

21 July 2009



Markets are at their most fascinating – and most challenging – when price action diverges from what an objective assessment of the relevant news might suggest.

By and large, economic data and corporate announcements in June were consistent with continued improvement in global economic conditions. And yet world equities declined 9% peak-to-trough, the first notable correction in the rally that began in early March.

Several factors provided an excuse for nervous investors to take equity risk off the table it seems – a weak US jobs report, the

looming second quarter corporate reporting season and the prospect of a dull market during the summer months. The lack of confidence in the current rally is illustrated by the increasing reliance within the investment community on ‘technical analysis’ (following stock price chart patterns), which provoked some commentators in early July to forecast further significant declines in major stock markets. There is nothing wrong with technical analysis (indeed, it is a tool we regularly use at Ashburton), but when the consensus market view among previously ‘fundamental’ investors is all of a sudden based on a spurious chart pattern (in this case the ‘head and shoulders top’) it is often advantageous to move in the opposite direction.

“We believe the Asian region will benefit disproportionately from low global interest rates and the economic rebound that is taking shape, as well as offering high domestic growth potential in China and India.”

Accordingly, we increased equity weightings for our [Multi Asset Funds](#) during the weakness in late June and early July. At 45%, the equity weighting in our Asset Management funds is the highest it has been for several years. As in recent months, we continue to favour Asian markets, which including Japan account for roughly 50% of our equity exposure currently. The remaining exposure is split evenly between Europe and the US. We believe the Asian region will benefit disproportionately from low global interest rates and the economic rebound that is taking shape, as well as offering high domestic growth potential in China and India.

While we are confident that GDP growth in Asia will outpace that in the developed world, the risk to our current equity allocation concerns valuations and what they say about relative profits growth expectations. Following their impressive rally, emerging markets are now trading at a valuation premium to developed markets. This no doubt reflects a consensus expectation that growth in emerging market profits will outpace western profits, in spite of the productivity gains and cost-

21 July 2009

cutting so evident among US corporations in particular, many of which will benefit from exposure to Asia anyway. Our current regional allocation reflects a belief that the trend of Asia-ex Japan equity out-performance will continue, but we must recognise that the scope for out-performance is not as great as it was at the start of the year. Should the valuation gap between developed and emerging markets widen materially we will have to revisit our regional equity strategy.

Away from equities, we also see a number of attractive opportunities in the bond market. We maintain significant weightings in long-dated German bunds and 20-year US TIPS (inflation-linked treasuries) and we have recently added a position in Australian bonds. Despite the country's relative economic resilience, we believe the interest rate hikes priced into the Australian bond market are excessive and therefore view today's yields as highly attractive. We continue to hold a variety of investment grade corporate bonds (7% weighting) and supranational bonds (issued by the likes of the World Bank, Inter-American Development Bank or European Investment Bank). Following weakness in May and early June, we added a position in US 10-year treasuries although we closed out the position earlier this month for a gain of over 4%.

We believe the bonds highlighted above to be fundamentally attractive in their own right, but they also offer diversification qualities given increased equity weightings across our multi-asset funds.

“We also see a number of attractive opportunities in the bond market...they also offer diversification qualities given increased equity weightings across our Multi Asset Funds.”

Currency strategy has changed only moderately over the past several weeks. Of the four majors, sterling is our preferred currency, followed by the US dollar ahead of the euro or yen. While the dollar may well weaken during periods of renewed risk appetite, we are sceptical of many of the bear stories regarding the dollar's long-term decline against the other majors.

To summarise, the highest level of G7 unemployment for a generation indicates that the world economy remains depressed. However, in forward-looking financial markets what matters is how events turn out relative to what was previously expected. As we have argued all year, the dramatic collapse in risk assets experienced in 2008 scarred investors and led to a collective state of excessive pessimism despite evidence that policymakers were launching the most aggressive policy response in history.

It is clear from the performance of Asian markets that concerns over Chinese growth are fading. But we continue to believe investors largely underestimate the potential for a broader global economic recovery. The rapid reversal of June's stock market weakness may be the first sign that

21 July 2009

some trenchant bears are capitulating. It is very plausible that more will follow. This view underpins our positive stance towards equities and other risk assets, although we emphasise also our continued search for cheap, uncorrelated assets as a source of diversified returns.

ENDS

Ashburton (Jersey) Limited and Ashburton Fund Managers are regulated by the Jersey Financial Services Commission. Ashburton Global Funds is a Protected Cell Company and a recognised fund in the UK under Article 270 of the Financial Services and Markets Act 2000. The prospectus of the fund can be viewed at RMB Asset Management International Limited, 2 London Bridge, London, SE1 9RA. The value of Investments and the income from them can go down as well as up, and you may not recover the amount of your original investment. Past performance is not necessarily a guide to future performance. Where investments involve exposure to a currency other than that in which the fund is denominated, changes in rates of exchange may cause the value of the investments to go up or down. The United Kingdom Financial Services Compensation Scheme does not apply for investors in the fund. Nevertheless, in certain circumstances, the Collective Investment Funds (Recognised Funds) (Compensation for Investors)(Jersey)Regulations 1988 (as amended) may provide compensation for investors.

Ashburton (Jersey) Limited has its registered office at 17 Hilary Street, St Helier, Jersey JE4 8SJ. Ashburton (Jersey) Limited is registered as a Foreign Investment Services Provider in South Africa in accordance with Section 8 of the Financial Advisory & Intermediary Services Act 2002.