FINURA

PARTNERS

POINTS OF VIEW

MONTHLY COMMENTARY FROM PARMENION INVESTMENT MANAGEMENT

Globally equities continue to churn higher with volatility conspicuosly absent. Fundamentals remain in the most part on a quiet recovery helped by the continued central bank support. Politics however continues to take centre stage with Trump's misjudgements, Macron's success and Corbyn's surprising revival in the UK election polls.

Index

Index	May Return (£ base)
FTSE World Index	2.48%
FTSE USA TR GBP	1.59%
FTSE Europe ex UK TR GBP	5.17%
FTSE Japan TR GBP	3.26%
FTSE 100	4.92%
FTSE all share	4.36%
FTSE EM	1.80%

*Source FE June 17. Past performance is not an indication of future returns. The value of investments and any income from them is not guaranteed and can go down as well as up.

United States

Treasuries rallied and equities sold off on the 17th driven by increased potential for only the third impeachment in American political history. The US constitution states only the most serious offenses should be pursued under this mechanism, specifically "treason, bribery, or other high crimes and misdemeanours". The S&P 500 fell almost 2% which was a large move given the lack of volatility present in markets. In fact, it was the largest daily fall since September.

Even so, the wall of money continues to exert its pressure and we saw a recovery in markets – closing at new highs by month end. Conversely, the bond market paints a slightly different picture, where yields remained depressed as we close the month. Whitehouse success in re-packaging the deal to repeal Obamacare in such a way to garner sufficient approval from the House of Representatives was initially received well by the bond market, with 10bp added to the 10 year yield, however all gains were reversed and more, by month end, suggesting a more gloomy outlook than the story painted by the stock market.

This has all unfolded under a steadying and strong, if slightly less improving fundamental picture, however one positive enough for the Fed to continue their rhetoric of a further rate rise in June. Unemployment remains at lows with many other signs of strength in the labour market, while ISM non-manufacturing Purchasing Manager's Index indicators continue to improve. The more important ISM manufacturing PMI disappointed early in the month while inflation was a little 'soggy', but the Fed points to idiosyncratic factors that will be transitory in their impact, curtailing positive price appreciation.

US 10yr Treasury Yield

Source Bloomberg.com May 17

S&P 500 Index

Source FT.com May 17

United Kingdom

The FTSE 100 finished the month strongly as an opinion poll implying Jeremy Corbyn had cut the Tories lead to 5 points pressured Sterling in combination with signs of an economic slowdown. Having previously rallied to above 1.3 on expectation of a Tory landslide and strong mandate for Brexit negotiations, the recent narrowing of Theresa May's lead has been a boost to the large cap exporters from the currency translation effect. Conversely, the prospect of real wage cuts as the weak currency imports cost push inflation is a burden on domestically focused corporates. Having said that, the labour market remained healthy and retail sales published in May were very positive even if the manufacturing production disappointed.

Europe

Europe began the month with an important victory for the centrists as Macron defeated Le Pen by two to one. Publically, much of the political risk has been lifted and another vote against extremist politics (after the Dutch election) has helped lift European stocks consistently across 2017. Macron has the ambition to make large waves across France, with labour reform, reductions in corporate tax and an ambitious combination of spending cuts and government stimulus. While his fledgling party – La Republique En Marche – may have mirrored its leader in its remarkable rise, for Macron to succeed it needs success in the parliamentary elections scheduled for June.

The election will clearly matter, not least for Macron's labour market reforms, but it should also help highlight the popularity of the European project in France, more so than what could be implied from the presidential contest. Europe-domiciled actively managed funds held more than €162bn in French assets at the end of last year, €45bn more than Germany,

emphasising the importance the presidential, and now future parliamentary elections will have on this asset class. Further, average daily flows into ETF's that track European equities have surged to more than $570M since Macron won the first round election compared to daily outflows of $130M over the past 12 months. Flows imply investors feel the risks have dissipated and are buying into Macron's reform agenda, however, like Trump, he faces many hurdles to success which must moderate our optimism.

Japan

The Japanese labour market continues to tighten, as highlighted last month, overtaking the bubble peak of 1990 for job openings to applicants during May. While Abe's economic stimulus now has companies looking for workers, there is still little upward pressure on wages. One difference to 1990 needs to be pointed out. Back in the boom years it was a rapid growth in jobs creating the labour market tightness whereas today it is a lack of supply. More clearly positive news for the administration was an unexpected increase in Preliminary GDP growth for Q1, up to 0.5% from 0.3% the previous quarter.

Emerging Markets

Less than 2 weeks after China said it would open up its domestic market to US rating agencies, Moody's has cut the country's credit rating for the first time in 25 years given the financial and economic risks they observe. While this has had little immediate impact – domestic investors paying little attention to this foreign ratings agent – the medium term impact could be larger given many sovereign wealth funds have explicit mandates that require bonds above a certain rating. The downgrade leaves China on a par with Israel, the Saudi's and the Czech Republic. Elsewhere, Brazilian stocks fell over 8%, alongside currency depreciation, as the story broke that President Michel Temer had endorsed bribe payments. Constitutional constraints make a general election unlikely before 2018, implying any form of exit from office by the president will freeze economic reforms, leaving growth potential in hiatus.

Returning home, we await the outcome of the General Election and the start, in earnest, of the UK's Brexit negotiations.

*All performance data quoted in this article is derived from FE Analytics.

Any figures quoted are for illustrative purposes and should not be taken as a forecast or guarantee. Past performance should not be seen as an indication of future returns and clients may get back less than they have invested.

First published on 1st June 2017 by Parmenion Investment Management.

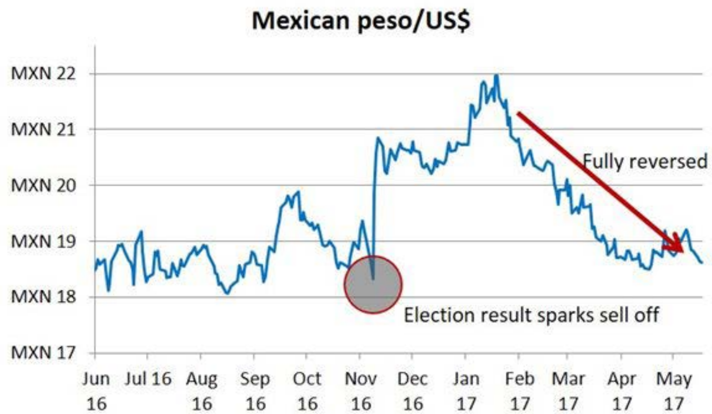
DO MARKETS REALLY CARE ABOUT THE POLITICS?

Financial commentators are always looking to justify market moves. And with politicians never short of wind they provide a convenient source of noise to justify any conceivable price action.

This fitting-the-story-to-the-facts overstates the role politics play in financial markets. That's not to say politics doesn't have a huge impact at times, how else could one explain the dramatic market moves following Brexit, Donald Trump and the French election? It's just that these occasions are infrequent and, in each of these cases the event started a binary moment for something that financial markets care a lot about.

In purely financial terms the Brexit vote is simply about access to the EU economy. The "Trump trade" is about deficit expansion (infrastructure spending and especially tax cuts). The French election only mattered because it could've catalysed the euro's demise. The rest is largely just noise that makes for interesting headlines or is relevant to other stakeholders. Tweets, firings, debates and meetings may give clarity on the probabilities of certain outcomes but their impact on prices should be viewed with scepticism.

Even in cases where something seemingly dramatic happens, the ultimate effect is usually pretty benign. The ride the Mexican peso has been on since the US presidential election is a great, example of this. Given all the noise before the election about the border wall, etc., etc., there was a very aggressive move in the peso, weakening after the result became clear from Mex$ 18 to over Mex$ 22 to the dollar – a ~20% move. It may be hard to believe, but this move has completely reversed despite little changing regarding plans for walls and taxes.



SOURCE: Bloomberg

We position our client's portfolios conservatively ahead of such events - where the outcome has a binary outcome – a stance that added significant value last year where we did not anticipate the result of either the EU referendum or the US presidential election. This approach of not overestimating our own forecasting abilities is the foundation of our investment philosophy. We know how difficult it is to forecast events, and how correctly anticipating the market's reaction further compounds the challenge.

Investing in uncertain times

We think it is easier (and better) to focus on companies whose earnings are less dependent on the global outlook. While this may not be the most exciting of strategies, well-managed companies with strong balance sheets and an attractive competitive advantage can offer investors a steady and sustainable way of achieving growth. This is because they have traditionally offered higher returns on capital and they have the ability to distribute excess cash to shareholders rather than constantly having to re-invest in their own business.

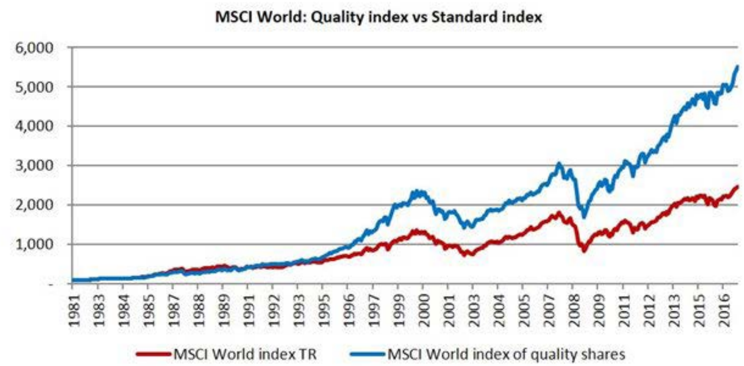
Quality stocks exist in all sectors (albeit some more than others), and across all geographies. It is very difficult to predict what the wider theme of the day is going to be and, within our own stock picking, we don't spend much energy on this risky approach. Rather, we spend our time looking for businesses with:

1. Growing industries, like technology, healthcare, consumer goods, etc. We don't want to swim upstream, no matter how well the business is run
2. Stable business models that are very difficult to replicate
3. Powerful brands, patents, and/or scale, as these are all barriers to entry, and give companies pricing power and stable margins. We know roughly, for example, what the earnings are likely to be for Johnson & Johnson next year, but it's anyone's guess what some new hot fashion stock will earn
4. Strong management teams that have a track record of delivering returns to shareholders by allocating capital well and running a tight ship
5. Financial statements that show the business is not overly indebted
6. Products that are not commoditised. We want companies that are in control of pricing, rather than the market dictating this.

Once we have identified the businesses we want to own, we wait for bad news, or a poor quarterly earnings report. This usually spooks the market and gives us a chance to buy a great business at a price where the returns we expect make sense over the longer term.

How do quality stocks perform versus 'normal' stocks?

The chart below shows how quality stocks have outperformed the standard index over the last 30 years. Where the graph shows an upward trend, it means that quality stocks outperformed normal, and vice versa.



SOURCE: Bloomberg

Past performance is not a reliable indicator of future results.

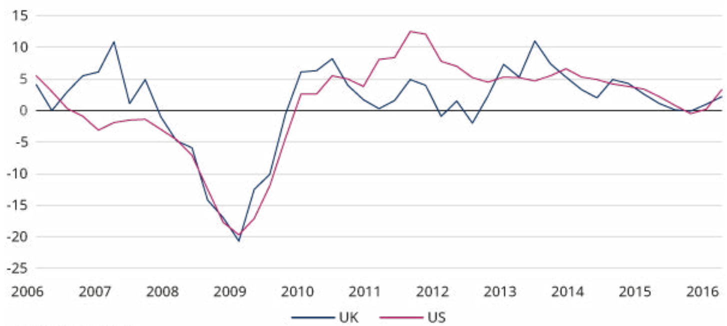
We know quality stocks are not always as fast growing, but because they don't have upsets nearly as often their long term performance has been exceptional. Of course their share price can fall like any other stock, and their earnings will suffer if the economy is suffering, but the underlying businesses are more resilient and they usually bounce back very quickly once confidence returns. In times of political uncertainty this approach can offer some piece of mind.

First published on 18th May 2017 by Matthew Brittain, Investment Analyst at Sanlam UK.

US AND UK FIXED INVESTMENT REVIVED IN Q1

The UK and the US saw a strong pick-up in fixed investment in Q1 2017 after more than two years of subdued spending. The Bank of England Agents' survey pointed to increased investment intention in Q1 2017 amid resilient credit availability to corporates whilst US fixed investment rose at the fastest pace in five years in Q1 2017 and was consistent with the surge in corporate confidence post-election.

Fixed investment growth – UK vs. US (% YoY)



Source: Datastream.

Both UK and US GDP growth slowed in the first quarter (Q1) of 2017, undermined by slower growth in household consumption as higher inflation eroded spending power. On the positive side, both economies saw a strong pickup in fixed investment (investment in physical assets such as machinery, land, buildings, vehicles and technology) after more than two years of subdued spending. In the UK, fixed investment picked up +1.2% in Q1, the strongest pace in nearly two years.

Reflecting this, business investment saw its first positive year-on-year growth since Q4 2015. In the US, fixed investment expanded at +2.9% in Q1, the fastest pace in five years. The revival in the investment cycle is crucial to longer-term trends in productivity, wage and GDP growth. So, what were the drivers behind the revival in corporate spending as the year began and are they sustainable?

In the UK, the pick up in business investment was due to the increase in other machinery and equipment, and intellectual property products, particularly software data. The Bank of England Agents' summary of business conditions stated that investment intentions increased in Q1, reflecting stronger demand and an easing in uncertainty over shorter-term projects due to better than expected economic activity.

It was revealed that firms had been going ahead with strategies designed to mitigate increased labour and material costs, while the rising shift to e-commerce encouraged investment in digital marketing, online capacity and logistics. The development was in line with our view that businesses will invest more to deal with challenges relating to Brexit and rising recruitment difficulty.

Another important factor to consider when looking at business investment is the availability of credit. So far, credit conditions for non-financial corporates have remained good and the latest Bank of England Credit Conditions Survey reported resilient credit availability, this is likely to remain supportive to business investment.

In the US, the surge in fixed investment was led by structures, due to the surge in oil rig counts and mining-related activity as a result of the recovery in oil prices. Residential, equipment and intellectual property investment also contributed positively. This was consistent with the surge in corporate confidence, as reflected by the National Federation of Independent Businesses (NFIB) survey.

The US NFIB Index soared during the post-election period and has subsequently remained elevated despite rising doubts about President Trump's delivery of pro-growth policies. Also, the pick-up in fixed investment suggested the gradual rise in interest rates has not been a hindrance to capital spending. On the contrary, we believe the prolonged period of ultra-low interest rates has reduced the incentive for corporates to take risks, and that the normalisation in monetary policy will be a catalyst to revive much-needed animal spirits.

Looking ahead, two things that may restrain the growth in US capital spending are the marked slowdown in credit to non-financial corporates and the impending taper of the Fed's balance sheet later in the year. On the positive side, strong US corporate cash holdings and potential business-friendly policies will be supportive.

First published on 2nd June 2017 by Janet Mui, Global Economist at Cazenove Capital Management..

8 THINGS YOU NEED TO KNOW ABOUT INHERITANCE TAX

Increasing numbers of people might become liable for inheritance tax payments if property prices continue their historic trend. However, 2016's new inheritance tax legislation and residence nil rate band may ease this problem for some. Legislation is constantly evolving, so you should be reviewing your will regularly – perhaps every five years.

1. The nil rate band has been frozen

Inheritance tax is a tax on the estate of someone who has died. There's normally no tax to pay if the value of the estate is below the current nil rate band (NRB) of £325,000 – married couples and civil partners can have a joint allowance of £650,000 – but any assets above these thresholds are taxed at 40%.

The NRB, which was set in 2009, has now been frozen by HMRC until 5 April 2021. So, if assets increase in value during this time, more people will come to own estates worth more than the £325,000 limit, thereby making them liable for inheritance tax. "However, there are various exemptions that need to be considered," says Paul McKie, Wealth Planning Director at Sanlam. "For example, if you leave everything to your spouse, civil partner or a charity, there is no tax to pay."

2. Wills need to be reviewed and updated

It is a common misconception that having a will in place mitigates your inheritance tax liability. In fact, the main purpose of a will is to dictate who will inherit your assets. It also helps to speed up the probate process. "Legislation is constantly evolving, so you should be reviewing your will regularly – perhaps every five years, if there are no significant changes in the meantime," advises McKie. "If the will contradicts the legislation, then you could end up paying unnecessary tax."

3. Property will be treated separately...

Property is one area set to significantly eat into the NRB, or potentially exceed it. Because of this, many people consider giving away or 'gifting' their property to children, which may reduce their inheritance tax liability, but this does remove the security and control of owning a home in old age. To try to combat this issue, the Government is introducing a new residence nil rate band (RNRB).

"As the name suggests, it considers property specifically," says McKie, "and will be phased in over a four-year period, starting from the 2017/18 tax year. It is available to everybody and does potentially solve some problems."

The RNRB is only available where the main residence passes to children – including step, foster or adopted – or linear descendants on death. "It is important to note that RNRB could be lost if the property is directed into a discretionary trust," says McKie, "so any existing wills should be reviewed to ensure that they benefit from the new rule changes. In London and the South East in particular, though, properties can be so expensive that they will go above the threshold and people will lose out anyway."

4. ... but large estate owners may not benefit

The RNRB will be reduced by £1 for every £2 that the deceased net estate exceeds £2m. So, when it is introduced in 2017, any estate worth more than £2.2m will lose all of the additional benefit. By 2021, when the full allowance of £175,000 is in force, estates worth more than £2.35m will lose all of the extra allowance. These individuals should consider some good-quality planning to mitigate the tax.

5. Both nil rate band types are transferable

Both the RNRB and NRB can be transferred between spouses and civil partners. In other words, the unused percentage of the NRB or RNRB can be transferred from the estate of one spouse to the other and then claimed on the second death. "You can do some planning to utilise the NRB effectively," says McKie. "For example, you can give your NRB band to your children or grandchildren to avoid it being included in the spousal exemption."

6. Downsizing can be accommodated...

The Government recognises that people may wish to downsize to a smaller property later in life, often with a lower value. If this happens, the RNRB that applied to someone's former property can be retained and still be applied to their estate if the replacement property and assets form part of the estate, and if these properties and assets pass to direct descendants. This means that the family home doesn't need to be owned on death to qualify.

7. ... but multiple homes do not qualify

You can only elect one residential property to qualify for the relief, and it will be down to the personal representatives of the estate to elect the appropriate one. This cannot be a property that's never been their main residence, such as a buy-to-let property. "It's something to be aware of if you have two or three properties and have lived in them all," says McKie. "One may be worth more than the others, because of the location for example, so you can elect that and make the allowances work more efficiently."

8. Property ownership can make a difference

Many people own their homes as 'joint tenants', so they have equal rights to the whole property. This means that on the first death, the house automatically passes to the surviving spouse with no inheritance tax. In this scenario, the NRB and RNRB are also passed to the surviving spouse – so, if the estate is valued at more than £2m on the death of second person, the tapering rules will apply; but above £2.2m (in 2017), the full allowance will be lost. "However, switching the property ownership to 'tenants in common' can add some flexibility," says McKie. "This enables each spouse to own different shares of the property and then control who receives their share when they die. This could preserve both spouses' RNRB by keeping each of their assets below the £2m threshold."

Speak to your financial adviser to learn how inheritance tax regulation applies to you. **The Financial Conduct Authority does not regulate tax and trust advice.**

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