BARINGS

Barings Multi Asset Strategy

September 2016

Khiem Do

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The World since the Global Financial Crisis of 2008

Floating in unchartered waters

The 'New Normal': sluggish growth, uneven distribution

- High levels of debt, transferred from private to public
- Demographic dividends fading
- Excess capacity built up in China and Emerging world
- Rich gets richer, poor gets poorer

"Anti-Depression" Policy Tools: from 'unconventional' monetary policy to ….

- ZIRP
- QE
- NIRP
- Next comes …. Helicopter Money?

'Bubbles' formation:

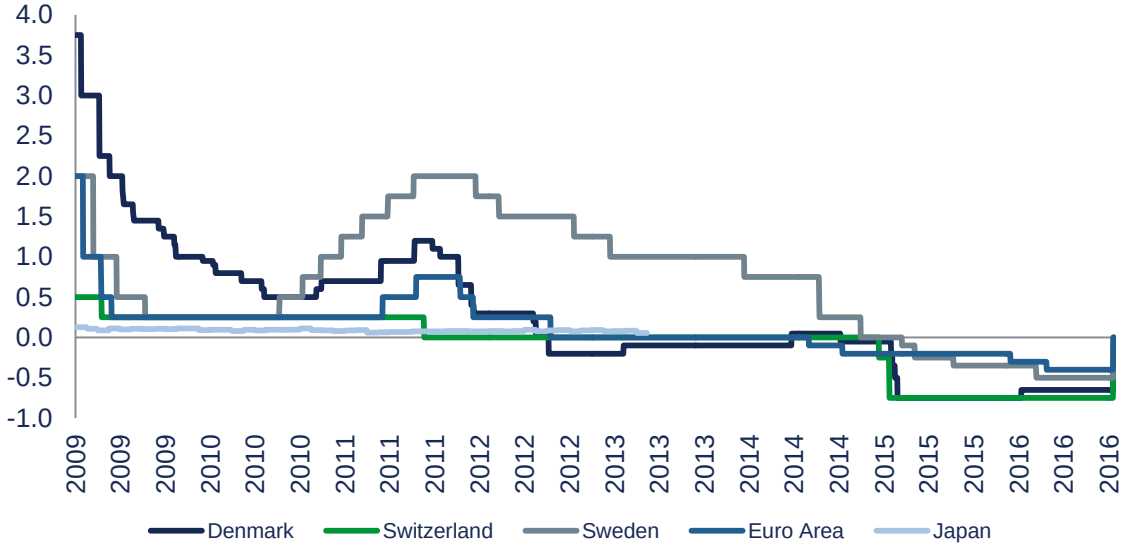
- Commodities in 2008-09
- Luxury property in 2014-15
- Bonds in 2016
- Equities in ….. 2017???

Source: Barings, as at September 2016.

“Unconventional” monetary policy

Extreme desperation or sensible policy?

Cash rates trend since 2009 (%, p.a.)



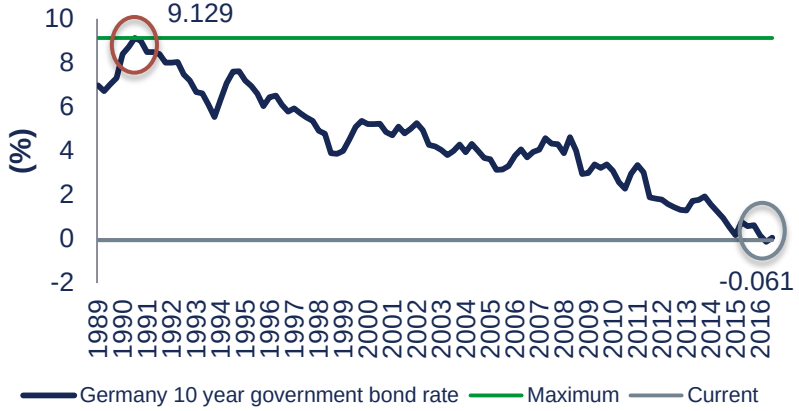
Will the negative interest rate policy in Europe and Japan prove to be a big mistake?

Source: Citigroup, as at September 2016

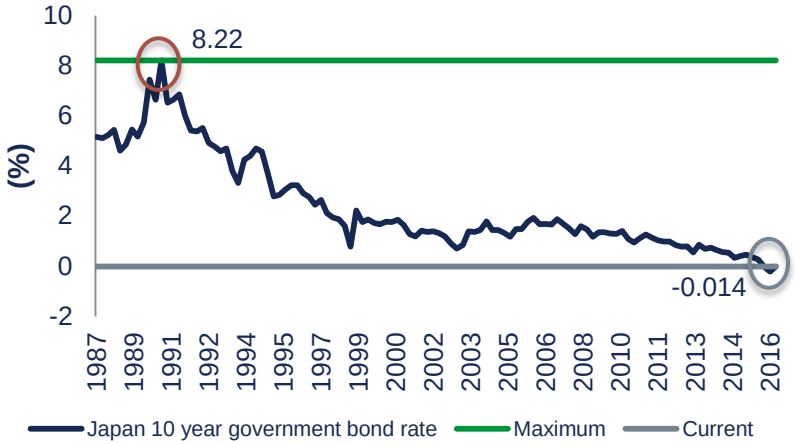
Long-Term Government Bond Yields

Discounting worst-case scenarios of deflation and secular stagnation?

Germany 10 year government bond yield



Japan 10 year government bond yield



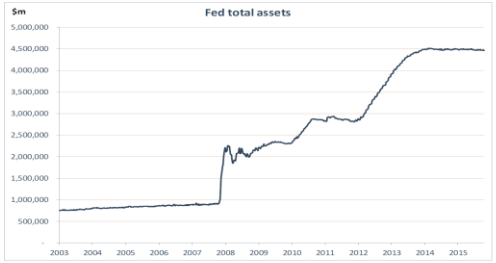
What if this was simply the result of massive central banks' buying via QE programs?
What would happen when central banks stop buying and start selling back to the market?

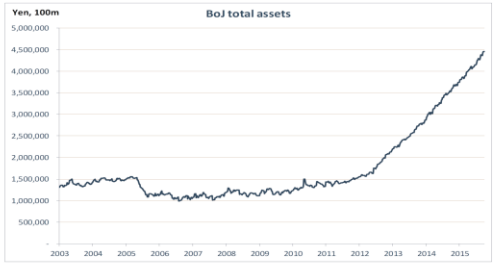
Source: Bloomberg, Barings, September 2016

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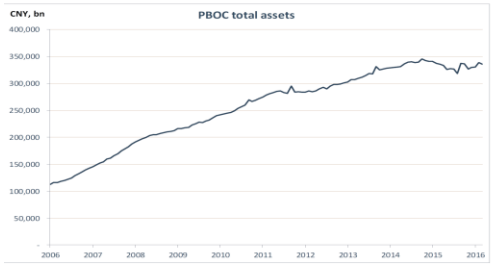
Central Bank balance sheets

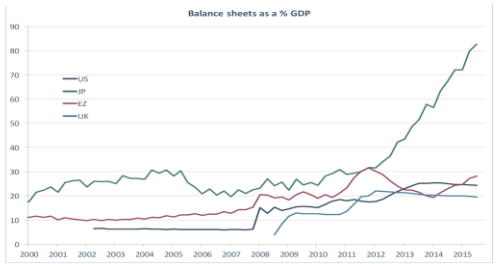
Still expanding at a total global level











BoJ, ECB, PBoC and BoE (soon) are still pumping money, while the Fed is holding

Source: Strategic Policy Group, Barings, as at September 2016

Current Investors' Concerns

Still many!

What if Mr Trump wins the elections and rules both Houses ?

- How dramatic will the changes in the US economy / financial markets and global counterparts be?

Further Fed Rate hikes:

- Market dislocations if much more aggressive than what the market currently discounts !

"Taper Tantrum":

- Will the European (and Japanese ?) QE program end in 2017 ?

BREXIT's contagion effect on Europe:

- Shock if more EU members want to exit

China's L-shaped economy:

- What does an "L-shaped growth" trend mean ?
- RMB and banking NPLs still posing big risks ?

'Deflationary' world … OR … just 'low nominal growth' world ?

- Low nominal GDP and core inflation (even after many years of ZIRP, QE & and, recently, negative interest rates) >>> impact on corporates' sales & revenue growth ?

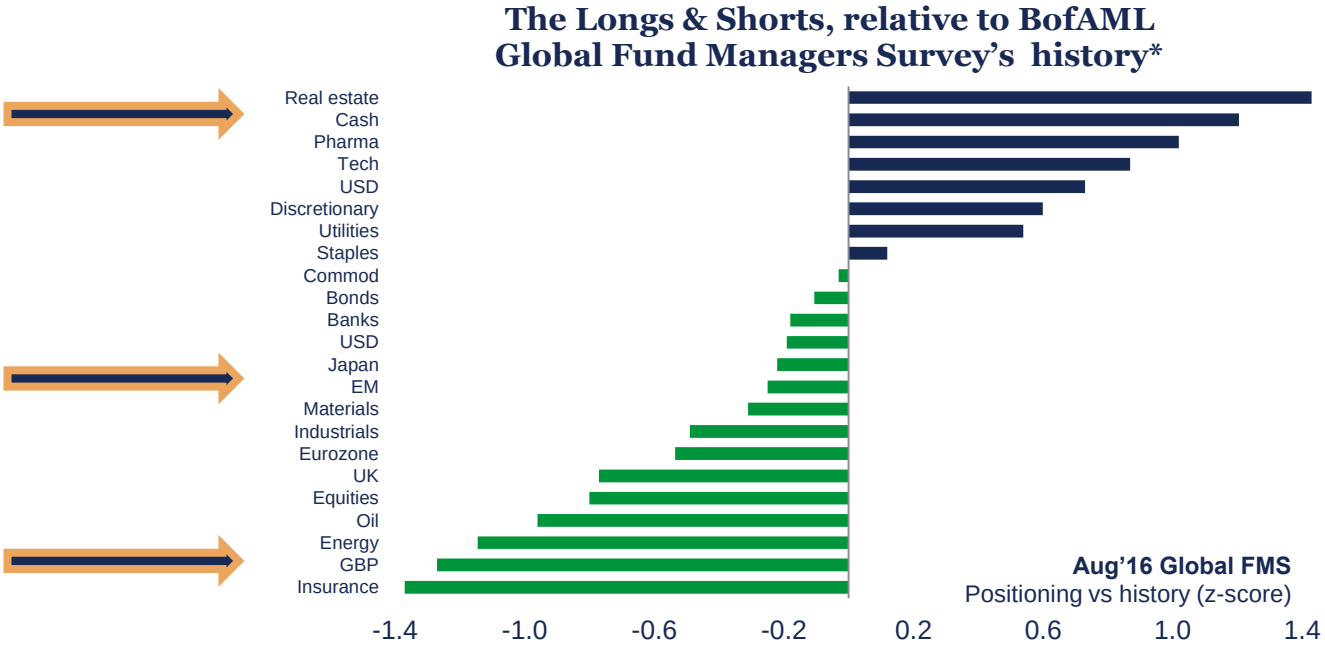
Short- and long-term risks are being continuously quantified and assessed

Source: Barings, as at September 2016

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Investors' Investment Preferences

Cash and defensive asset classes are preferred



Global investors remain moderately risk-averse

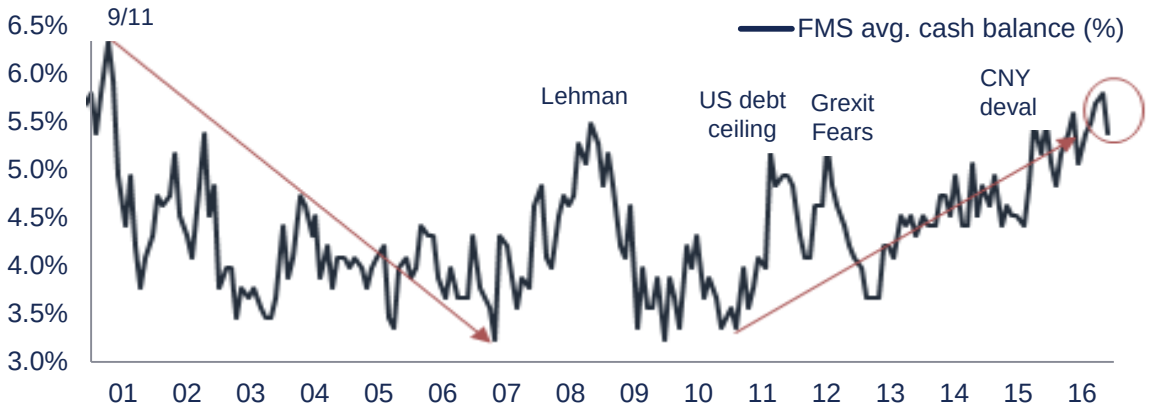
* FMS: Fund Manager Survey, data since 2006 for commodities & real estate; data since 2001 for equities, bonds & cash; note USD & EUR are based on valuation

Source: BofA Merrill Lynch Global Fund Manager Survey, as at August 2016

Investors' Current Cash Position

Still defensive

Global Fund Manager Survey's average cash balance (%)



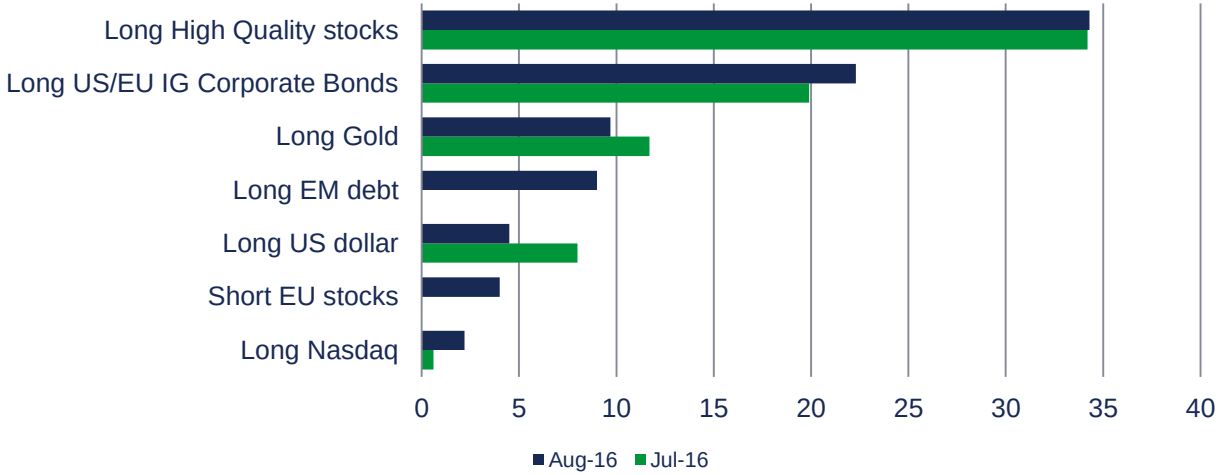
What impact on Equities if the relatively high cash were to be re-deployed in equity markets ?

Source: BofA Merrill Lynch Global Fund Manager Survey, as at August 2016.

Investors' Preferred Positions

Emphasizing 'quality' and 'low beta'

"What do you think is currently the most crowded trade?"



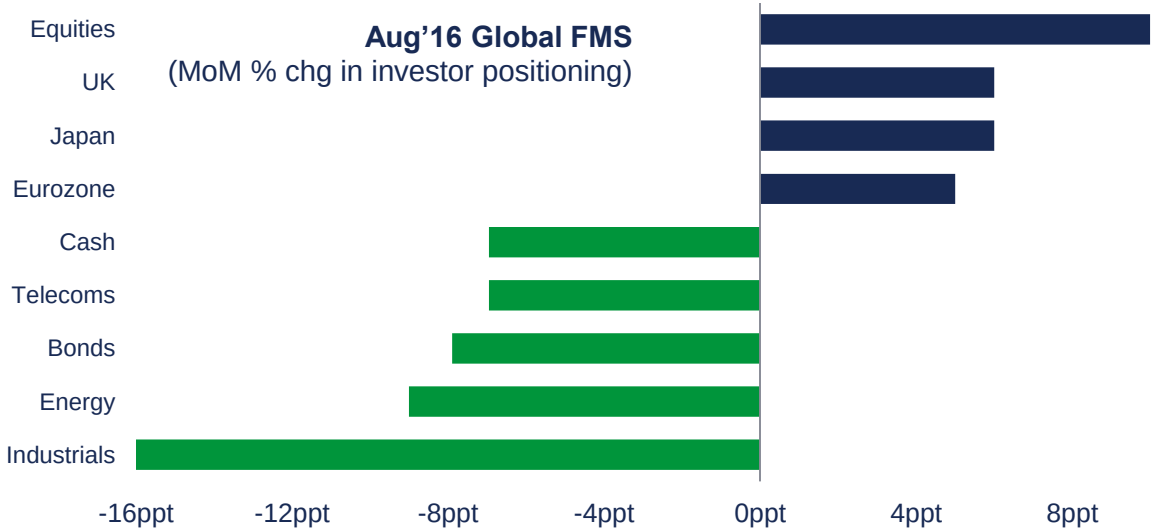
A very conservative view on global growth is implied from the above

Source: BofA Merrill Lynch Global Fund Manager Survey, as at August 2016.

Investors' Recent Portfolio Moves

Taking on more risk …

Month-on-Month Changes to Global FMS* positioning (Aug'16 vs Jul'16)



… to hedge their bets, as Equities and other risky asset classes rallied after BREXIT

(again, it seemed like a defensive move ?)

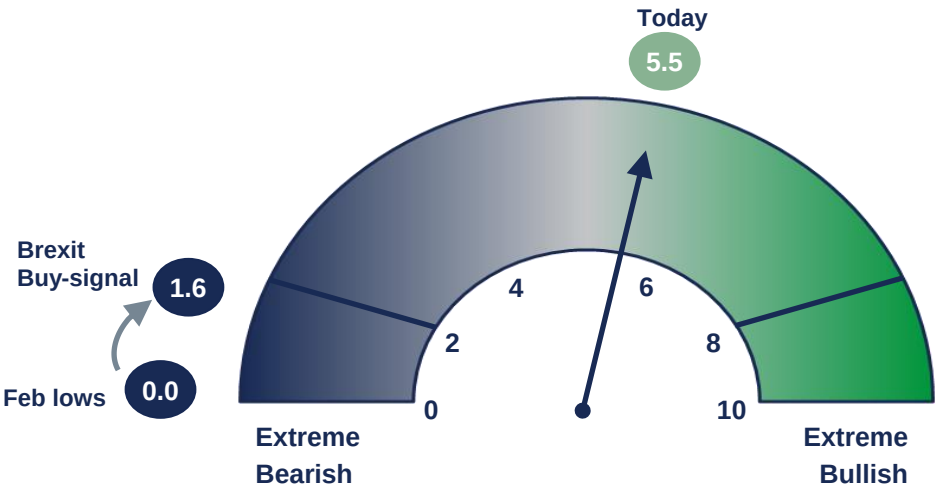
* FMS: Fund Manager Survey

Source: BofA Merrill Lynch Global Fund Manager Survey, as at August 2016.

Global Investors' Sentiment

Was excessively bearish, now 'neutral'

The BofAML Bull & Bear Index (scale from 0-10)



Buying in 'extreme bearish' levels has almost always tended to pay off

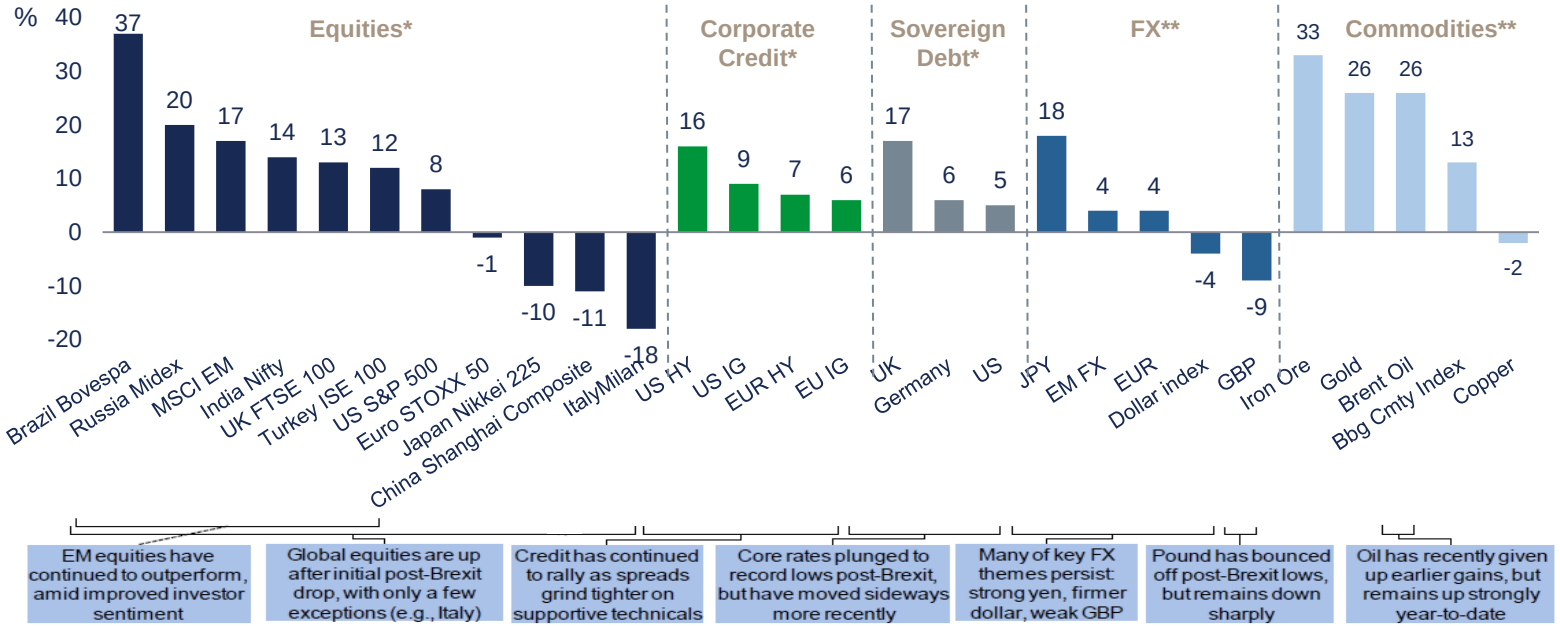
(NB: sentiment was very bearish post-BREXIT, and served as a good trading buy signal)

Source: BofAML Global Investment Strategy and EPFR Global, as at 8 September 2016

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Global Asset Classes Performance

2016 YTD returns



A volatile YTD session, with Equities bouncing strongly post-Brexit (except Japan & Europe). Commodities retained their strength.

Note: (*) Total return accounts for both income (interest or dividends) and capital appreciation, in local currency terms.
(**) FX, Commodities are spot returns.
Source: Bloomberg Finance LP, Deutsche Bank Research. As of 6th September 2016

Global Economic Growth Outlook

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Global Economic Growth in next 12 Months

Moderate growth is our base case, but still below long-term equilibrium

GDP growth (%)

	2011	2012	2013	2014	2015	2016F	2017F
World	3.4	2.7	2.6	2.8	2.7	2.3	2.6
US	1.6	2.2	1.5	2.4	2.6	1.4	1.8
Eurozone	1.7	-0.8	-0.2	0.9	1.6	1.6	1.3
Japan	-0.4	1.7	1.6	-0.1	0.6	0.8	1.1
China	9.0	7.7	7.7	7.3	6.9	6.7	6.4
Asia ex Japan	7.4	6.4	6.6	6.4	6.0	5.8	5.6
Global Emerging	6.4	5.1	5.1	4.6	3.8	3.8	4.4

Forecasts for Europe and China are deemed slightly optimistic, while those of the US may be a bit conservative?

Source: JP Morgan, as at September 2016

China's "L-shaped" Economy

Good or bad?



In a slow global economy, a 5 to 6.50% annual GDP growth rate for China would be a good outcome!

Source: Bloomberg, Barings, August 2016.

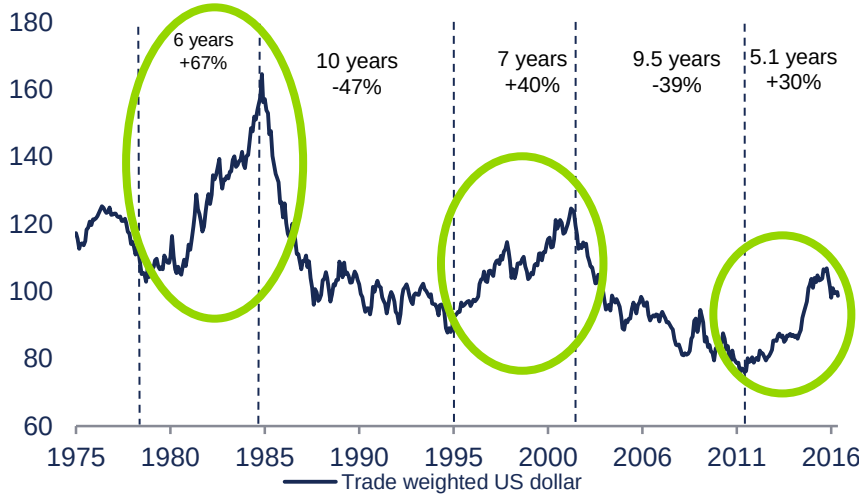
Strong US Dollar

But … has it peaked?

USD vs DXY (trade-weighted US dollar):
Before & after Fed tightening



Is the US Dollar rally nearing its peak, and about to resume its long-term downtrend?



Long-term, the USD appears to be a fundamentally weak currency.
Positive implications for Emerging financial assets if it has already peaked in this cycle!

Source: (Left) MSCI and Credit Suisse, as at September 2016. (Right) Thomson Reuters and Credit Suisse Research, as at September 2016.

Fed Fund rates

What money market and bond investors are pricing in

What the Fed Fund Rate (FFR) would be, based on the futures market* in the next two years:

Data as at Sept 22nd

- November 2016: 0.43% *(21% chance of a hike)*
- December 2016: 0.51% *(61% chance of a hike)*
- September 2017: 0.68% *(79% chance of a hike)*

* December 2017: 0.72% *(82% chance of a hike)*

Market is betting on a delay of the FFR hike until late '16 or H1 '17, and a very gradual 'normalisation' of interest rate policy

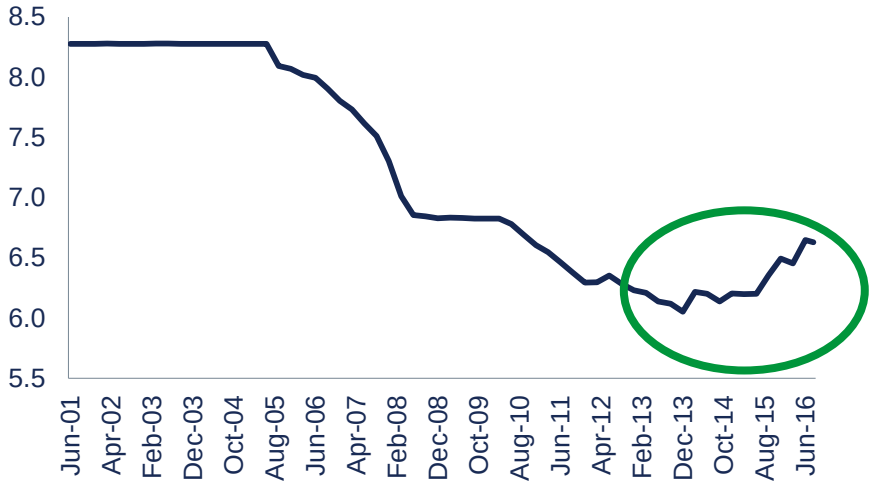
* FF rate futures

Source: Bloomberg and Barings, as at Sept 22nd, 2016

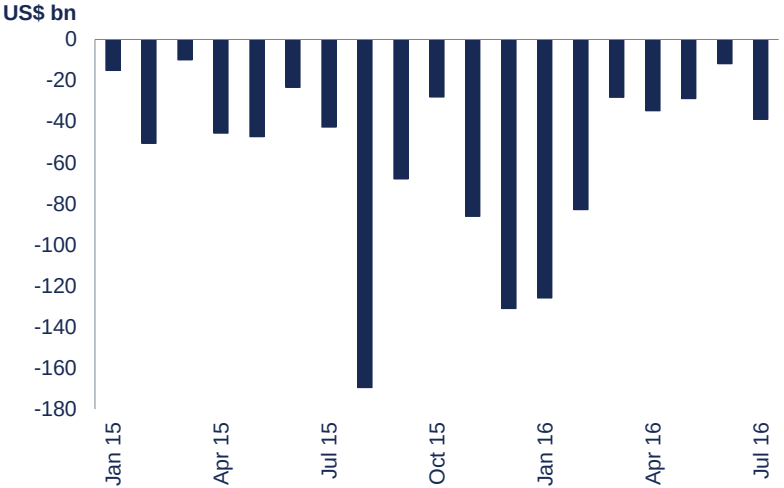
A Global Risk Factor: The RMB

Steady or fast?

Offshore RMB vs USD (past 15 years)



Monthly estimates of capital outflows from China (USD bn)



Fragile trend in the RMB continued … As longs as it does not fall significantly in one day, global investors may tolerate its gradual downward adjustment?

Source : SAFE, JP Morgan, Bloomberg, August 2016

Global Equity Markets

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Global Sales & EPS Growth

A review of the past four years & 2016 YTD

	Earnings per share growth					Sales per share growth				
	2012	2013	2014	2015	2016 (est)	2012	2013	2014	2015	2016 (est)
World	**0.2%**	**4.7%**	**2.5%**	**-3.2%**	**-0.5%**	**0.9%**	**-1.2%**	**-2.8%**	**-6.8%**	**+2.6%**
USA	5.9%	6.5%	7.9%	0.4%	**+0.2%**	1.6%	3.0%	4.5%	-2.1%	**+1.7%**
Europe ex UK	-3.1%	2.0%	-8.6%	-1.7%	-2.4%	8.2%	-1.8%	-12.5%	-8.7%	**+1.7%**
United Kingdom	-7.5%	-5.5%	1.3%	-16.7%	-4.2%	-0.3%	0.4%	1.1%	-15.0%	**+0.8%**
Japan	-7.6%	59.2%	19.3%	9.1%	-6.1%	0.5%	6.6%	3.8%	-4.8%	-3.8%
EM	-2.9%	-0.7%	-8.8%	-15.5%	**+0.2%**	6.3%	1.5%	-4.8%	-18.1%	**+1.9%**

Disappointing trends over past few years, but H1 '16 appears to have marked the start of an upturn?

Source: Factset, Barings, Sept 2016

Global and EM/Asian Equity Markets:

Earnings growth forecasts and valuations

	P/E (x)		Div. Yield (%)	P/BV (x)	Earnings growth (%)				ROE (%)
Country	Current Trailing	12m fwd	Current Trailing	Current Trailing	2014	2015E	2016E	2017E	2017E
Global	17.2	15.7	2.5	2.0	4.3	(3.4)	1.3	13.0	12.6
USA	19.2	17.5	2.1	2.7	5.6	0.2	1.1	13.2	15.1
Europe	16.3	15.1	3.6	1.7	1.2	(5.7)	(1.6)	13.2	11.5
Japan	16.1	13.8	2.3	1.2	75.2	4.0	(3.4)	10.0	8.0
Emerging Markets	14.2	12.8	2.5	1.5	1.5	(7.0)	6.1	13.4	11.4
EMF Asia	14.1	12.9	2.4	1.5	3.9	2.2	2.5	12.0	11.7
China	13.5	12.3	2.3	1.6	6.0	(3.4)	(0.4)	14.7	12.5

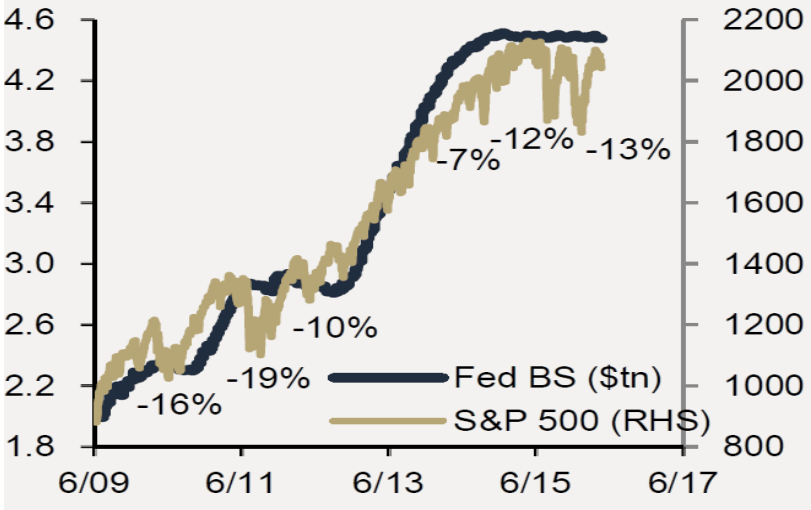
As the reduction in the equity risk premium in all equity markets has occurred, delivery of earnings and EPS revisions will be their key driver.

Source: IBES, MSCI and JP Morgan estimates, as at September 2016.

Has the 7-year US Bull Market Peaked yet?

Still a 50/50 bet

Fed balance sheet vs S&P 500



Global asset class flows, $mn

	Week (% AUM)	YTD	YTD (%AUM)
Equities	0.1%	-129,898	-1.7%
ETFs	0.2%	62,573	2.8%
LO	-0.1%	-192,461	-3.6%
Bonds	0.1%	154,639	4.5%
Commodities	0.7%	32,978	26.3%
Money-market	-0.4%	-85,044	-2.3%

* week of September 7th, 2016

Massive redemptions in US and global equity funds YTD suggest that future positive corporate profits plus M&A newsflows and return of equity buying could spark a significant rally in H2 and 2017!

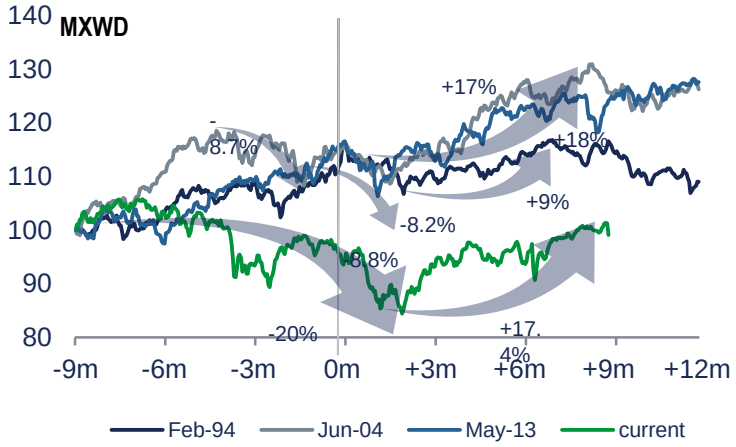
Source: (Left) BofAML Global Research, Bloomberg, May 2016; (Right) BofAML Global Investment Strategy, EPFR Global, September 2016

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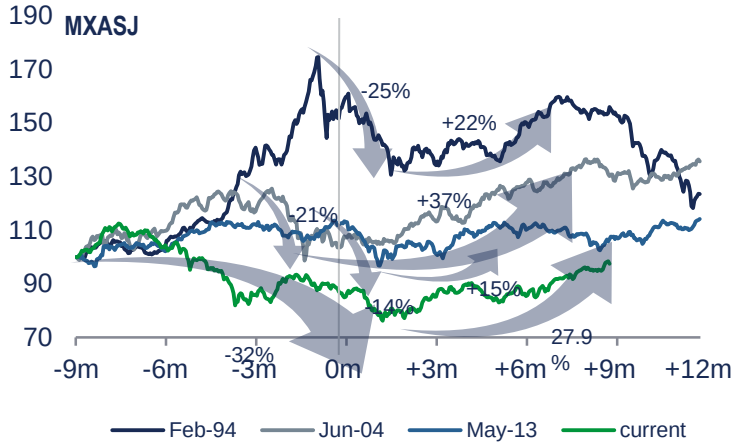
Impact of US Fed Rate hikes on Equity markets:

Correction, then back to trend?

MSCI World performance: Around Fed tightening



MSCI Asia ex Japan performance: Around Fed tightening



Correction in Jan-Feb was short-lived.

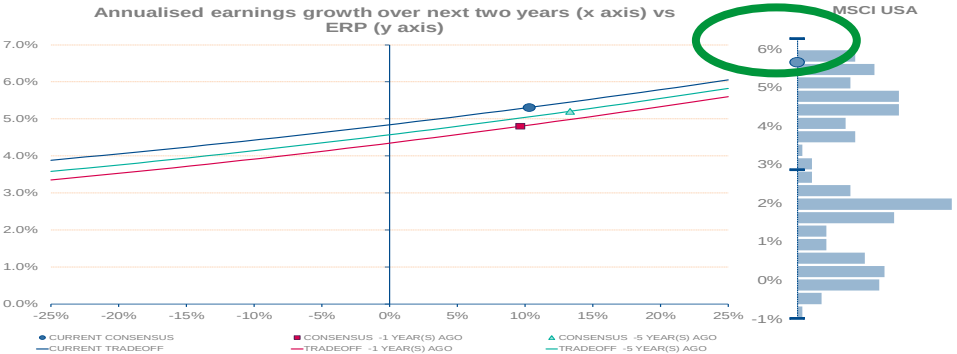
March marked the start of the equity rally, with more expected to come?

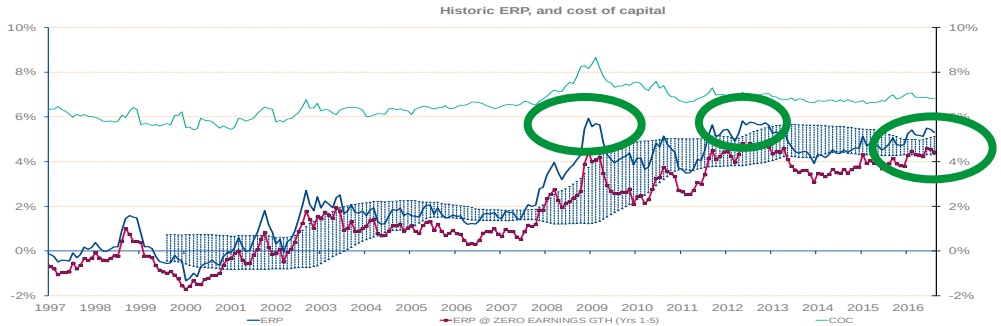
Source: MSCI, Credit Suisse, September 2016.

Barings Cross-Asset Valuation Analysis

US equity market valuation

MSCI USA ERP charts



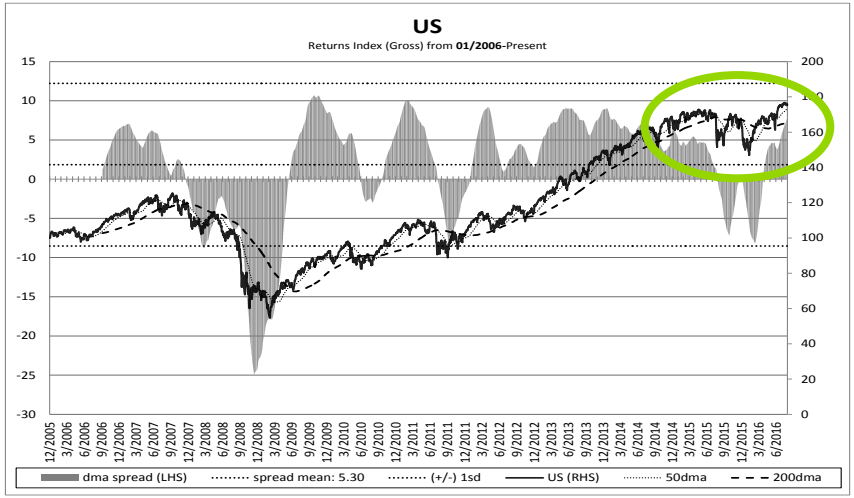


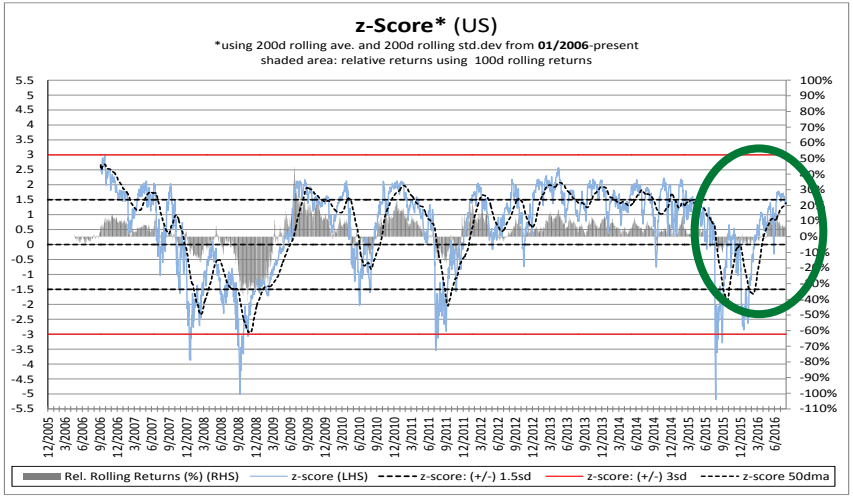
High equity risk premium in the US suggests better relative valuation in favour of equities vs bonds

Source: Strategic Policy Group, Barings, as at September 2016.

US Equity – World's Leading Equity Market

Now back with bullish momentum, after 2 years of range-trading

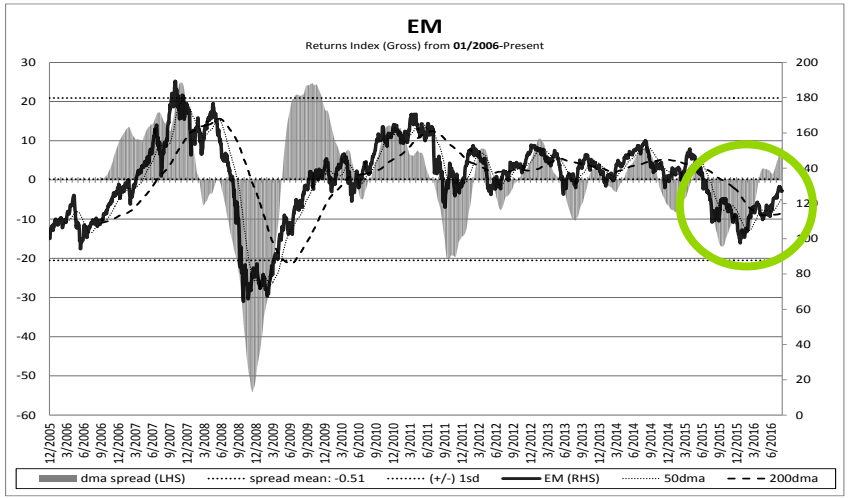


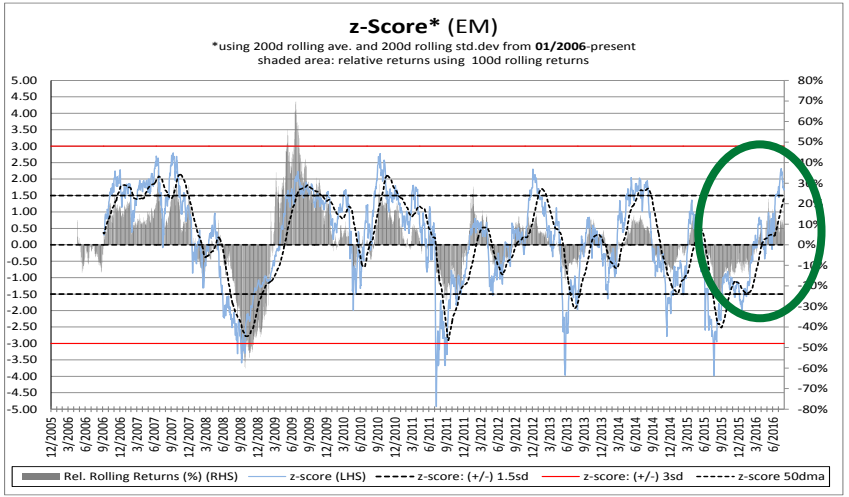


Source: Barings and Factset, as at September 2016.

GEM Equity: Recovery phase, after 2 years in a bear mode

Recent bounce is promising !





Source: Barings and Factset, as at September 2016.

Global Asset Allocation Strategy

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Highlights of Outlook for H2 ’16 and 2017

Sales and Profit growth expected to re-emerge

Corporate revenue and profit growth expected to resume

- 2015 and H1 ‘16 disappointed
- Encouraging signs of an upturn in H2 ‘16 and 2017

Global economy expected to continue to grow, but sub-par

- US and China/India are expected to lead, with Europe and Japan contributing

Expanding fiscal policy expected to complement monetary policy

- “Unconventional monetary” policies boosted asset prices, but did not bring about higher real incomes to low-income households
- We expect fiscal policies to play a bigger role in 2017 and beyond

Positive factors likely to continue to boost “economic-sensitive” assets

Source: Barings, as at September 2016

Barings Global Asset Allocation

Current tactical directions (as at 13 September 2016)

		Avoid (5)	Not Preferred (4)	Neutral (3)	Preferred (2)	Strongly Preferred (1)
Overall			OECD Government Bonds	**Cash (4)** Equity Credit (IG) / Property	EM Local Credit (HY) Indexed-Linked	
Equities	Country		**US (3)** **UK (3)**	Europe Singapore / Hong Kong EM LATAM / EM Europe Australia / Canada	EM Asia Japan	
Equities	Sectors		Consumer Staples Healthcare	Materials / Energy Utilities / Industrials Info Tech	**Financials (3)** Consumer Disc Telco	
Equities	Style			**Income (2)** Size (Small Caps) / Growth Quality / Momentum	**Value (3)**	
Bonds			Japan Italy / Germany	UK	US	
Currency vs. US$			JP¥	£ Gold €UR		

Source: Barings, as at 13 September 2016

Highlighted boxes denote a change in the asset class's score *(data in brackets ( ) denote last months' score)*

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Representative Portfolio's AA (as at 31/8/2016)

Portfolio overall risk position: Medium

- Latest portfolio asset allocation action: added to risk by adding to high yield corporate bonds and Equities (China/HK), and reduced exposure to O.E.C.D. government bonds and Cash.

Equity sub-portfolio

- Overweight in Asia, Japan and Europe. Main focus in stock selection process is on companies which are leaders in their respective field, with a solid business franchise and a long-term track record in delivering profit growth, overlaid by selective high-yielding stocks.

Fixed Income sub-portfolio

- Main emphasis is on capital preservation, and, where it makes fundamental sense, incremental yield.

Current Portfolio	% of NAV	Asset class sub-total (% of NAV)
Bonds		**37.2**
O.E.C.D. Government Bonds	14.3	
Investment Grade Corporate Bonds	9.1	
High Yield Corporate Bonds	6.0	
EM/Asian Government Bonds	7.8	
Equities		**55.6**
Asia Pacific exc. Japan & GEM	17.4	
Global exc. above	38.2	
Alternatives (Gold, etc.)		**--**
Cash & T-bills		**7.2**
Total		**100%**

Source: Barings, as at 31 August 2016

Asset Allocation (as at 31/8/2016)

Portfolio overall risk position: Medium

- Latest portfolio asset allocation action: added to risk by adding to Equities (China/HK), and reduced exposure to Cash

Equity sub-portfolio

- Added exposure to Asian Pacific exc. Japan equities (China/HK) Still maintained O/W Europe, Japan and, to a lesser extent, US and China/Asia.
- Main focus in stock selection process is on companies which are leaders in their respective field, with a solid business franchise and a long-term track record in delivering profit growth, overlaid by selective high-yielding stocks.

Fixed Income sub-portfolio

- Main emphasis is on capital preservation, and, where it makes fundamental sense, incremental yield.

Current Portfolio	% of NAV	Asset class sub-total (% of NAV)
Bonds		**13.2**
O.E.C.D. Government Bonds	7.6	
Investment Grade Corporate Bonds	4.2	
China Investment Grade Bonds	1.4	
Equities		**78.7**
HK-China	26.8	
Other Asia Pacific & GEMs	11.8	
Developed Markets	40.1	
Global Income Multi-Assets		**0.9**
Cash & T-Bills		**7.2**
Total		**100%**

Source: Barings, as at 31 August 2016

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