

CIPFA

Meeting the Challenge
of Good Governance

Macro & Economic
Update

London / Manchester

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Allianz 
Global Investors

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Understand. Act.

Agenda

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Setting the
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Setting the scene

Our Clients' Strategic Challenge

5 key conclusions from a UK perspective...

Understand.

1. Financial Repression remains in place globally
2. Global growth low, slow and fragile
3. BREXIT it is !

4. Concerns over Chinese Renminbi overdone
5. The UK has performed OK since GPC but structural flaws persist...

Act.

1. The "Hunt for Income" or capital appreciation are now global challenges
2. As China rebalances, the World will have to create its own growth
3. The UK and Europe face 2-3 years of political and economic uncertainty which might be worse for the EU as Sterling will take the strain for the UK - but a prolonged period of UNCERTAINTY will ensue
4. Only a minor devaluation further expected from here
5. The UK needs to keep reforming to promote investment over consumption

 With Volatility rising, be ACTIVE - Agile Confident Thorough

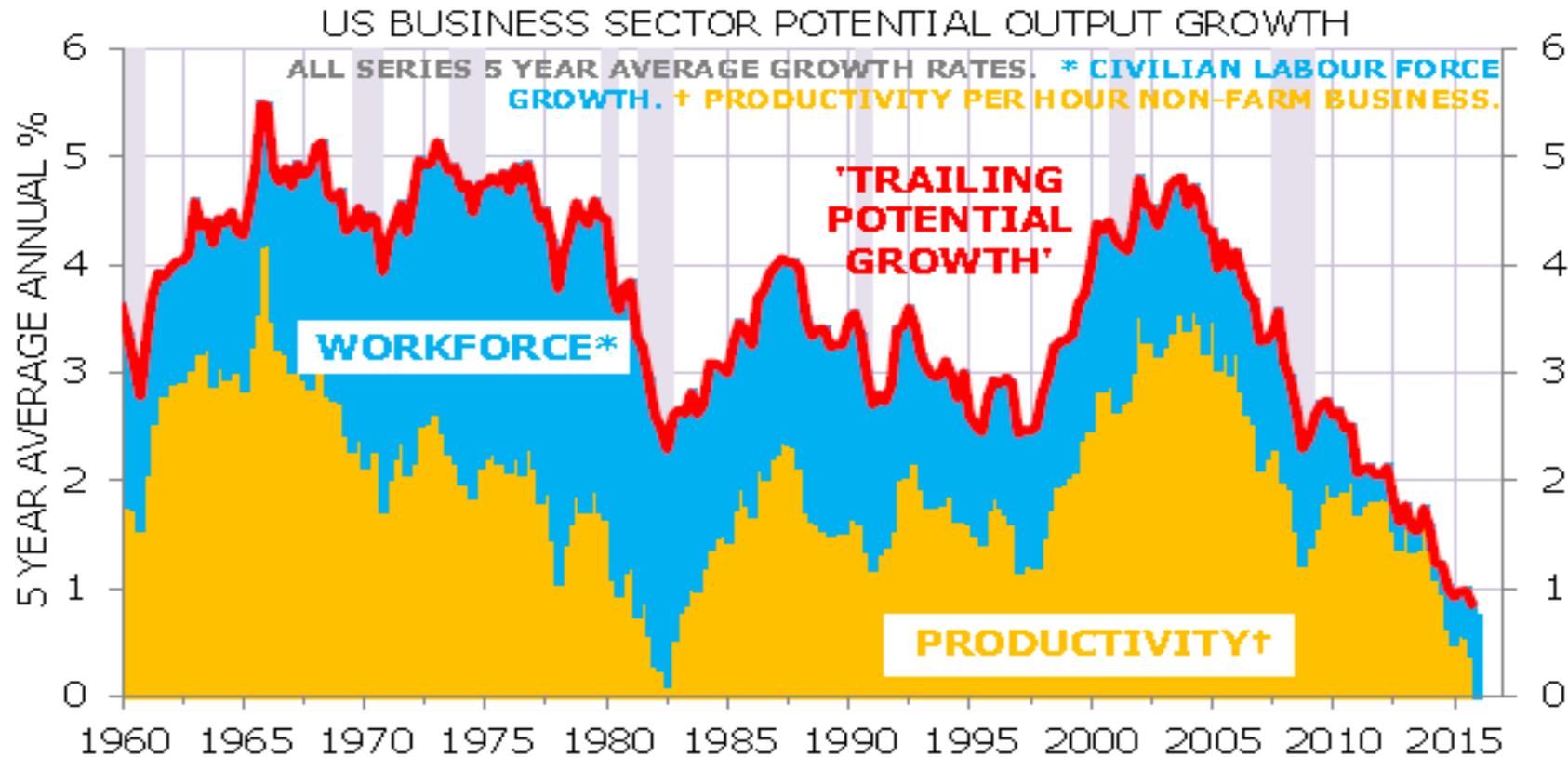
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Key Macro Topics

The Trailing New Normal

- what reversion to the mean or recovery to come ?



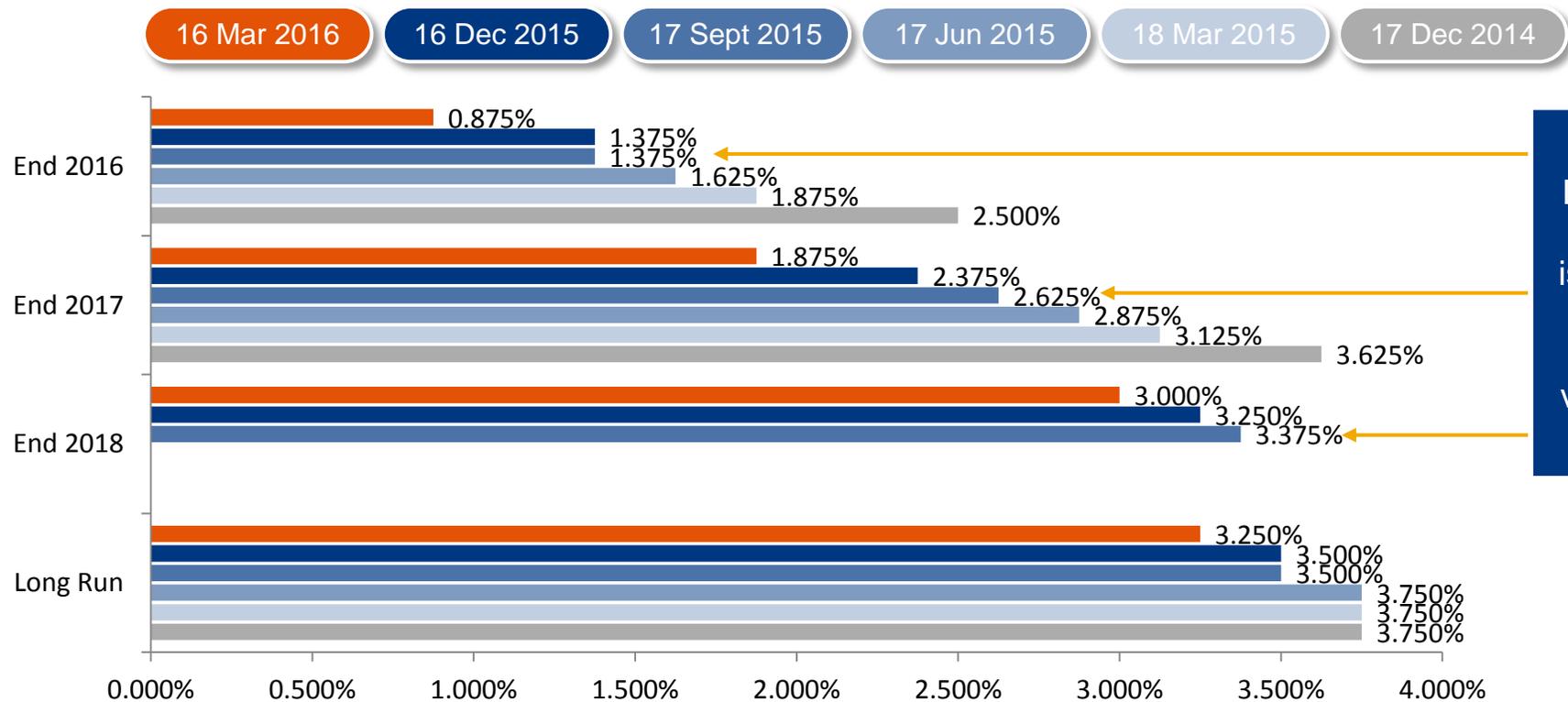
Source: BEA, NBER; Minack Advisors

Data sourced on May 2016

Post the GFC, US potential growth now seems to be

Global Monetary Policy Divergence ...Financial Repression at work

Median Year-end Fed Funds Rate Projection (Per the FOMC “Dots”)



Longer term peak rates is supportive of higher equity valuations...

US policymakers have slashed their interest rate expectations amid continuing inflation disappointments and rising “international” risks...lower for longer

RMB – Not the start of a currency war

CNY Trade Weighted Index – 5 years

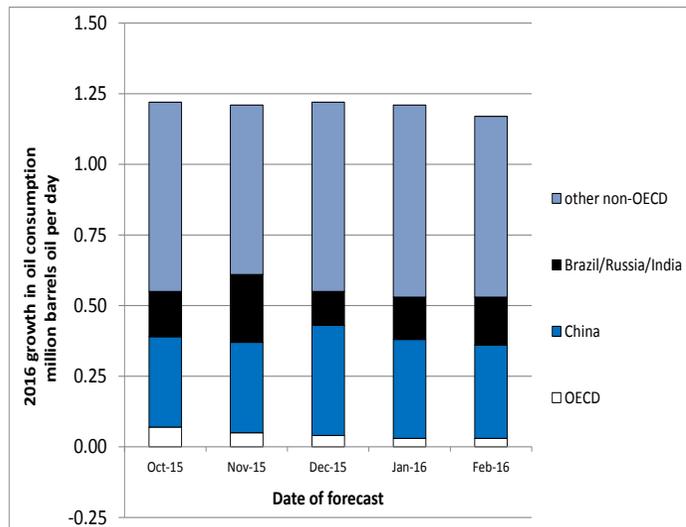


Despite global fears, it is not in China's self-interest to devalue substantially, as it would lessen consumer spending power

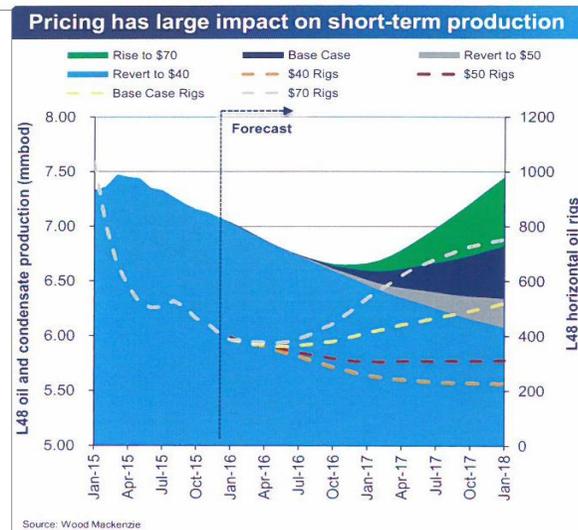
Oil Market

- **1) Oil demand is still growing 1-1.2Mb/d**
- EM demand for oil remains strong, IEA's "missing barrels" suggests **demand is being under-estimated;**
- **2) US shale oil production is in accelerating decline**
- **3) Oil supply/demand crosses over in 2H16, 2017 in deficit by up to 2Mb/d**

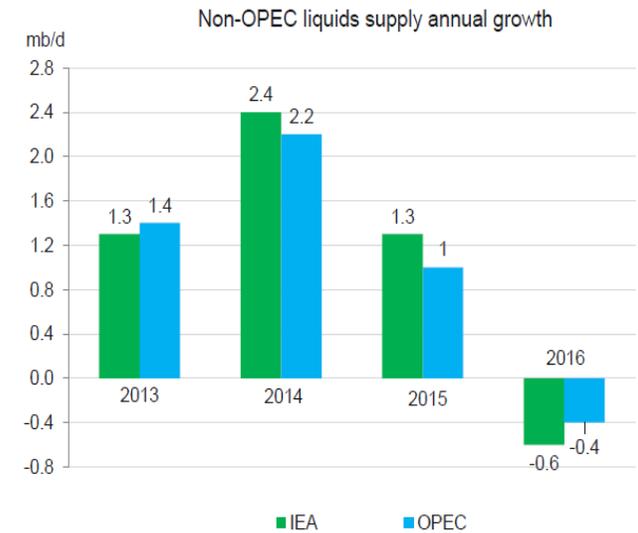
1) IEA 2016 oil demand growth = +1.2Mb/d



2) US shale production forecasts going down



3) Global oil market in balance in 2H16



- OPEC production freeze is precursor to further talks, could see some production curtailed mid-2016. Saudi anticipated an oil price decline as a consequence of their actions, but not this collapse- they need to fix the oil market too

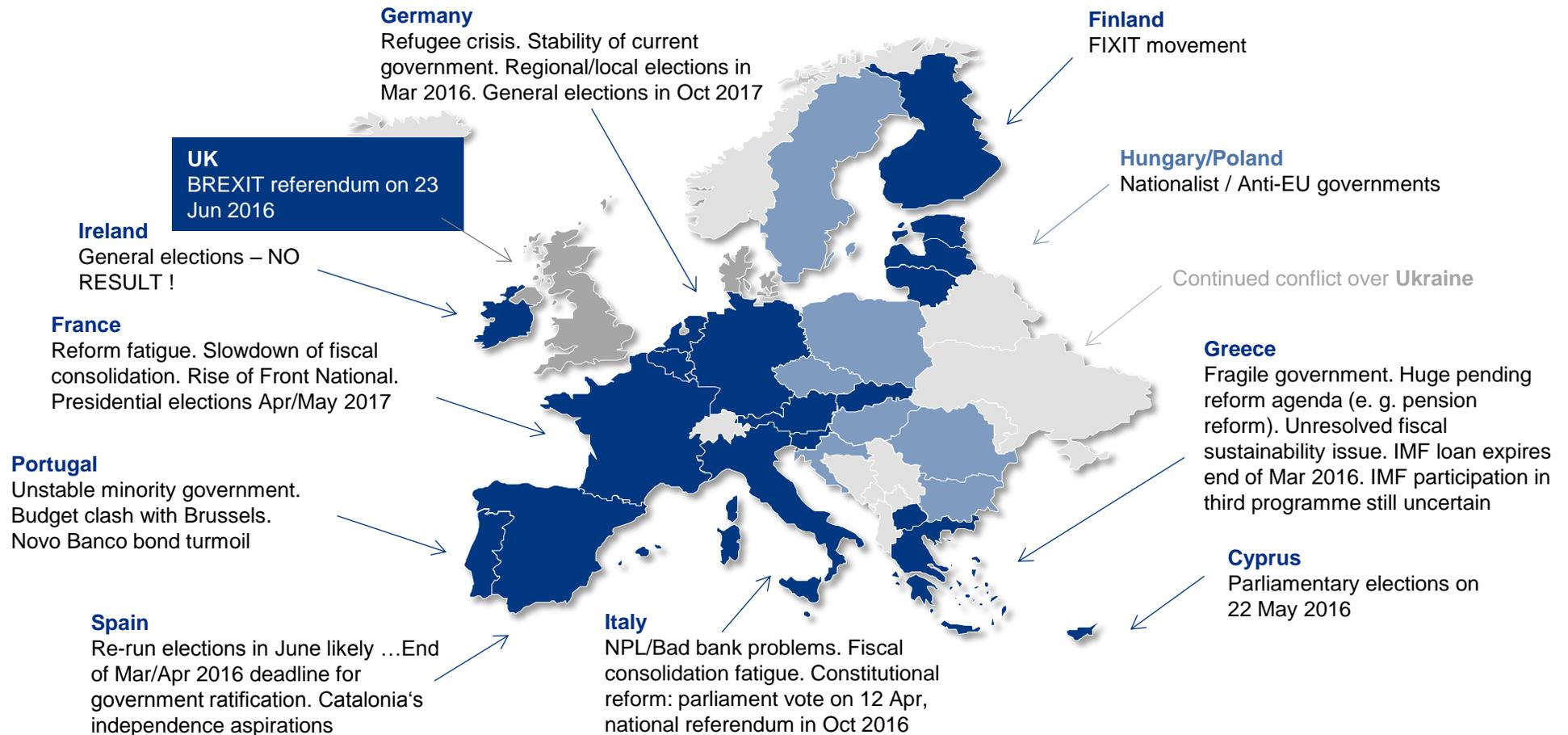
Positioning for the 2016 inflation spike is the DEFENSIVE trade NOT the AGGRESSIVE trade

Europe: not running short of political risks

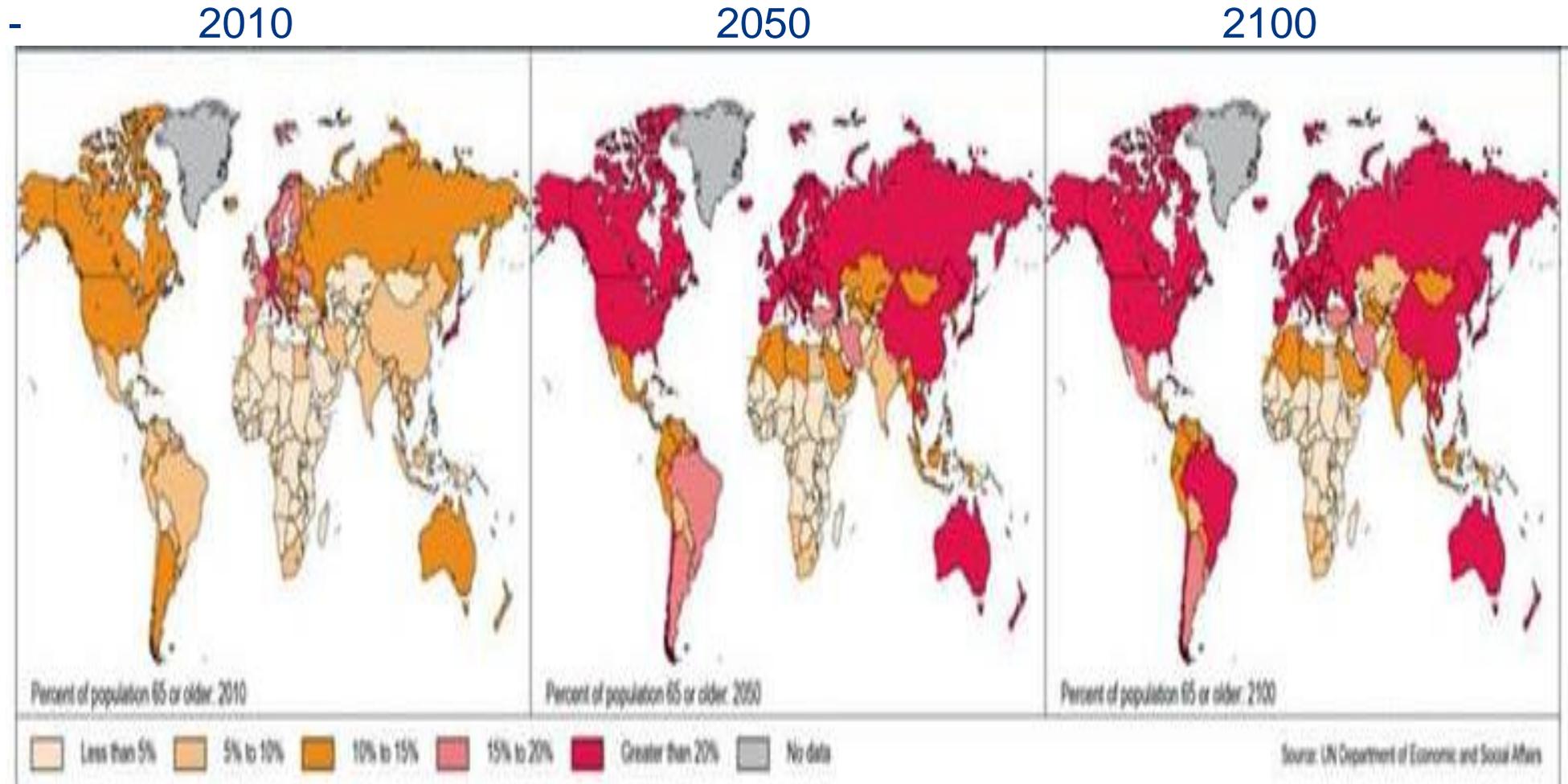
Eurozone

Refugee crisis. Growing centrifugal political forces.
Watering down of SGP/MIP. Incomplete banking union.
EU-wide stress test results in q3 2016.

- EMU member state 
- EU, non-EMU member state 
- EU member state with an opt-out 



Percentage of global population aged 65+



Ageing and longer life expectancy have gone global.....

Navigating the disruption theme

Why is it so hard to anticipate disruption...?

Disruption models

Happens when a new product or service creates a new market, weakens an existing one, transforms it, destroys an existing product, market or industry. It also lowers the cost of capital needed to compete, therefore allowing more competition and innovation.

Exponential technologies

Moore's Law + Kryder's Law + Hendy's Law + Butter's Law of Photonics - all generate exponential rate of improvements, not merely linear ones



Business Model innovation

Generally new entrants who radically challenge the status quo of an industry, such as SaaS or Uber. The "Sharing Economy" may alter capital allocations to Autos, Real estate, Utilities etc in the next 20 years dramatically

Product innovation

Current cars have 2000 moving parts and are expensive to maintain ...Electric Vehicles have only 20 moving parts...and they convert c 90% of electricity to power, whilst petrol only uses 20%...and as for Phones ...

The coming exponential technologies – how will we be affected?

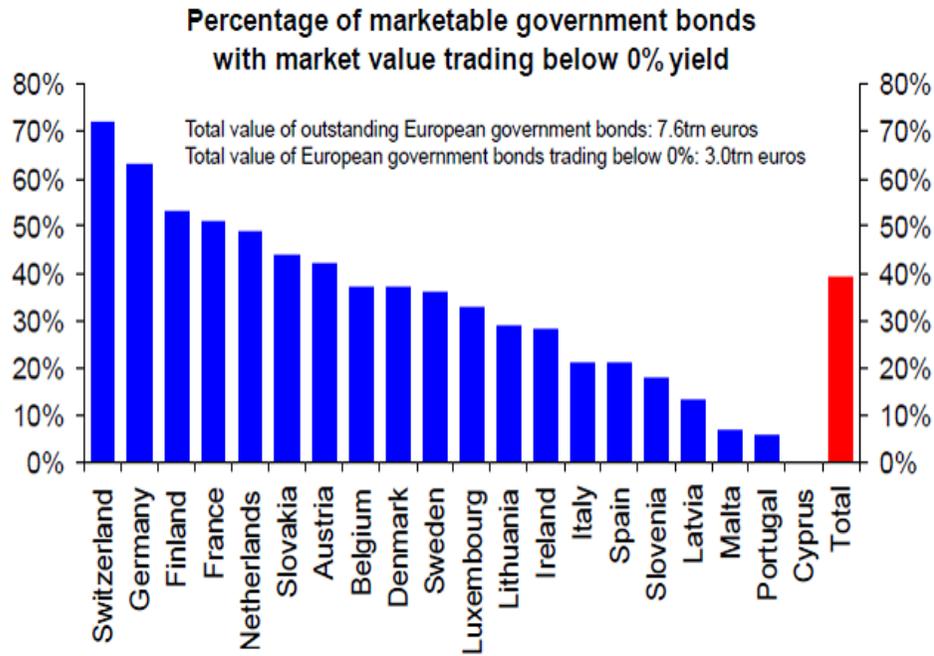
Sensors+Internet of Things/3D Printing/AI/Robotics/SolarPV
Energy Storage/the Cloud/Big data/E-Money + E-Finance



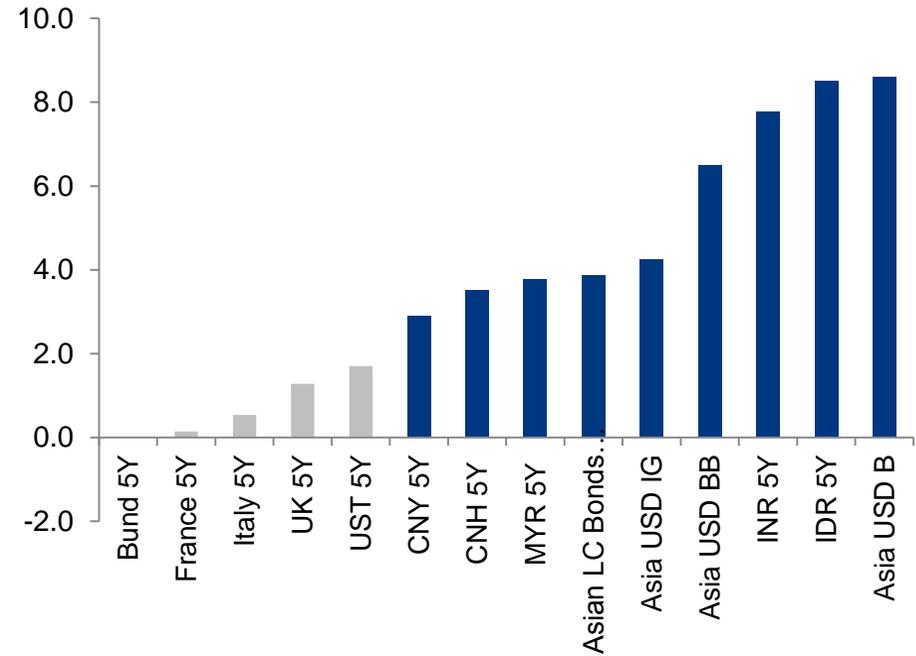
Differentiating between new products and new exponential technologies and their applications always leads to underestimating the potential for change and market or industry disruption...

It's all about yield – if you can find it

Negative interest rates on 40% of outstanding European government bonds¹



Yields in local currency terms² (%)

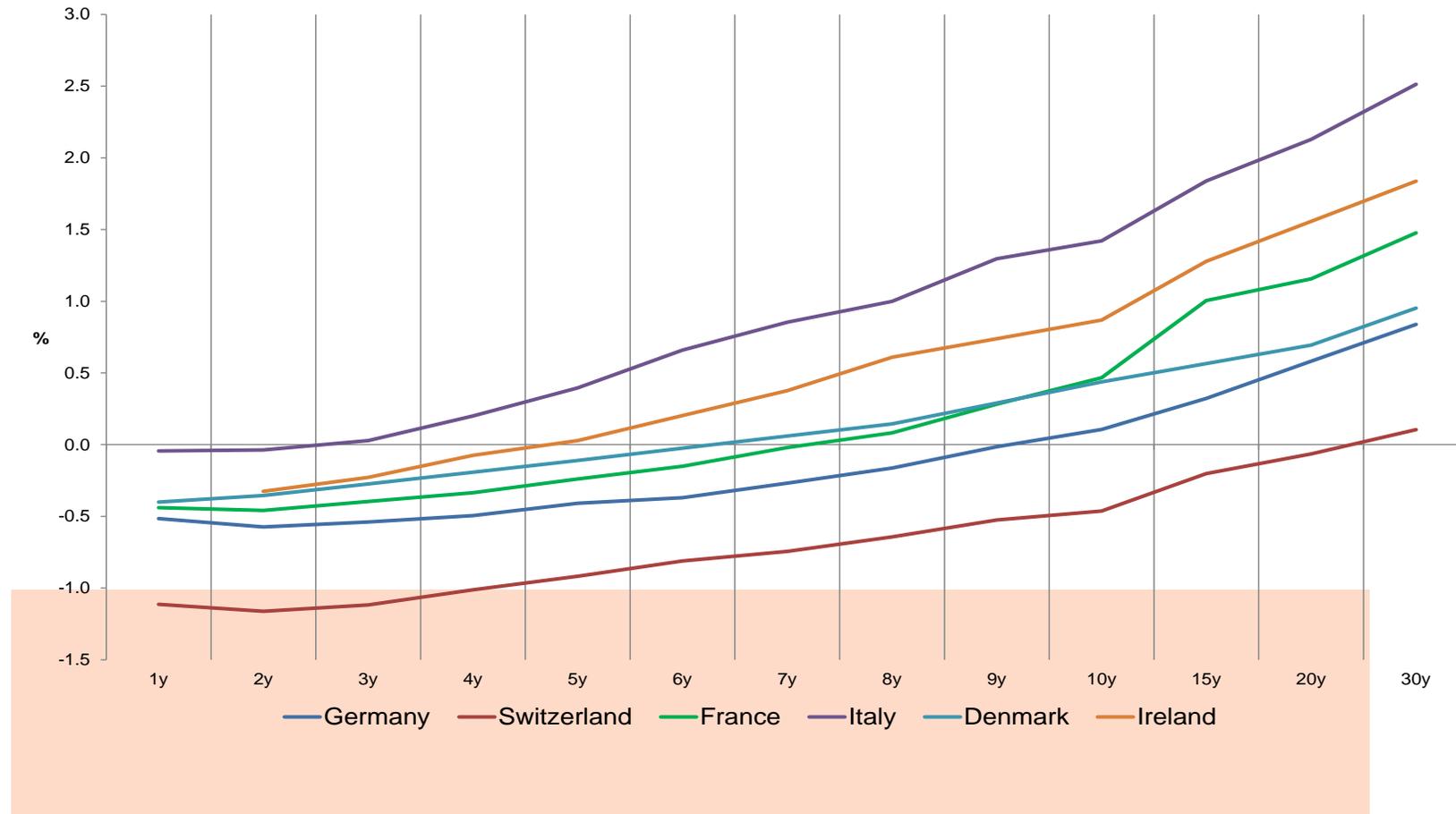


Most developed market yields to remain low - the search for yield will remain a theme in 2016

1. Source: Jack Di-Lizia, Bloomberg Finance LP, Deutsche Bank Research, as at 1 December 2015.
2. Source: Bloomberg, Allianz Global Investors, as at 4 December 2015.

However, “ Hunt for Income “ grows in Europe

Yield Curves Government Bonds in Europe

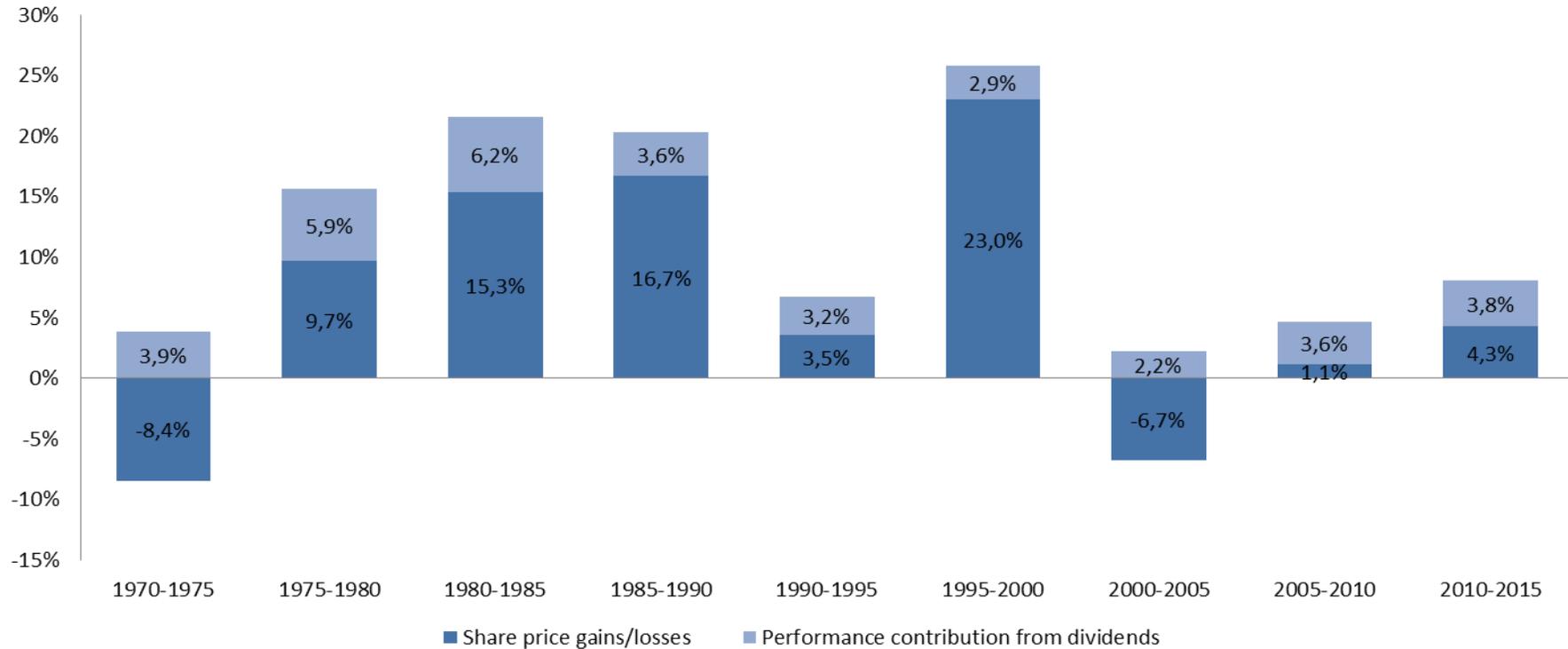


Ex Bank bonds, the income comes only from Equities in Europe

Source: Bloomberg/AGI, 29. February 2016.
Past performance is not a reliable indicator of future results. Forecasts are not a reliable indicator of future results.

Dividends – A Stabilising Factor for Investors

Performance contribution from dividends and MSCI Europe share prices since 1970 in five-year periods (% p.a.)



Dividends are a constant source of positive returns, increasingly....

3



Investment Conclusions

Summary - 5 things to remember for you investment strategy...

Understand.

- **Expect the low-growth, low-inflation environment to continue**
- There is **no alternative to taking risk**
- With beta returns low, **clients need alpha now more than ever**
- **Volatility should deliver opportunities for active management**
- **Diversification and avoiding the herd positioning** are even more relevant

Act.

- Pursue **explicit secular Growth strategies** to access the growth the World provides
- Consider **risk-reduction and lower volatility strategies**
- **Be Agile** in your investment choices within **SAA,TAA** and **Confident in PM investment process**
- Be **Thorough** with the Research resources available globally
- Leverage **suite of fixed income and dividend strategies** and **alternative strategies**



Be “ACTive” to protect your clients purchasing power

Books to read, and Neil's Global Strategist perspectives

Ray Kurzweil – The Singularity is near
 Tony Seba – Clean Disruption
 Dave Eggers – The Circle
 Niall Howe – Millennials Rising
 Michael Lewis – Flashboys
 Xi Jinping – The Governance of China
 Vasr Nasr – The Shia Revival
 Greg McKeown - Essentialism
 Martin Ford – The Rise of the Robots
 Adam Ferguson – When money dies
 Brian Kelly – Bitcoin Big Bang
 Geoff Colvin – Humans are Underrated



Neil Dwane on... Oil
The perspective from the Europe CIO Equity

28 September 2015

Agnostic on Oil, Positive on Big Oil Equities

Reflecting on the many market movements over the last two years, the collapse in oil is one of the most notable and remarkable, despite severe risks from Libya that added a risk of higher price rise.

Neil Dwane on... Equities
The perspective from the Europe CIO Equity

23 September 2015

Volatility, Volumes and VW Strike Equity Markets

Over the past 6 weeks, equity investors have been impacted by significant change in both volatility and confidence in equities. Why?

China
During the summer, China was obviously trying to rein in its falling equity market after having sponsored the more aggressive upward moves earlier in the year. The persistence of policy changes had only temporary effects on the levels of Chinese equity markets, which increasingly unnerved both domestic and international investors. This context of state-levels... a source of growth for the world has stalled.

US Monetary Policy
"Will she, won't she..." After months of uncertainty and much press and investor speculation, Janet Yellen and the US Federal Reserve did not raise rates, which was taken negatively. So good news is now bad news? The Fed did not raise rates despite a solid level of employment and a dull but stable US economy because it feared both a stronger US dollar, which makes exports less competitive, and because it was concerned about the slowdown and recessions emerging in China, Brazil and elsewhere. Gone are the days that the "US dollar is our currency and your problem!"

Neil Dwane on... the ECB
The perspective from the Global Strategist

26 October 2015

A reprise – more Draghi 2012 vintage – bravo, bravo!

Whilst sojourning in Malta this week, the European Central Bank (ECB) has come out from its deliberations in very dovish and robust form, and was far more convincing than expected – hence the rapid rise in European Equities, the fall in Eurozone (EZ) Sovereigns back into negative yields, and a 4% fall in the Euro. We are experiencing a rerun of the winter of 2014 when Fixed Income investors very successfully yet more frustration from savers over this pernicious rate.

Additionally, the ECB made it quite clear that all and other tools were still available for intervention in monetary policy and to intervene in time for Christmas: Presents all round!

Interestingly, the ECB has repeatedly stated that its monetary

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AllianzGI disruption topic is now on-line, @ www.allianzgi.com/disruption

Neil's Global Strategist perspectives can be found at: www.allianzgi.com

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Global Policy Council – the strategic view

Understand

Financial repression remains in place

Monetary policy globally will remain lower for longer

Slow, low and fragile economic growth

Global debt levels remain high and will increase

Politics and geo-politics are evolving rapidly

Geopolitical risk has risen in Europe, the Middle East

Cheap Beta offers no returns in fixed income and equities

Income investing works in Financial Repression

Some risk-taking is needed to earn a return

Act

Protecting purchasing power is crucial

The “hunt for income” is undiminished

With China rebalancing, low growth will persist

With no deleveraging, growth cannot accelerate

Policy & regulation adds to uncertainty, means Volatility

Prepare for uncertainty and volatility

Alpha is now needed to generate returns

Dividend income is a major driver of returns for Equities

With Volatility rising, investors must be ACTIVE



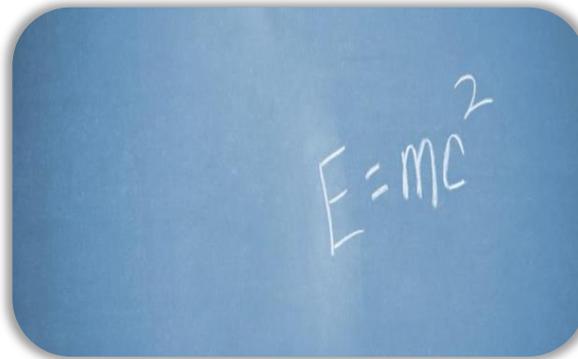
With Volatility rising, be ACTIVE – Agile Confident Thorough

What's to come in 2016?



25 years of the Web

- Central Banks effectiveness
- Iran
- China
- India
- World trade



100 years of Relativity

- US HY attractiveness
- Growth investing
- Equity Income attractive
- Disruption
- Climate Change



40 years of Concorde

- Oil
- Capex cycle over
- Nuclear decommissioning
- Threat of Cyber
- Technology and disruption

Clear dominant themes... China, Rebalancing and Disruption

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