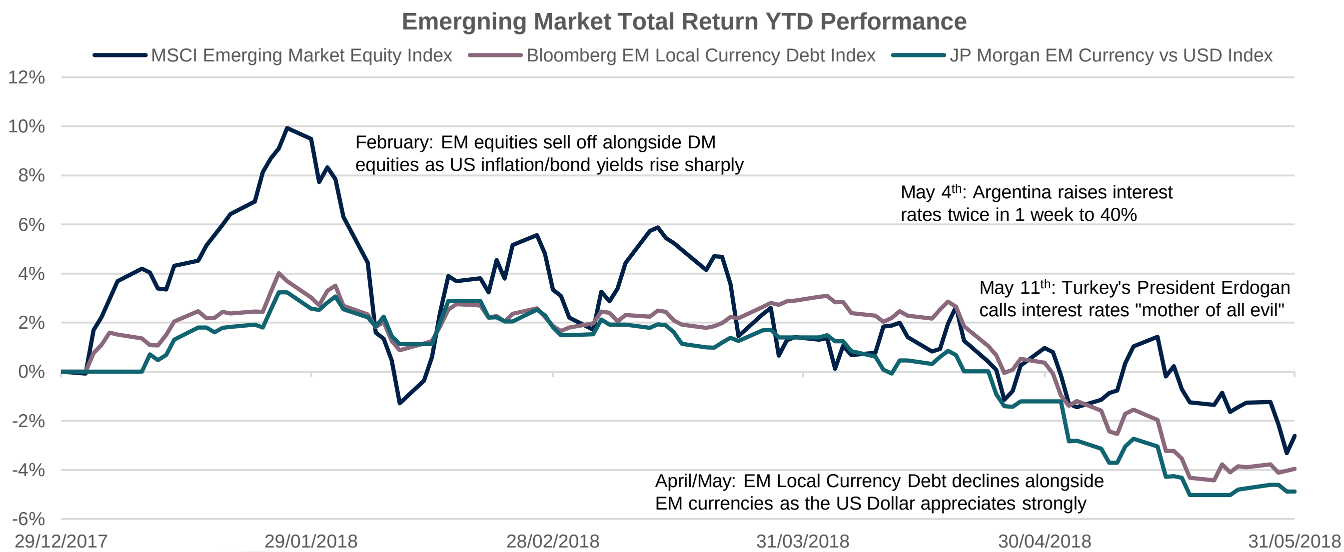
SIGNIA TALKING POINTS

May 2018

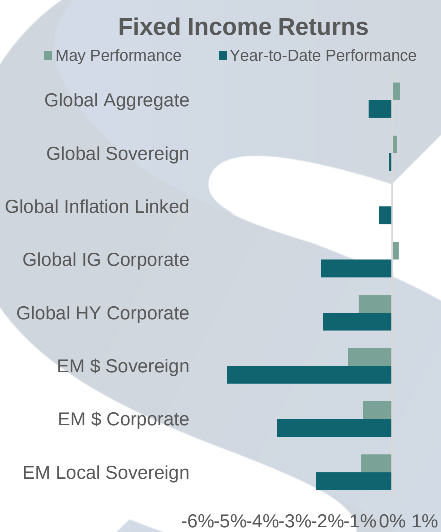
Emerging Markets: Sell in May and go away… but don't go far!

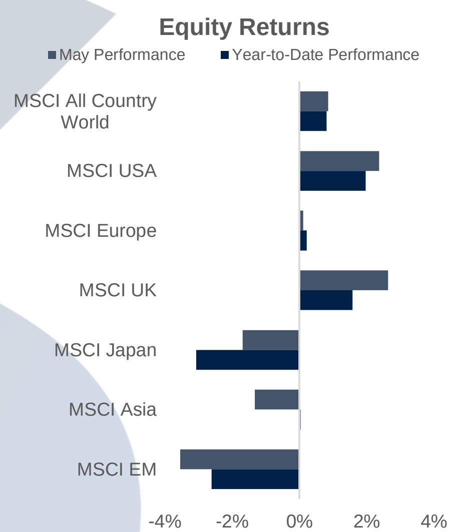
In 2017, we had the strongest year for many emerging market (EM) assets since 2009, and one of the strongest starts on record in January this year for EM equities. 2018 has subsequently seen a dramatic turnaround for the asset class that has surprised most market participants. The tipping point was early February, when a strong US inflation indicator caused bond yields to rise too far too fast for equity markets to stomach, causing large equity market declines, led by developed markets. EM local bonds and EM currency returns, however, suffered lower drawdowns and held their positive returns until April, when a combination of weak European economic data and idiosyncratic issues in Argentina and Turkey helped spur a resurgent US Dollar.

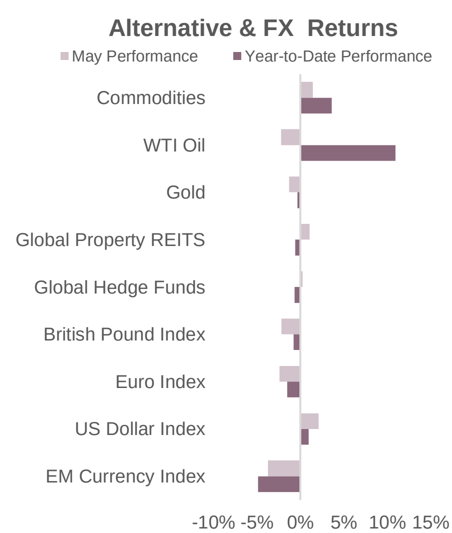
In Argentina, the central bank is battling to tame hyperinflation with consumer prices still rising by 23% per annum, and in Turkey, political leaders have turned their backs on financial markets amidst increasing authoritarianism. Both countries have seen their currencies free fall as investors and businesses withdraw their capital. Whilst these EM episodes are concerning, they remain a minority within the broader EM environment, which continues to grow at 5% GDP clip, or twice the pace of advanced economies.



Source: Bloomberg







Global Agg: Bloomberg Global Aggregate TR Hedged GBP; Global Sovereign: Bloomberg Global Treasury TR Hedged GBP; Global IL: Bloomberg World Govt Inflation Linked Bonds 1-10Y TR Hedged GBP; Global IG: Bloomberg Global Corporate TR Hedged GBP; Global HY: Bloomberg Global High Yield TR Hedged GBP; EM$ Sov: Bloomberg Emerging Markets Sovereigns TR Hedged GBP; EM% Corp: Bloomberg EM USD Corporate 10% Cap Hedged GBP; EM Local Sov: Bloomberg EM Local Currency Govt TR Unhedged GBP; Equities: MSCI indices reflect net total returns in local currency, except Asia and EM in USD; Commodities: Bloomberg Commodity TR Index; Global Property REITS: FTSE EPRA/NAREIT Global Index; Global Hedge Fund: HFRX Global Hedge Fund Index; British Pound: Bloomberg British Pound Index; Euro: Bloomberg Euro Index; US Dollar: Bloomberg US Dollar Index; EM Currency: JP Morgan Emerging Market Currency Index. Source: Bloomberg. Data as at 31/05/2018.

Fixed Income

- Emerging Markets suffered the most this month, especially EM local debt as EM FX currencies were hurt due to the strengthening US dollar. Despite continued strong fundamentals, there was some over-reaction as investors 'sold first and asked questions later'
- Global sovereign bonds also suffered as US treasury yields spiked at over 3% due to inflation fears and news in Italy of the formation of a Eurosceptic government had a contagion effect on core and peripheral yields, with the latter spiking in a more pronounced manner
- Corporate bond spreads widened due to global risk events and strong new issuance, with European financial corporates hit particularly hard due to events in Italy

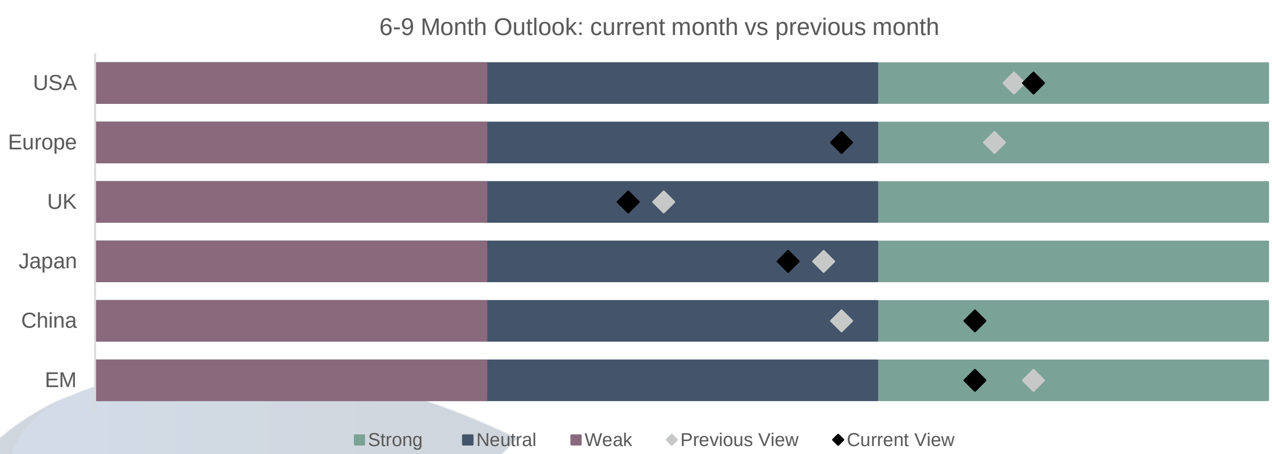
Equities

- US equities posted a strong month, as robust economic data outweighed trade barrier concerns
- European markets achieved modest positive returns, with Italian politics unsettling investor sentiment
- UK equities were the best performer for the second month running, with further weakness in Sterling buoying the main market
- Emerging markets were again the worst performer, the result of a continued US Dollar strength

Alternatives & FX

- The broad commodity index moved modestly higher on the month as Industrial metals rallied on further US tariff announcements
- Despite a broad rise in commodities, oil prices fell on the news that OPEC may increase production
- In a risk-off month for currencies, the Yen and US dollar rallied against most major currencies. The Brazilian Real and Mexican Peso were amongst the worst performers as trucker strikes led to a slowdown in Brazilian activity and the US announced traffic measures on steel and aluminium trade with Mexico

Signia Macroeconomic Outlook



Source: Signia Wealth. **Data as at 31/05/2018**

- USA: Tailwinds from tax cuts, expansionary fiscal policy and regulatory easing are supporting consumer and business sentiment and this has extended the second longest US economic expansion in history (108 months), now in the latter stages of its cycle but still running strong. Rising trade war tensions with key trading partners is a notable risk but currently poses a minimal economic threat.
- Europe: Economic and earnings recoveries are earlier in their cycles but have lost momentum recently from several key headwinds, namely a less accommodative European Central Bank, rising concerns of a trade war with the USA, harsh weather conditions and a late winter this year across the northern nations, and populist uprisings across the southern nations.
- UK: Real wage growth is now positive as employee earnings growth accelerates to the highest since 2015 and pressures from high consumer price inflation ease. However, risks remain balanced as existential Brexit uncertainty with the European Union continues to weigh on corporate sentiment and business investment.
- Japan: The Bank of Japan remains committed to stimulating consumer price inflation which is picking up from a low base and supported by a tight and growing labour market. Prime Minister Abe's ratings have suffered considerably by a prolonged political scandal.
- China: Curbing pollution levels is an environmental positive but comes at an economic cost by slowing industrial output growth at a time when the corporate sector is deleveraging and economic growth is slowing. The Chinese central bank has a new governor who is trying to stimulate the economy by spurring credit growth.
- Emerging Markets: Strong economic growth is being tested by a strengthening US dollar and isolated political risks in Turkey and Argentina, but buoyant commodity prices and synchronous global economic growth continue to offer a boost to the broader EM complex.

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