



Investment Outlook

**House View from
Informed Choice**

4th Quarter 2011

Published: 4th October 2011

Informed Choice
Independent Financial Advice

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First edition published in Great Britain 2011.
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Informed Choice is the leading firm of Chartered Financial Planners, working with individuals, trustees and business owners to help them to build, manage and protect their wealth.

We were named **IFA of the Year** at the Money Marketing Financial Services Awards 2010 and we are four times winners of the **Gold Standard for Independent Financial Advice** at the Gold Standard Awards. We were named **Best IFA Firm** at the unbiased.co.uk Media IFA of the Year Awards 2011.



We are a firm of Chartered Financial Planners. This means we have satisfied rigorous criteria relating to professional qualifications and ethical good practice. It means you can be confident that you are dealing with one of the UK's leading firms that is wholly committed to providing you with the best possible advice, service and support.

Our quarterly Investment Outlook report sets out our views on the general investment climate and creates a robust framework for our investment advice decisions. It also enables us to make tactical alterations to our strategic asset allocation models.

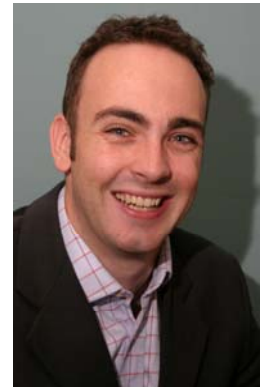
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Introduction

Martin Bamford CFP APFS
Chartered Financial Planner
Managing Director



Welcome to our Investment Outlook report for the fourth quarter of 2011. We publish this document once a quarter to record the conclusions of our formal Investment Committee process.

This process puts us in a very strong position to make tactical asset allocation decisions to exploit short term market conditions and any investment opportunities.

The eurozone sovereign debt crisis continues to dominate investor sentiment, with the likelihood of at least a partial default from Greece increasing on a daily basis. Combined with negative economic data globally, we cannot blame investors for taking a more cautious position.

Over the summer, the stock markets have been the scene of extreme levels of volatility. The end of September saw the FTSE 100 index of leading UK company shares finish its worst quarter of performance in a decade, falling in value by 13.7% since the start of July.

Of course it hasn't all been bad news. Investors in well diversified portfolios, with exposure to non-equity assets, have seen negatively correlated returns from fixed interest securities. The IMA UK Gilt sector returned 7.54% over the three months to the end of September and our clients will have achieved a 6.09% return over three months from their holding in the Royal London Index Linked Gilt fund.

At the start of the third quarter we made a series of positive tactical moves; we increased allocations to UK Corporate Bonds and cut allocations to UK, European and US Equities. Our House View for the final quarter of the year is to broadly maintain our current positions and allocations, as the continued volatility in the markets makes it difficult to time bold tactical adjustments to portfolios.

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One change we are introducing to our portfolios this quarter is to replace the Newton Growth fund with the HSBC FTSE 100 ETF. We placed the Newton Growth fund under review on 7th September, immediately upon learning about plans by BNY Mellon to merge this fund with the Newton Income fund. The Newton Growth fund was 'soft closed' to investors on 1st October.

Our decision to use an Exchange Traded Fund (ETF) in the UK Equity space follows a detailed review of the sector, and failing to identify a suitable actively managed fund as a replacement for the Newton Growth fund.

With ETFs receiving some negative press recently, it is important to point out that the HSBC FTSE 100 ETF (and the HSBC S&P 500 ETF) we recommend to clients within our portfolios use full physical replication, have UK reporting status and have segregated liability to protect investor assets. We apply this robust criteria when selecting suitable ETFs so as to avoid the inherent risks associated with synthetic replication techniques and other potential issues in the ETF sector.

We hope that you find this report interesting and we would welcome your feedback. Please do email us at hello@icl-ifa.co.uk or call us on 01483 274566 with any questions you have. You can also engage with us via Twitter at @informedchoice.

Martin Bamford.

4th October 2011

Cash

There are indications that the Bank of England will extend its asset purchase programme of quantitative easing, perhaps by £50bn to a total of £250bn. This is likely to help kick start the elusive economic growth that has been absent from the UK recently, although it is unlikely to have any dramatic impact on the economy.

The Bank Rate remains on hold at the historic low of 0.5% and some economists now believe it will remain there until at least 2014, creating an unprecedented period of time when interest rates are so low.

There is some speculation that a further rate cut to 0.25% could occur in the final quarter of this year, although it seems more likely that the Bank will extend quantitative easing than further cut rates.

Our House View for Cash is to remain **neutral**, partially to accommodate our more tactically cautious position overall as we continue to maintain reduced exposure to risk assets within our portfolios.

Fixed Interest

UK Corporate Bonds

We remain relatively positive about the prospects for corporate debt, as overvalued government debt pushes investors further up the risk spectrum in search of returns.

The default rate, even for higher yielding corporate bonds, remains reasonably low and corporate balance sheets are generally healthy. The higher yielding end of the credit spectrum continues to look relatively attractive compared to other fixed interest securities.

Investors should however be careful about replicating equity risks in the fixed interest parts of their portfolios by focusing too much on higher yield corporate debt.

Our House View for UK Corporate Bonds is to remain **overweight**, with a continued emphasis on high yield debt and selective fund management.

UK Index Linked

Price inflation remains stubbornly high in the UK and well above the Bank target of 2% for CPI. The latest CPI figures for the twelve months to August show CPI at 4.5%, up from 4.4% the previous month.

We continue to expect inflation to fall back towards target from the start of next year, when the impact of the VAT rise at the start of 2011 starts to fall out of the equation. By this time, global energy prices may have also reduced as a result of lower global economic activity.

This asset class has once again delivered strong returns for investors over the past quarter, and we continue to have concerns around the attractiveness or otherwise of valuations. As a result, our House View is to remain **neutral**.

UK Gilts

We agree with the views of Fidelity's Ian Spreadbury who recently suggested that the current yields from ten-year gilts of just over 2% are disconnected from the expectations of between 3% and 3.5% nominal GDP growth. As a result, gilt yields look quite expensive.

The expensive valuation of Gilts makes investors less likely to view these as a safe haven in the event of a further market crisis. That said, Standard & Poor's have just confirmed the UK's AAA credit rating and, now that the US has been downgraded to AA+, the true safe havens for nervous investors are harder to find.

Our House View for UK Gilts is to remain **underweight**. Whilst further quantitative easing from the Bank of England could push yields even lower, the risks associated with buying at these historically expensive valuations outweigh the potential benefit from slightly lower yields.

Equities

UK Equities

As we write this latest report, the FTSE 100 has fallen below 5,000 points and is trading on a price/earnings ratio of 9.6. This compares to a historic average P/E ratio of around 13, and suggests that UK Equities represent good value for investors who are prepared to tolerate short-term volatility.

The latest Pricewaterhouse Coopers and CBI survey found the UK finance sector in a poorer than expected state. The sector has recently experienced its slowest quarter since June 2010 and expects to experience a further slowdown in the final quarter of the year, shedding as many as 8,000 jobs in response.

There are concerns that the introduction of a Europe-wide tax on financial transactions would be particularly damaging for the UK, with London an important financial centre. Whilst the proposed 'Tobin' tax could raise £50bn a year if it is implemented as planned in 2014, it would risk pushing investors away from investments domiciled in Europe.

Standard & Poor's has confirmed the UK's AAA credit rating, with a stable outlook. Whilst a local and global economic slowdown will inevitably have an impact on UK businesses, Standard & Poor's like the UK's diversified economy and flexible fiscal monetary policy, as well as the public debt reduction measures being implemented by the coalition government.

Our outlook for UK Equities is to remain **neutral** until the markets become less volatile and the outlook becomes more stable. Certainly investor sentiment in the UK is being influenced by the eurozone sovereign debt crisis, which requires resolution before markets can confidently regain recent losses.

European Equities

Issues surrounding Greek sovereign debts, and the risk of contagion across the eurozone, continue to dominate investor sentiment both in the European Equities asset class and across global equities.

It now looks increasingly likely that Greece will default. This might not mean full bankruptcy, although investors in Greek sovereign debt will need to accept a 'haircut' and the markets appear to be pricing in this eventuality.

Greece looks likely to miss the deficit reduction targets imposed by the European Union and International Monetary Fund as a prerequisite for accessing a further tranche of bailout funds. They have a deficit target of 7.6% of GDP in 2011, and look likely to only reach 8.5% of GDP. This is a big improvement from their 10.5% of GDP budget deficit from last year, but not quite enough to convince their neighbours to front further cash as part of a rescue package.

With European equity markets falling in value by around a quarter over the past three months, there is undoubtedly value to be had. The EURO STOXX 50 index, which consists of the 50 largest companies from countries in the European Monetary Union, is currently trading on a price/earnings ratio of 8.6 and is nearly a third lower than its value earlier this year.

It is pleasing to note that our preferred European Equity fund, Jupiter European, has done a good job in outperforming its sector average, delivering -8.79% over the twelve months to the end of September 2011 compared with a sector average return of -11.37%. We believe in an active management style in Europe where there are diverse economies and sectors. In our opinion this makes European Equities unsuitable for a passive investment strategy.

Despite these indications of value, it would take a very brave investor to increase their exposure to European Equities until political leaders are able to come up with much firmer intentions to resolve the eurozone sovereign debt crisis.

Our House View for European Equities is to remain **underweight**. The future for eurozone sovereign debt and the impact on European companies of a full or partial default in Greece all remains too uncertain to consider increasing tactical allocations at this time.

North American Equities

The latest initiative from the Federal Reserve, dubbed 'Operation Twist', sees them selling \$400bn of short-term bonds and using the proceeds to purchase long-term Treasury Notes and bonds, in an attempt to reduce long-term interest rates. Whilst not injecting any new money into the economy, this course of action should result in lower borrowing costs for businesses and consumers.

At the same time as they launched Operation Twist, the Fed pointed to continuing weakness in the jobs markets and "significant downside risks to the economic outlook, including strains in global financial markets".

Earlier this summer, the US lost its coveted AAA credit rating from Standard & Poor's, although it has since maintained its top ratings from other agencies. Whilst now rated at AA+ by Standard & Poor's, the US economy remains in relatively robust health and the downgrade had more to do with political indecision than economic strength.

A global economic slowdown could dampen the export demand that has to date supported continued growth in the US economy. The domestic consumer market remains in poor shape, with particular issues in the jobs and housing markets.

Our House View for North American Equities is to remain **neutral**.

Japan Equities

It is always difficult to differentiate between the Japanese economy and Japanese businesses. Of course investors are backing the latter when investing in Japanese Equities, although the issues surrounding the former can be incredibly off-putting.

Valuations for Japanese companies are at a historic low. As we write this, the Nikkei 225 in Tokyo is trading at under 8,500 and has a price-earnings ratio of around 15.8.

The earthquake and tsunami earlier this year clearly had an impact on productivity levels, although Japanese companies continue to deliver strong earnings growth and rising dividend yields. There is continued evidence of merger and acquisition activity.

Our House View for Japan Equities is to **remain underweight**. Whilst there appears to be some value in Japanese companies, we continue to believe it is too soon to risk exposing additional investor cash to this asset class whilst uncertainty outweighs the positive attributes of Japanese companies.

Asia ex-Japan Equities

Inflation remains a concern in some areas of this region, although it is not particularly a concern for Asia in general. CPI inflation is some 0.7% above the ten year average when China and India are excluded from the calculation.

The rate of economic growth in Asia remains robust, with a GDP growth forecast of 7.5% in 2011 and only slightly lower in 2012. Asian companies appear to be in good financial shape and, supported by high gross personal savings and low government debts, this region has the ability to ride out any global economic slowdown which could reduce external demand.

We remain positive about the outlook for the region, with reportedly increased levels of interregional trade becoming more important as external demand risks fading away for a time.

Our House View for Asia ex-Japan Equities is to remain **overweight**.

Emerging Market Equities

We are likely to see a contrast between the slowdown in economic growth from developed economies globally with continued strong growth from many emerging market economies. A short term dip in commodity prices as a result of this developed market slowdown could result in emerging markets escalating their own economic growth to benefit from cheaper prices.

Investors should rely on fund managers to take an active approach to stock selection in this asset class, taking advantage where possible of attractive valuations in specific sectors. Sentiment in response to the eurozone debt crisis and global economic slowdown is moving investors away from equities in general, often creating value opportunities in these recently 'hotter' markets where value has been hard to find.

Our House View for Emerging Market Equities is to **remain neutral**. We continue to believe that it is important to have a good level of geographical and sector diversification within Emerging Market Equities, to reduce the possibility of overexposure to one or more countries which could overheat.

Property

Commercial property in the UK has remained quite stable against a backdrop of extreme volatility in equity asset classes and other investments more generally. The latest IPD figures to the end of July 2011 show a total return from this asset class of 5.1% over the year.

There remain regional differences in the commercial property market, with better performance coming from London and the South East, particularly in the office and retail sectors. The retail sector in the right areas continues to perform strongly, avoiding many of the issues faced by the retail sector in the face of a consumer spending crunch.

Yields from 'real' commercial property remain very strong, particularly relative to cash. Managing liquidity remains an issue for some funds, as managers will need to balance short-term demands for redemptions with the desire to purchase property at attractive valuations.

The outlook for this asset class remains reasonably stable, with a positive return likely as long as sentiment from other investment asset classes does not dampen enthusiasm for asset-backed investments.

Our House View for UK commercial property is to remain **neutral**.

Current House View

- Cash – neutral
- UK Corporate Bonds – overweight
- UK Index Linked – neutral
- UK Gilts – underweight
- UK Equities – neutral
- European Equities – underweight
- North American Equities – neutral
- Japan Equities – underweight
- Asia ex-Japan Equities – overweight
- Emerging Market Equities – neutral
- Property – neutral

The terms 'overweight', 'neutral' and 'underweight' represent our view of tactical asset allocation adjustments to a well diversified strategic portfolio.