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## Highlights

In May, risky assets fell across the board. Fiscal issues in the Eurozone periphery deepened and economic momentum moderated in both developed and emerging markets, dampening investor sentiment.

Signs of a deceleration in global growth prospects from previous months raised concerns that demand could falter. Reflecting the risk off environment, commodities posted their biggest monthly drop in a year.

## May Market Recap

Global developed equities fell 1.2% in May, while emerging markets declined 1.6% as further signs of deterioration in economic momentum emerged. For instance, in the US, the ISM manufacturing index fell sharply to 53.5 in May from 60.4 in April, its lowest level since September 2009. US employment data also displayed a notable loss of momentum. Non-farm payrolls increased by only 54,000 in May, the smallest increase in eight months, versus an expected increase of 165,000.

In addition, Greece remained a key focus of attention over the course of the month. The country's worsening fiscal crisis led to multiple credit rating

downgrades from rating agencies, Moody's, S&P and Fitch. Moody's cut its rating of Greece by three notches from B1 to Caa1, and raised the probability of default to 50%. A second bailout package involving the European Union, International Monetary Fund and European Central Bank is likely to be announced although details over any new plan remain uncertain. Benefiting from the increased risk aversion, US treasuries rose 1.5%, making it one of the best performing asset classes.

## Outlook and Strategy

Overall our constructive view on risky assets remains intact, while recognising that there is greater uncertainty than previously around inflationary and policy risks. Reflecting this, our tactical positions are relatively small and we continue to be strongly diversified.

The global economic recovery continues to progress. While we have seen a slowdown in the pace of momentum, the majority of data releases still remain in expansionary territory and point towards durable, albeit moderate economic growth in developed nations. Furthermore, we also expect ongoing strength in emerging economies.





In terms of risks to our central scenario, in the developed world, there is the potential negative impact of fiscal tightening on economic growth. In addition, the prospects for labour markets and consumption remain unclear, despite some signs of stabilisation. In emerging markets, our main concern is the prospect of further monetary tightening, which could impact global growth prospects, given that emerging economies have been an important engine behind the global economic recovery to date.

At an asset class level, we maintain a modest overweight position in both developed and emerging market equities relative to cash and government bonds. The market remains supported by liquidity, driven by not only by capital injections of central banks but also by the high levels of cash on corporate balance sheets. This is positive for equities as it gives companies flexibility to improve returns to shareholders via greater dividends, share buy-backs or M&A activity. In summary, equities are supported by the collective backdrop of positive economic growth, reasonable earnings growth forecasts for 2011 and undemanding stock valuations, not least relative to cash and government bonds.

Within the context of developed market equities, we maintain a moderate preference for Japanese equities on a currency-hedged basis. Although there may be short-term volatility, we believe this market offers an attractive opportunity as the current price-to-earnings ratio is still trading below the historic average. Within emerging markets, we continue to favour Russia on the basis of attractive stock valuations on both a relative and absolute basis, and signs of improving economic conditions. The major risk to the Russian equity market is a further decline in oil prices, which is not our central view.

Furthermore, we have recently initiated a tactical overweight position in China. Chinese equities look particularly attractive, trading at a discount to other emerging countries and relative to their own history. In addition, inflation in China is exhibiting signs of peaking amid further central bank tightening.

In fixed income, the fiscal situation of developed countries has put pressure on government bonds and our outlook is still cautious. In addition, central banks have started to act in response to rising inflationary fears, most notably in the eurozone. Nevertheless, an aggressive response could aggravate the uphill struggle facing eurozone peripheral economies that have yet to address their large debt issues. Therefore, although a moderate increase in rates is expected, we do not anticipate an aggressive tightening cycle to begin at this stage. Our preference remains for developed market corporate bonds, and particularly non-investment grade ('high yield') bonds as they benefit from the favourable conditions for corporate earnings and their extra yield has the potential to offer some protection should government bond yields rise once more. Turning to US dollar-denominated emerging market debt, we continue to believe that while favourable relative to developed government bonds, the asset class looks less attractive than developed high yield and other developed corporate debt. Furthermore, we also have a moderately negative view on global developed inflation-linked bonds, largely because inflation in the developed world remains manageable, despite recent increases. As a result, global inflation linked bonds look expensive in relation with nominal bonds.

## Short-Term Investment Outlook (6-12 months)



	ASSET CLASS	CURRENT VIEW*	REASONING
<b>EQUITY</b>	Global Developed Market Equity	Neutral	<ul style="list-style-type: none"> <li>Equity valuations relative to cash and especially government debt remain attractive, plus liquidity remains supportive. There continue to be risks to the economic recovery, but our core scenario is for positive, although sub-trend growth.</li> </ul>
	US Equity	Neutral	<ul style="list-style-type: none"> <li>Whilst, recent economic news-flow and corporate earnings have been encouraging, unemployment remains elevated at over 9%.</li> </ul>
	Europe Equity (including the UK)	Neutral	<ul style="list-style-type: none"> <li>Economic conditions remain mixed. UK growth has slowed, austerity measures are in the process of being rolled out in parts of Europe and the economic health of peripheral eurozone countries remains uncertain. That said, liquidity remains supportive, and corporate earnings news in Europe has been encouraging.</li> </ul>
	Japan Equity	Positive	<ul style="list-style-type: none"> <li>Within equities, we maintain our overweight to Japanese equities. Although there may be short-term market volatility following the devastating earthquake and tsunami, we believe this offers an attractive opportunity as the current price-to-earnings ratio is still trading far below the historic average.</li> </ul>
	Asia ex-Japan Equity	Neutral	<ul style="list-style-type: none"> <li>From a macroeconomic perspective, the outlook remains generally positive with strength in both the manufacturing and consumer sectors. At a country level, we prefer Chinese equities relative to other Asian emerging markets. Valuations are favourable and inflation is exhibiting early signs of peaking amid further central bank tightening.</li> </ul>
	Global Emerging Markets	Neutral	<ul style="list-style-type: none"> <li>Emerging countries are likely to continue to lead the economic recovery, due to robust domestic consumption and strong intra-regional trade. That said, like developed markets, emerging market equities are exposed to volatility stemming from the question marks around the sustainability of the global economic recovery, exacerbated by the monetary tightening cycle that has already begun in a number of key emerging economies.</li> </ul>
	Latin America Equity	Neutral	<ul style="list-style-type: none"> <li>The economic performance of Latin American countries remains strong and earnings growth estimates for 2011 look reasonable. Nonetheless, the good news seems to be well reflected in market prices and relative valuation measures show no strong signals. We, therefore, retain our neutral stance.</li> </ul>
	Middle East Equity	Neutral	<ul style="list-style-type: none"> <li>Given the political unrest within the region, in the short-term we expect volatility to persist affecting the overall performance. The investment potential will be largely dependent on oil prices and supply uncertainties.</li> </ul>
	Eastern Europe Equity	Neutral	<ul style="list-style-type: none"> <li>Manufacturing data has varied within the different countries. At a country level, we favour Russian equities. Russia's economic activity has been encouraging, while valuations for Russian equities are attractive in both absolute and relative terms.</li> </ul>

<b>FIXED INCOME</b>	US Government Bonds	Negative	<ul style="list-style-type: none"> <li>Excess capacity in developed markets and the commitment of the Fed to remain accommodative are generally supportive for low yields. However, the market is still offering little value relative to history and, downside risks remain, particularly in relation to fiscal policy. Within fixed income, we prefer to own corporate debt, where we see greater total return opportunities.</li> </ul>
	Euro Government Bonds	Negative	<ul style="list-style-type: none"> <li>We have a negative stance on eurozone government bonds relative to cash. This is due to uncertainties regarding the economic health of eurozone peripheral countries. In addition, valuations of these bonds do not look particularly attractive; they offer limited protection against negative surprises.</li> </ul>
	Investment Grade Corporate	Positive	<ul style="list-style-type: none"> <li>Strong corporate earnings results, the view that major central banks will keep interest rates low and strong demand for yield have boosted investment grade corporate bonds. With momentum likely to remain positive, we continue to be positive on the asset class.</li> </ul>
	High Yield	Positive	<ul style="list-style-type: none"> <li>High yield bonds continue to look attractive on a total return basis. We have retained our positive view on the asset class given better-than-expected corporate results, declining default rates and growing expectations that interest rates could remain at low levels due to global economic growth uncertainties.</li> </ul>
	Sovereign USD Denominated Emerging Markets Debt	Negative	<ul style="list-style-type: none"> <li>While sovereign US dollar-denominated emerging market debt continues to look less attractive on valuation grounds than developed market corporate debt, and high yield in particular – they remain more attractive relative to government bonds.</li> </ul>
	Global Developed Inflation-Linked Bonds	Negative	<ul style="list-style-type: none"> <li>Despite recent increases, inflation looks manageable in developed markets. As a result global inflation linked bonds look expensive in comparison with nominal bonds.</li> </ul>



	ASSET CLASS	CURRENT VIEW	REASONING
<b>OTHER INVESTMENTS</b>	Oil	Between the range of US\$90 to US\$110 per barrel	<ul style="list-style-type: none"> <li>Last month we raised our target range for the oil price to \$90 - \$110. We maintain this forecast as supply and demand forces appear reasonably balanced at present. However, short-term volatility is expected while unrest in the MENA region persists.</li> </ul>
	Gold	Neutral Between the range of US\$1,250 to US\$1,400 per troy ounce	<ul style="list-style-type: none"> <li>We maintain our neutral stance on gold. Quantitative easing combined with ongoing macroeconomic uncertainty, remain supportive factors for this precious metal. That said, economic fundamentals continued to improve in many economies globally, suggesting the economic recovery is making good progress. Balancing these factors, we expect gold will trade in a between a range of US\$1,250 to US\$1,400 per troy ounce in the near-term.</li> </ul>
	Commercial Real Estate (unlisted markets)	Neutral	<ul style="list-style-type: none"> <li>Despite generally weak occupier markets, demand for prime investments in core markets in the US and Europe has increased and is expected to continue to rise in the short-term. Whilst some opportunities exist, we remain cautious for these markets overall. More positive economic growth in Asia Pacific is expected to be largely off-set by large development pipelines in key markets in China, India and Singapore, and wide regional variations remain. UK property yields remain above our view of fair value and significantly higher than gilt yields. However, short-term performance is expected to be muted, largely due to subdued occupier markets.</li> </ul>
<b>CURRENCY</b>	Euro, British Pound Sterling, Japanese Yen and the US Dollar	Neutral	<ul style="list-style-type: none"> <li>Valuation indicators are not sending any clear signals at present. We see both event-driven and sentiment-driven risks contributing to ongoing volatility. We thus continue to have a neutral view on currency exposures.</li> </ul>

\*within the broad asset class

### Summary:

Overall, we have maintained a moderately overweight position in global equities relative to both government bonds and cash. Within the context of developed market equities, we remain moderately positive on Japan. Although the earthquake will have a negative short-term economic impact, we continue to see valuations and policy support as a favourable backdrop for Japanese equities. Within emerging market equities, our favoured markets are China and Russia based on valuations and encouraging macroeconomic performance.

In fixed income, we have a negative view on government bonds relative to cash. We have a positive stance on corporate debt – particularly high yield. Positives for corporate bonds include attractive valuations and favourable issuer fundamentals. Our central economic scenario is for slow but positive growth in the major developed markets, a backdrop that is typically positive for credit markets.

With regard to the four major developed market currencies, it is likely that heightened volatility will continue. Valuation measures are not currently providing strong signals and we therefore have a neutral stance on currency positions.



## Macro Assessment

### US:

#### **US data releases were disappointing, indicating a slowdown in activity.**

- Annualised first quarter GDP figures came in at 1.8% q-o-q, lower than the fourth quarter of 2010 figure of 3.1% q-o-q.
- The ISM Manufacturing index fell to 53.5 in May, well below the previous month's reading of 60.4. Industrial production growth was also poor, coming in flat in April against an expected 0.4% month-on-month rise.
- In the same month, the US leading indicators index fell by 0.3% while the Philadelphia Fed Manufacturing survey also slipped notably to +3.9 in May from +18.5 in April.
- US employment data displayed a notable loss of momentum, with non-farm payrolls increasing by only 54,000, the smallest increase in eight months, versus an expected increase of 165,000.

### Europe ex-UK:

#### **The economic picture was fairly mixed in May, despite signs that the economic recovery was still ongoing.**

- GDP growth was stronger than expected in first quarter, coming in at 0.8% quarter-on-quarter. This was mainly driven by the larger nations such as Germany (1.5% quarter-on-quarter) and France (1.0% quarter-on-quarter).
- However, in line with other developed regions, PMI indices showed signs of moderation. The Manufacturing index dropped to 54.6 in May from 58.0 in April, while the Services index also surprised on the downside, falling to 55.4.
- Labour market data and consumer activity remained disappointing. Eurozone unemployment was unchanged in March, at 9.9% while retail sales declined by 1.0% on a month-on-month basis in March, following a 0.1% fall a month earlier.

- Also weighing on the region's outlook, the economic performance of the larger economies of Germany and France continued to contrast with the situation in the peripheral countries.
- Greece returned to centre stage in May. Rating agencies S&P and Fitch downgraded the country's long-term credit rating amid fears that Greece's debt would have to be restructured. Discussions are ongoing over the possibility of a second bail out package although the outcome of these talks is far from certain.

### UK:

#### **The UK economic news-flow was generally mixed in May.**

- Economic growth moved back into positive territory in the first quarter of 2011, but remains subdued. GDP growth came in at 0.5% quarter-on-quarter, meeting expectations.
- A slowdown in activity was evident in other indicators. For example, the Manufacturing PMI index softened, from 54.6 in April to 52.1 in May, while industrial production missed expectations, coming in at 0.3% month-on-month in March.
- There was some encouraging data though. Retail sales growth bounced in April, beating expectations, up 1.2% month-on-month in April.
- Labour market conditions showed some improvements too, with the unemployment rate unexpectedly falling in March, to 7.7%. That said, jobless claims were disappointing rising by 12.4k in April against a 0.7k rise in March and the Nationwide Consumer Confidence Index fell to 43 in April.
- UK inflation increased again in April to its highest level since September 2008. The year-on-year CPI came in at 4.5%, up from 4.0% year-on-year in March, while core CPI came in at +3.7% y-o-y against 3.2% a month earlier.

## Japan:

### The data was reflective of the March earthquake and its impact on economic activity.

- First quarter GDP fell by 0.9% quarter-on-quarter, while fourth quarter GDP was revised down to -0.8% quarter-on-quarter, taking the economy into recession. Given the tragic natural disasters in March, a fall was expected but not to the reported extent.
- The data showed weakness across all areas. Consumption data was badly hit. Retail sales declined by 7.8% month-on-month in March and the Consumer Confidence index declined from 38.6 in March to 33.1 in April.
- In addition, the April PMI manufacturing index slipped to 45.7 from 46.4 in March. March export growth was also negative, posting a 2.2% year-on-year contraction, the first fall in 16 months.
- On the supply side however, April industrial production bounced 1.0% m-o-m in April having plunged by 15.3% m-o-m in March.
- On inflation, prices rose for the first time in five months. National year-on-year CPI rose by 0.3% in April although core CPI remained negative, at -0.1% year-on-year, suggesting that deflationary pressures persist.



## Emerging Markets:

**Emerging markets continue to display impressive economic performance, despite signs of moderation and ongoing monetary tightening.**

- Export growth remained robust in April despite falls from the previous month. In particular, China's growth in exports remains strong at 29.9% year-on-year in April but below the 35.8% year-on-year we saw in March. Indian and South Korean exports showed similar trends.
- Manufacturing and industrial activity followed a similar trend, moderating somewhat but buoyant overall, as suggested by ongoing positive readings for PMI manufacturing indices and industrial production for the BRIC countries.
- Furthermore, consumption remains a key driver of growth and stronger than in developed economies.
- Overall, the ongoing economic strength, combined with rising levels of inflation, continue to lead policy makers to increase rates. In the last month, Brazil, India and Russia have seen an increase in their benchmark interest rates while China has increased the reserve requirement ratio.



# Equity Markets

## Global Developed Markets:

- Liquidity is expected to remain a positive factor for equity markets in general. Despite modestly higher levels of inflation in developed nations, central banks are likely to maintain accommodative monetary policies in 2011 and increase rates only gradually, if necessary.
- In addition, the US will continue to maintain its balance sheet by reinvesting proceeds of maturing mortgage-backed securities and Treasury holdings after the second wave of quantitative easing expires at the end of June.
- Valuations in all major equity markets are at undemanding levels, and macroeconomic data is still positive, although less so than previously.
- Therefore, as the positive backdrop for equities is still applicable, we maintain a modest overweight position in equities against cash and government bonds.

## US:

- The earnings outlook for US equities remains supportive. Companies continued to report strong results, whilst expectations for US earnings growth are sound, at 17.0% for 2011 and 13.7% for 2012. Moreover, elevated IPO and M&A activity is also a positive sign.
- From a valuation perspective, equities continue to look attractive, particularly when compared to government bonds and cash.
- Monetary policy remains accommodative in the US, and we expect it to remain so through 2011, despite recently rising inflation.
- However, a number of risks temper the positive picture. For example, economic momentum has started to deteriorate which may have a negative impact on equity returns.
- On balance, we maintain our modest overweight allocation to US and other equity markets relative to government bonds and cash.

## Europe:

- Although peripheral eurozone issues remain a concern, overall, economic activity is positive in both the UK and the eurozone. We continue to expect moderate growth in 2011 in both the UK and eurozone.
- From a valuation perspective, eurozone and UK equities are trading at reasonably undemanding levels, particularly relative to government bonds and cash, with their 12-month forward price / earnings ratios at 10.0x and 9.8x respectively.
- In addition, our central view is still for rates to remain broadly accommodative in 2011 due to the potential impact on fragile growth in the region.
- Therefore, we maintain a modest overweight position in equities against cash and government bonds.

## Japan:

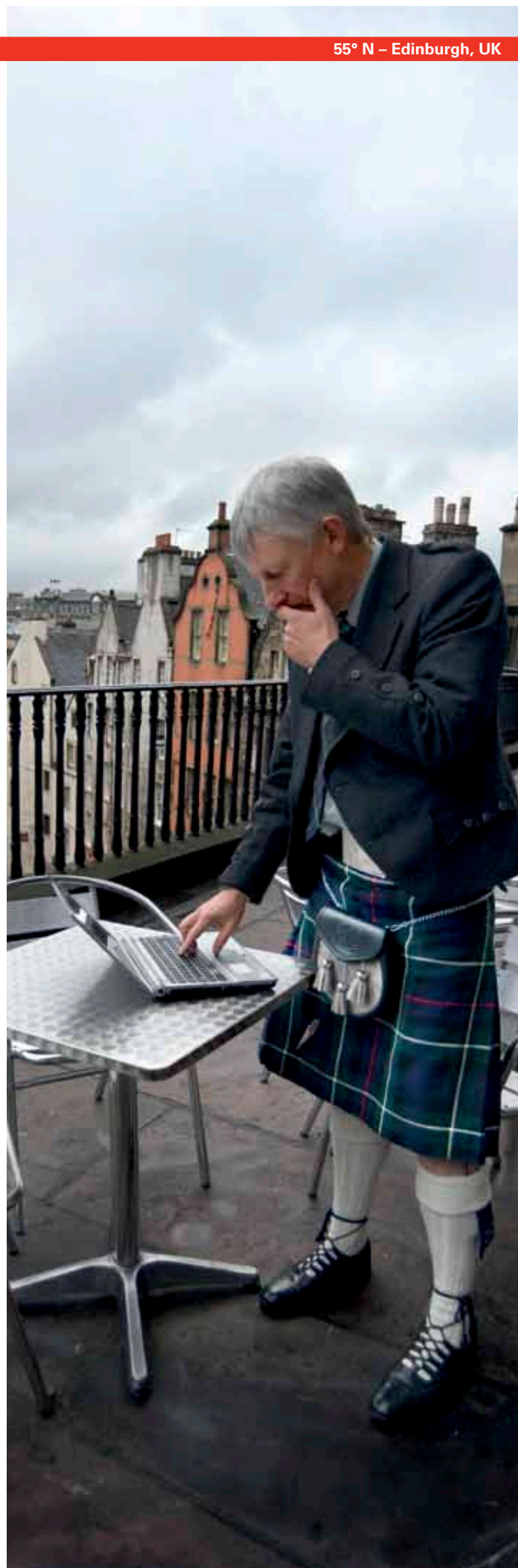
- Although we can expect data in the short-term to remain weak, we believe that the market has priced in these effects and as such, the impact on the equity market performance may not be significant.
- We expect the central bank to continue providing necessary liquidity to the financial system and reconstruction efforts.
- In recognition of the growth potential from reconstruction activity, Consensus Economics revised up their 2012 economic growth forecast to 2.8%.
- In terms of valuation, Japanese equities are trading at a 12-month forward price earnings ratio of 13.1 xs as of the end of May, well below their historic average.
- We maintain our positive stance on equities relative to government bonds. Within developed equities, we moderately favour Japan, despite recognising that the short-term disruption effects may not have fully played out.

### Global Emerging Markets:

- Based on a 12-month forward price / earnings measure, valuations decreased to 10.4 from 11.2 last month. This level compares favourably with the long-term historic average of 13.6 (since 1987).
- Retracement in commodity prices and policy actions by central banks are starting to take effect, easing inflation concerns.
- This is balanced by the negative global factors of moderating (but still positive) global growth, large fiscal deficits in developed markets and weakening debt dynamics in the eurozone periphery.
- The case for emerging markets nevertheless remains positive on the back of strong fundamentals and ample global liquidity.
- At a country level, we prefer Chinese and Russian equities relative to other emerging markets. Chinese equity valuations are favourable and inflation is exhibiting early signs of peaking amid further central bank tightening.
- Russian equities are also of interest, particularly as macroeconomic data remains supportive and there is potential for earnings forecasts to be revised up. The major risk to the Russian equity market is a further decline in oil prices, which is not our central view.

### Asia ex-Japan:

- Despite monetary tightening, Asian ex Japan countries recorded strong growth, albeit off recent peaks, and generally above that of other emerging countries. Monetary tightening is likely to continue as inflation pressures are still evident, but the focus is now switching to when the rate tightening cycles may end as we may be seeing early signs of inflation moderating.
- Earnings growth forecasts for 2011 remain strong, at 15.8%, which continues to look attainable given the current growth outlook.
- In terms of valuations, Asia ex-Japan equities were trading at a 12-month forward price to earnings ratio of 11.7 at the end of May, which is still reasonable, compared to other markets and its own history. Chinese equities in particular look attractive, standing at a discount to other emerging countries and to their own history.
- Overall, we maintain our preference for equities versus government bonds and cash. Whilst we do not expect Asia ex Japan equities to outperform in aggregate relative to other equity markets, we highlight Chinese equities as offering an attractive opportunity within the region at present.



### Latin America:

- The economic performance of Latin American countries remains strong and earnings growth estimates for 2011 look encouraging and in line with our assessment of the business and consumption environment globally.
- Having said that, the good news seems to be reflected in market prices and relative valuation measures show no strong signals.

### Middle East:

- The situation in the Middle East and North Africa remained a concern.
- Libyan oil output has slumped as the conflict between its government and insurgents forced major oil companies there to suspend operations and evacuate staff.
- We continue to monitor events in the region very carefully to assess the impact on oil supply and prices.
- A long-lasting increase in oil prices combined with deterioration in oil supply is likely to be detrimental to economic growth. So far, though, this is not our central scenario.

### Eastern Europe:

- In Eastern Europe, the data for Russia was more buoyant. Real retail sales growth came in at 5.6% in March in Russia, which beat consensus forecasts. First quarter GDP numbers were slightly better-than-anticipated. In Russia, year-on-year GDP growth was 4.1%, compared to 4.5% in the fourth quarter.
- At the country level, we continue to like Russian equities relative to other emerging markets. Macroeconomic data remains supportive and valuations are attractive on a relative basis.



## Fixed Income

### USD Government Bonds:

- We continue to expect the Federal Funds rate to remain at the current low levels for some time.
- Although recent data releases have been disappointing, the economic recovery in the US remains in place.
- In the medium-term, we continue to expect bond yields to back up, as investors are unlikely to tolerate negative real rates.
- Furthermore, the fiscal position of the US continues to pose upside risks to yield premiums in the Treasury market.
- Overall, we retain our modestly cautious view on US Treasuries relative to other asset classes. Within fixed income markets, we continue to prefer corporate bonds, both investment grade and high yield.

### Eurozone Government Bonds:

- The overriding mood in the financial markets is still volatile and uncertainties regarding the economic health of eurozone peripheral countries remain, more particularly surrounding the risk of some form of debt restructuring in Greece.
- Although the bond markets of peripheral eurozone nations are priced to compensate for some risk, the final solution to the debt difficulties is not clear, making it hard to evaluate whether the pricing is sufficiently attractive.
- The European Central Bank have been the only major developed central bank thus far to raise rates. The focus now lies on the extent of future additional rate hikes. European Central Bank President Trichet indicated that the pace of interest rate increases would not be as rapid as some estimates had suggested.

- Therefore, against this backdrop, we maintain a cautious outlook for eurozone government bonds against cash. Overall, within fixed income, our preference remains for corporate rather than sovereign debt.

### Investment Grade Corporate:

- Despite the increase in risk-aversion during May and relative strength in core government bonds, the resilience of investment grade corporate bonds as an asset class was a notable theme for the month. As such, our tactical preference for corporate bonds continues to be rewarded.
- The earnings environment continues to reinforce our positive view. Investment grade corporate balance sheets remain healthy and the first quarter earnings season has been better-than-expected.
- The expectations for corporate earnings growth in 2011 remain encouraging, at 15.2% for developed markets in aggregate, according to IBES data.
- The low interest rate backdrop is likely to continue to fuel strong investor demand for yield. At the same time, supply has remained strong, therefore on balance; this has prevented credit spreads from narrowing significantly in the last few months.
- Overall, we believe that the current environment is still favourable for credit and therefore we continue to prefer investment grade bonds relative to government bonds. Within credit, we favour high yield bonds over investment grade, as their extra yield offers greater protection should government bond yields rise.





### High Yield:

- Although economic growth remains lacklustre in the major developed economies, corporate balance sheets remain in good health and companies are continuing to meet their debt payments. In the US, for example, only 10 companies have defaulted this year, compared with 26 over the same period of 2010, according to S&P.
- The global annualised speculative grade default rate stood at 2.28% in April, as measured by S&P. This remains very low relative to history, and reinforces our positive view on the asset class, despite a slight increase from March's level of 2.07%.
- Our central scenario for a low inflation, modest growth environment is likely to keep monetary policy accommodative and therefore demand for high yield bonds should remain high. Overall, we retain our positive view on the asset class.

### Sovereign USD Denominated Emerging Markets:

- The long-term trend of improving structural fundamentals for emerging economies coupled with a broad global growth environment are supportive of emerging markets and emerging market debt spreads have the potential for modest further tightening.

- Emerging market debt spreads are low by historical standards but still appear attractive relative to yields of developed market sovereign bonds. All other things being equal, this should keep the asset class in favour with investors.
- We continue to prefer developed market high yield debt to USD denominated emerging market sovereign debt since the former has a better risk-reward profile.

### Global Inflation-Linked Bonds:

- In developed economies, inflation is expected to be relatively contained in the near-term, as high unemployment and tighter fiscal policies are likely to weigh on growth.
- The global inflation-linked bond market looks expensive relative to nominals and we retain an underweight stance.

## Other Investments

### Oil:

- The oil price decreased from USD114/bbl at the end of April to USD103/bbl at the end of May.
- Overall, it appears the supply picture is largely unchanged and the impact from Libyan oil supply disruption minimal. However, ongoing unrest in the Middle East continues to create some risk of supply uncertainties.
- Although global growth is moderating, the absolute levels remain positive and, in emerging economies, quite strong.
- The macro environment does not suggest a significant reduction in oil demand and hence we maintain our expectation for oil to trade in a range of USD 90-110 p/b on a 6 to 12 month view.

### Gold:

- Actions by the US Federal Reserve are likely to continue to provide liquidity and potentially weaken the US dollar further, both of which are likely to drive commodity prices, including gold, higher.
- Increased inflationary risks are adding to the attractiveness of holding the metal as well.
- However, some factors remain unsupportive, such as rising interest rates outside the US, as has been seen in some emerging economies.
- While we are not fundamentally positive on gold on a medium-to-long-term basis, we recognise over the short-term this can act as an effective diversification tool in portfolios.

### Commercial Real Estate (unlisted):

- The UK remains our preferred market over the medium to long-term due to the yield level, which, although lower than last summer, sufficiently prices in the weak occupier market.
- Asia Pacific has the strongest rental growth prospects, particularly in the short-term, although recent strong capital value growth has reduced yields to a less attractive level, with the potential for a correction in values over the medium-to-long-term.

- In the US, despite weak occupier markets, pricing for prime assets in top-tier markets, such as New York and Washington D.C., has increased rapidly, and cap rates are back to pre-crisis levels. This has reduced their relative attractiveness. However, there are significant regional differences, and pricing for other segments of the market remains subdued. Selected opportunities may appear as demand broadens from its current narrow focus.
- In the eurozone, capital values generally remain expensive on a relative basis, following a smaller peak to trough correction compared with other regions. However, there are significant country and local variations within the region, and we expect stock specific opportunities to emerge.


### Currency:

- Last month we noted that the negative risk to the euro from the peripheral eurozone had the potential to reverse its 2011 strengthening trend which has proved to be the case. The euro remains at risk to this significant negative factor, balanced by the positive factors of increasing euro interest rates and strong growth in the core economies.
- In previous months we have also noted that the markets were expecting UK interest rates to start rising sooner than we were. Consensus expectations for a rate increase have now fallen on the back of weaker UK growth numbers, more in line with our view. Sterling is unlikely to enjoy imminent interest rate support.
- In the long-term, we continue to see value in emerging market currencies due to the higher growth prospects of these regions. Short-term volatility is likely to continue to be a feature of investing in these currencies.
- We remain neutral in our exposures to major currencies.

## Long-Term Investment Outlook (Three to Five Years)



	ASSET CLASS	CURRENT VIEW	REASONING
	Developed Market Equities	Positive	<ul style="list-style-type: none"> <li>Average rate of growth somewhat subdued in the developed world. Yet exposure to higher growth areas like emerging markets will benefit earnings growth and dividend growth and are likely to keep average nominal returns at high single digit levels.</li> </ul>
	Emerging Market Equities	Positive	<ul style="list-style-type: none"> <li>Expected to outperform developed market equities thanks to a favourable structural backdrop including improved fiscal management and trade balances, labour force expansion and rapid urbanisation.</li> </ul>
	Developed Market Sovereign Bonds	Negative	<ul style="list-style-type: none"> <li>Comparatively low level of yield and issues around public debt are likely to keep average returns relatively subdued.</li> </ul>
	Developed Markets Credit	Positive	<ul style="list-style-type: none"> <li>The level of spread continues to be attractive on a historical basis and corporate balance sheets in developed markets are generally in good shape. This is likely to keep average return for credit assets above respective government bonds.</li> </ul>
	High Yield	Positive	<ul style="list-style-type: none"> <li>The level of spread continues to be attractive on a historical basis and corporate balance sheets in developed markets are generally in good shape. This is likely to keep average return for high yield credit assets above respective government bonds.</li> </ul>
	Emerging Market Sovereign Debt	Positive	<ul style="list-style-type: none"> <li>Structural improvements such as improved fiscal management and trade balances, labour force expansion and rapid urbanisation along with reasonable valuation levels are likely to lead to outperformance of emerging market debt relative to cash and developed market sovereign debt.</li> </ul>
	Developed Market Inflation-Linked Bonds	Neutral	<ul style="list-style-type: none"> <li>Inflation expectations are likely to remain contained due to subdued growth in developed markets. In addition, independent central banks are focused on keeping price pressures under control. However, if higher inflation in emerging markets is not dealt with effectively, it could feed through to developed markets over the medium-term.</li> </ul>
	Commodities	Positive	<ul style="list-style-type: none"> <li>Growth in emerging markets likely to remain an element of support for this asset class.</li> </ul>
	Developed Cash Rates	Negative	<ul style="list-style-type: none"> <li>Subdued economic growth and stimulus measures are likely to keep rates at low levels for the foreseeable future.</li> </ul>

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