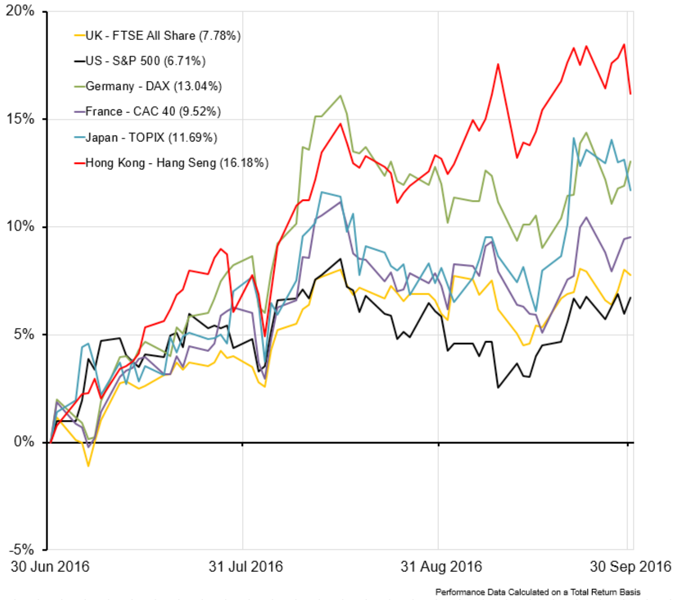
AUTUMN OUTLOOK

REVIEW OF THE PAST QUARTER:

The third quarter of the year saw a great deal of political turbulence which equity markets brushed off in the end. The appointment of Theresa May as the new prime minister and the accompanying changes in the UK government cushioned the effect of the Brexit vote on markets, and the dismal forecasts for the UK economy in the event of an out vote have yet to manifest. Indeed, UK economic indicators showed stable readings in the months following the June referendum, despite the fall in the value of Sterling. However, safe haven bond yields have grinded lower once again, showing there is still concern about the longer term effects of the vote. The Bank of England's decision to cut interest rates to historic lows may have absorbed a potential shock or been unnecessary, we will never know, but it has certainly added impetus to falling yields.

There were surprises elsewhere in the world as well, as Donald Trump won the Republican candidacy for US president. However, the US economy also showed signs of health, making the case for a potential Fed hike later in the year, and the S&P 500 surged to historic highs in the summer months. Meanwhile, the unsuccessful coup attempt in Turkey reminded investors that there is no end to the potential uncertainty, particularly in emerging markets, which have ironically become something of a safe haven for some investors thanks to this quarter's turmoil in the UK and US.



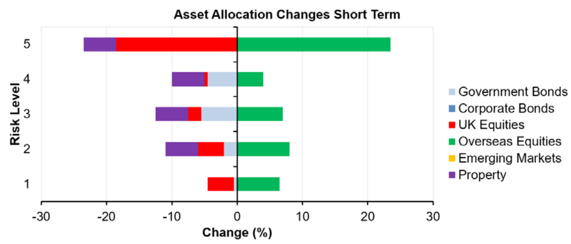
ASSET CLASS RETURNS

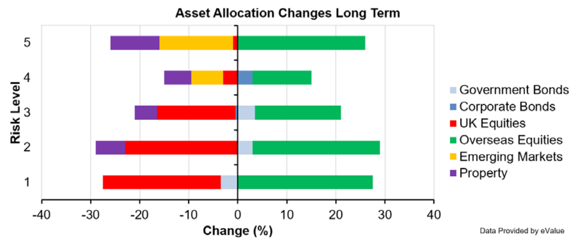
UK	US	Japan	Europe	Emerging Markets	Commodities	Property	Corporate Bond	Gilts	Cash
+7.78%	+6.71%	+11.76%	+10.92%	+12.20%	+0.28%	-2.51%	+7.09%	+2.34%	+0.07%

THE ACTUARIAL VIEW:

The last market outlook was released just days after the UK's vote to leave the European Union. At the time uncertainty was all-pervading, markets were surprised as shares, interest rates and sterling all fell. In truth not much has changed in the intervening three months, there are still too many unknowns to understand the economic impact of an EU exit. Nevertheless, there can be little doubt that Brexit is going to dominate discussions about the economy for some time and because of this it is only prudent to make large changes to asset allocations in order to reflect this.

With large uncertainties surrounding the UK market it makes sense for there to be a radical repositioning of the equity content towards other developed markets. Whereas UK equity previously made up the core of the portfolios this has been replaced by the US, Europe and Japan. Emerging market exposure has been completely removed thanks to a trend down in recent earnings forecasts. Meanwhile the UK property market has been badly hit by Brexit, causing its removal at lower and higher levels, although it still provides diversification at mid-levels. In summary the changes can be seen as a shift towards equity where risk permits.





WHAT TO LOOK FOR IN Q4:

- **Bank of England (BoE) Monetary Policy Committee Meetings:** The next meetings are scheduled for 3 November and 15 December. The BoE decided to cut interest rates to 0.25 per cent in August, along with renewing monetary stimulus with a series of bond-purchase packages. The next MPC meeting will be closely watched as further stimulus measures are possible if the economy shows any signs of lagging behind.
- **Federal Reserve Meetings:** The next meetings are scheduled for 1-2 November and 13-14 December. The Fed's Chair Janet Yellen has hinted that the case for a rate hike later in the year is building, as employment and manufacturing data have gathered momentum.
- **Governing Council of the ECB:** The next meetings will be held on 20 October and 8 December. The latest decision on monetary policy was to hold the overnight interest rate for banks at its current negative levels and extend the quantitative easing programme until next year at least. The ECB will be in a reflective mood, as a number of important policy decisions will come to light in late 2016: the Italian referendum outcome, further scrutiny on the Southern Eurozone members', and the real terms of the Brexit divorce.
- **US Presidential Elections:** The polling day is November 8, with the contest becoming increasingly tighter as campaigns gain momentum, although the Democratic candidate is deemed the more probable winner. The effect on US business and consumer sentiment is difficult to predict, but a Trump victory could hurt emerging markets in particular.

ASSET CLASS SCENARIOS:

UK EQUITY

Most Likely: Actions from the Bank of England this summer has helped to ease fears from the market. As a result, we expect inflationary assets such as UK equities to benefit from this new round of quantitative easing. Nevertheless, political uncertainty around the conditions for a Brexit and the US election should weight on their performance and investors should not be surprised by a temporary spike in volatility.

Worst Case: The market does not like uncertainty and any negative news on the conditions to extricate from the EU may push UK equity markets lower. Investors will also pay a lot of attention to the housing market and consumer sentiment in order to assess their resilience. Bond-proxy stocks might also be impacted by the Fed's decision to increase its base rate.

Best Case: A positive for UK equities could be a further jump in inflation, as a direct result of the decline in sterling. This would give a boost to companies deriving a majority of their revenues from overseas as well as companies with strong pricing power. Few UK domestic names might also benefit from a prolonged rally in value, as investors are desperate to identify the latest pockets of cheap value.

CASH

Most Likely: Rates will remain low if not be lowered further, and inflation may pick up, reducing he appeal of cash. However, with the large amount of political and economic uncertainty in global markets, cash will retain its safe haven appeal.

Worst Case: If a post-Brexit rally in both equity and bond markets continues, supported by loose monetary policy, the relative return on cash will fall. This could be coupled with a spike in inflation as companies pass on the costs of a depreciation in sterling post-Brexit vote.

Best Case: Realistically, the best case for cash is that UK rates remain where they are and that inflation is slow to appear in the consumer prices index as companies see their profit margins decrease rather than raise prices for consumers.

GLOBAL EQUITY

Most Likely: Central bank policy remains supportive of markets, although short-term volatility on the back of political risk and speculation about interest rate rises is likely. If the polls stay neck and neck until the US election in November markets could take fright and sell off.

Worst Case: Rate rises would likely see sell-offs, although we doubt they would be significant falls. A greater risk is political instability: a victory for Donald Trump in the US election or a defeat for Italian Prime Minister Matteo Renzi in the upcoming constitutional vote, could see investors take fright about the prospects for global trade on the one hand and the strength of the European Union on the other.

Best Case: Improving economic data from the US and the Fed keeping rates low would be the best mix for global equity markets, although would arguably be storing up problems for the longer term.

FIXED INCOME

Most Likely: We think it most likely core safe haven bonds remain range bound as growth and inflation data is mediocre. Policy from the Bank of England is likely to remain supportive of bond markets and we expect the Fed to continue to be very cautious in raising rates gradually.

Worst Case: If growth and inflation start to accelerate in the US then yields could fall substantially, even on core safe haven bonds, especially if central banks tighten policy aggressively at the same time. A shift to fiscal policy – cutting taxes and spending more – could potentially shift market attention onto the solvency of sovereign states, pushing bond yields up.

Best Case: If markets retain confidence in the ability of central banks to do further monetary easing, while growth and inflation remain low, we could see limited gains for bond yields, even in the government sector.

EMERGING MARKET EQUITY

Most Likely: The region should be supported by the currencies remaining steady or advancing against the pound, while overall political stability is greater than last year and fundamentals are improving, which should lead to a good period for equity markets.

Worst Case: An aggressive series of rate hikes by the US Federal Reserve could see capital flow back out of the regions. Any political instability or signs of trouble in China due to leverage could exacerbate this.

Best Case: The US keeps rates where they are and investors continue to seek higher-yielding assets in the developing world. Politics remain stable in Brazil and Russia and China's economy hits or beats expectations.

PROPERTY

Most Likely: In the UK, the property market continues its slow recovery, with physical property funds reopening and REITs posting small gains, reflecting the uncertain environment. The depreciation of the pound sterling supports the attractiveness of the asset class to overseas investors. Long term fundamentals remain unchanged.

Worst Case: Volatility rises on the back of poor negotiations between the UK and the EU, dampening investor confidence and stopping all expansion projects and any property developments. The prospect of a recession could see properties further marked down. While this is a problem for domestic investors, overseas investors could take advantage of a further depreciation of the pound sterling.

Best Case: Brexit negotiations starts with the UK in a position of power, improving investor sentiment and lifting property prices up. The BoE maintains low interest rates, keeping the gap with yielding assets such as property wide. This would be exacerbated in the case of rate cut.