SARANAC
PARTNERS

Investment Committee Update

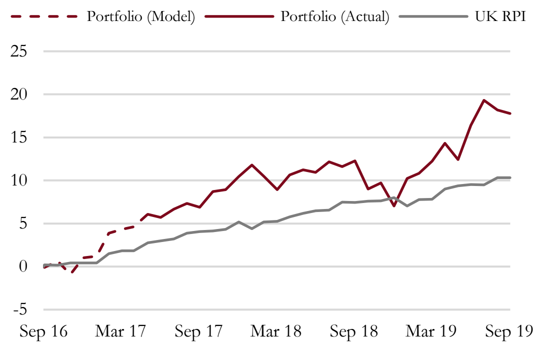
October 2019

AT A GLANCE

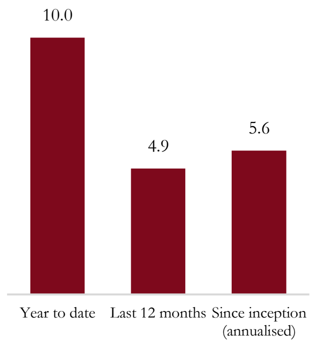
- Our view of the global economy is little changed this month as economic and market data continues to be consistent with recent trends.
- Therefore, we have made no changes to portfolios at the aggregate level.
- We believe we are in the late stages of the cycle, where equity markets should modestly outperform other asset classes, but where risks to the downside are as great as opportunities for upside.
- Macro momentum continues to slow and there are few signs of any response to easing in monetary policy.
- Furthermore, ongoing geopolitical uncertainty is capping potential upside and growth.
- Therefore, we maintain our overall portfolio positioning with equity allocations of around 35% supported by a put option strategy to protect against potential market falls.
- Last month we reduced our risk exposure in the fixed income component of the portfolio, reducing our allocation to high yield markets and emerging market debt.
- We continue to hold a significant allocation to alternatives, including gold, which has performed strongly since the start of the year and adds significant diversification within portfolios.

Multi-asset strategy (sterling moderate risk)

Performance (%)



Periodic returns (%)



Monthly returns (%)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
2016									0.1	0.7	-1.6	1.9	1.0
2017	0.2	2.6	0.4	0.3	1.4	-0.4	0.9	0.6	0.4	1.7	0.2	1.4	9.4
2018	1.2	-1.2	-1.4	1.6	0.6	-0.3	1.1	-0.5	0.6	-2.9	0.6	-2.4	-3.1
2019	3.0	0.5	1.3	1.9	-1.7	3.5	2.5	-1.0	-0.3				10.0

Source: Saranac Partners.
Performance figures from inception (31 December 2016) are based on model portfolios, simulated from a full record of trading decisions and execution levels are readily available for review. Dividends have been included on an accruals basis. All performance is shown exclusive of fees.

MARKET PERSPECTIVES

Our view on markets is little changed this month as economic and market data has been consistent with recent trends. Our central view is that the economy has entered the late stages of the cycle.

Zeitgeist: the long-term context

We continue to believe the economy is in the late stages of the cycle – a period in which equity markets should modestly outperform other asset classes, but where the risks to the downside are as great as opportunities for upside. We believe that an environment of weak growth and further policy response (both monetary and fiscal) is the most likely scenario in the near term.

Macro drivers: medium-term environment

Macro momentum continues to slow and there a few signs of any response to monetary easing.

In particular, Europe continues to struggle with a weak manufacturing sector and there is little evidence of a recovery in growth in China. The US continues to outperform other regions but is also slowing.

However, while manufacturing activity remains weak there has been little evidence of spill-over into the broader economy. Non-manufacturing sectors, employment data and consumer spending continue to be more resilient.

Geopolitics remains a headwind for the global economy and the numerous political hotspots are capping potential upside to markets and constraining overall growth.

We see the resolution of geopolitical tensions, especially trade, as a possible catalyst for improved momentum in the economy and the equity market.

Signals: short-term indicators

We continue to be biased towards more positive market scenarios, which are consistent with indicators from our proprietary Global Growth Matrix. However, we do recognise that macro momentum is slowing and there is a reasonable risk of a market correction. Conversely, resolution of any of the pervading political issues may trigger an improvement in outlook.

In aggregate and as a broad indicator, our risk appetite lies between 3 and 4 on a scale from 1 to 10. Therefore, we are cautious on the near-term outlook, but not outright bearish.

ASSET ALLOCATION

Our asset allocation is unchanged this month. For a moderate risk portfolio, we hold around 40% in fixed income, 35% in equities and 25% in alternative assets (gold and hedge funds).

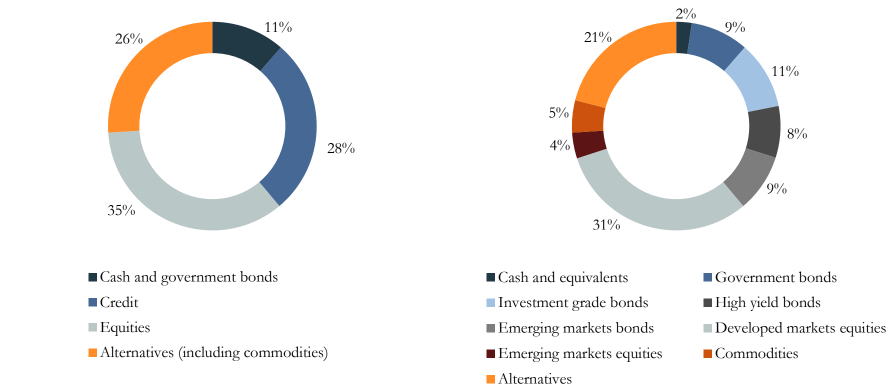
These allocations exclude the option strategy, which protects about half the equity exposure, significantly reducing risk. Furthermore, the allocation to alternative assets is unusually high due to the late stage of the cycle and ultra-low yield environment.

EQUITIES

We continue to maintain our core equity allocation this month, with a 35% allocation to equity markets and protection of approximately half the equity exposure.

Recent investment flows have shown an extreme shift from equities to bonds. While this would usually lead to a fall in equity prices, significant share repurchase programmes have supported prices.

Multi-asset strategy (sterling moderate risk)



Source: Saranac Partners.

Growth equities have been outperforming value equities
1 January 2018 = 0%

Source: Saranac Partners, MSCI.

We have also reviewed relative valuations in both the equity and bond markets. While equity valuations continue to be at the more expensive end of their past range, we believe they continue to offer better value than bonds.

The US market is more expensive than other regions but we believe this reflects the far stronger earnings growth the US has generated throughout this cycle, as well as higher margins and stronger returns.

Equity markets experienced an extreme rotation over the past month, out of momentum and growth stocks, which have enjoyed a strong period of outperformance, and into the unloved value sectors.

This move coincided with the recent rise in bond yields from their past lows, which supported the performance of financial stocks (a key component of the value sector).

While we do not see this as the start of a sustained period of outperformance for value stocks, it may signal a more balanced market going forward after the recent outperformance of momentum stocks.

In an economic environment in which growth is scarce, we believe stocks able to demonstrate strong underlying growth, as well as cash flow generation, will continue to outperform the market.

FIXED INCOME

Our analysis of market valuations suggests credit markets are fairly valued when considering the incremental spread they offer over government bonds. Spreads have tightened modestly in recent months and are in the middle of their historic range.

Credit spreads have proved reliable indicators of economic stress in the past and we take comfort from the fact that these spreads have been notably stable.

Government bond yields have risen from their historic lows over the summer but are still at very low levels driven by negative interest rates in Europe and Japan, low inflation and weak growth.

We see scope for some further increases in yields but given the subdued outlook for economic growth, we believe government bond yields are not far from fair value.

Bond markets expect further interest rate cuts from the US Federal Reserve this year (one cut) and next (two cuts) and further easing from both the ECB and the Bank of England over the next six to 12 months.

We have maintained our fixed income positions this month, following our de-risking of fixed income portfolios in August.

ALTERNATIVES

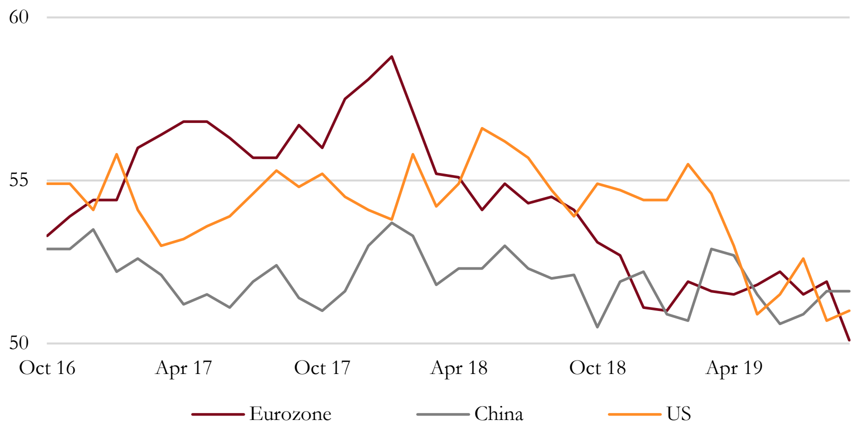
Portfolios currently have around a 20% allocation to alternatives and a further 5% allocation to gold. We continue to monitor gold prices and look for an opportunity to execute a call option strategy to participate in any further gold price rise. As yet there has not been a suitable entry point for the trade.

CURRENCIES

We do not have particularly strong views on currencies at the moment, although we are closely following the volatility seen in sterling as it responds to developments in the Brexit process. In August we implemented an option strategy for sterling portfolios, which protects against a sharp rise in sterling. Given the rising probability of an extension to the Brexit timeline, we are looking into extending this protection further out into 2020.

Taking the global economy's pulse

The purchasing managers' index (PMI) is an economic indicator derived from monthly surveys sent to supply chain managers within private companies across 19 industries. The results provide an insight into sales, employment, inventory and pricing. It is considered a leading indicator because it reacts to consumer demand and therefore gives an early indication of an economy's health.



Source: Saranac Partners, MSCI.

16 St James's Street
London SW1A 1ER
+44 (0)20 7509 5700