LONDON WALL PARTNERS

INDEPENDENT FINANCIAL ADVICE

INVESTMENT MARKETS COMMENTARY
TO 30 NOVEMBER 2016

London Wall Partners LLP
Salisbury House
London Wall
London
EC2M 5QQ

+44 (0) 20 3696 6801 (Direct)
+44 (0) 7740 308 206 (Mobile)
+44 (0) 20 7117 1177 (Fax)
nick.fletcher@londonwallpartners.com

1. Investment markets commentary to 30 November 2016

The last twelve months were largely characterised by subdued global economic growth and inflation, owing to constrained corporate and consumer sentiment. Most central banks continued to keep policy loose or extend stimulus measures to prolong the economic cycle; though US interest rates were increased modestly at the end of 2015 and are likely to be again in due course, interest rates remain at historically low levels around the world. It seems increasingly likely now that governments in developed economies will complement central bank policy with increased public spending to strengthen economic growth; this has latterly contributed to gains in inflation expectations and bond yields. The diminishing impact of the oil price decline from annualised figures will also begin to have an upward pressure on inflation in the coming months.

Even before the EU referendum, mediocre growth and low interest rates looked likely to persist in the UK and Continental Europe for the rest of 2016 and 2017. Though the impact of the UK's decision to leave the EU appears to have not yet had a materially adverse impact, it could constrain economic activity in the UK once the negotiation process begins, as businesses delay their investment plans. The Bank of England ("BoE") reacted to the change in outlook in August 2016 with an interest rate cut to 0.25%, and joined the European Central Bank ("ECB") in expanding its Quantitative Easing ("QE") programme. The referendum result was greeted with a renewed bout of sterling weakness, as shown in chart 1 below, and while this should lead to higher prices for imported goods in the UK in due course, inflation is unlikely to increase to a level which causes concern.

Chart 1 – Sterling trade-weighted index: 1 January 2015 to 30 November 2016.

Another currency which has seen a sharp movement is the Japanese yen, which is traditionally seen as a safe haven asset, and started to strengthen in early 2016 as worries concerning Chinese growth undermined confidence in financial markets.

Bond markets had initially responded to these developments in a positive manner, with UK and US government bond prices reaching new highs in summer 2016. Conventional government bonds however gave back some of their earlier gains towards the end of the reporting period as bond yields turned higher, while index-linked bonds in the UK fared better owing to the prospect of higher inflation.

Stock market returns have varied. The Japanese and European stocks markets declined in local currency terms over the last year, but sterling weakness ensured UK investors enjoyed positive returns in company shares in all major regions over both six and twelve months.

Summary of global market performance

Table 1 below shows that during the year to 30 November 2016, global company shares (as measured by the FTSE All-World Index) returned 25.8% in sterling terms, while UK company shares (as measured by the FTSE All-Share Index) gained 9.8%. UK government bonds delivered a total return of 5.3%, with index-linked bonds rising 9.9%. UK commercial property returned 1.8%.

Table 1 - Six and twelve month market returns.

	% Total Return			
	Six months		Twelve months	
Index	**local**	**£**	**local**	**£**
FTSE All-World	5.9	21.1	4.9	25.8
FTSE All-Share (£)	9.6	9.6	9.8	9.8
S&P 500 ($)	5.7	23.1	7.3	29.3
FTSE Europe ex-UK	0.3	11.6	-6.2	13.0
TOPIX (Y)	7.6	22.0	-4.9	23.9
FTSE All-World Asia ex-Japan	7.7	26.0	9.1	31.7
FTSE Emerging Markets	8.8	27.2	10.4	32.9
FTSE UK Govt 5-15 years (£)	1.6	1.6	5.3	5.3
FTSE UK Govt I-L 5-15 years (£)	8.2	8.2	9.9	9.9
iBOXX £ Corp Bonds 5-15 years (£)	3.9	3.9	7.6	7.6
IPD All Property (£)	-1.6	-1.6	1.8	1.8
Gold Bullion ($)	-1.4	14.8	12.4	35.4

Table 2 overleaf shows returns over longer term periods. During the last three and five years stock and property markets have generated the strongest returns; US and Japanese (TOPIX) company shares have performed particularly well, while emerging markets and Asia ex-Japan have generally lagged. Bond and property markets have also produced positive returns.

Table 2 – Three and five year market returns.

Index	% Total Return			
	Three years		Five years	
	local	£	local	£
FTSE All-World	22.0	46.0	77.5	98.5
FTSE All-Share (£)	15.7	15.7	55.4	55.4
S&P 500 ($)	27.3	66.9	90.1	139.3
FTSE Europe ex-UK	13.3	18.3	66.1	68.0
TOPIX (Y)	24.1	46.2	123.9	92.0
FTSE All-World Asia ex-Japan	12.0	33.1	48.7	63.8
FTSE Emerging Markets	12.1	25.6	39.4	37.7
FTSE UK Govt 5-15 years (£)	18.2	18.2	22.0	22.0
FTSE UK Govt I-L 5-15 years (£)	18.2	18.2	25.5	25.5
iBOXX £ Corp Bonds 5-15 years (£)	22.3	22.3	53.8	53.8
IPD All Property (£)	39.7	39.7	56.2	56.2
Gold Bullion ($)	-4.8	24.8	-31.0	-13.1

Notes:

1. Figures as at 30 November 2016.
2. All figures include income reinvested.
3. Local currency indicated in index name, for single country indices.
4. Investment Property Databank ("IPD") Index may be subject to retrospective revision. The returns of non-sterling assets may increase or decrease as a result of currency fluctuations.
5. See appendix for further Regulatory Information and Disclosures.
6. Source: FE Analytics.

2. Economic and stock market outlook

While the global economic growth outlook is subdued, the current resilience of the US economy gives us confidence that we are still in an elongated economic upturn worldwide. This should enable stock markets to continue to progress, but may lead to higher interest rates and bond yields as recently observed: our recommended allocations favour company shares and reflect a cautious stance on bonds. In our view, high quality companies with resilient earnings are well placed to deliver strong returns to shareholders. In addition, we believe smaller companies and private equity offer attractive long term growth potential, so are advocating allocations to specialist funds in these areas. We continue to recommend allocations to UK commercial real estate; while the Brexit referendum result led some investors to dispose of UK property shares and funds, we believe the asset class should continue to deliver competitive returns in the long term. There is likely to be a beneficial impact of sterling weakness on international investor interest in due course and increased tourism should benefit certain segments of the sector; investments in UK commercial property also provide portfolio diversification.

We are mindful of a number of risks to our central case. One is that current stimulus measures fail to maintain an economic expansion; this would most likely lead to a setback in stock markets and further gains for government bonds, but it may subsequently engender further QE and other measures aimed at restoring market confidence, such as increased government spending.

Another risk is that inflation finally accelerates in a manner which requires interest rates to be increased; this would make cash an attractive asset and undermine the valuations of other financial instruments, though company shares should recover in due course. We will continue to be alert to the possibility of these adverse scenarios developing, but recommend that clients maintain diversified portfolios to protect against any shorter term changes in economic sentiment.

Further details of our outlook for asset classes and regions are discussed in the subsequent sections.

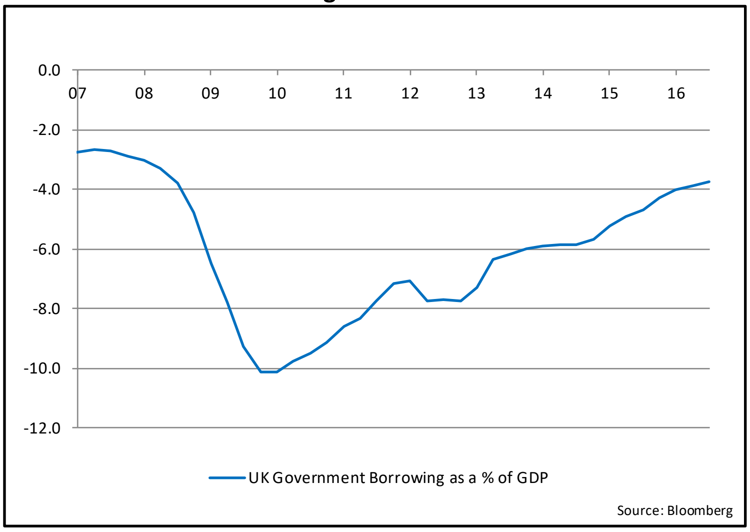
2.1. UK

- The UK economy was in a relatively good position ahead of the Brexit vote; the service sector was growing apace and consumers were supported by a buoyant housing market, rising real wages and a fall in unemployment to a 7-year low of 4.9%.

- In the run up to and following the UK's decision to leave the EU, business investment and hiring plans have been delayed. Ongoing uncertainty over Britain's future trading arrangements and access to the single market is likely to remain a headwind for growth, albeit recent economic indicators suggest a recession is unlikely.

- The extent to which the economy slows will depend on how businesses and consumers respond to fiscal and monetary stimulus measures, and developments in negotiations with the EU. The Government's finances have improved since the financial crisis; as seen in chart 2 below, the budget deficit was over 10% of GDP in 2009 but has since declined to below 4%. The Chancellor of the Exchequer, Philip Hammond, announced greater infrastructure investment as part of his first Autumn Statement, but retained flexibility to respond to developments in the economy as Brexit negotiations unfold.

Chart 2: UK Government budget deficit as a % of GDP.



- Sterling's sharp decline has begun to put upward pressure on inflation, which has risen to 0.9%, as the price of imported goods rises in sterling terms (e.g. food). The BoE currently expects CPI inflation to peak at 2.7% during the second half of 2017. Bond yields in the UK have latterly risen in response to higher inflation expectations.

- The share prices of larger companies in the UK stock market with international operations have risen notably since the vote, given the positive impact of sterling weakness on overseas profits. Conversely, more domestic-focussed sectors have been under pressure in light of UK economic uncertainty, though they have risen from the lows reached immediately after the Brexit vote.

- The FTSE All-Share Index provided a total return of +9.8% during the past six and twelve months.

2.2. US

- The US economy appears to be growing at a reasonable rate. The consumer sector remains robust, reflected in a buoyant housing market, and job growth remains strong; meanwhile, the industrial and manufacturing sectors have shown signs of improvement.

- While markets initially ruled out the prospect of a second US interest rate rise in 2016 following Brexit, strong jobs data over the summer and comments from Federal Reserve members raised this prospect again. Donald Trump's victory in the US election does not appear to have changed the Federal Reserve's outlook.

- The US stock market rose modestly over the past year in local terms, having reached a new high in November 2016. Our belief has been the US market in aggregate is unlikely to trade at a materially higher level given full valuations, and corporate margins generally have little room to expand further. Nonetheless, selective opportunities remain and we recommend maintaining an allocation to the US for diversification purposes given its more resilient, defensive properties. Corporate-friendly policy changes, such as cuts in corporation tax, would also be supportive.

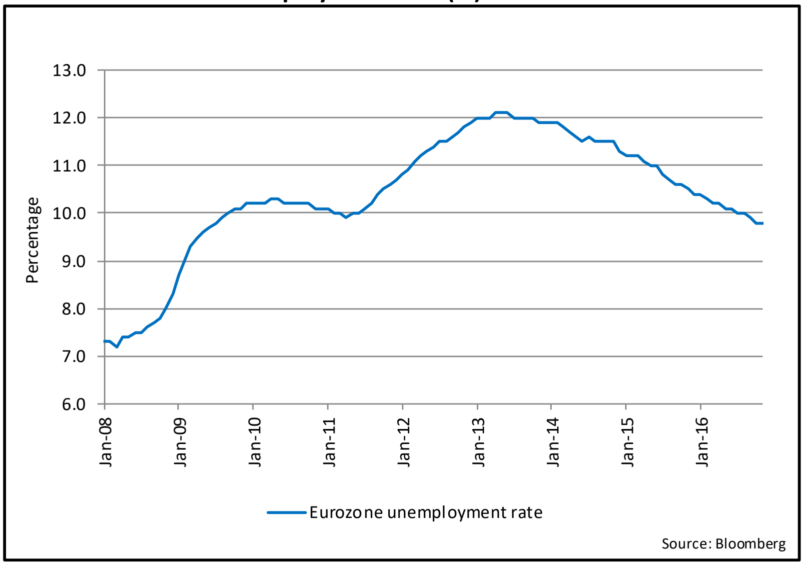
- During the last six and twelve months, the S&P 500 provided a total return in dollars of +5.7% and +7.3%. When translated into sterling, the total returns were +23.1% and +29.3%, respectively.

2.3. Europe ex-UK

- European economic data has been resilient over the past year, underpinned by consumer demand. The region will be vulnerable to any spillover effects from Brexit, which is likely to be addressed by further stimulus measures, but at this stage the data has remained largely encouraging. The extension of the ECB's QE programme to investment grade corporate bonds in June 2016 should also provide liquidity support to European markets.

- Improving economic conditions have led to steady declines in the unemployment rate from a record high of over 12% reached in 2013, as seen in chart 3 below. If the economic recovery is not materially disrupted, the labour market should improve yet further.

Chart 3 – Eurozone unemployment rate (%) since 2008.



- Though Brexit uncertainty may impact domestic consumer demand, smaller companies should continue to benefit from the increased availability of bank credit; growth in Eurozone bank lending turned positive last year for the first time since 2013 and continued to improve over the summer.

- A challenge to this has been concerns over bad debts in the Italian banking system. While authorities appreciate the importance of addressing the issue without causing wider contagion, the political upheaval in Italy that may ensue following the Italian Prime Minister's resignation adds further complexity.

- We are also mindful of national elections taking place in Germany, France and the Netherlands in 2017, which could complicate Brexit negotiations. The political elite will be keen to suppress the rise of anti-EU, populist sentiment, even more so following Trump's victory; in Germany immigration levels have been particularly controversial, helping a nationalist party win a state election. European authorities will take some comfort that non-mainstream parties fell short of expectations in the re-run Spanish elections in June 2016 and the Presidential election in Austria.

- During the last six months, the FTSE Europe ex-UK Index provided a total return in local currency of +0.3%, and -6.2% during the last year. When translated into sterling, the returns were +11.6% and +13.0% respectively.

2.4. Japan

- While the economy has not yet responded to the Japanese Government's or the Bank of Japan's policy efforts yet, inflation has begun to show signs of improvement and the labour market has tightened.

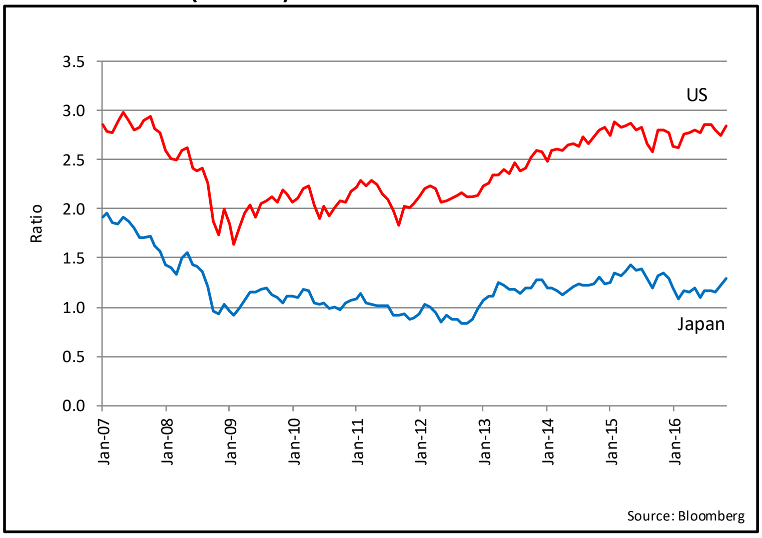
- Victory for Prime Minister Abe in Upper House elections in July 2016 had spurred hopes of further economic stimulus measures to boost the economy. This came to fruition in early August 2016 when a record fiscal stimulus package worth $45bn was announced, focusing on infrastructure spending, such as ports and high-speed railways.

- Increases in Japanese Government bond yields suggest some scepticism over how much further monetary easing can go. Meanwhile, the government's fiscal expansion marked an important move away from austerity; this was the first such change by a major developed economy since the financial crisis.

- Cyclical sectors of the Japanese stock market have come back into favour after an extended period of underperformance. Nonetheless, our primary rationale for investing in Japan is not centred on macroeconomic issues, but rather the Government's corporate reform agenda; this is encouraging companies to continue to take steps to increase their return on equity through share buybacks and dividend increases, funded from the high levels of cash many Japanese companies have on their balance sheets.

- The Japanese stock market is attractively valued at a price to book ratio c.55% cheaper than the US, as seen in chart 4 overleaf.

Chart 4 – Price-to-book ratio of the Japanese stock market (blue line) and the US stock market (red line).



- During the last six months, the TOPIX Index provided a total return in yen of +7.6%, and -4.9% during the last year. When translated into sterling, the returns were +22.0% and +23.9%, respectively.

2.5 Asia Pacific ex-Japan

- The region incorporates emerging countries such as China and India, as well as more developed economies such as Australia and Hong Kong.

- In the early part of the reporting period, the region's stock markets came under pressure from growth concerns, volatility in Chinese markets and expectations of higher US interest rates; these concerns eased in the latter six months.

- The economy in China appears to be reacting to the stimulus packages of recent months. The Government is also seeking to modernise its tax system, which will include lower rates of VAT. Nonetheless challenges remain, including historic problems of corporate overinvestment and bad debts in the banking system.

- The Chinese yuan stabilised over the summer on a trade-weighted basis after depreciating for much of this year (see chart 5 below); unlike at the beginning of 2016, the yuan declined without undermining market confidence and a more competitive currency should provide support to the economy. The Government may be wary of cutting interest rates from their current level of 4.35%, as it could refocus the market's attention on a weaker currency, and in particular the yuan's continued decline against the US dollar which the trade-weighted index doesn't reflect.

Chart 5 – Chinese yuan trade-weighted index: 2014 to 30 November 2016.

- In India, the Government's annual budget in February 2016 was well-received and appeared to restore some confidence in the economic and market outlook. Markets had grown sceptical about the Government's reform agenda, but this received a major boost in August 2016 after the Government finally received approval for the landmark "Goods and Services Tax". This tax will be equivalent to VAT in the UK, and will bring India under one common marketplace in the coming year; it is expected to raise economic growth and tax receipts.

- Most countries in Asia are benefitting from lower energy and commodity prices, given they are net oil importers. This is easing pressure on inflation, thereby providing central banks the scope to cut interest rates further.

- Asian stock market valuations are attractive relative to history and developed markets, and the long term secular growth outlook remains stronger than for developed economies. We continue to favour allocations to the region.

- During the last six months, the FTSE All-World Asia ex-Japan Index provided a total return of +7.7% in local currency and +9.1% during the last year. When translated into sterling, the returns were +26.0% and +31.7%, respectively.

2.6. Emerging markets

- The majority of emerging markets are in Asia and therefore emerging market sector returns tend to correlate closely with Asia ex-Japan returns.

- Non-Asian emerging markets, such as Brazil and Russia, came under particular pressure in the early part of the reporting period owing to their reliance on commodity markets, as did countries with large current account deficits such as Turkey.

- Though the performance of emerging markets had improved in 2016, a number of headwinds still remain, including a strong US dollar and structural and political challenges that are more pervasive in many emerging market countries. We continue to favour allocations focusing on Asia.

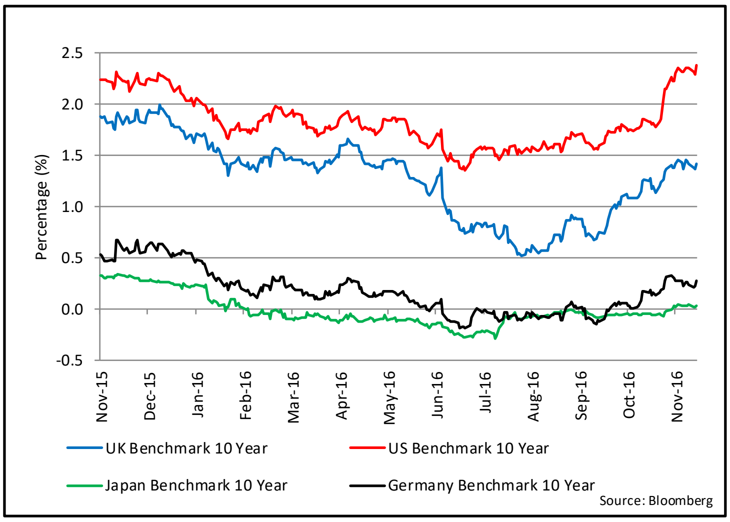
- During the last six months, the FTSE Emerging Markets Index's total return in local currency was +8.8%, and +10.4% during the past year. When translated into sterling, returns were +27.2% and +32.9%, respectively.

3. Bonds and Cash

3.1. Conventional government bonds

- UK and US Government bonds generated positive returns over the past twelve months, with most of the gains coming at the start of 2016 and in the wake of the UK's EU referendum in June 2016. Conventional gilt and US Treasury yields, which are inversely related to their prices, reached new lows in summer 2016. There has since been a notable upturn in UK and US Government bond yields primarily due to higher inflation expectations.

Chart 6 – Government borrowing costs; 10 year bond yields in the major economies.



- Given that at 30 November 2016 the majority of conventional gilts offered a negative capital return to maturity, they are unattractive to UK taxpayers since capital losses cannot be offset against capital gains on other assets, and income tax is payable on the interest.

- We continue to recommend a zero or very low weighting in UK conventional gilts, preferring any conventional government bond allocations to be made to US Treasury bonds. These offer a more attractive yield than UK gilts, provide superior protection against a deterioration in the global economic outlook and offer currency diversification.

- During the last six months, the FTSE UK Government 5-15 Years Index provided a total return of +1.6%, and +5.3% during the last year.

3.2. Index-linked bonds

- Index-linked gilts ("ILGs") provide diversification to protect portfolios from an upturn in inflation and, based on current inflation expectations, offer a positive total return if held to redemption. Given that UK inflation is expected to increase in the coming year, ILGs have attractions.

- Though, like conventional bonds, ILGs offer modest expected redemption yields, low coupon stocks are tax efficient as they offer a larger share of the expected return in tax-free capital gains, rather than taxed income. In the UK, ILGs track the RPI measure of inflation; this has supported performance, since RPI is typically about 1% per annum higher than the officially targeted CPI measure of inflation.

- During the last six and twelve months, the FTSE UK Government Index-Linked Bonds 5-15 Years Index returned +8.2% and +9.9%, respectively.

3.3. Corporate bonds

- We do not believe the yields on sterling corporate bonds exceed those on UK government bonds by a sufficient amount to justify taking corporate credit risk within the bond allocation; the yield premium as at 30 November 2016 was only 1.2%.

- During the last six and twelve months the iBOXX Sterling Corporate Bonds 5-15 Years Index provided a total return of +3.9% and +7.6%, respectively.

3.4. Cash

- Sterling interest rates remain at record lows, having been reduced further in August 2016. The BoE indicated they could cut the main interest rate again if the UK economy deteriorated.

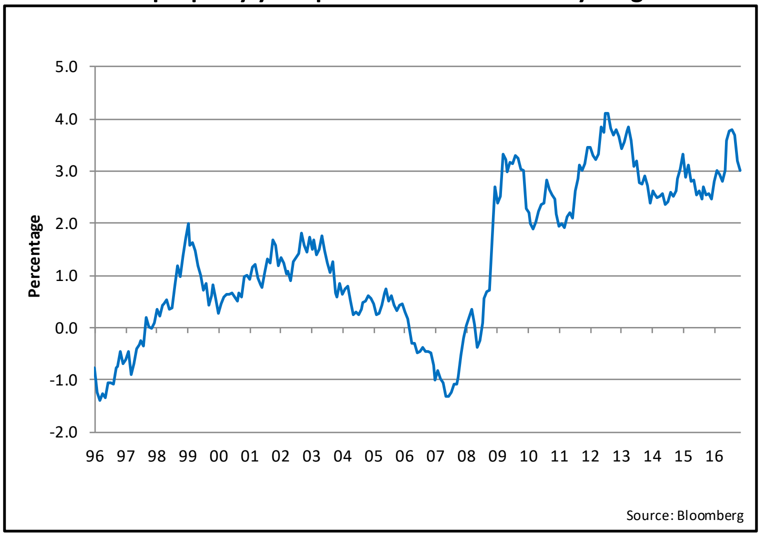
4. Real assets

4.1. UK Commercial Real Estate

- The outlook for UK commercial property has been challenged since the outcome of the EU referendum, which resulted in declines of listed property shares and the temporary suspension of dealing in many open-ended property funds.

- While property returns are expected to moderate going forwards, largely due to limited capital growth, the sector continues to offer an attractive income return; the IPD yield premium relative to UK gilts is currently 3.0%, as seen in chart 7 below.

Chart 7 – IPD property yield premium relative to 10 year gilts over 20 years.



- Weaker sterling makes the UK a more attractive tourist destination, which should benefit the hotel and retail sectors, such as the West End of London. It also reduces the cost of UK real estate for international investors in their own currencies, which, combined with declines in capital values, makes UK property an attractive proposition for overseas investors.

- Our property recommendations have been focused on funds with a low Central London weighting, particularly to City offices, which has proved to be appropriate. The South East of England and other major regional cities have a tighter supply / demand balance than London, where we remain cautious over the City office market.

- We believe property should continue to deliver competitive returns over the long term; over the 20 years to 30 November 2016 the IPD UK property index has returned 2.3% p.a. more than the UK stock market, as measured by the FTSE All-Share index. Moreover, investing in property improves the diversification of portfolios; during the stock market setbacks of August 2015 and February 2016 real estate was a resilient asset class.

- The IPD All Property Index of UK commercial real estate declined 1.6% over the last six months, but increased by 1.8% over the year.

4.2. Gold

- Despite inflation remaining low, the price of gold has risen over the last twelve months due to its safe-haven appeal. US dollar strength enhanced returns in sterling terms.

- Gold returned -1.4% in dollar terms during the last six months and +12.4% over the past year. When translated into sterling, returns were +14.8% and +35.4%, respectively.

To discuss this note, or any other matter, please contact Nick Fletcher on 020 3696 6801, or any member of the London Wall Partners investment team on 020 3696 6805.

Appendix - Regulatory Information and Disclosures

Table 3 – Discrete twelve-month total returns in local currency.

	Return (%) for the 12 months to:				
Index	**30.11.16**	**30.11.15**	**30.11.14**	**30.11.13**	**30.11.12**
FTSE All-World	4.9	3.0	12.8	26.7	14.8
FTSE All-Share (£)	9.8	0.6	4.7	19.8	12.1
S&P 500 ($)	7.3	2.1	16.2	29.5	15.4
FTSE Europe ex-UK	-6.2	11.0	8.8	24.4	17.8
TOPIX (Y)	-4.9	14.2	14.3	64.2	9.9
FTSE All-World Asia ex-Japan	9.1	-4.8	7.8	13.8	16.6
FTSE Emerging Markets	10.4	-7.2	9.5	9.1	14.0
FTSE UK Govt 5-15 years (£)	5.3	3.2	8.8	-3.6	7.1
FTSE UK Govt I-L 5-15 years (£)	9.9	-0.3	7.8	-0.9	7.1
iBOXX £ Corp Bonds 5-15 years (£)	7.6	3.3	10.1	3.9	21.0
IPD All Property (£)	1.8	14.4	20.0	9.1	2.5
Gold Bullion ($)	12.4	-10.4	-5.5	-27.6	0.3

Table 4 – Discrete twelve-month total returns in sterling.

	Return (%) for the 12 months to:				
Index	**30.11.16**	**30.11.15**	**30.11.14**	**30.11.13**	**30.11.12**
FTSE All-World	25.8	2.1	13.6	21.5	12.0
FTSE All-Share (£)	9.8	0.6	4.7	19.8	12.1
S&P 500 ($)	29.3	6.2	21.5	26.7	13.2
FTSE Europe ex-UK	13.0	0.1	4.6	25.8	12.9
TOPIX (Y)	23.9	14.4	3.1	29.4	1.5
FTSE All-World Asia ex-Japan	31.7	-7.6	9.4	5.5	16.6
FTSE Emerging Markets	32.9	-14.1	10.0	0.6	9.0
FTSE UK Govt 5-15 years (£)	5.3	3.2	8.8	-3.6	7.1
FTSE UK Govt I-L 5-15 years (£)	9.9	-0.3	7.8	-0.9	7.1
iBOXX £ Corp Bonds 5-15 years (£)	7.6	3.3	10.1	3.9	21.0
IPD All Property (£)	1.8	14.4	20.0	9.1	2.5
Gold Bullion ($)	35.4	-6.8	-1.2	-29.2	-1.6

Notes:
1. All figures include income reinvested.
2. Local currency indicated in index name, for single country indices. The returns of non-sterling assets may increase or decrease as a result of currency fluctuations.
3. Investment Property Databank ("IPD") Index may be subject to retrospective revision.
4. Source: FE Analytics.