

Private
Bank

Market Perspectives

July 2019





Foreword

As we turn to the second half of 2019, all economic data points to an extended late cycle with any recession a distant threat. Although volatility is likely to remain relatively high this year, we take a look at the benefits of being invested, compared to trying to time the market.

Back in April, we thought that there were signs of inflation coming in higher than was being priced by the market. While inflation might still surprise to the upside, especially if trade tensions escalate, risks have faded. So we have removed our inflation investment theme.

There was a surge in bonds offering negative yields last month, after the US Federal Reserve signaled that more rate cuts were on the cards. With investors looking for ways to enhance returns, emerging markets bonds may be part of the answer. That said, selection will be key.

With interest rates low and geopolitical tensions to the fore, private equity may have a role to play in globally-diversified, multi-asset portfolios. The asset class has little correlation with bonds and commodities, offering diversification benefits.

The bounce seen in global equities in June was a welcome relief after May's sell-off. Focusing on equities with a quality bias still looks like the best approach, despite the high valuations. And with equities unlikely to climb much more over the rest of 2019, active strategies are preferable to passive ones.

Yours

A handwritten signature in black ink, appearing to read 'JCG', written over a horizontal line.

Jean-Christophe Gerard
Head of Investments Private Bank and
Interim Head of Private Bank EMEA



Contents

- 4 Revisiting our investment themes
- 5 Time to be selective in equities
- 6 Time in, not timing, the market counts
- 8 After the rally, focus on carry
- 10 Rates likely to be range-bound after the rally
- 12 Getting to grips with private equity
- 14 Multi-asset portfolio allocation

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Revisiting our investment themes

As we turn to the second half of the year, we see fewer catalysts for inflation to surprise to the upside.

In April, we defined our four investment themes for the next few months: 1) Investing in a late cycle; 2) Enhancing total return with carry and yield; 3) Inflation surprise risks; and 4) Tactical opportunities. The latest data and market developments reinforce our confidence in all our investment themes, except for inflation surprise risks, which we close today.

All data points to an extended late cycle

The data confirms that we are late cycle, but at the same time we do not see a recession on the horizon. Manufacturing data have been slowing globally and trade tensions threaten to deepen the issue. That said, European manufacturing seems to have reached a trough while US data weakness is payback for strong inventory built up in the six months to March.

“We do not see a recession on the horizon.”

The typical imbalances that end an economic cycle (corporate and/or household debt, housing market overheating or banking sector instability) are not yet observable and central banks turned ever more dovish in June. For this reason, we continue to recommend a quality bias in equities, despite high valuations, and recommend active strategies over passive ones. In fixed income, we think that emerging markets sovereign bonds offer attractive prospects at this stage of the cycle.

Inflation surprises less likely

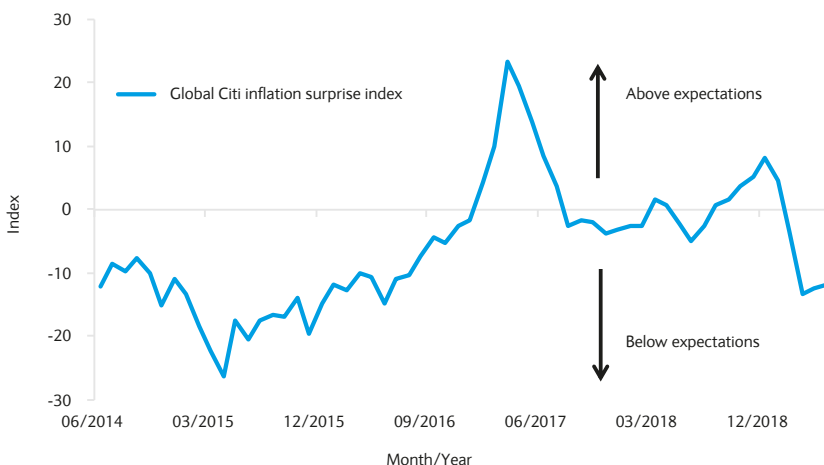
Back in April, we thought that some indicators pointed towards risks of higher inflation. Extremely tight labour markets in a few major countries, risks of unanticipated higher commodity

prices and flaring trade tensions were all risks that could have impacted inflation more than the market had priced. However, inflation figures continue to disappoint.

“We do not see the inflation investment theme as compelling at this stage.”

The global Citi inflation surprise index (see chart), which compares actual releases to expectations, continues to be negative. Central banks in the US, Europe and Japan are struggling to get inflation back to their target. Wage growth remains muted, trade tensions are easing and oil prices are off their highs. While inflation might still surprise to the upside, especially if trade tensions escalate, risks have faded. So we do not see the inflation investment theme as compelling at this stage.

Inflation continues to disappoint



Source: Bloomberg

Yield enhancement and tactical opportunities still relevant

We continue to seek strategies to enhance total return with yields and carry. The volatility increases seen across asset classes since April, which is typical of a late-cycle environment, provides opportunities to collect carry by selling volatility or getting higher coupons from products.

We favour dividend growers with strong free cash flow. In addition, the spike in volatility in the last three months provided tactical opportunities across asset classes. We will continue to look for those.



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Time to be selective in equities

After a strong first half for equities, valuations may struggle to climb much over the rest of 2019, so being selective in allocating to equities will be crucial.

Improving trade tensions and a dovish turn from the US Federal Reserve (Fed) and the European Central Bank (ECB) bolstered risk assets in June, notably equities, after the market weakness seen in May. So where next for equities in the second half of 2019?

Top of the range

The S&P 500 Index is trading around the 2900 level. However, last month we argued that the S&P was likely to trade in a range of between 2700 to 2900 and end the year between 2900-3000. So we advise being selective when investing in equities and not relying on indices to deliver much more return.

“We advise being selective when investing in equities.”

While the upside in broad developed market indices is likely limited from here, we continue to see opportunities. For this reason, we advocate active management over passive, as single-stock selection is going to be necessary to achieve high returns from current equity market levels.

The risk of a melt-up

The conjunction of a dovish Fed and ECB, a trade agreement between the US and China and a rebound in manufacturing activity, would trigger another leg-up in equities.

While lower yields would likely push valuation multiples higher, improved fundamental data could generate positive earnings momentum. Furthermore, earnings expectations, notably in the US, are cautious and upward revisions could help equity markets to rise further.

However, the scenario above is not our base case. The ebb and flow of risks is unlikely to vanish soon and equities could fluctuate accordingly.

Preference for US equities and emerging markets

From a regional perspective, we continue to have a preference for US equities and emerging markets (EM). A more dovish Fed, coupled with a more conciliatory tone between large regions on global trade, could help EM to perform well over the rest of the year.

The outlook is more challenging for European equities. Financials, the largest sector across the European benchmark, is struggling with low interest rates and the recent easing bias from the ECB will likely worsen the situation.

Favoured sectors

We prefer consumer discretionary, healthcare and communication services. Those sectors offer structural growth, a much sought-after characteristic in a low-growth environment. Consumer discretionary benefits from a healthy household sector on the back of a historically low unemployment rate. Communication services benefit from the growing trend in digitalisation and online services. Meanwhile, healthcare offers structural growth due partly to an ageing population, with a defensive bias.

“The ebb and flow of risks is unlikely to vanish soon and equities could fluctuate accordingly.”



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Time in, not timing, the market counts

In a period of escalating trade tensions, recession fears and elevated volatility levels, it is all too easy to forget the power of long-term investing.

Fighting cautious instincts

The longest period of economic expansion on record, coupled with surging geopolitical anxiety, has clients questioning if this cycle is coming to an end. Indeed, it has encouraged some to hold off investing in risk assets, or reduce exposure, and hold a significant proportion of their portfolio in cash.

In order to preserve the long-term purchasing power of their wealth, investors need to generate a return that is equal to or preferably higher than inflation. To meet that requirement, historically low interest rates have forced many to put money in higher-risk strategies rather than cash deposits.

Moving up the risk curve unnerves some clients in the short term, especially during challenging periods such as last year: equities, fixed income and cash all generated negative real returns in many markets in 2018. Out of the major asset classes, global equities were punished the most, posting their weakest performance since the financial crisis. This rather shocked investors who may have become complacent after years of positive real returns and low levels of volatility.

Equities have rebounded this year. But, a persistent wave of negative headlines continues to disturb markets. The flaring up of trade tensions in May and the consequent US\$2tn fall in equity values was a reminder of how quickly

stock markets can move over a short period of time. Against the backdrop of rising volatility and macro concerns, it is not surprising clients have been cautious about if and when to increase their exposure to risk assets.

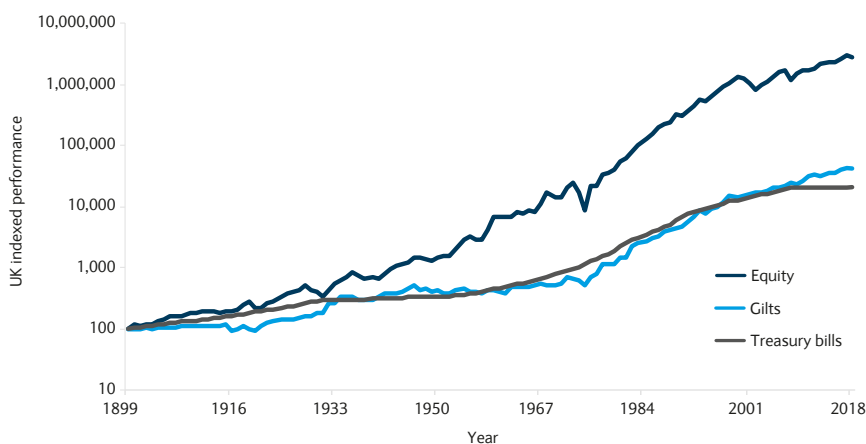
When to invest?

History shows that identifying the perfect point to buy an investment is a difficult, if not impossible, game to play.

For long-term equity investors, the most effective entry point has generally been when headlines are the darkest and markets are weak and cheap. However, emotionally this can often be a difficult decision to make. Many investors invest when headlines are positive and equities are expensive. This means investors are vulnerable to buying high and selling low.

“Investors are vulnerable to buying high and selling low.”

Equities outperform over the long term



Source: Barclays Equity Gilt Study, April 2019

What to invest in?

After appreciating the need to invest, the next hurdles to overcome are where to put your money to work and over what time horizon. The Barclays Equity Gilt Study 2019 shows the nominal performance of £100 invested in cash, bonds or equities between 1899 and 2018 (see chart).

The Barclays' study shows that £100 invested in cash in 1899 would be worth just over £20,000 today. If invested in gilts, the same £100 would be worth close to £42,000. However, £100 invested in equities in 1899 would now be worth around £2.7m. While the data provides compelling evidence of equities' outperformance over 118 years, most of us have far shorter investment horizons.

Time is on your side

Many market participants spend much energy trying to gauge the direction of stock markets in the short term. That effort would be better spent by considering the probability of outperformance across the major asset classes over a range of time periods.

Again we can turn to the Barclays Equity Gilt Study for the answer. UK equities outperformed cash for two consecutive years in 81 out of the 118 periods studied. So, while the probability of equities beating cash over two years in a row is 69%, extend the holding period to 10 years and your chances of beating cash rise to 91%. The corresponding equity outperformance comparison versus bonds is 68% over two years and 77% over ten.

Understanding the long-term risk/reward profile of different asset classes should help investors make a more informed choice. Getting invested and staying invested through a balanced, globally diversified portfolio with a large weighting to equities has consistently given clients a much better chance of preserving and growing their wealth throughout different cycles. Time in the market is far more important than timing the market.

“Extend the period to 10 years and your chances of [equities] beating cash rise to 91%.”

UK equity performance statistics since 1899

	Number of consecutive years				
	2	3	4	5	10
Outperform cash	81	83	85	87	100
Underperform cash	37	34	31	28	10
Total number of years	118	117	116	115	110
Probability of equity outperformance	69%	71%	73%	76%	91%
Outperform bonds	80	87	87	83	85
Underperform bonds	38	30	29	32	25
Total number of years	118	117	116	115	110
Probability of equity outperformance	68%	74%	75%	72%	77%

Source: Barclays Equity Gilts Survey, April 2019



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After the rally, focus on carry

With increasingly dovish central banks and investors chasing yield opportunities, emerging markets bonds remain an option for global investors.

After the recent bond rally, yields in the developed markets are trading at depressed levels. Investors continue to look for alternatives and emerging markets offer enhanced yields. Volatility will likely increase due to global growth concerns, therefore selection will be key, but emerging markets bonds still offer an attractive risk-reward.

“Emerging markets bonds still offer an attractive risk-reward.”

Attractive yield opportunities

We highlighted in our previous publications that emerging markets bonds offer attractive yields on an absolute and relative basis, relative to investment grade or high yield sectors in developed markets.

Historically, accommodative central bank policy has supported flows into emerging markets bonds, which has supported bond prices. Meanwhile, central banks, like the US Federal Reserve Bank (Fed) or European Central Bank (ECB), paved the way for looser monetary policy in June. This has led to another wave of flows into emerging markets in the search for enhanced yields.

Not only emerging markets debt, but US and European high yield bonds have also delivered exceptional returns this year. We still believe that emerging markets bonds are preferable to high

yield alternatives, although selection in both markets is key.

In the following sections we compare key aspects between emerging markets and high yield debt.

Default risk

Default rates for US high yield and emerging markets bonds are at historical lows. Emerging markets corporate default rates (12-month trailing) of 1.4% in 2018 were significantly lower than the historical average of 2.8%. In the US, high yield default rates are also at depressed levels, at 2.8%, while European default rates for speculative corporates were 1.3% by end of last year.

“Default rates for both US high yield and emerging markets bonds are at historical lows.”

Given that more challenging market and economic conditions lie ahead, it is likely that default risk will increase from the current depressed levels globally. That said, supportive financial conditions and moderate growth should limit the risk of a sudden spike in both markets.

In the developed world, defaults among high yield bonds will likely occur with issuers who maintain a high operating leverage. Naturally, these can be found among smaller-sized issuers as opposed to established blue chip heavyweights.

Different dynamics

Historically, the dynamics of default rates within emerging markets differ from the developed markets. Default rates in these segments were usually clustered in certain regions or countries, coinciding with times when they were in distress. During 2001-2002 for example, Argentina accounted for nearly 40% of emerging markets corporate defaults. In 2015-2016, the sharp decline in commodity prices saw a surge in default rates in Latin America, specifically in Brazil, which was hit by recession and bribery scandals. In the same period, default rates in Asia-Pacific continued to decline.

It is important to note that, while the proportion of non-financial corporate investment grade issuers in emerging markets stood at around 20% 20 years ago, today investment grade issuers make up roughly 50%. The improved credit quality should be taken into account when comparing US high yield and emerging markets over the long term.

Cyclicality

While both high yield and emerging markets are prone to downturns, the dynamics are different.

Given the very high integration in the global value chain, Asian issuers are highly exposed to global growth and vulnerable to any global slowdown. Unsurprisingly, this makes the region most vulnerable to the ongoing trade tensions.

Meanwhile, oil and commodity exporting countries are dependent on the commodity cycle. While supply-driven commodity price weakness may be looked through by investors, given the more temporary nature, demand driven weakness will have a more sustained effect on fiscal balances. The oil price volatility may lead to some pressure for oil producers like Brazil, Russia and the Gulf states, most notably Oman.

Overall, however, we believe that countries like Brazil and India, for example, should be able to cope well, even in a situation where either growth or commodity prices decline.

In the developed world we believe that companies with high operating leverage and cyclical exposure can be vulnerable in a period of declining operating profit. In this environment interest coverage can drop sharply, putting coupon payments and redemption at risk.

Additionally, US oil producers which have a comparable high breakeven cost for oil, will suffer when oil becomes more volatile. In such a scenario, we would favour national energy champions of established emerging markets countries to US high yield energy issuers.

“US oil producers which have a comparable high oil breakeven cost, will suffer when oil becomes more volatile.”

Spread levels

The recent Fed-induced rally led to a substantial tightening of both emerging markets and high yield bond spreads. While the average spread of the Bloomberg Barclays Emerging Market Aggregate Bond Index is just short of 300 basis points (bps), US high yield average spreads are trading at 380 bps.

High yield bonds may seem to offer better value than emerging markets bonds. However, the risks underlying lower quality issuers in the high yield markets reveal themselves in times of economic uncertainty. For example, during the sell-off in late 2018, average spreads of US high yield bonds widened dramatically to 540 bps from 300 bps, while the average spread of emerging markets bonds widened to 350 bps from 280 bps in the same period.

Looking back to the 2015/2016 commodity crisis, the higher beta of US high yield spreads became even clearer: average spreads of emerging markets bonds widened by 160 bps while the average spread of US high yield bonds widened by 440 bps causing significantly higher price volatility.

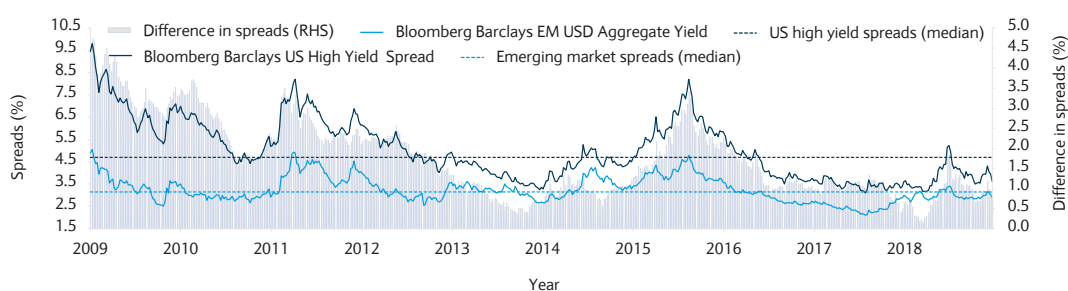
Higher spread volatility

In an environment where spread volatility is likely to increase, we think that emerging markets bond spreads offer better value than high yield spreads. But again, selection will be key.

Although we are not expecting a US recession in the near term, it is worth noting that emerging markets bond spreads traded at their tightest level around 10 months before the last two US recessions. Meanwhile, US high yield bonds saw their tightest levels 18 months before. This suggests a longer period of stable returns is available in emerging markets bonds in a late-cycle environment.

“The risks underlying lower quality issuers in the high yield markets reveal themselves in times of economic uncertainty.”

US HY spreads more volatile than EM spreads





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Rates likely to be range-bound after the rally

Dovish central banks have triggered a global rally in rates. In the short to medium term, rates are likely to stay in the current range, with lower trending inflation expectations will be the focus in the longer term.

A football manager's decisions are often wrong in the eyes of the supporters. And when the team is not successful, the president of the club usually joins in. Sounds all too familiar to Jerome Powell, chair of the US Federal Reserve (Fed) who is facing criticism from some market participants and the US president alike.

Fed signals a move

In its June meeting the Fed has indicated that rate cuts are very likely. Markets quickly priced in a 100% chance of a 25 basis point (bps) rate cut in July which we agree with.

After last month's aggressive moves in the rate markets, it is hard to keep up. Is the yield curve still inverted or flat? Which part of the curve is inverted? How does it compare with other bond markets? The graph below illustrates recent developments in the EUR, GBP and USD sovereign curves.

US yield curve to steepen at short end

While the US sovereign curve was already flat at the beginning of the year, the market started to price in several rate cuts which has led to an inversion in the six month to the 2 and 3-year part of the curve. This has led to a slight steepening between the 10 and 2-year section of the curve. It is likely that the overall curve will soon start to steepen slightly for two reasons.

Firstly, lower Fed policy rates will resolve the inversion at the short end of the curve while rates in the longer end only have limited downside potential, at least in the medium term. Secondly, the overbought situation in the US long end of the bond market makes rates vulnerable to some retracement. In the long term, rates will closely watch the lower trending inflation expectations. This could keep yields at lower levels for some time.

The economic data does not clearly point to a recession in the short term, which would be needed to warrant another leg down in the long end of the curve. A neutral positioning is justified in our view.

“Markets quickly priced in a 100% chance of a 25 basis point rate cut in July.”

European yields to stay low for longer

In Europe, the central bank's more dovish policy language last month indicates that yields will stay low for longer amid a weaker growth outlook for the region, trade uncertainties and lower trending inflation expectations.

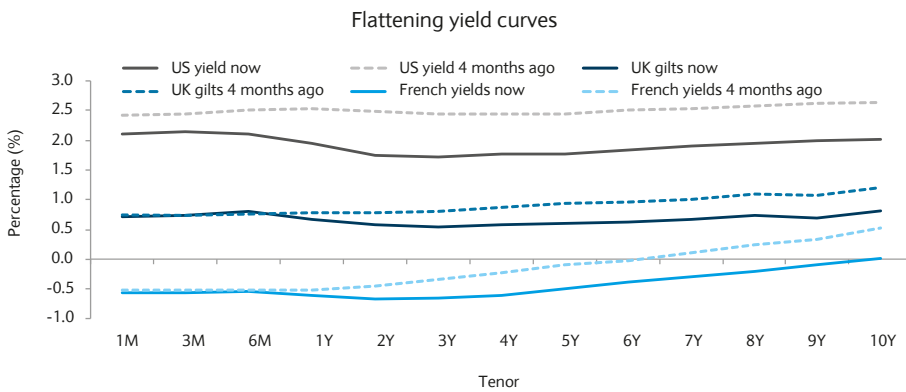
Unsurprisingly, longer tenors started to price in the policy shift, leading to a flattening of the curve, while the longer end (illustrated by the French sovereign curve) is still relatively steep. Given the potential effects of the trade tensions to Europe's core economies, Italian political uncertainty and weaker inflation expectations, a further flattening seems likely, suggesting deeper negative yields at the long end.

Higher UK interest rates look unlikely

The Bank of England (BOE) still tries to put the case forward that gradual rate hikes are likely once Brexit is resolved, justifying this with the excess demand in the UK economy. We expect the market to price out any possibility of rate hikes very soon. The economic data does not seem to support the BOE's ambition. Meanwhile, increased Brexit uncertainty will result in further pressure on the UK economy.

Investment grade bonds of longer duration offer a moderate carry and enhanced yield while providing a hedge should the UK economy deteriorate.

“Further flattening seems likely, suggesting deeper negative yields at the long end.”



Source: Bloomberg



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Getting to grips with private equity

Investing in private equity assets can help diversify portfolios and provide attractive risk-adjusted returns in a low-yield world. However, picking the type of private equity investment that meets your needs is key.

Private equity: the basics

Private equity (PE) is commonly described as an equity or equity-related investment into a company that is not publicly listed. PE can be accessed by direct investment into private companies or indirectly through fund exposure.

Long-term investment

Since capital flowing into PE funds tends to be committed for several years, PE is considered a long-term asset with typical fund terms of around 10 years. The cash flow cycle of the fund is characterised by negative cash flows (the so-called J-curve) during the investment period (which is usually three to five years) where capital is committed into companies.

“PE is considered a long-term asset with a typical fund terms length of around 10 years.”

Fund managers will seek to add value to the underlying company, via operational improvements, international expansion and mergers or acquisitions over a four to six-year period.

Once the business plans have been executed, the company will be exited. The exit could be achieved through a listing on the public markets, private sale to larger corporates or even

to other PE funds with different investment criteria. After the exit has been made, the proceeds will be repaid to the investors.

There are several types of PE investments which target different stages of a company lifecycle and also different sizes of company. Venture capital is deployed in the early days of a company from initial idea through to revenue generation. Growth investment targets the next phase, as a company becomes well-established; while buyout investment occurs in more mature firms. Within buyout, companies range from small cap (minimum \$50-\$100m company size) through to mega cap (\$5bn+). This gives investors a wide selection of investment opportunities alongside diversification benefits.

Investment rationale

The fundamental reason to invest into PE is the potential to enhance returns significantly compared to more traditional investments. While PE and equity markets tend to have a high correlation, studies show that over 10 years PE has historically outperformed global equities by 4%. Another positive of PE includes its low correlation to other traditional investments (sovereign bonds, investment grade credit and commodities) which offers important diversification benefits in a multi-asset portfolio.

“PE has historically outperformed global equities by 4%.”

Key risks

Some key risks to consider for PE are an investment in a “blind pool”, where it is not known at the outset which companies the fund will invest in, the length of time capital will be committed before being deployed and the time-span required to generate positive returns for investors, following an initial period of negative returns.

It is for these reasons that we believe these risks can be mitigated through secondary funds, as mentioned in the May issue of “Market Perspectives”. The secondaries market has been growing at a rapid rate of 25% annually since 2010 with \$74bn traded in 2018 and about \$90-120bn expected to be traded within five years offering a wide range of buyers, sellers and assets alike. The market has historically been resilient across economic cycles, with lower return volatility compared to other PE asset classes, such as venture capital and buyouts.

“The secondaries market has been growing at 25% annually since 2010.”

Important factors worth noting with secondary funds are that:

1. They invest in funds after the initial investments are made (around years 4-7), when portfolios are already significantly funded and generating liquidity. Therefore, the element of blind pool investing is less prevalent, as most of the capital has already been called and invested.
2. By entering in at the later stages, the J-curve is likely to be mitigated and so a return on investment would likely happen over a shorter time horizon, as companies are closer to an exit process.
3. Due to the above two points, secondary investments have a lower multiple of invested capital versus investing in a fund from year one. However, the shorter investment holding periods ensure a comparable internal rate of return.

Enhanced risk-adjusted returns

Although the risk involved remains higher compared to more traditional asset classes, due to PE's long-term horizon and illiquidity, PE offers an enhanced risk-return profile which is especially attractive in the current low-rate environment. Recent studies reported that allocating a high percentage of a portfolio to PE generates larger returns than portfolios with minimal allocations.

Specifically, on a 20-year horizon, investors with more than 15% exposure to PE have been rewarded with a median annualised return of 8.1%. This, along with the immediate diversification benefits, provides a strong case for considering secondary investments core to an investor's private market portfolio.

Deciding what suits

Investors should assess carefully what types of PE investments suit them better, based on their liquidity needs, risk profile and expected returns. In general, we recommend exposure to PE via secondary funds to capture the illiquidity and complexity premium available in private markets, while mitigating some of the risks and ensuring high levels of diversification.

“On a 20-year horizon, investors with more than 15% exposure to PE have been rewarded with a median annualised return of 8.1%.”



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Multi-asset portfolio allocation

Barclays Private Bank discusses asset allocation recommendations within the context of a multi-asset class portfolio. Our views elsewhere in the publication are absolute and within the context of each asset class.

Cash and short duration bonds: neutral

Our preference for higher quality, liquid opportunities makes short duration bonds look attractive from a risk-return perspective, especially in the context of an inverted yield curve.

Nonetheless, we maintain a neutral exposure to the asset class, as real interest rates remain negative in most regions.

Fixed income: neutral

We see moderate risk-return opportunities in fixed income, given the recent spread tightening and late-cycle dynamics. Sovereign rates are less attractive in the context of a low yield environment and we see the higher-quality segment of corporate credits as a better alternative, given their relative safety and additional yield.

We remain cautious on the riskier parts of corporate debt, as high yield spreads look unappealing for the level of risk taken, at a time when credit events may be on the rise. Emerging markets bonds remain our favourite call to enhance returns at this stage in the cycle, due to their yield pickup.

Developed government bonds: neutral

Developed government bonds worldwide have been losing their appeal as rates edged down amid lower economic growth, inflation and monetary policy expectations. The ongoing trade spat has further depressed yields as investors rotated out of risky assets into the safety of

sovereign bonds. Given this backdrop, we anticipate the asset class to predominantly be a diversifier rather than a major source of returns.

Although US dollar real rates remain at historically low levels, they are still too attractive to ignore, relative to the other developed bond markets.

Given the potential effects of the trade tensions to Europe's core economies, Italian political uncertainty and weaker inflation expectations, European bond markets are likely to see a further flattening, suggesting deeper negative yields at the long end.

The Bank of England (BOE) still tries to suggest that gradual rate hikes are likely once Brexit is resolved, with excess demand in the UK economy. We expect the market to price out any possibility of rate hikes very soon. The economic data does not seem to support the BOE's ambition. Meanwhile, increased Brexit uncertainty will result in further pressure for the UK economy.

Investment grade bonds: neutral

A still benign macro outlook and easing interest rates should be broadly positive for investment grade bonds. Nevertheless, we remain neutral on the asset class, amid mounting concerns over the rising pile of corporate debt.

Although spreads have tightened significantly since the beginning of this year, we believe investment grade bonds will continue to earn some carry and thus outperform low yielding government bonds, specifically in Europe.

High yield bonds: low conviction

While default rates are at historically low levels and corporate fundamentals remain robust, we maintain low conviction to the asset class, as margin pressure typically increases late in the economic cycle.

Following the recent rally in riskier assets, high yield bonds look expensive. Spreads are tight by historical standards, which we do not view as attractive in the context of the credit and liquidity risk taken and the returns available from other asset classes.

Emerging markets bonds: neutral

The US Federal Reserve's (Fed) accommodative stance should continue to provide some relief to the largely dollar-denominated emerging markets (EM) debt market, despite the recent weakness of local currencies.

Although choppy energy prices and the escalation in trade disputes provided a headwind to emerging markets bonds, credit quality hasn't deteriorated and economic momentum remains reasonably positive.

Spreads have tightened since the beginning of the year as investor flows reverted back into EM bonds amid improving sentiment, but they remain wide versus high yield bonds. We favour US dollar emerging markets hard-currency bonds due to their relatively attractive valuations.

Equities: positive

Positioning in growth companies and in particular developed markets is our preference, given our view that in the late cycle alpha (actively selecting equity) outperforms beta (passively following an index).

The recent repricing in emerging markets equities resulting from trade tensions provides what we believe is a short-to-medium term entry point. However, not all emerging markets are created equal, with structural trends in Asia appearing to provide more attractive opportunities than Latin America.

But in the context of a multi-asset portfolio with a long-term investment timeframe, we have a higher conviction in developed market equities and remain neutral on emerging markets equities.

Developed market equities: high conviction

Earnings growth is still expansionary, albeit slowing, with growth forecast to be low-to-mid single digits over the year ahead. Healthy fundamentals continue to underpin the investment case for this asset class, while valuations are not excessively stretched compared to history.

Although investor sentiment has been tested by renewed trade turmoil, less restrictive central banks and fairly constructive macro data from both sides of the Atlantic should support recovery globally and lift the asset class further.

We favour active management and selective stock picking of companies with strong balance sheets, although we are agnostic on the geographical allocation of our equity positions. We focus on businesses with high cash returns on capital, with conservative capital structures and ideally an ability to reinvest cash in future growth at equally high rates of return. The US tends to offer more opportunities to invest in these kind of businesses, meaning that North America remains the largest geographical weighting within the equity allocation.

Emerging markets equities: neutral

While markets have grown increasingly cautious following heightened protectionism fears, emerging markets equities should benefit from attractive valuations and steady economic activity in the region, underpinning expansionary, albeit softening, growth.

We expect fiscal and monetary easing in China to counteract a slowdown in the region and limit downside risk to earnings expectations. Trade tensions still pose a risk but will likely dissipate as economic pragmatism should eventually prevail.

Other assets: negative

Alternative asset classes will continue to provide diversification to our portfolio, but are not expected to be the main drivers of returns. Gold is set to benefit from its status as safe haven in the late cycle, while real estate and alternative trading strategies are underpinned by a weak investment case.

Commodities: neutral

The sole exposure within commodities continues to be our position in gold which we view as complementary to the other risk mitigating assets in the portfolio, especially in light of the low interest rate environment and global trade fears.

We find little attraction in this asset class outside of precious metals and find our risk budget better deployed elsewhere.

Real estate: low conviction

Real estate should provide mild diversification benefits, although the asset class faces structural challenges from the rise of online retailers and weaker economic growth could prove to be a headwind.

Alternative trading strategies: low conviction

We maintain a low conviction in alternatives due to their high expense and a lack of investment opportunities in this space. The limited use of leverage should further cap returns for the asset class.

Nonetheless, the recent spike in volatility caused by renewed trade tensions may lift the asset class, at least in the short term.

Investments can fall as well as rise in value. Your capital or the income generated from your investment may be at risk.

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