



GLOBAL ASSET ALLOCATION: THE VIEW FROM THE UK

December 2020

MARKET INSIGHTS

As of 30 November 2020

Digging for Value

Promising news on COVID-19 vaccines has triggered optimism for a return to normal next year, buoying deeply cyclical segments of the market that have been the hardest hit by shutdowns. November saw a strong rebound in many of these unloved sectors, including materials, energy, financials and industrials. Following a period of meaningful underperformance, a significant beneficiary of the abrupt rotation away from technology-heavy growth sectors has been emerging markets (EM) value stocks, which have more than 50% exposure to these sectors. Expectations in 2021 for unleashed pent-up global demand, increased fiscal spending, aggressive monetary policies and higher energy prices could provide a strong backdrop for cyclical companies in EM. An additional boost could come from a rebound in EM currencies, as they face less depreciatory pressure versus the US dollar. Ignored for nearly a decade, EM value companies may finally see more interest from investors as they dig for cyclical opportunities with very attractive valuations.

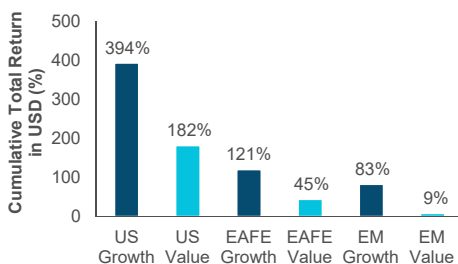
Cleaning House

A wave of defaults across some highly rated—including AAA—Chinese companies with perceived state support have shaken local markets causing investors to reassess risk in the growing Chinese bond market. The Chinese corporate bond market has grown substantially over the past decade since the global financial crisis as China sought to open its capital markets to foreign buyers and increase its representation in the Bloomberg Barclays Global Aggregate Index. Although there were signs of bond market weakness heading into the coronavirus pandemic, China policymakers were forced to pull back on credit reform initiatives as economic conditions deteriorated, temporarily masking potential solvency issues. However, with the recent improvement in economic growth, policymakers have begun re-tightening financial conditions, exposing the overhang of weak corporates, many of which have been kept alive by forbearance. Chinese authorities may see the current economic strength as an opportunity to clean up weak companies, which, in the long run, could improve the perception of Chinese corporate credit markets.

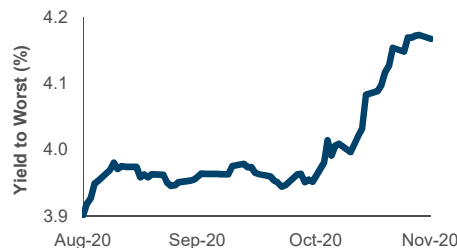
Feeling Blue?

After Democratic candidate Joe Biden won the US presidential election and Democrats retained control of the House of Representatives last month, markets seemingly cheered the prospects of a split government, with the US Senate likely to remain controlled by the Republicans. However, the balance of power remains uncertain, hinging on the result of two very close runoff elections in Georgia on 5 January 2021. If Republicans win either of the Georgia runoff races, they will retain control of the Senate. However, if they were to lose both seats to the Democrats, the result would be a 50/50 split in the Senate with the tie-breaker vote going to the new vice president, tipping power in favour of the Democrats. With Democrats in control of the presidency, House of Representatives and Senate, markets may begin to factor in the likelihood of more progressive policies on taxes and tighter regulation. Given the market's strong rebound in November, driven by positive vaccine news and prospects for a balanced political environment, the market could be in for a negative shock.

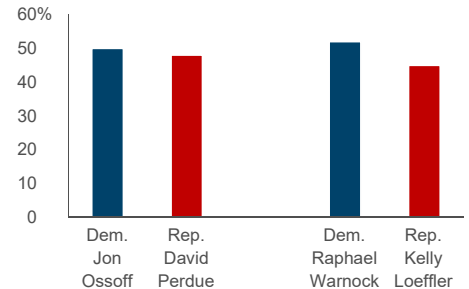
10-Year Cumulative Total Return (USD) by Regional Style
As of 30 November 2020



Chinese Corporate Bond Index¹ Yield to Worst
As of 30 November 2020



Georgia Senate Race Election Poll
As of 2 December 2020



Past performance is not a reliable indicator of future performance.

US Growth = Russell 1000 Growth Index, US Value = Russell 1000 Value Index, EAFE Growth = MSCI EAFE Growth Index, EAFE Value = MSCI EAFE Value Index, EM Growth = MSCI Emerging Markets Growth Index, EM Value = MSCI Emerging Markets Value Index.

¹Chinese Corporate Bond Index represented by Bloomberg Barclays China Aggregate Corporate Bond Index.

Sources: London Stock Exchange Group plc and its group undertakings (collectively, the "LSE Group"), MSCI, Bloomberg Finance L.P., Bloomberg Index Services Limited and SurveyUSA (see Additional Disclosures).



Positives

Negatives

United Kingdom

- Encouraging vaccine news means that there is light at the end of the tunnel for the UK economy, which is heavily services-based
- An exuberant housing market could help support consumption in the short term, driven by stamp duty cuts and pent-up demand

- Longer-term restrictions imposed on exit from the second national lockdown will be impactful
- The transition to new trade arrangements will be very economically disruptive
- Projections forecast 11.5% of gross domestic product structural fiscal tightening for 2021
- Combination of risks makes a move to negative interest rates more likely, which will weigh on sterling

Developed Europe

- Higher exposure to more cyclically oriented sectors that should benefit from economic recovery
- Monetary and fiscal policy remain accommodative
- Equity valuations remain attractive
- Strong long-term euro outlook

- Second wave of virus leading to new lockdowns
- Elongated process to enact further stimulus
- Brexit likely to negatively impact trade
- Limited scope for European Central Bank to stimulate further

United States

- Potential for additional round of fiscal support
- Monetary policy remains very accommodative
- Healthy consumer balance sheets and high savings rate
- Low rates driving strong housing market

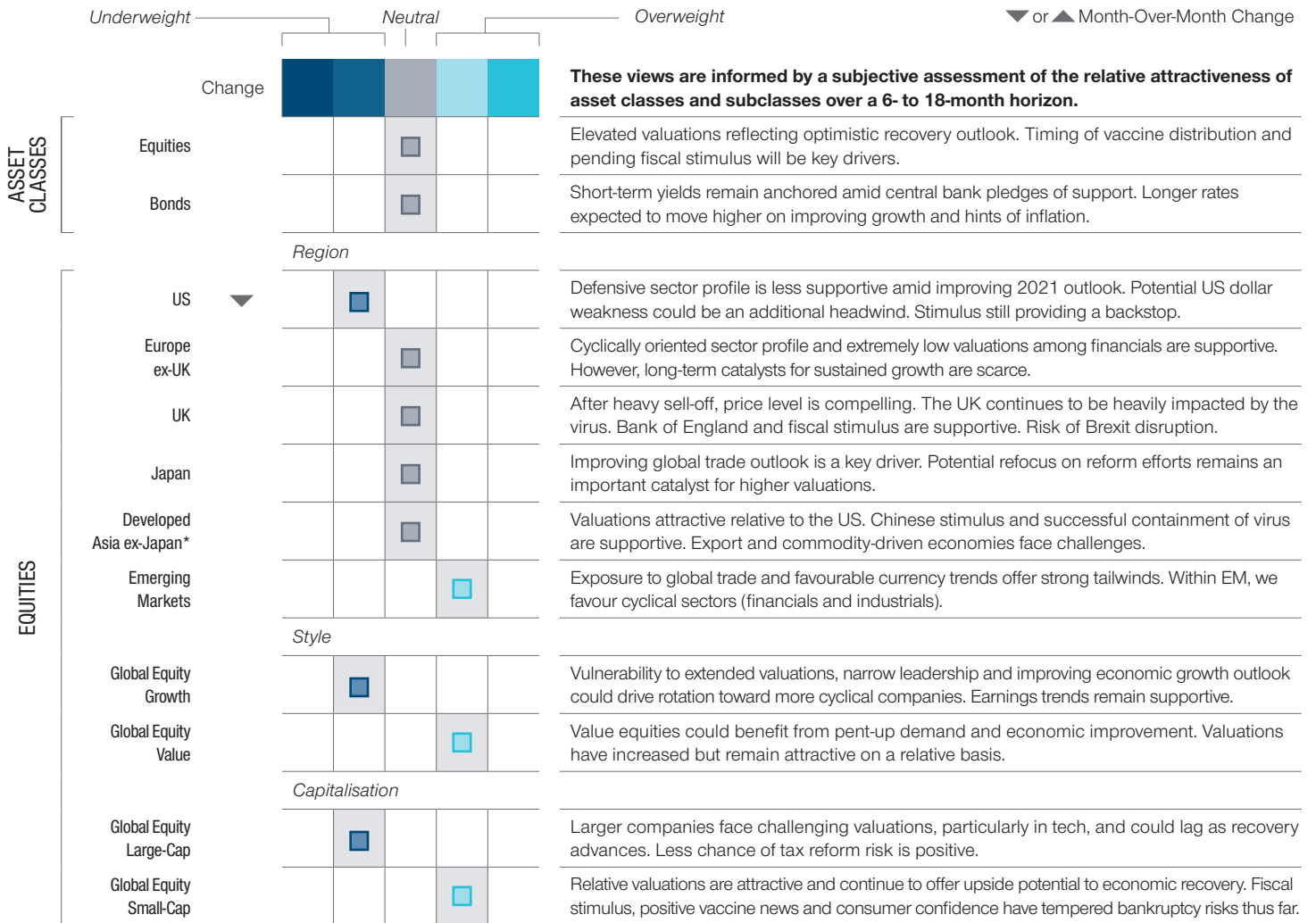
- Heightened political uncertainty
- Increasing COVID-19 cases
- Elevated corporate and government debt levels
- US dollar weakness

 **Positives** **Negatives**

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| Japan | <ul style="list-style-type: none">▪ The economy continues to recover, while further stimulus measures are also expected▪ Equity momentum has been fuelled by strong money supply and foreign inflows; despite setting new highs, equity markets remain reasonably valued relative to peers▪ While current recovery will be centred on traditional industries like automakers, Japan Inc. is changing with a push toward digitisation | <ul style="list-style-type: none">▪ The economic recovery has been slower than in other developed economies, while a resurgence in COVID-19 cases has led to curbs of certain stimulus programmes▪ Equity markets reaching new highs might lead to some profit taking in the near term▪ Market indicators continue to signal a stronger yen, which would reduce companies' competitiveness and profitability |
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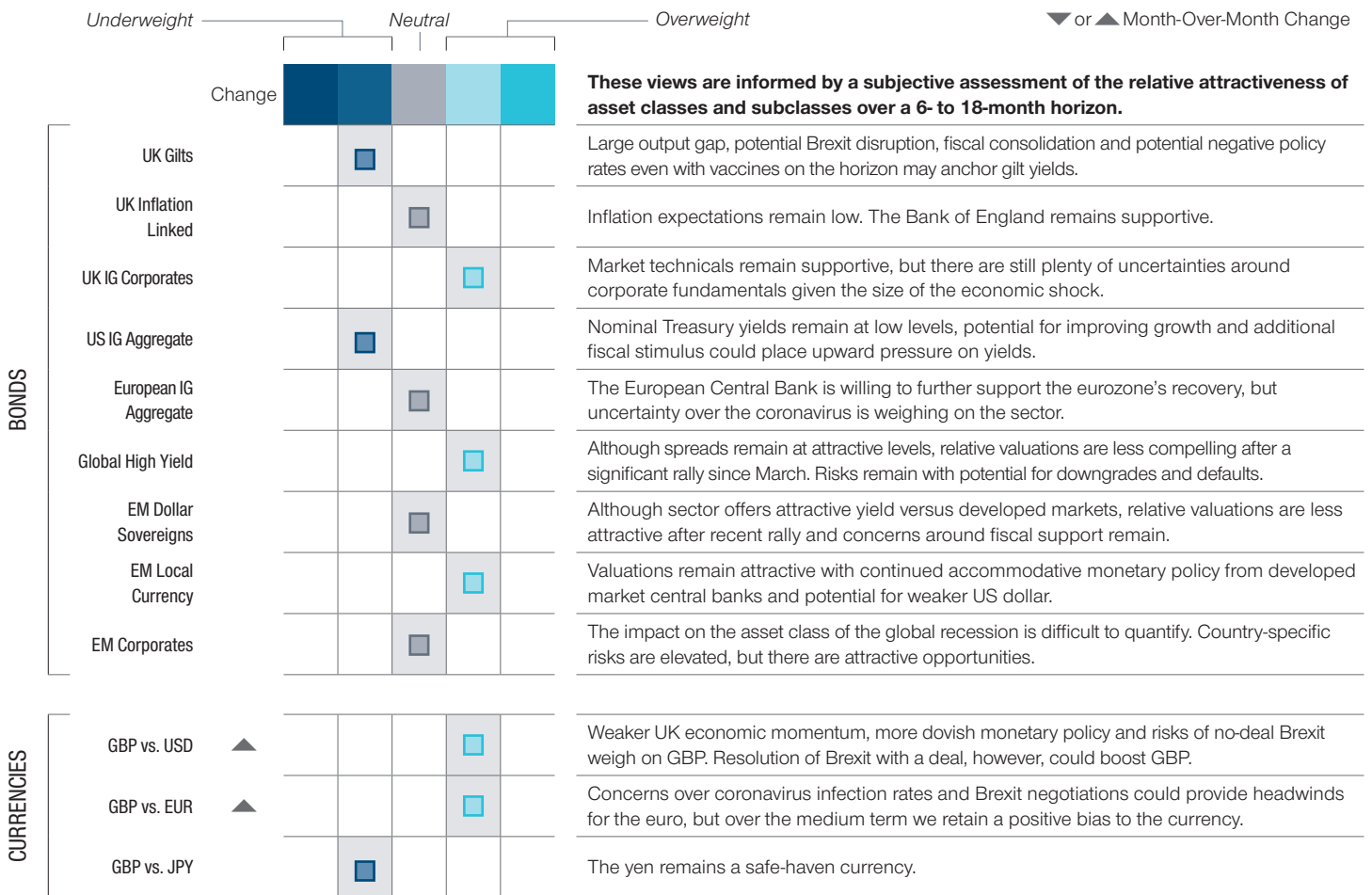
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| Asia Pacific
ex-Japan | <ul style="list-style-type: none">▪ Positive economic growth momentum in China should continue well into 2021, with a clear focus on domestic consumption▪ We expect the renminbi to remain strong and Chinese bonds to stay attractive given the global low-yield environment▪ Australian consumer spending should continue to be supported by pent-up demand and an improving job market▪ The Australian economy could outperform in the near term after effectively containing a COVID-19 outbreak | <ul style="list-style-type: none">▪ China may be the first major economy to normalise monetary and fiscal policy since it effectively contained COVID-19 outbreaks early▪ Tech regulations and the suspension of Ant Group's record initial public offering create headwinds for market leaders▪ Risk exists that support measures could be wound down too quickly, creating a hangover effect if the fiscal tap is turned off▪ A strong Australian dollar might be the target of future measures from the central bank |
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| Emerging
Markets | <ul style="list-style-type: none">▪ Chinese economy has largely rebounded▪ US dollar weakness▪ Exposure to cyclical areas of economy should benefit from broad global recovery▪ Equity valuations attractive relative to developed markets | <ul style="list-style-type: none">▪ Limited ability to enact fiscal stimulus (excluding China)▪ Highly sensitive to global industrial production and trade trends, which have improved but remain muted▪ Capacity and infrastructure to combat COVID-19 varies |
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* Includes Australia



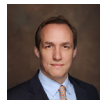
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