they have perhaps less need or desire to sell right now." (Ken Frazier, CEO of Merck and Co., July 27, 2018).

Biotechnology

Sentiment on major biotechnology remains poor relative to emerging biotechnology, despite historically low valuations. Each of the large biotechnology companies has lead assets that will encounter competitive pressure or loss of exclusivity over the next five years. Fears over the sustainability of revenue growth for the large capitalisation players has kept share performance muted. We believe the large capitalisation names

will eventually enjoy a positive rerating once they are able to demonstrate that their pipelines are sufficient to offset the future revenue decline of their lead assets. M&A, which has been very quiet for most of the year, could also spur a rerating of shares. Investor concerns about the midterm elections in November and potential drug pricing legislation if the Democrats take the House and/or the Senate were also likely keeping shares in check. However, now that the election has resulted in a split Congress, we expect drug pricing headlines to continue but the threat of meaningful legislation to subside.

In contrast, emerging biotechnology continues to benefit from the increasing speed of innovation, new technologies and a favourable regulatory environment. Advances in treatment modalities, including gene therapy, gene editing and cellular therapy, have expanded the possibilities for drug development in previously untreatable or incurable diseases, with many of these efforts driven by emerging biotechnology companies.

Additionally, under new administration, the FDA has undertaken an effort to be more accommodating of drug development and innovation, particularly in rare, orphan diseases in which traditional regulatory standards may be difficult to uphold. We see this environment as supportive for further growth in biotechnology and remain positive on the sector. Further, the near-record number of new biotechnology IPOs suggests investors remain keenly interested in the sector and remain able to deploy capital into new companies.

Pharmaceuticals

Pharmaceutical stocks proved to be an interesting case study during the half year, an enigma in which, despite facing some potentially industry changing headwinds, the stocks posted some of their strongest gains this century. In other words, generalist rotation into the group was less about the fundamentals of the industry and rather a view on the rest of the equity markets. With the sudden volatility in technology stocks and the threat of trade wars rumbling on, investors jumped to a “risk-off” mentality, blindly looking for value over growth and defensive positioning that became de rigueur for the second half of the half year.

The macro environment, which most recently proved quite favourable for these stocks could change however. Continued upward pressure on interest rates and as the 10-Year U.S. Treasury Yield breaks out to multi-year highs above 3.0%, pharmaceutical company share prices could suffer as investors chase yields elsewhere. Pending U.S. Federal midterm elections in November 2018 added to a volatile October. However, the election resulted in a split Congress, with the Republican Party adding to their majority in the Senate whilst the Democratic Party took a small majority in the House of Representatives. We view this result as likely a best-case scenario as “gridlock” in Washington significantly reduces the probability of industry altering legislation. The near-term impact on the biopharma space should be limited. That said, drug-pricing headlines may not dissipate in 2019 and in fact may increase with Democratic-led committees in the House.

Overall, we regard the sector as being on a solid footing as we remain at or near the high end of the current innovation cycle. New product flow and pipelines are generally strong. But the cradle of innovation does not rest within large capitalisation pharmaceutical companies. That is still the domain of emerging biotechnology companies domiciled in the United States. Therefore, M&A must be a key mandate for these companies going forward, creating a partial air of uncertainty about the state of business development within large conglomerates and their ability to adjudicate about “the next big thing” within an environment that does not reward risk taking.

Other fundamentals are mixed and thus we regard this group of stocks as rather heterogeneous: diverse in character and content with disparate growth outlooks due to a variety of factors. First, some companies are in the midst of new product cycles, driving top line growth but perhaps more importantly, driving margin expansion and thus outsized earnings growth. Other companies may be slightly earlier in their new product cycle but due diligence can unearth innovation before the market rewards it.

A looming headwind for the group revolves around biosimilar competition for mega-blockbuster, incumbent brand molecules, in particular monoclonal antibodies. Whilst still early days, price and volume erosion rates in Europe were mixed depending on geography. In the U.S., current expectations are for milder penetration rates. This has yet to be observed and 2019 will be critical in evaluating this phenomenon. Fortunately, this risk is mostly consolidated within only a few companies.

In contrast, the performance of U.S.-focused specialty and generic pharmaceutical stocks was more varied in 2018 compared to their large capitalisation brethren. Specialty pharmaceutical stocks, in general, performed well benefiting from an improved pricing environment, effective new product launches, and positive proprietary pipeline disclosures.

Generic pharmaceutical stocks, on the other hand, were a mixed bag. Many generic companies underperformed due to continued pricing pressure in the U.S. market and delayed product approvals for complex but value driving generics. Interestingly, the riskiest generic companies were some of the best performers in this group, as investors overlooked debt-laden balance sheets to reward the management teams of companies with extremely depressed valuations executing turnaround strategies.

Although improved investor sentiment has driven a valuation recovery in the specialty and generic pharmaceutical sector, we believe further multiple expansion is likely as proprietary pipelines remain undervalued for many companies. In addition, we anticipate an uptick in significant business development and M&A activity, especially for specialty pharmaceutical companies, as net leverage within this group is relatively low.

Medical Technology and Devices

Despite mostly higher share prices in 2018 – and thus higher valuations – trends in the Medical Devices sector remain favourable. We highlight several key metrics pointing toward a continuation of strong organic sales growth which can continue to drive stocks higher. First, the economy. Consumer confidence in the United States, by far the largest market for devices, remains at multi-year highs. Second, unemployment in the United States is approaching a 50-year low. Third, research and development (R&D) spending as a percentage of sales for the industry remains at elevated levels, an encouraging sign for a continued innovation cycle. Finally, the rate of new Premarket Approvals (PMAs) by the FDA has accelerated over the past five years, which should sustain sales growth for the next five plus years.

Undeniably, valuations remain high, but we believe current levels are warranted given the growth profile of many large capitalisation companies in the sector. Specifically, we are looking for high-single digit to low double-digit organic sales growth, further augmented by M&A, and strong cost controls leading to low to mid-teens earnings per share growth.

Turning to stock selection, we continue to prefer specific device areas where both innovation and demand are high, such as cardiology. Surgical robotics – where technology advances have been and will continue to be disruptive to historical surgical paradigms – remains a hot area. We have renewed interest in diabetes – given the sheer market size and potential for several new product cycles to drive elevated growth

rates for manufacturers. Finally, extremities implants/biologics are at the early stages of the adoption curve and can make astute investment opportunities.

Life Science Tools and Services

It has been an eventful period for the Life Science Tools & Services sector. The prospect of trade wars affected the sector due to its high exposure to China. Whilst first quarter earnings were mixed as some companies had idiosyncratic mishaps, second quarter earnings demonstrated broad re-acceleration to all-time highs in organic growth and allayed fears of the near-term impact of tariffs.

Therefore, with the sector at an all-time high in organic growth and near an all-time high in valuation, questions have persisted around the sustainability of growth in 2019 as well as the impact of tariffs and foreign exchange. Whilst we expect that growth will moderate somewhat in 2019 due to the difficulty of overcoming tough comparisons in 2018, we believe that the sector's business mix has fundamentally shifted. Companies have pivoted towards durable, higher growth biopharmaceutical markets and away from cyclical industrial markets, and we expect the sector to sustainably grow at "new normal" levels of 5% plus, significantly higher than the days of 3-4% prior to 2017.

Though we acknowledge that tariffs and trade war rhetoric will be significant drivers of sector sentiment, we see tariff concerns as overblown, as sales of life science tools to China have remained robust throughout the year. Moreover, domestic companies lack legitimate local technology and capabilities that could displace global tools companies. Finally, we view valuations as elevated but justifiable with strong market demand being offset somewhat by macro concerns.

Healthcare Services

Healthcare payor and provider stocks have performed well during the half year driven by a trio of factors: positive fundamental trends, M&A activity, and corporate tax reform. Specifically, utilisation is modestly higher in a strengthening U.S. economy, but at least a small uptick was captured in managed care pricing. The U.S. Department of Justice approved two pending vertical mergers, altering the landscape of the industry and removing an overhang. Finally, lower U.S. tax rates are most favourable to healthcare services companies that operate almost exclusively domestically.

Given the outcome of the U.S. midterm elections and resulting division in power of the U.S. Congress, we remain bullish on health maintenance organisations. These companies stand to benefit from relatively stable cost trends, margin expansion thanks to the best Medicare reimbursement rates in a decade (the current administration supports privatisation), better investment income from interest rates and potentially more vertical integration. In contrast, we are bearish on drug supply chain companies, including distributors, which will be negatively impacted by government regulation aimed at reducing drug price increases.

Emerging Markets

In China, our investment strategy continues to focus on leaders in innovation and high-quality generics in the pharmaceutical sector. The China FDA is committed to improve the efficiency of their drug approval system and to increase the quality of generic drugs sold in China.

During the period, the scope of mandatory quality consistency evaluation for generic drugs, currently marketed in China, expanded from oral dosage to injection. Meanwhile, we see the increasing cost control pressure from the state medical insurance schemes and expect potentially aggressive price cuts of branded generic drugs in the next year.

The macro environment and market sentiment in China in the past six months were not favourable. We are in the midst of U.S.-China trade tension and as a result the Chinese currency depreciated by approximately 9%.

We have been cautious and conservative about participating in biotechnology IPOs on the Hong Kong Stock Exchange due to the rich valuations. The exchange amended its Main Board Listing Rules (Listing Rules) in 2017 to allow pre-revenue New Economy companies to list on the Main Board. We are patiently waiting for opportunities to participate when the asset is priced at a more reasonable valuation.

Despite regulatory headwinds and policy changes, the Indian pharmaceutical industry has surprisingly experienced prescription volume-driven growth rate acceleration. The industry grew approximately 9% during the half year and benefited from several positive volume drivers including rising disposable income, the rising prevalence of chronic diseases, improving medical infrastructure and increasing insurance coverage. Price improvement also had a modest positive impact on industry growth. Overall, the current period's industry growth rate markedly exceeded last year's figure (-4%), which was depressed by trade inventory corrections stemming from the introduction of the Goods and Services Tax (GST).

Looking ahead, we anticipate more of the same strong tailwinds with favourable volume growth and, to a lesser extent, slightly improved pricing, sustaining mid-to-high single digit industry growth. We are closely monitoring the roll out of the National Health Protection Scheme (NHPS), a government funded healthcare programme that will expand health insurance coverage throughout the country. At present, over 60% of India's healthcare expenditure is "out of pocket" and NHPS is expected to reduce this burden and boost healthcare consumption overall as a result.

Exports to the ever-important U.S. market account for more than 40% of Indian pharmaceutical revenues and companies with a significant U.S. presence continue to experience significant pricing erosion due to customer consolidation and increased Abbreviated New Drug Application (ANDA) approval rates at the FDA. The pace of decline has moderated somewhat to high single digits compared with the mid-teens decline witnessed a year ago, as afflicted companies trim their product portfolio in response to weaker pricing. Price declines are likely to be partially offset by rupee depreciation against U.S. dollar. Despite these challenges, the U.S. market remains a major source of profitability for a majority of Indian generic companies. Indian companies have begun realigning U.S. efforts by focusing on complex and specialty products and stepping up supportive investments in R&D, regulatory compliance and quality improvement. As a result, our focus remains on Indian pharmaceutical companies with increasing U.S. exposure, clean regulatory track records and differentiated generic pipelines.

Additionally, Indian pharmaceutical companies continue to benefit from the high double-digit growth rates registered in emerging markets such as South East Asia, Middle East, Africa, and Eastern Europe. Many companies have increased exposure to these geographies via a local manufacturing presence (either organic or acquired) or supply agreements with large distributors. We prefer Indian pharmaceutical companies with exposure to these high growth emerging markets since it could provide some offset to the challenging trends encountered in the U.S. market.

2019

The current period saw healthcare stocks trade on a number of different factors, from macro headwinds and tailwinds and on mostly positive fundamentals as well. For 2019, we expect a shift to more of a focus on fundamentals to drive share prices. First, political controversy should ebb given the drug pricing noise should recede and the election

cycle should be silent. Second, the secular demand and consumption of healthcare goods and services remains strong. Third, healthcare valuations for the most part are reasonable.

However, as market volatility has spiked in October, its potential impact to returns cannot be ignored. Whilst difficult to predict, it may be reasonable to assume that volatility may remain elevated into 2019 as long as trade negotiations, Brexit, U.S. federal policy, and other macro factors remain in flux.

That said, innovation-driven growth remains at the forefront of our bullish view of the healthcare sector. The current new product cycle across the industry is clearly the best since the "me too" days of the 1990s. Whilst biosimilars will become more prominent in 2019, the industry is not facing a patent cliff as it did in the 2000s. In addition, the regulatory environment is very supportive with record setting new drug approval rates. Overall, we expect many performance generating opportunities to exist as this golden age of innovation continues.

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Infrastructure

(compare infrastructure funds **here**)

Ian Russell, chairman, HICL: Political uncertainty in the UK remains a key risk. Commentary around the possibility of nationalisation of infrastructure assets ignores the considerable benefits that private capital brings to the public sector in terms of ring-fenced capital maintenance budgets, private sector management expertise and resource, and the transfer of significant operational risk away from the public sector. More practically, nationalisation would be highly complex and come at a considerable cost to tax payers.

Acknowledgement of the benefits of responsible private sector participation in infrastructure stewardship will be crucial for any government to secure investment in the infrastructure required to underpin the delivery of public services in the future. In that context, policies and regulation aimed at addressing and penalising the excesses of some past owners of water companies in England and Wales, while tempting in the current political climate, are retrograde and risk undermining the confidence of long-term, responsible investors.

Demand for infrastructure investments continues to be strong, reflecting the development of the asset class over the past 20 years. Recent significant transaction activity includes the takeover of John Laing Infrastructure Fund. This demonstrated that pricing for investments continues to be elevated whilst investors seek long-term, stable income. The takeover of JLIF showed that certain investors are not overly concerned by the current UK political climate. We take some reassurance from the comment in the 2018 Budget speech that the current government will "honour existing contracts".

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Property

(compare Property: Direct – UK funds **here**)

Brian Bickell, chief executive, Shaftesbury: London is one of the leading global cities. It has the largest economy of any Western European city and contributes almost one quarter of UK GDP. The breadth of its economy encompasses:

- a world-leading financial and commercial centre;
- a major hub for creative industries, from technology to media;
- a globally-recognised location for education and research;
- home to world-class visual and performing arts facilities; and
- a valuable visitor economy, attracting more international tourists than any city in the western hemisphere as well as huge numbers of local and domestic visitors.

This unique combination of features means London is not solely reliant on the fortunes of the wider UK economy. Although the uncertainty surrounding the implications of Brexit for the UK economy are having an adverse impact on business and consumer confidence, London is much less affected. It continues to attract domestic and international businesses and investment, with medium-term growth projections for London out-performing national forecasts.

At the heart of the city, the West End draws over 200 million visits annually. Its huge working population provides a regular, daily customer base for its retail, restaurant and leisure businesses. Importantly, throughout the week and particularly around weekends, local, domestic and international visitors arrive in their millions to enjoy its tourist and cultural attractions as well as unrivalled shopping, dining and leisure choices. Together with its residential population, the West End offers a busy, seven-days-a-week trading environment, and a more-affluent customer base, which underpins its prosperity and appeal to businesses.

London's extensive transport infrastructure makes the West End accessible not only to Londoners, but also to the large population in the south east who commute or visit for a day out. The five main Underground stations in the West End currently handle some 225 million passengers annually. The opening of the Elizabeth Line, now expected late next year, will add 10% to London's transport capacity and will improve the West End's transport connectivity materially. The new Tottenham Court Road and Bond Street interchanges are forecast to be handling 200 million passengers annually by the mid-2020s.

Uncertainty surrounding our departure from the EU and future trading and other arrangements with the EU27, together with structural changes in traditional national retailing patterns, continue to affect nationwide business confidence and investment, economic growth and consumer spending. However, the global attractions of London and the West End to businesses and huge numbers of local, domestic and international visitors, together with their broad-based economies, create an operating environment which is insulated from the impact of national headwinds and has good long-term growth prospects.

Although we are seeing longer letting periods for the largest space we have to offer, general demand continues to be firm, buoyed by the trading conditions our tenants are reporting.

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Nicholas Thompson, chairman, Picton Property Income: Clearly the coming months are important in terms of the Brexit negotiations and our future relationship with the EU and more widely in terms of global trade. Despite the recent uncertainty, the UK economy has been reasonably resilient, as have the fortunes of the property market and we remain cautiously optimistic; however, we believe it is right to be prudent in the short term until we have greater clarity. For many of our occupiers it appears that it is business as usual.

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Mark Burton, chairman, AEW UK REIT: Britain's exit from the European Union is approaching and by the end of 2018 it should be clear whether this is to be with or without a trade deal. Whilst the general opinion is that a "no deal" scenario would have a negative impact on the property market, it is hoped that some clarity will make it easier for businesses to plan and invest, regardless of the outcome. London offices - the sector most likely to be negatively impacted.

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AEW UK REIT:

UK Economic Outlook

The longer term outlook remains uncertain as global economic growth has begun to soften with tariff wars between the US and China having an impact. Although UK unemployment has remained low, wage growth has struggled to keep up with inflation and real wage growth was only 0.1% for the three months to 30 June 2018.

One of the key sources of uncertainty remains that of Brexit and the possibility of the UK leaving the EU without a trade deal. This is a very real possibility after European Council President, Donald Tusk, rejected Theresa May's proposals at an EU summit in September 2018. Although the Irish border issue remains a stumbling block, it is hoped that the outlook will become clearer during the remaining months of 2018. The EU had been considering a special summit in November 2018 to agree the terms of the UK's withdrawal, however a lack of progress during September and October 2018 could mean that December 2018 will be the final opportunity to reach an agreement. If the UK government cannot deliver a Brexit deal, the possibility of a general election could also bring about further uncertainty in terms of political leadership and policy.

However, against this mixed economic outlook, UK property continues to perform well.

UK Real Estate Outlook

The UK commercial property market continues to perform strongly, driven by an annual income return of over 5% for the year to June 2018 (IPD). The yield gap between property and the risk-free rate has remained well above the long-run average during 2018 and the upswing in the property cycle has been extended by a prolonged period of low interest rates and the weight of investment. Although official interest rates were raised during August 2018, expectations are that upward pressure on property yields is not imminent.

The lack of clarity regarding the Brexit terms remains a major concern for the market however, it is generally acknowledged that any impact would be felt most strongly in the office sector, particularly in the City of London. The results of negotiations during the remainder of 2018 should give more clarity as to the final outcome however, we have seen a weakening in investment activity across the market as a whole so far in 2018, compared with the comparative period of 2017. We are seeing notable polarisation between performance delivered by the sectors, with industrials delivering

higher total returns and the retail market continuing to struggle with poor sales and numerous company voluntary arrangements ('CVA's).

Industrial

The industrial sector continues to outperform other sectors. The strong performance is in part due to retailers investing heavily in their supply chains to meet logistics demands but is also as a result of a lack of any significant development activity undertaken in smaller units during the current cycle. As tenant demand is increasing there is limited supply of stock and this is leading to rental growth in strong locations across the country.

We expect to see continued growth in the industrial sector, both in terms of income and capital value.

Offices

We expect office rents outside London to remain stable in the coming years, as development in most cities has already peaked. Higher residential values and the relaxation of planning controls mean that many towns and cities are losing both office and industrial space.

Alternatives

There has been a recent trend towards non-mainstream sectors, as investors seek to benefit from greater diversification as well as accessing long-term income trends. We expect the alternatives sector to grow further as investors seek long income or higher yields.

Retail

Structural issues have been seen most notably in the retail sector where a number of administrations, CVA's and store rationalisations by occupiers have turned investor sentiment against the sector.

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Allan Lockhart, chief executive, NewRiver REIT: The way that people live, work and consume continues to evolve. There is a growing trend of local authorities purchasing shopping centre assets in order to gain greater control over their town centres and better meet the needs of their communities. However, in most cases local authorities lack the personnel, expertise or relationships to successfully asset manage these centres in-house, and are seeking a partner with the scale, relationships and proven track record to manage them on their behalf.

Click & Collect

According to research by GlobalData, the value of click & collect transactions is forecast to grow by 46% over the next five years to £9.8bn, following an estimated 12% in 2018. As the channel grows, consumers are increasingly demanding convenient collections close to their home or work, and retailers are investing heavily in-store and in their supply chains to improve click & collect infrastructure, as well as using third-party collection points to expand their reach. Town centres, retail parks and neighbourhood shops currently account for over 70% of all click & collect locations.

Residential development

As the UK's urban population increases, national planning policy has become strongly supportive of residential development in town centres, including in the airspace above commercial premises.

Outlook

We expect the challenges faced by the UK retail sector to continue in the near-term. We see diverging performance between retailers in the growing, online-resilient sub-sectors focused on essential goods and services and those in the structurally-challenged sub-sectors severely impacted by low consumer confidence, the rise of e-commerce, and market overcapacity. In pubs we have seen wet-led community pubs outperform, while destination and food-led pubs have been impacted by the wider malaise in the casual dining sector, and we expect this trend to continue into the future.

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Hugh Seaborn, chairman, TR Property: As we move into the second half of the financial year, there appears to have been a change in the mood and equity markets around the globe have been subject to a sell-off.

Macro risks abound with the potential escalation in the US/China trade war whilst geo-political concerns are heightened. Closer to home Brexit dominates and the UK will be the hardest hit by a poor outcome, however collectively there are no economic winners from this negotiation and growth across Europe will also suffer. The European Union is also being put to the test again, this time by Italy's breach of the budget deficit rules.

Whilst the ECB has flagged the termination of its bond buying programme ('quantitative easing') and signalled an intention to resume a normalised interest rate cycle we think that it is quite possible that this will be deferred further if economic growth is dampened.

If interest costs continue at these very low levels the ability of many property companies to offer investors high, sustainable, growing earnings will underpin valuations.

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Marcus Phayre-Mudge, manager, TR Property: Investment volumes have remained remarkedly robust across the sectors favoured by cross border capital, namely office markets in dominant cities across Europe. London continues to surprise us with high transaction volumes and yields which have remained firm over the period even as reduced rental growth prospects become reality. Currency continues to play a strong part in international investors' thinking with GBP battered by Brexit concerns. Q2 Central London investment volume at £4.3bn was the strongest quarter since early 2017. The trophy purchases by Asian buyers continued with CK Asset Holdings acquiring 5 Broadgate for £1.0bn from British Land/GIC reflecting an initial yield of sub 4%. The quality of asset remains paramount with (mainly) foreign buyers happy to continue to pay record pricing but only for the best. Retail remains entirely bereft of investor demand except in London where overseas buyers acquired trophy assets such as Burlington Arcade (£300m, 3.2% yield) and 135 New Bond Street sold to a Singaporean investor for £180m and 3% initial yield.

Regional UK shopping centre volumes hit a record. However this was a record low of £120m of transactions in a quarter. Such low volumes augers poorly for future pricing, the gap between buyer and sellers' expectations must narrow and that will come with sellers' capitulation. The shopping centre sector drew large numbers of leveraged buyers in the recovery post the GFC, attracted by the high cash yields available when utilising cheap debt to acquire relatively high yielding assets. Unfortunately the rent rolls at many centres have come under pressure from CVAs and retailers unable to pay the passing rent as their business models continue to be ravaged by online alternatives. Debt default lies ahead for some of these centres.

Logistics remains the sector 'du jour' with record yields being paid and transaction volumes 33% ahead of the 10 year average reaching £3.7bn in the first half. Unlike the

office market the majority of capital deployed was domestic (70%) with Tritax Bigbox continuing to set record pricing with the forward commitment of £120m of Amazon at Darlington. The same management team have also set records in Europe buying for their new vehicle Eurobox which raised £300m in July. They recently purchased Mango's global distribution hub outside Barcelona (€150m) followed shortly by Amazon's new Italian 1.5m sq ft triple level facility 35km north of Rome. We understand both deals reflected initial yields of 5%.

Alternative asset classes such as self storage, student accommodation and hotels remain popular. The UK student accommodation market is the most mature across Europe and transaction volumes reached £1.4bn in H1 and are forecast to reach £4bn for 2018 making the sector the second most important after offices. Quite something given its embryonic nature a decade ago.

Offices

Data on Central London office take up continues to be obscured by the growth in flexible office providers who are not the ultimate users of the space. Q2 saw 700,000 sq ft of take up by flexible providers in 21 deals. This follows on from the Q4 2017 record quarter of 26 separate transactions. This new type of quasi occupier makes it hard to use long term averages to understand whether there is genuine equilibrium in the market. We think not. However what is visibly helping to maintain rental levels is the lack of supply, particularly of larger space. The exception being Docklands which does have supply well ahead of its long term average. Tech businesses are still expanding seemingly regardless of Brexit fears. A large letting of over 0.4m sq ft at Kings Cross is expected before the year end and will be a useful barometer of current pricing for this emerging, but superbly connected, submarket.

In contrast the Paris region experienced its best H1 since 2007 with take up of more than 1.3m sq metres, a 15% increase year on year and 25% ahead of the 10 year average. Much like the London market between 2012 and 2016, Paris has seen a surge in take up across all unit sizes with growing and dynamic tech based businesses becoming an increasingly important element of take up. Volume was also fuelled by a large number of pre-lets as larger tenants insulate themselves from predicted medium term space shortages. WeWork continues to grab headlines and deals with 4 new sites in Paris in the first half. Vacancy for the entire Paris region dropped to 5.2% and Paris Centre West (the core CBD) reached a record of 2.2%. La Defense also saw a vacancy rate of 5.3% but there are a number of large completions due in 2019 which will result in increased vacancy in that sub-market.

The theme of falling vacancy and rising rents is a consistent one across all Continental European cities with Stockholm, Berlin and Munich showing the fastest growth rates. Madrid and Barcelona vacancy levels are dropping fast but they were coming down from elevated levels. Madrid still has 12.2% vacancy in its outer ring (outside the M-30) but just 6.8% inside the M-30 and it is this inner segment where rental growth is accelerating.

Retail

UK standard retail unit vacancy stands at 12.4% as measured by Knight Frank. This figure has risen over H1 as more retailers seek to restructure their physical estates either through negotiation or by using CVAs. Q2 saw high profile casualties such as House of Fraser, Poundworld and Mothercare. Rising business rates and minimum wage requirements alongside the well reported loss of sales to online competition continues to drive down investors' expectations of rental growth. Indeed UK retail sales continue to rise but online is still capturing all that growth with high street sales volumes continuing to slip. The provision of more food and beverage (F&B) has underpinned

tenant demand in shopping centres over the last few years with the rapid rise in demand for more casual dining. However over expansion has ensnared a number of operators with the likes of Jamie's, Byron Burger, Prezzo and Carluccio's all seeking to close units or face bankruptcy. This niche submarket is now undergoing a contraction which is likely to coincide with weaker consumer confidence as real wage growth peters out in the face of higher imported inflation.

Once again Continental Europe appears to be having greater success at weathering these difficult conditions. Online penetration is lower (to varying degrees) when compared to the UK, but this is just a 'more slowly melting ice cube'. The convenience and competitive pricing of online will drive its growth across all markets. However our expectation of relative resilience across Europe is due to a broad mix of factors from cultural reluctance to have (fresh) food chosen by someone else through to much more competitive pricing of retail space (when compared with the UK). Much like in the UK, investors are shying away from secondary or sub-regional centres but in many cases the underlying performance as measured by rent roll resilience has been much stronger than their UK counterparts.

Distribution and Industrial

In the UK supply has begun to respond to the apparent ever strengthening demand for distribution space. In the +100,000 sq ft market supply at 10.6m sq ft in June 2018 is 20% ahead of a year earlier. This is still below the 10 year average and pre-lets remain at elevated levels accounting for about one third of take up - an encouraging statistic as it confirms that occupiers want to commit early and satisfy their forecasted demand.

The picture of broad and sustained demand is equally the case across Western Europe with pockets of record take up. Madrid has seen record take up last year with over 850,000 sq m compared to long run averages of c500,000 sq m. Yields (as discussed earlier) continue to be driven downwards as investors remain confident of further rental growth.

France has seen a pause in rental growth with subdued leasing levels in H1 compared to the two previous record years. However, evidence would point to a shortage of availability in the key metropolitan areas with supply dropping 20% year on year in the key Ile-de-France market and this will keep rents rising.

Residential

[*For*] German residential fundamental market conditions remain sound with underlying rental growth c3% and structural undersupply evident in all markets. Berlin, which has been top of the growth league table for several years has begun to suffer from local authority intervention in certain jurisdictions. In some areas, developers are unable to push through modernisation programmes which enables them to charge open market rather than restricted rents. Some boroughs are also restricting the ability to sell individual apartments (as opposed to blocks). We are not overly concerned, such interventions merely drive up values in the longer run through constraining development in the short term.

[*In*] Sweden, the central bank's macro-prudential tools have constrained house price growth but tenant demand is as robust as before given rising employment and wage growth. Affordability remains the watchword. Private equity firms have spotted the attractive combination of this demand imbalance coupled with submarket state controlled rents in properties which are in dire need of refurbishment.

London residential new build, particularly over £1,000 per ft, continues to suffer from the headwinds identified in previous reports. This Central London weakness has rippled

out to other regional markets in its sphere of influence and the cost of moving has reduced transaction volumes and pricing evidence which in turn deters activity.

Student accommodation

According to UCAS, overall acceptances for places at university were down by 1.1% for 2018/19, with UK acceptances down by 1.9%, despite a near 3% fall in the number of UK 18-year olds. However, EU students placed has grown by 3%, with non-EU international students growing by 4%. UCAS data also shows that there are now clear divisions in the market, with acceptances to higher tariff universities growing by 1%, whilst those accepted by lower tariff institutions have fallen by 3%. We keep a watchful eye on new supply with the current pipeline adding 4.3% to the overall stock. Crucially full time student numbers still outweigh purpose-built student accommodation (PBSA) by 3:1.

Outlook

In late May, I commented that we expected divergence in performance between those real estate businesses with rental growth prospects and the rest to widen. This was indeed the case as we moved through the summer and up into September as investors focused on the likelihood of rising interest rates and therefore sought out businesses whose earnings were responding positively to economic growth (the precursor to increased rates). Not surprisingly those markets where investors expected there to be lower (or negative growth) saw dramatically reduced exposure and this included virtually all pan European retail property but also a broad swathe of UK property companies.

September and post the half year into October saw a dramatic change of investor sentiment. Eurozone growth eased to an annualised rate of 1.7% during the third quarter, the Italian fiscal confrontation reached unchartered territory and the UK economy continues to suffer from the collective uncertainty surrounding the Brexit negotiations. Our view is that this is likely to encourage all four central banks across Europe to ensure a highly accommodative interest rate normalisation cycle. The European economies still need to absorb the monetary tightening effects of the (well flagged) termination of QE stimulus and the end of the bond buying programme. They will not all cope equally. This recent price correction saw the better companies, those priced for growth, hit hardest. Higher yielding names benefit disproportionately if long term rates stay lower for longer even if they have little growth. If the expectation of rate rises is deferred, the sector as a whole will benefit and the cheapest names will offer value investors an opportunity. However we continue to believe that focusing on those businesses with growth prospects is a much more viable long term strategy. The US, which has clearly entered a rising rate cycle offers useful observations. In essence sectors with either structural growth potential and/or pricing power in their chosen submarket outperform in a rising rate environment. Higher yield may look cheap but any renewed inflationary pressures will not help those business models.

October also saw renewed M&A activity with the potential 'take private' of Intu by a consortium led by its largest shareholder. Private property companies away from the scrutiny of public markets, can potentially afford to utilise much higher levels of leverage compared to their listed cousins. There remains an abundance of capital (equity and debt) and as I wrote in May, target stocks are likely to be the cheaper and higher yielding names in unloved sectors. This would also help put a floor on the equity market's bearish valuation of listed companies.

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Michael Wrobel, chairman, Civitas Social Housing: The government continues to be supportive of Specialist Supported Housing, with further funding allocated to mental

health services. This increasing financial support is in reaction to continued demand for quality care in the community for people with a number of different care needs.

In the market generally there remains significant uncertainty due to Britain's exit from the EU, which is due to occur in March 2019.

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Residential Secure Income:

Shared Ownership and Sub-market rent Housing

The case for raising equity-like capital within the social housing sector has increased since our IPO with the main Housing Association developers responding to government calls to increase the supply of housing. Under current arrangements this leads to increasing indebtedness, with a number of Housing Associations nearing their debt capacity. The annual publication by the then Homes and Communities Agency (Global Accounts of Registered Providers, Dec 2017) shows a slow but steady growth in debt as a proportion of net book value of properties. A recent survey by Savills (The Savills Housing Sector Survey June 2018 in association with the Social Housing magazine) demonstrates that, in terms of financing additional supply, the most quoted barrier within the business is gearing capacity. In order to increase supply, Housing Associations need to overcome several barriers, ranging from access to land, financial constraints and increases in planning obligations for affordable housing. The growing trend for equity-like capital to fund new social housing is becoming more prevalent and is the only way that long-term capacity to develop can be assured.

Local Authority Housing

Unfortunately, many Local Authorities, especially those in South East England, have in recent years experienced significant increases in households presenting as homeless. This is primarily a result of the critical shortage of both affordable and market housing, exacerbated by reforms to the Local Housing Allowance. Together these factors have left Local Authorities with a statutory duty to find housing for increasing numbers of households but without the permanent homes to do so. The recently enacted Homelessness Reduction Act has further added to the pressure on Local Authorities to find housing solutions in order to prevent homelessness building upon the Housing Act 1996, as amended by the Homelessness Act 2002, which places a duty on Local Authorities to secure accommodation for unintentionally homeless people who are in priority need. According to published reports, England had 79,880 households in Temporary Accommodation at the end of March 2018, and the households included 123,130 children. Demand for Temporary Accommodation has grown by over 70% since March 2011. Whilst the recent announcement by the government to remove the cap on Local Authorities borrowing through their Housing Revenue Account will allow some Local Authorities to begin to address their housing requirements, the depth of the problem is such that we still see huge demand from Local Authorities.

Retirement Rental Housing

The UK population continues to age, with opportunities for downsizing for over 60's historically limited to renting sheltered accommodation owned by charities and Local Authorities, or buying into age-restricted accommodation blocks, which can expose the resident to significant transaction costs on entry and on departure. Surveys indicate that 25% of UK over 55's would like to buy or rent in a retirement village. However, the market is faced with a lack of supply of specialised retirement living options.

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Civitas Social Housing: The Government has continued to show its strong support for social housing generally and Specialist Supported Housing in particular through a range of measures including a return to the CPI +1% maximum annual rent inflator for general needs social housing rents, additional grant funding for Housing Associations to develop new social housing and a confirmation that the government consultation on Funding for Supported Housing had concluded that funding would continue to be provided by Central Government rather than from Local Authority budgets.

The Regulator of Social Housing ("RSH") separated from Homes England in September 2018 and will now be responsible for regulating all social housing providers whilst Homes England will focus solely on investment. The RSH is in consultation with the housing sector on a range of regulatory issues to ensure their approach is suitable for the future. This takes into account the post-Grenfell environment and the increased focus on health and safety and consumer rights.

The RSH has published its sector risk profile for 2018, an annual publication which reviews what it believes to be the risks that exist within the sector as guidance for Housing Associations. This includes appropriate and sensible matters that Housing Associations should consider before entering into lease arrangements.

Demand for high-quality Specialist Supported Housing is high and there is increasing competition for assets. The Company continues to decline unsuitable transactions and utilises its relationships, existing agreements and buying power to acquire good quality properties at competitive prices that remain within the yield range set out at the time of IPO in 2016, whilst noting that there has been an element of yield compression within the market.

Wider market and Policy Context

The key policy driver for Civitas's investment strategy is the Government's recognition of the need to move vulnerable individuals out of large institutional facilities, such as residential homes and secure hospital units, into community-based social housing. This Government focus followed on from the Winterbourne View scandal and Stephen Bubb's review which recognised vulnerable people can be at risk of abuse in institutional care. The Care Act 2014 and the Government's Transforming Care Agenda has sought to encourage this shift towards increasing the availability of community-based, supported housing.

A report by Mencap, a leading UK charity for people with learning disabilities, shows that demand for SSH is rising. It projects that demand for SSH will increase from a baseline of 22,000 - 30,000 SSH units (typically occupied by multiple people) in 2017/18 in England to 25,500 - 33,500 units by 2021/22 and to 29,000 - 37,000 units by 2027/28. This is driven by:

- The population of people with learning disabilities is growing due to higher survival rates at birth and increasing life expectancy
- Government policy, particularly the Transforming Care Agenda, which promotes moving people out of institutional settings to community-based housing alternatives that promote independent living
- Decline in informal support networks and at-home care, with more working mothers and increases in single-parent families

Unlike regular social housing, SSH is developed directly in accordance with local authorities' or the health services' strategic priorities. For most tenants of SSH, the alternatives would be care homes or long-stay NHS beds. Neither of these environments promote independent living.

From the report, there is strong evidence that SSH both delivers social impact and is a cost-effective way of providing housing to those with complex needs. SSH has a lower overall cost to local authorities compared to residential or institutional care. The Mencap report found that a person living in SSH requires, on average, state funding of £1,569 per week for care and housing costs. This is a reduction of £191 per week when compared to a residential care placement, or £1,931 per week when compared to an inpatient place.

Most if not all of people living in SSH will be eligible for and claim Housing Benefit to cover the cost of their accommodation. In August 2018 the Government published a briefing paper 'Funding for Supported Housing: Government Response to Two Consultations' confirming this funding mechanism would continue.

The decision was taken that all supported housing will have its core rent and additional housing costs funded through Housing Benefit - rather than being devolved to a Local Authority controlled budget. This has been a welcome safeguard and is a positive sign the government acknowledges the importance of funding SSH for vulnerable people.

In August 2018, the government also published the social housing green paper "A New Deal for Social Housing". A key theme in this was the need to expand the supply of social housing overall. The government continues to target the building of 300,000 new homes per year with greater emphasis on the need for additional social homes.

To stimulate the growth in Social Housing overall, the government has also announced it intends to make it easier for Local Authorities to build new homes by raising their borrowing cap by £1 billion - this will be distributed across areas of high demand.

Private finance will have a key role to play if the government is to reach its target of 300,000 homes a year and increasing the availability of SSH.

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Assura: Under a new Secretary of State for Health, the NHS is planning the allocation of its additional funding with a renewed focus on illness prevention. This focus leans to investment in primary care, partnership working with community healthcare services and social prescribing. Further detail for NHS capital investment will come with next year's spending review, but with private finance initiatives ("PFI") ruled out by the Chancellor, good value public private partnership options for investment in community healthcare buildings, such as third party development, can play an important role.

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Renewable energy

(compare renewable energy funds **here**)

NextEnergy Solar: During the period, the Consultants revised their forecasts for the UK wholesale power price upwards on average and project a lower real growth rate. Factors that contributed to these revisions include the stronger commodity prices in the near-term relative to recent years driven by the expectation of cold winters, a decline in gas storage as well as oil supply in the UK and the increasing demand from gas generation. In the long-term, wholesale prices are expected to increase in line with gas and carbon prices but counterbalanced by the growth in low-cost renewable generation.

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John Laing Environmental Assets: In the period under review, short-term [*electricity*] prices have increased significantly, from £49/MWh for winter contracts at 31 March 2018 to £69/MWh at this period end. Post the period end, electricity prices have started to fall back, demonstrating the inherent variability in these revenues.

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Resources

(compare commodities and natural resources funds **here**)

Andre Liebenberg, chief executive officer, Yellowcake: The $U3O_8$ spot market demonstrated notable price strengthening during the period. After reporting a yearly low point of USD 20.50/ lb in April, the spot price rose to USD 27.35/ lb $U3O_8$ at the end of September and has since risen to USD 29.15/ lb $U3O_8$.

Monthly spot market transactions averaged slightly more than 5.0 million lb $U3O_8$ during the January to June period, but rose significantly during the July to September period to an all-time high quarterly volume, resulting in 69.7 million lb of $U3O_8$ transacted in the year to the end of September. The monthly level of transactions during July totalled 15.3 million lb of $U3O_8$, which was the highest monthly quantity on record, followed by 11.8 million lb $U3O_8$ in August, the second highest monthly volume on record.

Critical market factors included the purchasing of physical product by investment entities, *(especially Yellow Cake)*; announcements by Kazakhstan that annual uranium output continues to be reduced to a target level 20% below previously planned 2018-2020 production and Cameco extending the suspension of operations at the McArthur River/Key Lake facility (18 million lb $U3O_8$/ year) for an indeterminate period. In addition to the McArthur River suspension, Cameco also announced their intention to implement market purchases totalling 11-15 million lb $U3O_8$ through 2019 in order to meet existing contractual delivery commitments.

In the United States, the U.S. Department of Commerce ("USDOC") initiated an investigation into the national security aspects of high levels of foreign uranium importation in support of commercial nuclear reactor operations. Two U.S. uranium production companies have requested government-mandated purchase requirements equating to 25% of annual domestic uranium consumption (11-12 million lb $U3O_8$/ year) in order to support an economically-viable domestic nuclear fuel cycle. The USDOC has until 15 April 2019 to submit its findings and recommendation to the United States Administration, which then must issue a final determination within 90 days.

The reactor restart program in Japan continues to progress with nine reactors now operating and a further six units approved for operations by the Nuclear Regulatory Authority. Subject to all governmental requirements being satisfied, Japanese utilities anticipate a total of 32 reactors could be operating by 2026-2027.

The Chinese commercial nuclear power program continues to expand with a total of 43 operating reactors (40.7 Gigawatt Electrical ("GWe")) as of August 2018, and an additional 15 units (16.3 GWe) under active construction. The current official plan is to reach total installed nuclear generating capacity of 150 GWe by 2035.

Looking forward, we expect current market trends to continue as investments in physical uranium, nuclear fuel trader purchasing and producer buying dominate the near-term market.

QuotedData

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