Parallel
Investment Management

Quarterly Update – April 2015

Market Backdrop

Despite a generally strong start to the year from global equity markets there was a marked increase in volatility in January as investors digested the success of the left-wing Syriza party in the Greek elections, the Swiss central bank's surprise decision to remove the currency peg to the Euro, and the ECB's long-expected announcement that it intended to launch a significant package of quantitative easing (QE).

The IMF added to the uncertainty by announcing that it was down-grading its forecast for global growth in 2015 despite the expectation of a generally positive impact from lower oil prices. This was further compounded by weak economic data, increasing uncertainty of the timing of any interest rate rise in the US, as well as growing concerns over deflation in the Eurozone.

February witnessed the release of more positive economic data and global equity markets responded accordingly, supported by the news that Greece had brokered a short-term deal with its Eurozone partners, oil prices beginning to show some signs of stability, and a number of central banks cutting interest rates.

However, in the US the rise in job numbers above expectation caused markets to wobble as investors began to assume that interest rates would rise sooner rather than later, although market sentiment was quickly buoyed by reassuring language from the US Federal Reserve.

Despite March being a broadly positive month for equities, the quarter closed as it began with heightened volatility in global markets as a combination of variable economic news and geopolitical concerns dominated the headlines. Improving economic data from the Eurozone was broadly positive for its markets, although this was in contrast to the US which appeared to stutter on the back of inclement weather conditions and a slowdown in corporate earnings as the US dollar continued to strengthen.

Investors took profits from technology stocks after a very strong run, and markets were weighed down by tensions in the Middle East, the increasingly likelihood that Greece would be forced to exit the euro, and the uncertainty over the possible shape of the next UK government after the May general election.

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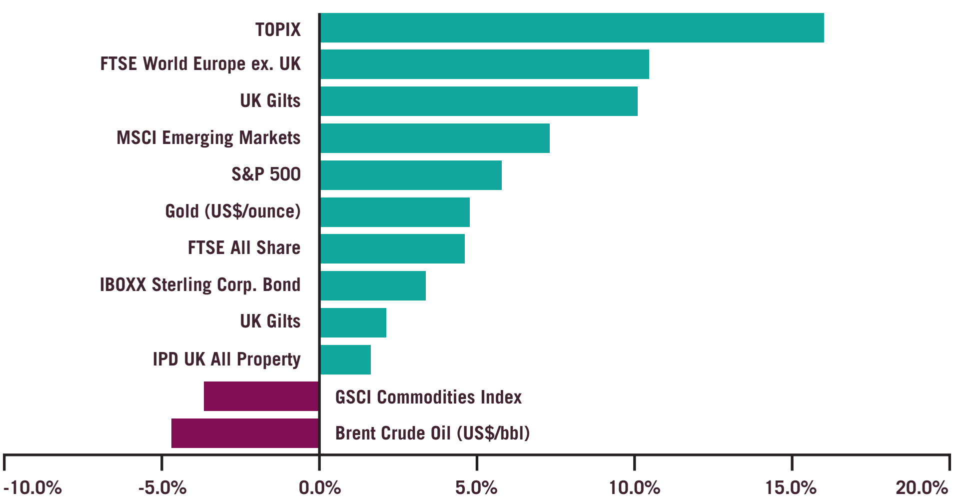
Asset Class Returns – Q1 2015



Data source: FE Analytics – rebased in Pounds Sterling

Equities

UK

UK equities rose over the period although a poor March tarnished the strong returns achieved in the first two months.

Falling inflation (largely reflecting reduced energy costs), positive employment figures, rising weekly earnings, and improving economic data from the manufacturing and service sectors are all indicative of a continuing economic recovery.

The Bank of England is expected to remain largely accommodative with its low interest rate policy, possibly until early 2016, and this should be supportive of UK share prices.

In the short term the uncertain outcome of the forthcoming general election is expected to act as a headwind to the market and we expect frequent bouts of volatility.

US

After a very disappointing start to the year reflecting both economic and geopolitical concerns (with only the strength of the dollar versus sterling offsetting a poor return for a sterling investor), US equity markets rose to record highs in February and ended the period with a net positive return, albeit with heightened volatility.

The deal between Greece and its Eurozone partners over its bailout extension, and carefully crafted comments by Janet Yellen, (the chairwoman of the Federal Reserve Board), that the US central bank was in no hurry to raise borrowing costs created some market momentum.

Despite a decline in retail sales in January and February due to severe weather and a labour dispute in the West Coast ports, both of which have now passed, economic data released continued to indicate an increasingly solid recovery with growth in both the US labour market and consumer confidence.

The rise of the US dollar and the strengthening of the US labour market are beginning to show early signs of impacting upon earnings and this could create a headwind for the broad equity market in the coming months.

Outlook for Equity Regions

Region	View
UK	Neutral
Europe	Neutral
US	Neutral
Japan	Positive
Asia Pacific	Neutral
Emerging Markets	Neutral

Eurozone

European equity markets have enjoyed a strong Q1 generating positive returns in each month as investors reacted favourably to the ECB's Quantitative Easing programme and some signs of an improving economy.

Consumer spending shows signs of strengthening on the back of lower energy prices, a weaker currency and low interest rates.

Data covering retail sales, industrial production and Purchasing Managers Indices (PMIs) were positive for a number of the major economies and, although remaining in negative territory, inflation figures have shown some encouraging signs of improvement.

Although pleasing, growth in the region is unlikely to accelerate rapidly given the relatively high unemployment rate and the prospect of either a Greek default or a messy 'Grexit'.

Although the challenges facing the Eurozone are significant the relative improvement in cyclical stocks (those more sensitive to economic cycles) over defensive stocks is a positive signal.

Japan

Japanese stocks were the top performers of the major equity markets in the period and in February the Topix index reached its highest level since 2007.

Although somewhat erratic and from a low base, domestic macroeconomic data is showing some signs of improvement and there is increasing hope that if the current trend continues Japan will have an opportunity to come out of the deflationary trap where it has been marooned for over 15 years.

Much rests on the ability of prime Minister Abe to introduce structural reform and it is likely that the central bank will need to apply further monetary stimulus before long.

Despite the strong equity market returns achieved over the last year, Japan still offers significant stock specific opportunities as the economy changes to being led by consumer spending and the creation of new businesses and industries aimed at an ageing and declining population.

Asia Pacific

Despite a strong positive quarter for Asian equity markets the flow of the returns was somewhat erratic with February generating a small negative return in sterling terms.

Market gains were driven by a combination of the central banks of some countries easing monetary policies (ie reducing interest rates), ongoing country-specific reforms, as well as improved global investor sentiment stimulated by the ECB's expansion of its asset purchase programme.

On a country-specific level Thailand may struggle to shake off the effects of the recent political turmoil, and energy-exporting countries such as Malaysia and Indonesia are expected to be hurt by the current low oil prices.

However, lower oil prices and the continuation of loose monetary policy should support the recovery in most economies in the region.

Fixed Interest

The positive return achieved in Q1 by both UK sovereign and corporate debt as well as global sovereign bonds masked considerable volatility through the period.

The quarter started strongly as bonds rallied on the back of persistent low global inflation (aided by the decline in oil prices) which put pressure on the ECB to announce a QE programme through a large scale purchase of government bonds.

February saw core government bond yields rise (and capital values fall) following strong US employment data stimulating fears that US interest rates would soon increase, and in the UK there was selling pressure on gilts following the release of positive economic data.

The period ended more positively and, with interest rates expected to remain low (save for in the US), investors' continuing search for yield under the shadow of a plethora of geopolitical risks is expected to continue support for the asset class.

Emerging Markets

In sterling terms the emerging markets sector had a positive quarter outperforming both the US and UK equity markets but the monthly returns varied considerably.

Equity markets as well as currencies displayed heightened volatility, the latter primarily in response to action by the central banks of several countries, including India and Russia, in cutting interest rates.

At the start of the quarter the gains in emerging Asia offset the declines in Latin America, with oil-importing countries generally faring better given the benefits of lower oil prices, although in February both Emerging Europe and Latin America rebounded.

Of the large emerging market countries the economies of both Brazil and Russia are expected to struggle, and although the growth prospects for China look less attractive than those of India, the authorities have the tools at hand to support the economy.

The outlook for the sector is mixed with a country-selective approach most likely to reward investors.

Outlook for Asset Classes

Asset Class	View
Equities	Positive
Fixed Interest	Neutral
Property	Positive
Commodities	Negative
Absolute Return	Positive
Cash	Negative

Alternatives: Commodities/Absolute Return/Property

Commodities have had a tough first quarter with the S&P GSCI Index (a composite of both hard and soft commodities) recording a negative return as oversupply, a stronger dollar and weak crude oil prices weighed on the price of many raw materials.

Much focus is on the prospects for the Chinese economy, the world's largest consumer of industrial metals and the biggest importer of crude oil and with growth slowing the short term outlook for commodities is weak.

The **absolute return** sector posted a positive if unexciting quarter, and with volatility expected to increase as the year progresses the outlook is for continued positive returns.

With 2014 being such a strong year for property it was always likely that 2015 would herald the start of a return to more sustainable growth rates, and Q1 has witnessed positive returns.

The attraction of **property** yields relative to other asset classes remains and, although we expect demand for property to compress yields, confidence and investor interest is beginning to return to prime regional and some secondary markets characterised by a lack of supply.

Portfolio Overview

Performance for the period ending 31st March 2015 (%)

Portfolio	Descriptor	Quarter	1 Year	2 Years	3 Years
Parallel Multi Asset A	Defensive Growth	2.7	5.6	6.4	13.1
Parallel Multi Asset B	Conservative Growth	3.7	8.4	11.1	22.8
Parallel Multi Asset C	Cautious Growth	5.3	10.6	14.0	29.1
Parallel Multi Asset D	Balanced Growth	7.0	12.8	18.1	36.1
Parallel Multi Asset E	Adventurous Growth	7.7	13.1	17.7	36.3
Parallel Multi Asset F	Global Opportunities	7.9	13.6	17.2	34.4
Parallel Multi Asset B Income	Conservative Income	3.3	7.0	7.2	16.5
Parallel Multi Asset D Income	Balanced Income	5.2	10.9	12.7	29.8
Socially Responsible Growth		6.5	10.8	18.8	36.9

Figures quoted net of management fee. Source: FE Analytics

Fund Selection: Contributing Funds

Legg Mason Japan – this was our top performing fund over the quarter aided by positive stock selection and a strong Japanese equity market. The fund returned 17.1%, putting it in the top quartile in the IA Japan sector.

Premier Pan European Property – Pan European real estate securities continued their strong start to the year, with the fund returning 12.9% and placing it in the first quartile of the IA Property sector.

Jupiter European – European equity markets were buoyed by the actions of the ECB, which combined with positive stock selection, helped this fund return 12.6% over the quarter, outperforming the IA European sector and placing it top quartile.

Fund Selection: Detracting Funds

JP Morgan Natural Resources – this fund fell 4.2% over the quarter, primarily as a result of falling oil and commodity prices. We've reduce our exposure to this fund in the absence of any catalysts for a revival in commodity prices in the short term.

Aberdeen Absolute Return Bond – this fund fell 0.8% during the quarter and also underperformed its benchmark. This fund is currently under review.

TwentyFour Monument Bond – although in absolute terms this fund was one of our poorer performing funds, it delivered a modest gain of 0.2% and outperformed its benchmark. However the growing delay in interest rate rises is expected to hamper returns in the short term and so the fund is currently under review.

Portfolio Activity

During the quarter we conducted a number of changes to the portfolios, some of the main changes are:

Increased exposure to active US equities – We acknowledge that very few actively managed collective funds have demonstrated the ability to consistently outperform the US index (S&P 500), but consider that the stock-picking approach of active fund management could benefit the Portfolios through the next phase of the recovery cycle. We have therefore reduced our index tracker fund in favour of more active funds.

Currency hedging – Loose monetary policy together with the divergence in the relative stage of economic recovery between countries has already resulted in a substantial weakening in the value of the Yen and the Euro relative to other primary currencies. We expect this trend to continue and so we have taken the precaution of introducing some hedging to those Portfolios with exposure to Japan and continental Europe.