

# Thesis

# Asset Allocation

March 2011

Welcome to our new style of email bulletins. As a valued professional connection of Thesis we will be providing you with regular emails like this, with information on markets and products. We hope you will find them a valuable source of information.

## This Month

- A cautious start to 2011
- Fixed interest
- Equities
- Alternative assets

## A cautious start to 2011

The first month of 2011 saw the rally in developed markets pause for breath as events in the Middle East, and inflation concerns led to profit taking in Emerging Markets and bonds.

Returns in overseas investments were diluted by virtue of a stronger pound whilst, in terms of alternative assets, falls in gold and infrastructure were offset by rises in our hedge fund investments and (in our lower risk models) commercial property.

FTSE UK All-Share	-0.6%
USA S&P 500	+2.2%
FTSE World Europe - ex UK £	+0.3%
Japan Nikkei 225	+0.1%
FTSE All-World Asia Pacific ex Japan £	-3.7%
FTSE All-World All Emerging - £	-6.0%
FTSE Gilts All-Stocks index	-2.0%
Corp Bonds - Markit IBOXX STG Corporates	-0.9%

The net effect was a modest underperformance, the three key influences last month being our underweight gilts positions (positive) and overweight positions in emerging markets and gold (negative).

See the sections below to review the short term drivers and strategic changes to our models.

## Fixed interest

Bond prices are now discounting a 100bp rise in interest rates by the year end, with 25bp in May. But any deterioration in economic data before then and - with arch hawk Andrew Sentance due to leave the MPC after the May meeting - then a no change position is still possible.

## Equities

The US weighting in all the models has been increased following the continuing flow of positive corporate and economic data from America. This will be funded by a reduction in the emerging markets weighting. Whilst we remain positive on the earnings outlook for emerging markets medium term (and are maintaining an, albeit reduced, overweight position), it is likely that, in the short term, general risk aversion means the momentum will remain in the developed markets.

In Japan we are maintaining weightings but now investing only in funds where the currency risk is hedged out. With the yen up 7% against sterling since December, local interest rates still close to zero and on/off deflation projections then this helps to counterbalance the more attractive outlook for equities.

## Alternative assets

We have suspended new purchases of gold with a view to gaining exposure to agricultural commodities. The precise timing will depend on the relative attractions of the two asset classes and ongoing political and inflation developments. We decided that buying into direct commodities was not a satisfactory option as managed commodity funds have inconsistent track records, ETF returns did not match actual commodity prices because of futures being in contango and structured products incorporate issuer risk.

We considered the best route would therefore be via a specialist fund investing in global equities whose earnings are significantly sensitive to soft commodities. This provides exposure to the theme but without the high volatility of the commodities themselves, although obviously with greater sensitivity to equity markets.

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