Market Insights – Global Monthly Outlook

Global government bonds are expected to benefit from limited inflation risk

July 2016 (covering June 2016)

Index	June	YTD
MSCI World	USD -1.1%	1.0%
S&P 500	USD 0.3%	3.8%
MSCI Europe	EUR -4.2%	-6.7%
MSCI Asia Pac ex Japan	USD 2.2%	2.5%
Hong Kong Hang Seng	HKD 1.4%	-2.4%
Shanghai Composite (A-shares)	CNY 0.4%	-17.2%
Hang Seng China Enterprises (H-shares)	HKD 3.6%	-6.4%
Topix	JPY -9.6%	-18.5%

Source: Thomson Reuters Datastream, total returns in local currency unless otherwise stated. Data as at 30 June 2016. YTD refers to year-to-date.

Global Outlook

With markets completely wrong-footed by the decision of UK voters on 23 June to leave the European Union (EU), the immediate market reaction was extreme. In a classic risk-off move, equities around the world fell, and bond markets – particularly core government bond markets – went up, with yields for 10-year US Treasuries, German Bunds and UK Gilts experiencing historic lows.

While liquidity conditions may be favourable, global equities are expected to face cyclical and structural challenges. The uncertainty over growth and structural problems may also keep markets somewhat volatile. In terms of regional allocations, our preference continues to be for developed markets over emerging markets.

United States

- In the US, the S&P 500 index fell by 5.3% in the two trading days after the vote as global equity markets felt the impact of the surprise EU Referendum outcome. However, signs that the US Federal Reserve (Fed) might hold off on further tightening monetary conditions in 2016 helped US stock markets to bounce back.
- We continue to be positive on the relative strength of the US economy. Although the US dollar has reversed course since the start of the year as expectations for tightening were scaled back, the US is one of the few countries that has the ability to tighten without undermining growth in its economy.

Europe (including UK)

- In the UK, the Referendum result triggered a shock in sterling, sharp falls in share prices. Across Europe, equities declined in June as investors grappled with political and economic uncertainties following UK voter's decision to leave the EU.
- There are concerns that the positive impact of monetary policy is diminishing. Moreover, structural headwinds surrounding Brexit, as well as the high levels of excess leverage and negative geopolitical developments, are likely to weigh on growth in the region.

Asia Pacific (ex Hong Kong ex China ex Japan)

- Asian equity markets, on the other hand, ended the month generally higher, helped by the Fed's dovish remarks which reduced expectations that US interest rates will rise in the near term.
- Although accommodative policies are starting to feed through to supporting growth, and fiscal steps are being adopted, the economies in Asia will continue to face challenges with leverage and capacity, leading us to remain cautious toward Asia. Further policy efforts are expected if economic conditions require action.

Hong Kong and China (A-shares and H-shares)

- In China, the equity market rose marginally on some evidence of economic stabilisation and improving sentiment.
- Although accommodative policy measures may benefit certain sectors, there are a number of external and domestic challenges that will continue to weigh on growth, such as leverage, capacity and slow external demand. In Hong Kong, the weaknesses in consumer spending and housing demand are unlikely to turn around on a sustainable basis any time soon as mainland China demand weakens.

Japan

- In Japan, investors had remained risk averse ahead of the UK referendum on EU membership, with the unexpected shock outcome leading to another surge in Japan's yen and a drop in the country's equity market.
- The negative interest rates adopted by the central bank may have limited the impact on turning growth and sentiment around at a time various economic indicators are suggesting further economic weakness. Further fiscal measures and the ongoing improvement in corporate governance are some of the positive fundamental developments in Japan.

Fixed Income

- Bond markets provided strong returns through June with data from Merrill Lynch showing the Gilt market delivered its highest monthly return since 1986.
- Global government bonds are expected to continue to benefit from limited inflation risk. Moreover, periods of high volatility could lead to a 'flight to safety' in bonds.

Emerging Markets

- Global emerging equity markets also enjoyed a positive month, with the impact from the EU Referendum outcome having less of an impact on the asset class than anticipated.
- Sentiment towards emerging equity markets was boosted by expectations of easier overall global monetary policy for longer, with the futures market now pricing out any likely US interest rate hike until 2017.

Important information

This document has been prepared only for those persons to whom Invesco has provided it for informational purposes only. This document is not an offering of a financial product and is not intended for and should not be distributed to, or relied upon, by members of the public. Circulation, disclosure, or dissemination of all or any part of this document to any person without the consent of Invesco is prohibited.

This document may contain statements that are not purely historical in nature but are "forward-looking statements," which are based on certain assumptions of future events. Forward-looking statements are based on information available on the date hereof, and Invesco does not assume any duty to update any forward-looking statement. Actual events may differ from those assumed. There can be no assurance that forward-looking statements, including any projected returns, will materialize or that actual market conditions and/or performance results will not be materially different or worse than those presented.

The information in this document has been prepared without taking into account any investor's investment objectives, financial situation or particular needs. Before acting on the information the investor should consider its appropriateness having regard to their investment objectives, financial situation and needs.

You should note that this information:

- may contain references to amounts which are not in local currencies;
- may contain financial information which is not prepared in accordance with the laws or practices of your country of residence;
- may not address risks associated with investment in foreign currency denominated investments; and
- does not address local tax issues.

All material presented is compiled from sources believed to be reliable and current, but accuracy cannot be guaranteed. Investment involves risk. Please review all financial material carefully before investing. The opinions expressed are based on current market conditions and are subject to change without notice. These opinions may differ from those of other Invesco investment professionals.

The distribution and offering of this document in certain jurisdictions may be restricted by law. Persons into whose possession this marketing material may come are required to inform themselves about and to comply with any relevant restrictions. This does not constitute an offer or solicitation by anyone in any jurisdiction in which such an offer is not authorised or to any person to whom it is unlawful to make such an offer or solicitation.