



ASSET ALLOCATION STRATEGY

MARKET ANALYSIS AND PRINCIPAL INVESTMENT THEMES

OCTOBER 2018

AN UPBEAT
ENVIRONMENT
BUT RISKS ARE
BEING
OVERLOOKED

► Last month, we tactically reduced portfolio asset risk by returning to neutral on equity markets. For the moment, we are maintaining this stance. Global economic momentum is still very favourable in spite of a few concerns over China's slow down.



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Donald Trump's stimulus plan offers enough visibility on US economic momentum up to mid-2019, Europe's economic slowdown is still under control and China is focusing once again on traditional targeted lending stimulus to improve short term prospects at the expense of long term growth. But there are number of weak spots that suggest we should be more cautious than the environment would seem to warrant:

► **global liquidity** has not yet stopped contracting. The Fed's balance sheet has been shrinking at a faster rate since October 1st and the ECB will finalise plans to wind up quantitative easing at the end of 2018. Estimating the impact of these moves is extremely tricky but it can only be potentially negative insofar as quantitative easing proved such a stimulus for markets.

► **Italy's budget talks** are only just starting. Italian bond valuations are already largely discounting a number of risks but we cannot rule out further volatility.

► **Brexit talks** will be ramped up in the coming weeks. For several months, markets have been unruffled over the uncertain future of US-European Union relations. Rather remarkably, sterling has been less volatile against the euro in recent months than the Swedish kroner or the Swiss franc; the opposite is usually true. But the UK's political situation has become so complicated that we cannot be sure Theresa May has the leeway to find an acceptable compromise with the EU that her own party and parliament will then be able to approve. It is highly likely that Brexit will be a stronger source of market disruption in coming weeks.

► **the oil price** has perhaps risen a little too fast. The increase is a token of Middle Eastern tensions which are unlikely to abate in the near term but it could end up triggering concerns as it generally weighs on global growth and can also have unexpected consequences.



KEY POINTS

Neutral exposure
to market risk

Still underweight bonds

Since the beginning of the year, bond markets have overall witnessed an increase in interest rates and a widening in spreads. Bonds are slightly more attractive than they were but for the moment we remain underweight.



NEXT HEADLINE EVENTS

Next ECB meeting: October 25

Decision on Italy's debt by Standard & Poor's: October 26

Next BoJ meeting: October 30 & 31

Next Fed meeting: December 18 & 19

	OUR CONVICTIONS FOR OCTOBER*	CHANGES COMPARED TO THE PREVIOUS MONTH
EQUITIES	=	→
US	=	→
Europe	=	→
Euro	=	→
United Kingdom	=	→
Japan	=	→
Emerging countries	=/-	→
FIXED INCOME	-	→
US	=	→
Euro	-	→
Investment Grade	-	→
High Yield	=	→
Money market	=/+	→
DIVERSIFICATION		
Convertible bonds	=	→
Dollar	=	→

*Range of investment committee ratings on the asset class/geographical zone (from -/- to +/+). Source: Edmond de Rothschild Asset Management (France). Ratings at 05/10/2018.

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