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Points of View

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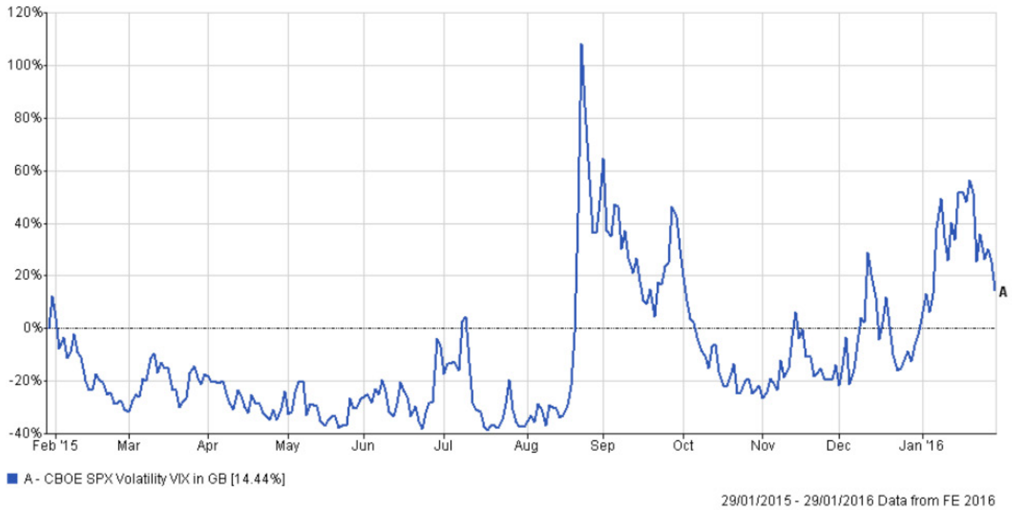
Any respite from market volatility in December proved to be short lived and markets have had a particularly difficult start to 2016. As noted last week, volatility has been on the rise again since November as a result of continued concerns over China, the Oil price and recession risks in the U.S.



Volatility 29.01.2015 - 29.01.2016

Despite a rally over the last few days in the period, equity markets around the world ended the month in negative territory with U.K. large caps being the worst performer finishing down 4.92% and the U.S. market being the best but still losing 1.29%.

"Safe haven" assets performed strongly in the risk off environment with Gilts and Index Linked Gilts gaining 2.79% and 4.07% respectively. Corporate credit fared less well, returning 0.65% and Strategic Bonds ended the month virtually flat.

UK

As mentioned previously, the U.K. stock market is heavily exposed to the Oil & Gas and Mining sectors, both of which suffered on the back of a renewed plunge in the Oil price. This combined with wider investor concern over the strength of the global economy meant that U.K. equities were the worst performing asset class this month. However, the lower Oil price should help bolster consumer confidence in the short term as this feeds into real wage growth. Volatility in U.K. markets, particularly Sterling, is likely to remain high as we approach the EU membership referendum. Uncertainty over the outcome is likely to defer investment in the UK by Corporations which may have an adverse impact on growth and financial markets in the short term.

US

A potential knock on effect of the lower Oil price is that the U.S. Fed might not be able to enact their anticipated four interest rate rises this year as inflation will take longer to come through. This means that the path of rate rises is likely to be shallower with perhaps only two or three hikes, which is more in line with market expectations.

As per the UK, the lower Oil price is a good thing for the consumer as real wage growth is rising in the U.S., as is household credit growth, which points towards a confident consumer and a continuing recovery. Whilst the outlook for the U.S. economy is uncertain, there are other reasons to be confident that a recession is not looming such as increasing consumer confidence, jobless claims trending lower and increasing housing starts. Having said that, the risks of recession have certainly risen over the past few weeks.

Europe

The ongoing threat of deflation in the Eurozone still looms over the economy and the ECB. Whilst the core rate of inflation reached 1.00% in January the headline rate came in at a mere 0.40%, well short of the 2%, or just below 2%, target. This has prompted further words of reassurance from Mr Draghi along with a hint that monetary policy will be eased yet further in March. All eyes then will be on the ECB in March for signs of further QE or a deeper cut to central bank deposit rates. Central bankers have demonstrated an ability to move markets over the past few years and one hopes that Mr Draghi manages to placate markets once again.

Japan

Governor Kuroda surprised the markets by introducing negative deposits rates, just 12 days after they were ruled out as a possibility. This sent the Yen tumbling versus the Dollar and markets around the world rallied. The hope is that the move will encourage banks to lend to the real economy which will, in turn, lead to greater consumer confidence and spending. This would point to domestically orientated companies being the primary beneficiaries if the policy is successful together with exporters if the Bank of Japan is successful in keeping the Yen weak.

Emerging markets

As a reminder, "Emerging Markets" are a diverse and broad set of economies each with their own tailwinds and headwinds. This makes selectivity in the Emerging Markets key and manager experience and skill is as important as ever. Generally speaking, the Emerging Markets have been hit with an almost perfect storm of a strong U.S. Dollar, plunging Oil price and a slowing China. All of this has led to extremely negative sentiment towards the region as a whole and depressed valuations. Therefore, on a long term view, the Emerging Markets are beginning to look attractive. However, there may be more volatility to come until path of the Chinese economy and U.S. rate rises appear more certain.

First published on 2nd Febraury by Stephen Lennon of Parmenion Investment Management.

It was a turbulent start to 2016 as renewed instability in the Chinese equity market and a further deterioration in the oil price saw global stockmarkets post steep negative returns. In bond markets, perceived safe havens rallied with Treasury, gilt and Bund yields declining.

US

US equities performed poorly in January as they were negatively impacted by both fears of slowing global growth (following events in China) and a decelerating domestic economy. The latter concern was underlined by news that GDP had expanded by a disappointing 0.7% in the fourth quarter of 2015. The S&P 500 fell by 5.0% over the month.

The financials sector lagged as expectations moderated about the number of times the Federal Reserve (Fed) would increase rates in 2016 after December's 25 basis point rise. Meanwhile, many of the highly-rated technology and consumer discretionary companies, which had performed so well in 2015, corrected sharply in the risk-off environment, including the 'FANGs' of Facebook, Amazon, Netflix and Google.

The energy sector was negatively impacted as investors anticipated a particularly difficult fourth-quarter earnings season, albeit an end-of-month recovery in crude oil prices mitigated some of the share price losses over the month. Meanwhile, Apple readied investors for a drop in sales in the quarter to March, as the market in general fretted about the impact of ongoing dollar strength and slowing global growth on the outlook for the multi-national blue chips in 2016.

Small and medium-sized companies underperformed amid the patchy domestic economic newsflow. While December US non-farm payrolls were robust, both retail sales and industrial production fell as a precursor to the poor fourth-quarter GDP print. Against this backdrop, defensive sectors performed relatively well, including telecommunication services, utilities and consumer staples.

Eurozone

European equities experienced a difficult start to the year with the MSCI EMU index returning -6.3%. Global concerns were a significant factor in the declines with weaker Chinese data and the ongoing oil price slump putting pressure on equity markets. Locally, worries over non-performing loans in the Italian banking sector were also to the fore. There was some respite towards month-end after Mario Draghi indicated that the European Central Bank (ECB) could reconsider its policy in March, leading some in the market to expect another 10 basis point cut in the deposit rate.

Italy was the weakest regional equity market amid pressure on the banks due to mounting concerns over their non-performing loans burden. The government's plan to deal with the problem was greeted with scepticism by the market; rather than creating a bad bank the approach relies on private investors buying bundles of loans with a government guarantee. The financials sector as a whole was weak, with Deutsche Bank reporting a €6.8 billion loss for 2015. The automobiles and components subsector came under significant pressure amid concern that other carmakers, aside from Volkswagen, may have circumvented emissions regulations. Amid the difficult market conditions, consumer staples was the only sector to post a positive return as investors sought out safe havens.

On the macroeconomic front, the flash composite purchasing managers' index slipped to 53.5 from 54.3 in December, indicating ongoing growth albeit that this was the slowest rate of expansion in almost a year. Eurozone annual inflation (consumer price index) ticked up to 0.4% in January from 0.2% in December. France saw fourth quarter GDP growth slow to 0.2% quarter on quarter while in Spain growth picked up to 0.8% quarter on quarter.

UK

The FTSE All-Share index recorded a loss of 3.1% amid continued weakness in commodity prices, which were dragged down by concerns about China and the global growth outlook. Small and mid-sized companies performed particularly poorly against a backdrop of growing fears for the domestic economy. These worries were also reflected in a pronounced fall in the value of sterling as expectations for the first rise in UK interest rates moved out.

The mining sector weighed on the market as a renewed fall in metal prices reignited concerns about the strength of balance sheets. However the energy companies bucked crude oil weakness as BG Group shareholders approved the merger with peer Royal Dutch Shell. Financials were a drag on the market, led by Asian-exposed Standard Chartered, while news of further provisions at Royal Bank of Scotland weighed on the UK domestic banks. In general, defensive parts of the market performed well, notably the tobacco sector after Imperial Tobacco struck a record high, in part following renewed merger & acquisition speculation.

Expectations for the "lift off" in rates moved out after Bank of England Governor Mark Carney gave a cautious synopsis for UK growth during a speech at the University of London. Like Chancellor George Osborne's own cautious outlook statement at the beginning of the month in Cardiff, Carney pointed to the potential for global macroeconomic uncertainties to impact upon the domestic economy.

With respective declines of 5.4% and 5.7%, the FTSE 250 (ex investment trusts) and FTSE Small Cap (ex investment trusts) indices fell markedly in excess of the FTSE 100 (-2.5%). Many of the UK market's domestically-focused sectors, including the general retailers, travel and leisure companies, and housebuilders, performed relatively poorly. However, the supermarkets recovered strongly, with Tesco's third-quarter and Christmas trading updates pleasing investors.

Japan

In common with many other global markets, Japanese equities were very weak in the first few weeks of 2016 before recovering some of the lost ground to close the month down 7.5% in local terms. The currency followed a similar reversal, but overall moves reduced the loss on the month to 3.8% for a sterling-based investor.

Market dynamics were dominated by a single event on the final trading day of the month when the Bank of Japan (BoJ), against all expectations, moved to implement a negative interest rate policy on excess reserves held at the central bank. In essence this is designed to incentivise banks to put excess cash to use in the economy rather than building up reserves at the BoJ. While the move is clearly in line with the BoJ's aim to increase inflationary expectations, the new policy will also have repercussions throughout the financial system and the real economy. In the process, the BoJ Governor, Mr Kuroda, has again demonstrated his ability to surprise financial markets, not least because he himself clearly ruled out such a move just a week ahead of the decision.

Investors had limited time to price in this change before the end of the month, and sector relative performance for January as a whole therefore tells us almost nothing. The new policy appears at face value to be bad for banks and, potentially, good for real estate. The bank sector did indeed close January down by 15.3% but, in truth, most of this happened before the policy announcement. Conversely, the real estate sector, which had been having a lacklustre month, leaped 9.5% in the final session.

Economic figures released during January were generally weaker than expected, including industrial production, retail sales and housing data. However, labour market data were more encouraging and inflation figures showed no significant deviation. Overall, there was nothing which could be viewed as a particularly strong trigger for the policy move.

January also saw the start of the quarterly earnings reports for the October to December period. As has become the trend in recent quarters, individual share price reactions in the immediate aftermath of results appear somewhat excessive. The scale and speed of these moves may be linked, at least in part, to the very high proportion of market trades now accounted for by short sellers in the Japanese market. While these positions don't typically influence long-term price setting in the market, they do appear to be adding significantly to day-to-day volatility, especially during results periods.

Asia (ex Japan)

Asia ex Japan equities had a turbulent start to 2016 as markets posted negative returns, with losses sparked by renewed market turmoil in China and a plunging oil price. Losses were later pared by monetary easing moves by Japan and indications that the ECB could follow suit. Chinese equities, via the onshore A-share markets, led the losses as stockmarkets were forced to close early twice within a week after a new circuit-breaking mechanism was triggered. The impending expiration of selling restrictions on major shareholders and a weakening of the Chinese yuan by the People's Bank of China were blamed for the heavy market falls. However, the Chinese authorities later extended the share-sale ban and suspended the circuit-breaker mechanism. Continued weak data for the Chinese economy also weighed on sentiment.

Meanwhile, in Hong Kong stocks also saw declines as market fears in China spilled over into the local stockmarket. Over the strait in Taiwan, the market was also down on worries over the global economy. In Korea, stocks finished in negative territory with competitive worries following China's devaluation of the yuan weighing on the local market given the economy's export-reliant growth model.
In ASEAN, Thailand was up on a better-than-expected reporting season for companies while Indonesian stocks gained after an interest rate cut by its central bank. Philippine stocks ended the month lower as its market saw heavy outflows on foreign investor selling. Indian equities also declined with China worries and the lack of progress on reforms weighing on investor sentiment.

Emerging markets

Emerging markets were negatively impacted by US dollar strength and growth concerns in January, and the MSCI Emerging Markets index declined in value to underperform the MSCI World index. In emerging Asia, Thailand generated a positive return, as the government announced it is considering the launch of new stimulus to boost the rural economy. China underperformed and was the weakest regional market. A series of factors accounted for the weak performance. These included ongoing yuan weakness compared to the US dollar, continued weak economic growth, and spill-over effect from the removal of selling restrictions in mainland stockmarkets. Uncertainty over currency policy was a significant headwind. Competitive currency pressures in the region have intensified following the BoJ's implementation of negative interest rates, which led the yen to weaken.

In Latin America, Peru was the strongest market, with large index stock Credicorp providing support. Brazil lagged and was the weakest regional market. Inflation reached 10.7%; however the central bank, contrary to expectations, left rates unchanged. Meanwhile other economic indicators showed further signs of deterioration.

In emerging Europe, Hungary was the standout market, owing to support from OTP Bank and Gedeon Richter. Russia registered a negative return at the margin, owing to rouble weakness, but outperformed. In South Africa, economic data continued to deteriorate and the central bank moved to hike rates 50bps to 6.75%. Greece was the weakest index market with banking stocks falling heavily.

Global bonds

In January, a sharp decline in risk appetite led to high levels of market volatility and weakness in risk assets. Instability in China's two principal equity markets overshadowed most other market drivers, particularly early in the month. The circuit-breakers designed to stem steep market declines were triggered twice, before being removed on 8 January. A further decline in the oil price exacerbated investor concerns, as the oil price reached a 12-year low in mid January. Perceived safe havens rallied, with Treasury, gilt and Bund yields declining. High grade corporate bonds were stable and high yield bond indices sold off.

The 10-year Treasury yield fell sharply from 2.27% to 1.92%, as the equivalent gilt yield fell 40 bps from 1.96% to 1.56%. The 10-year Bund yield dropped from 0.63% to 0.33%, shrugging off the investor disappointment from December in light of renewed global growth concerns.

The investment grade BofA Merrill Lynch Global Corporate index generated a total return of 0.48% as the high yield equivalent fell -1.44%1. The dispersion of returns across US dollar, sterling and euro markets was relatively narrow. Investment grade corporate bonds in all three currencies ended the month with positive returns, while all three high yield indices declined.

Emerging market debt indices saw significant declines early in the month before rallying to recover most of the set-back. The JP Morgan EMBI Global Diversified index fell -0.2%%. This is a 'hard currency' sovereign index, which tracks emerging market bonds traded in less volatile US dollars. The local currency JP Morgan GBI-EM Global Diversified Composite index rose 0.4%. In corporate bonds, the hard currency CEMBI Diversified Broad Composite fell -0.4%.

1 Investment grade bonds are the highest quality bonds as determined by a credit ratings agency. High yield bonds are more speculative, with a credit rating below investment grade.

First published on 8th Febraury 2016 by Cazenove Capital Management.

Market Overview from Sanlam UK

It was a foul January. The world lost the talents of Bowie, Lemmy and Rickman, the weather stayed wet and miserable, and by the 20th day the headlines called it the 'The Worst Month Ever for Markets'. The FTSE 100 gave up 9.1% in 2016's first twenty days; keep losing money at that rate and we'd be back in the Stone Age by August.

But the direction reversed, and by month-end the FTSE's losses were only 2.48%. Still bad, still the worst kick-off to a year since 2009, but not, in the end, a disaster.

And although share prices were down, UK government bonds, often overshadowed by the more exciting parts of the market, gained nearly 4% in January, while corporate bonds were broadly flat.

The major themes of late 2015 continued into January: slowing Chinese economic growth, low oil prices, and uncertainty over the right path for major interest rates all remained in the mix. The last one presents a challenge: how can it be correct to increase interest rates when inflation is nowhere to be seen and economies are slowing? And yet, how can it be right to keep them at these 'emergency' levels when unemployment continues to fall and consumer spending is strong? This question - in one form or another - is being asked right now in the central banks of most developed nations; the answers they come up with will affect us all.

Oil prices still hover around $30 a barrel. This is bad news in the short term, because the oil price feeds directly into the revenues of huge firms, such as Shell (Royal Dutch Shell PLC, London) who depend on it directly and make up a big chunk of the FTSE. But a falling oil price should be good news in the longer term. We've all seen petrol pump prices fall below £1 a litre for the first time in nearly a decade- this puts more money in our pockets and cuts the running costs of many types of business. But these positive factors take longer to show up in equity prices.

So, it's not been a good start, but there are eleven months of 2016 still to come.

Don't wait for the air to clear and share prices to calm down before you do anything. Embrace the chaos, make friends with uncertainty, and stick to your plans. Markets without turbulence are hardly markets at all.

First published by Sanlam UK on 4th February 2016.

Fixed and Individual Protection 2016

From 6 April 2016 the lifetime allowance will reduce from £1.25 million to £1 million, for the tax year 2016/17 and then this allowance will be increased in line with the consumer price index (CPI) from tax year 2018/19 onwards.

With the introduction of this reduction in the LTA, the Finance Bill 2016 has also made provisions for transitional protections for pension scheme members who may need to protect their pension savings from the lifetime allowance tax charge, depending upon the value of their total pension funds.

The two forms of protection that will be available from 6 April 2016 are fixed protection 2016 (FP16) and individual protection 2016 (IP16) and will be available for UK residents with total pension savings in excess of £1 million or who they think will have pension rights worth over £1 million by the time they take their benefits.

FP16 and IP16 will operate in a similar way to FP2014 and IP2014. For those individuals who obtain FP16, they will have a LTA equal to £1.25 million and for those who obtain IP16 they will have a protected LTA of the value of their pension savings as at 5 April 2016 which will be subject to an overall limit of £1.25 million. Individuals can apply for both FP16 and IP16, with FP16 taking precedence over IP16.

The conditions for maintaining FP16 include that:

- Individuals in defined contribution pension schemes must ensure that no further pension contributions are received by the scheme on or after 6 April 2016.
- Individuals in defined benefits schemes must not accrue further benefits above a 'relevant percentage' after 5 April 2016. The relevant percentage for defined benefit savings will normally be either the annual rate specified in scheme rules as of 9 December 2015 or CPI (if no rate is specified).

Individuals with IP16 are able to continue contributing to a registered pension scheme, subject to the rules governing pension contributions for UK registered pension schemes. However, they would be subject to the LTA charge on any excess savings over their personal LTA when they take their benefits.

How will it work?

The Autumn Statement delivered on 25 November 2015 announced that from July 2016 HMRC would be introducing a new online service for pension scheme members to apply for FP16 and IP16. However because the new service is not available until July 2016, interim measures will be implemented for those individuals wishing to apply for FP16 and IP16 between 6 April 2016 and when the new system goes live in July, to give individuals temporary protections.

The interim process requires scheme members to contact HMRC in writing with details of their intention to rely on either IP2016 or FP2016.

FP2016

For FP16, in addition to their name and national insurance number, the scheme member will need to provide HMRC with:

- a declaration that they do not hold primary protection
- a declaration that they do not hold enhanced protection
- a declaration that they do not hold fixed protection 2012
- a declaration that they do not hold fixed protection 2014

IP2016

For IP2016 the scheme member will need to provide HMRC with:

- details of their relevant amount
- a breakdown of their relevant amount (as at 5 April 2016) consisting of:

  - Amount A: Pre A Day Pensions in Payment (£)
  - Amount B: Post A Day BCE's (£)
  - Amount C: Uncrystallised Rights (£)
  - Amount D: Non UK Rights (£)
- a declaration that they do not hold primary protection
- a declaration that they do not hold IP14

For both FP16 and IP16 records held by HMRC will be checked against the details of the individual to ensure the declarations are correct. If no other valid protection is held (that precludes the member from holding FP16 or IP16) the scheme member will be issued with a temporary reference number for their protection to provide to their pension scheme administrator.

Individuals who apply for protection and/or take benefits during this interim process to protect their pension savings must make a full online application once this becomes available to ensure their pension savings continue to be protected from the LTA tax charge. A permanent reference number will be issued when the full application is made that the individual must provide to their pension administrators.

If the scheme member fails to make a full online application, their application for FP16 or IP16 made under the interim process will not be valid and they will be liable to a LTA tax charge on their pension savings above the LTA.

We expect more information on this over the coming weeks but we hope we have given you some food for thought on this subject that will assist you with dealing with clients who may be affected by the reduction in the LTA. If you have further queries on the content of this edition, or other technical queries, then please contact the Technical e-helpdesk at technical@sanlam.co.uk.

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