



Compass
2020 Outlook

 **BARCLAYS**



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“As the world economy revives unsteadily from its latest swoon, we use this edition of Compass to discuss both what happened in 2019 and some things to think about for 2020.”

December 2019



Signing off 2019 and ushering in 2020

As the world economy revives unsteadily from its latest swoon, we use this edition of Compass to discuss both what happened in 2019 and some things to think about for 2020. 2019 has certainly not been short of incident. The pinball-like narratives of Brexit and the US-China trade war have kept markets and commentators guessing throughout. The world economy has faltered, prompting many to again call time on this economic cycle.

As we describe in our various outlook themes, we still suspect such gloom is premature. The economic cycle is long in the tooth for sure, but age matters less here than commonly feared. Moreover, the manufacturing slump that has characterised much of this year seems to be bottoming out. Alongside this, developed world government spending is set to provide a little more support this coming year. Of course, we cannot be as confident about the trajectories of the Brexit and trade war sagas. With regards to the latter, we still see the approach of the 2020 Presidential campaign trail as a likely moderating factor. We discuss this and what we can and cannot predict about the US Presidential elections in more detail inside.

With regards to Brexit, the chances of the UK exiting the EU without a deal remain significantly lower than they were six months ago. They are certainly not zero though. Of all the major developed world economies, the UK likely offers the widest range of plausible outcomes over the next 12 months. For our part, we are still leaning against the pessimism implied by the UK's bond market in our multi-asset class funds and portfolios.

More broadly, we take a look at some themes we expect to continue to play an important role in the world's capital markets this coming year. Concern about the outlook for the world's fragile environment is starting to be reflected in growing investor appetite for investment strategies that can help. We look at where this trend has been and where it might be going.

Trend is another subject discussed in more detail in this edition of Compass. One of the most powerful, and indeed enduring, forces within capital markets is momentum. Roughly speaking, the idea that markets or investments can continue to trend in the direction they're going for much longer than perhaps rational long-term valuation would suggest. We examine this market force with a behavioural lens.

Finally, the 'rise and rise' of goal-based investing is examined in greater detail. With new technology enabling high-end, bespoke investment planning at a scale and a speed previously thought impossible, we look at some of the benefits for clients.

As usual, we wish you and your loved ones a restful and enjoyable festive season.

Warmest regards,

A handwritten signature in black ink, appearing to read 'Solomon Soquar'.

Solomon Soquar
Head of Barclays Investment Solutions

Siren Call

“Come this way, honoured Odysseus...Over all the generous earth we know everything that happens.” (Homer, Odyssey)

The past year has provided yet more compelling evidence for robust earplugs to be at the top of every investor’s Christmas list. Maybe Santa could helpfully block some websites and TV channels too. Last Christmas, the sirens, as usual singing of imminent economic doom, managed to lure many more unfortunate investors onto the rocks of disinvestment or excessive defence. Stock markets briefly plunged last December as we were again told that the end of the economic cycle was finally here.

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However, losses were soon made good. As the world economy proved itself fit to carry on without major catastrophe, stock markets rallied strongly (Figure 1). Those who had believed the (ever) over eager prophets of doom were left on the sidelines ruing their gloom.

To be fair, even to a committed advocate of the benefits of getting and staying invested, 2019 did not look like an especially appetising year. It certainly did not portend almost every major asset providing strong returns (Figure 2). The world economy has so far not slumped into recession as many feared; however, neither has it generated the kind of growth that would more normally be associated with such equity market returns. Quite the reverse in fact. The world economy has latterly been flirting with stall speed again, amidst a combative political backdrop, slower Chinese growth and a sharp manufacturing inventory cycle.

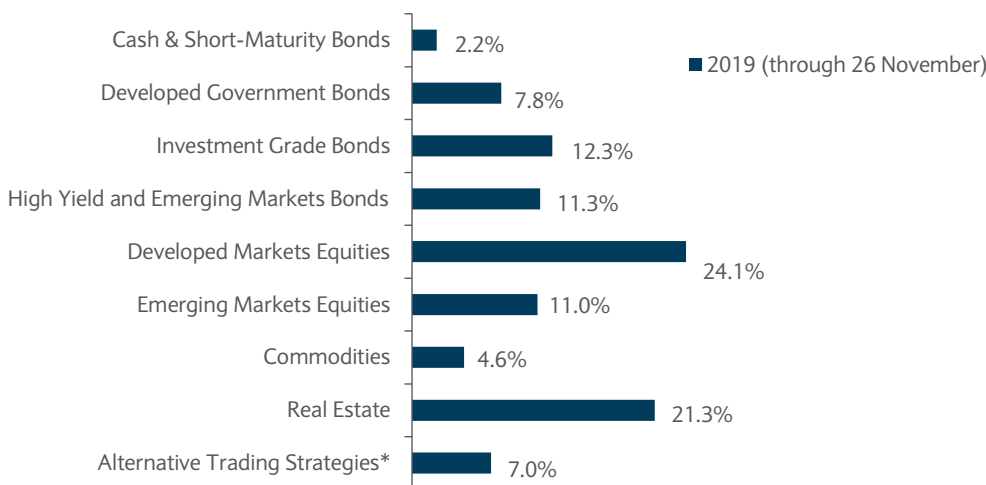
FIGURE 1: Stock markets have rallied this year



Source: FactSet, Barclays

Past performance is not a guide to future performance.

FIGURE 2: Every major asset class has provided strong returns



*ATS as of 25/11/19. Source: Factset, Barclays. Asset classes in USD. For the asset class indices and a table of historical discrete annual performance, please see the [Appendix](#).

Past performance is not a guide to future performance.

Perception vs. reality

In our ever more reductive world, much nuance and truth is wilfully marginalised in favour of something more sensational. Truthiness, factoids and fake news are the words of the moment. This missing nuance is important in capital markets where the box office stories remain the Trade War, Brexit, and the next recession. These stories have managed to hoard almost all of the available oxygen and, given their ability to still attract readership, are stretched to help explain more than they should or could.

For example, easily the most alluring explanation of the slowdown in China is the trade heat that this most mercurial of US administrations continues to apply. While there is a kernel of truth to this, it's an oversimplification.

China's slowing economy also owes itself to misaligned incentives. In the last few years, Chinese authorities have moved to turn the credit spigots down, both bank and non-bank. The aim was to combat the mushrooming potential for disruptive risks to financial stability. However, the problem was that it was the more efficient, profitable and less leveraged private companies that suffered the bulk of the squeeze. The remaining flows of credit naturally gravitated towards the areas of the economy benefiting from an implicit state guarantee – lumbering state-owned enterprises.

The trade war has certainly played its role in bruising private sector confidence the world over, just as recently cooling tensions may be helping the corporate sector find its feet (Figure 3). However, we remain wary of the caricature of the world economy as Pinocchio to President Trump's Geppetto.

FIGURE 3: Corporate sector is finding its feet



Source: FactSet, Barclays

Neither should we assume, as many seem to, that the Federal Reserve has control of any of the strings. These actors tend to have the ability to influence interest rates and confidence at the margin, but mostly there tend to be grander, less easily simplified forces in motion.

What matters

This year amply demonstrates the need to be 'on the pitch', fully invested at all times. We have less ability to see the future and the recessions that lie ahead than widely advertised. Those indicators that are of some use can only feasibly influence how we allocate at the edges of our diversified mix of assets. We have managed to slightly add to portfolio and fund performance again this year through just such tweaks and adjustments.

However, looking into 2020, surely we can say that the risks of a recession are higher still? Not necessarily. 2020 is already looking like a year when the world's governments decide to make more use of these basement interest rates to borrow and spend a bit more. With business confidence now in the process of stabilising at low levels, a moderate bounce is now in the offing.

More importantly for investors, the act of worrying about the next recession must not be allowed to overcome the instinct to invest for the future. The point about investing remains the ability to both fuel productivity and harvest its rewards. The timing and scale of these rewards has always been uncertain. However, the history of the world economy tells us that they are much more frequent and reliable than the recessions that occasionally punctuate this growth story.

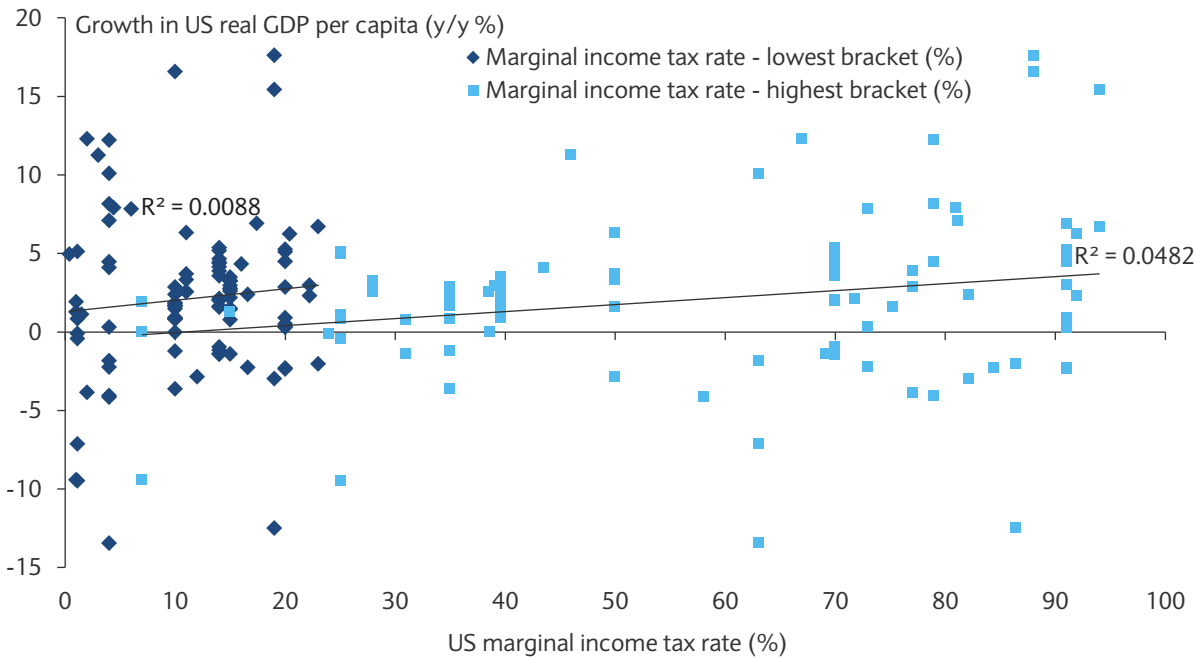
There will be plenty of politics to grapple with again next year. The campaign trail for the 2020 US Presidential elections will create deafening noise for investors. However, there will be very little signal in there.

Untrammelled power will not be conferred on the eventual victor. Trade tensions will likely remain no matter who wins, as will growing angst about the tech titans' increasingly apparent political and economic muscle. Developed world tax burdens may shift for both consumers and companies. However, for long-term investors this may be less important than many claim. History seems to indicate very little relationship between tax rates and the trend growth rate that is at the nexus of long-term investor returns (Figure 4). Again, we, and everyone else, lack the ability to predict such changes with the confidence necessary to actually make asset allocation decisions ahead of time.

So we should look to the new year with the usual mix of cautious optimism and humility that a study of the past gives us. Growth remains the norm. The political backdrop is certainly disconcerting in some parts at the moment, but remains less influential than feared.

Certainly, parts of the world's capital markets are expensive, perhaps dangerously so in some instances. Investors have been guilty of overpaying for safety and protection in a jittery economic cycle, in the long shadow cast by the Great Financial Crisis. However, we don't think stocks are prohibitively priced still, even if the profits outlook is a little meagre. A diversified, multi-asset class fund or portfolio predictably remains the best weapon to bring to bear on all of this uncertainty and opportunity... that and some earplugs.

FIGURE 4: Little relationship between tax and growth rates



Source: US Federal Reserve Economic Data, Barclays



2019
2020

Theme #1: Politics will continue to surprise

This is probably the easiest prediction to make for 2020. Such is the current state of Western political discourse, that even if the various scheduled political events don't provide a surprise, it will be a surprise in itself.

Nonetheless, it is obviously the run up to the US Presidential elections in November that is likely to dominate the airwaves for much of the year. The 45th President of the United States has so far proved to be one of its most newsworthy. While the field of Democrat challengers is yet to be whittled down to an eventual challenger, suffice it to say there is the potential for a starkly different direction in a number of areas of US policy in the wake of the election.

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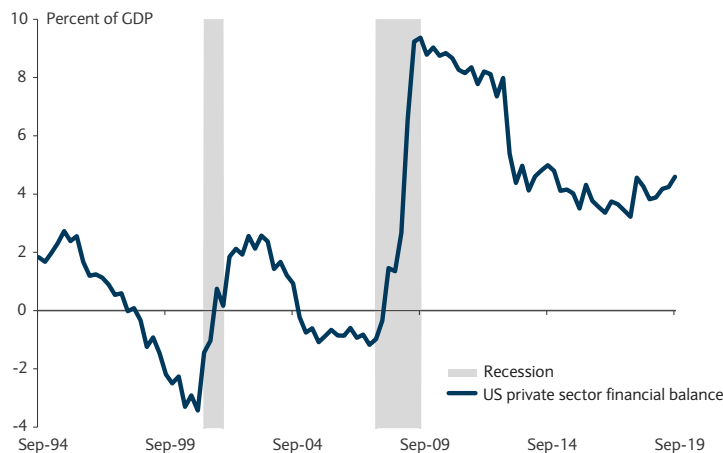
The question for investors is how should I plan for this event? Well, first of all, we should tune out those who tell us that they have an inside track here. There will be those who correctly called President Trump's election no doubt arguing that their secret sauce can work this time around too. Ignore them.

Predicting elections is one thing. Guessing at the potential policy implications, and when they might land, is another thing altogether. Institutional checks on executive power, changing priorities and rotating doors are parts of the story that tend to frustrate our ability to say anything particularly meaningful.

This will not stop many in the industry trying. Many will tout baskets of stocks or investments designed as prophylactic against one proposed policy or other. Such investments can seem alluringly specific – a surgical strategy. All we can say is that investors are very unlikely to be able to glean an edge here and we would urge caution. Thematic baskets are often more beneficial to sellers than buyers.

Changes in political direction at the country level are not terribly predictable. However, we can take some reassurance that such changes also tend not to be directly consequential in the way often feared. Much of the time, politicians are in yoke to the underlying economy and its pre-existing idiosyncrasies rather than the other way around. For the world's capital markets, it continues to be the US economy, not its president, that sets the beat.

FIGURE 1: Good or bad health?



Source: FactSet, Barclays

In such a context, it is the strong financial position of US households and companies that is most important. This is a state of economic health that both predates this US administration and may well survive it (Figure 1). Of course, none of this is to say that the White House, or any other major political power, is incapable of upsetting the economic apple cart. But history tells us such moments are both rarer than feared and less predictable than any of our current batch of soothsayers would admit. The answer, of course, is diversification.

As an aside, there is also an important lesson in all of this. It is really that the modern investing world allows us much more freedom in where we should accept the market return and where we should fight for something more. Getting the market return is now extremely inexpensive, free in some cases. This allows us the benefit of focusing our energies in the areas where we really think value can be added. For now, armchair political strategy is a fight we will gladly leave to others.



Theme #2: The next recession?

A few lights on our recession warning dashboard have been flashing amber this year. The risks of a recession have, at times, been higher than they've been for several years. The global manufacturing sector slumped amidst a slowing Chinese economy and rising trade tensions. So far, the world's consumers have managed to hold the line. Sharply lower interest rates at all maturities in more or less all countries have also probably helped.

Should I try and factor in the next recession when I'm thinking about my investments? It would seem bizarre to say 'no' wouldn't it? Particularly considering the severity of the last one? However, the problems are many, first among them predictability.

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Much as with major changes in political direction, recessions are often as unexpected as a power cut. If they were foreseeable, one has to wonder whether they would even exist at all – wouldn't everyone just take the necessary evasive action?

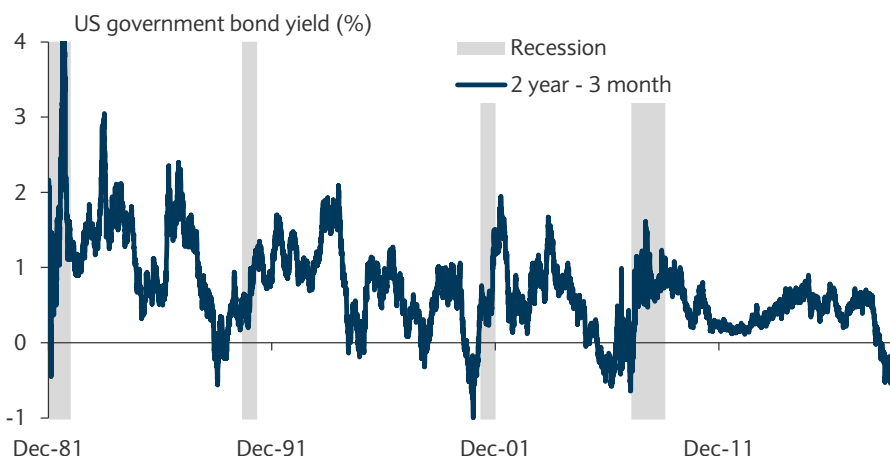
Most predicted recessions fail to materialise. Many investors have suffered significantly more in foregone returns in this economic cycle alone than they could ever hope to make up by swerving the next several downturns.

A second major problem is that even if you could see it coming, what would you do? Many in the industry seem to imagine that there is a pre-ordained 'recession portfolio'. Gold, Treasuries and other government bonds as well as a sprinkling of very defensive, economically well-insulated companies seem to be the order of the day. However, as we've pointed out before, capital markets are adaptive, a trait which can leave a blind adherence to such a portfolio more painful than the recession itself.

The point is that what has worked for past recessions doesn't always work in the next one, because everyone else may be thinking the same thing. Think about a centre forward who has to take consecutive penalties against the same goalkeeper. The goalkeeper can't just assume that the centre forward will kindly kick it in the same place over and over. Standing in the position that the previous penalty ended up could make the keeper look a fool.

How assets perform in certain environments all depends on what is already priced into those assets. For example, there's little point in buying bonds in anticipation of easier monetary policy if it's already priced in by investors (Figure 1).

FIGURE 1: US government bond yield and recessions



Source: FactSet, Barclays

The problem for investors right now is that this is an economic cycle where persistently frayed investor nerves have seen safety as a more-prized-than-usual trait. This is not too surprising. The last recession, a sort of global economic heart attack, was one for the history books. Such seizures are far from the norm (Figure 2) and nor are some of the capital markets horrors that accompanied it. However, the doomsayer trade has, of course, prospered in its shadow. The result is a world where safety is dear.

What to do?

As we've noted before, this all explains why we split our asset allocation process into two distinct parts. The overwhelming majority of the multi-asset-class funds and portfolios that we run for clients are organised by something called the Strategic Asset Allocation (SAA). This is our long-term portfolio foundation, and is essentially an exercise in investing humility. Rather than copy and paste the past, we remix historical patterns to imagine hundreds of thousands of possible futures. This guides our construction of diversified, all-weather allocations.

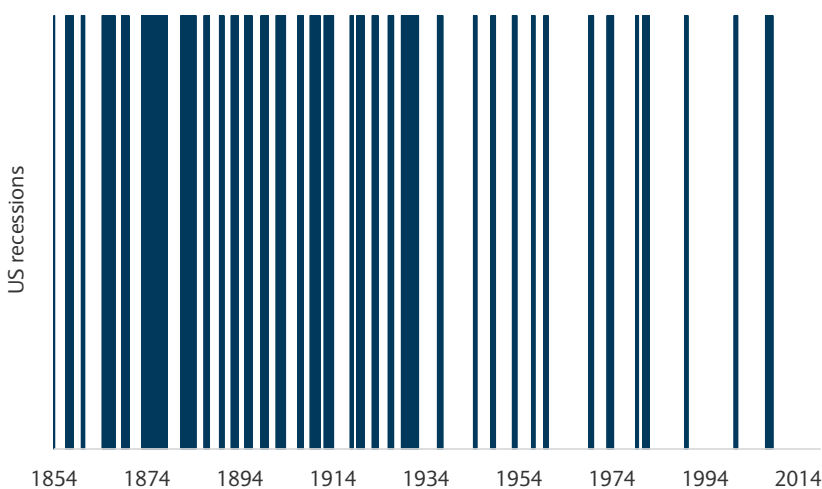
The second part of the process is called Tactical Asset Allocation (TAA). This is not where we dust off the crystal ball and squint into the future. It is instead a rigorous method by which we scour the world's capital markets, looking for

instances where particular assets may reflect misjudged risks or opportunities relative to our expectations. It relies more on an appreciation of where emotions or behavioural biases may be getting the better of the world's investors than any soothsaying.

Interestingly enough, recessions, or at least the threat of them, and highly emotional situations like Brexit, or even impeachment proceedings in the US, can provide such openings. Humility is always appropriate of course, and the point of the TAA is not to take positions on everything: it is to try and commit to positions only when you feel the odds are stacked in your favour. This does not mean that you will win every time; far from it. However, if you keep to this with sufficient discipline, you should continue to be able to add to performance, as we have over the last decade.

You can put your money to work in a risk-controlled portfolio/fund, driven by a multitude of industries and countries, with a subtle tilt here and there as opportunities arise. Or you can careen between extremes in the hope of outsmarting the world and outmanoeuvring the future. One of these approaches is likely to do well, even as recessions come and go. The other pretty much always leads to ruin and regret.

FIGURE 2: Recessions are the exception, not the norm



Source: FactSet, Barclays

Theme #3: A not so random walk down Wall Street

Benjamin Graham, a pioneer of investing, famously remarked that: “In the short run, the market is a voting machine, but in the long run it is a weighing machine”.

The essence of his statement is that over shorter periods the market reflects what is popular or unpopular at the time – which can deviate from what seems ‘rational’ – whereas over longer periods the market will assess the fundamental substance of investments and accurately reflect this in its price.

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While not always reflective of an investment’s long-term value, short-term returns may not be as random as a spin of the roulette wheel. The ‘animal spirits’ which guide markets are driven by the behaviour of individual investors, behaviour which we know is heavily influenced by emotion rather than entirely logical supposition. This behaviour is also far from random, and may lead to certain predictable phenomena¹. Phenomena such as momentum.

Financial not political movements

Momentum is when markets or investments continue to trend in the direction they’re going for much longer than most people assume possible or rational long-term valuation would suggest. Typically, a momentum investing strategy involves buying assets, most commonly stocks, that have experienced positive returns over a prior period and selling those that have seen negative performance recently. In other words, trend following.

The interesting thing about momentum is that it lacks a consensus for its existence. Academics and industry practitioners have posited many theories which broadly fall into two buckets; risk-based and behavioural-based. Our behavioural finance experience leads us to believe it is the latter which has more credibility, and here we explore it further. While there are too many potential cognitive effects at play to discuss them all in detail here, we can provide some reasoned thinking.

The many personalities of investor behaviour

Both over- and under-reaction by investors to news have a role to play and although these would appear to cancel each other out, they can, along with a myriad of other actions, reinforce each other. Rather than new information (good or bad news) being incorporated into prices immediately, it can be delayed. This could be, amongst other things, due to inattention², our risk averse nature or a reluctance to change our views. At the same time, investors tend to sell their winning positions too soon but hold onto losing positions too long³, which may provide another headwind for prices to reflect true value.

¹ Although it is possible to model individual behaviour understanding, the aggregate effect at a market level is much more difficult.

² Merton, Robert C., A Simple Model of Capital Market Equilibrium with Incomplete Information, *Journal of Finance* 42, 483-510 (1987).

³ Barber, Brad, and Terrance Odean, Trading is Hazardous to Your Wealth: The Common Stock Investment Performance of Individual Investors, *Journal of Finance* 55, 773-806 (2000).

After this initial under-reaction our bias to overweight more recent information, combined with overconfidence can cause us to simply extrapolate the recent price movements into the future. We are then pre-disposed to seek information that confirms this view which may explain why we react to old ‘stale’ news⁴. Now that prices have begun to move, the comfort from following the crowd then promotes herding behaviour, providing a feedback loop and reinforcing the delayed over-reaction and driving prices away from their rational value. This may explain why momentum has been shown to occur for longer than expected, for up to 12 months.

When does the music stop?

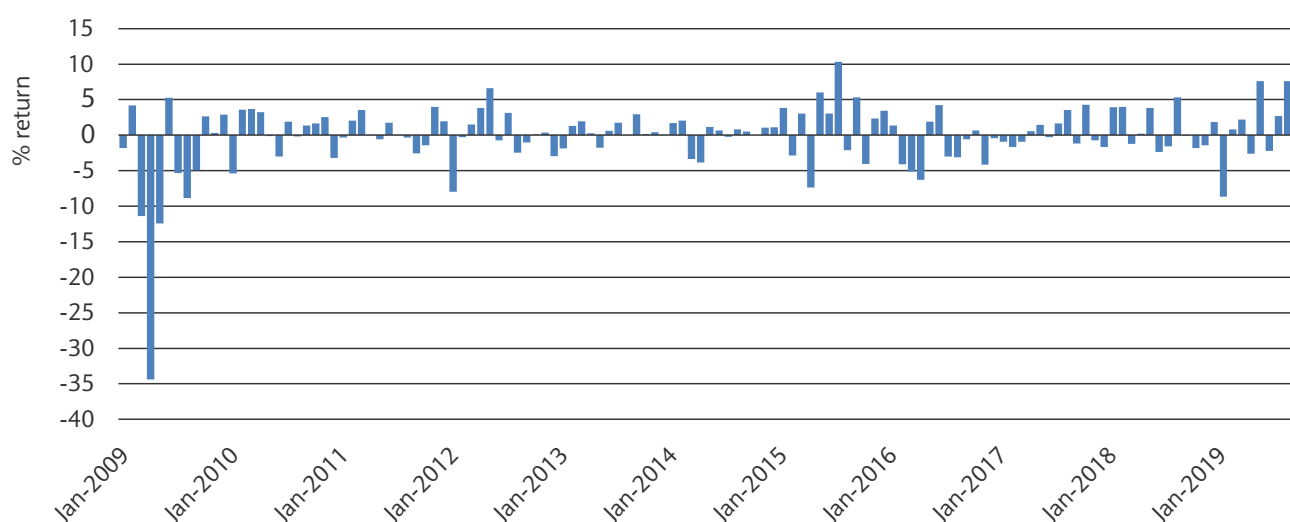
No matter the explanation, the issue with momentum investing, as with many investment strategies or styles, is that it works until it doesn’t. Where does the voting stop and the weighing start? Accurately predicting when this ‘irrationality’ will finish is incredibly difficult and so timing entry or exit seems impossible.

While momentum has been shown to deliver significant returns over the long term – MSCI World Momentum Index (see Appendix for discrete annual returns data) has delivered 13.7% annualised returns over the last 10 years (past performance is not a guide to future performance) – it is important to treat any ‘proven’ claims, especially from those with financial interests, with a pinch of salt. Markets can turn very sharply and momentum strategies can experience severe crashes as a result (Figure 1). In 2009, this strategy lost over 50% of its value. This reality will likely prove too much for even the most composed investors to bear.

Conclusion

Looking at an individual investment strategy highlights the importance of diversifying across sources of risk and return. A diversified mix of assets and investment styles not only dampens the impact of a particularly bad performance in one, it protects an investor from the sometimes unpredictable change in sentiment and human behaviour.

FIGURE 1: Monthly returns for the momentum strategy



Source: Ken French Data Library: Monthly Momentum Factor, https://mba.tuck.dartmouth.edu/pages/faculty/ken.french/Data_Library/det_mom_factor.html

Past performance is not a guide to future performance.

⁴ Tetlock, P.C., All the News That’s Fit to Reprint: Do Investors React to Stale Information, Review of Financial Studies vol. 24, 1481-1512 (2011).

Theme #4: Impact Investing: Past, present and future

Environmental, social and corporate governance (ESG) investing has enjoyed a fascinating journey over the decades. It has arrived at its latest iteration, named ‘Impact Investing’, only very recently. So what has this evolution looked like and where might it go next?

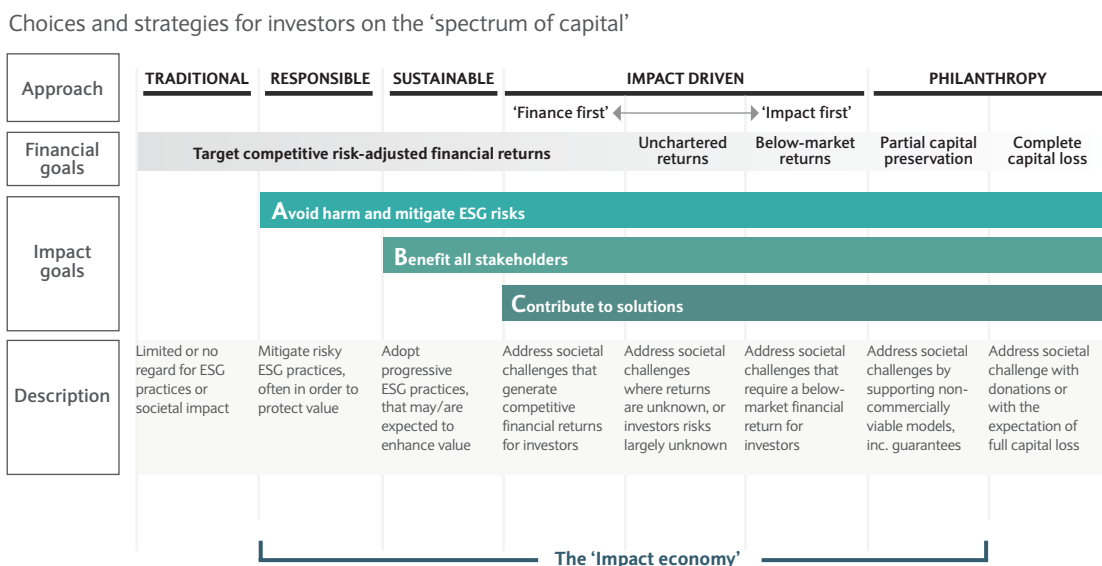
A very neat way of encapsulating this changing landscape is in Figure 1. We can place the investment funds universe today onto this continuum. The majority of funds are Traditional and sit in the far left box outside the ESG space. They invest in equities and/or bonds purely for financial gain. Moving rightwards we then step into the ESG space.

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The first step is to Responsible funds that simply exclude sectors and stocks that may cause harm to the planet or society. Obvious examples include tobacco stocks or cluster munitions stocks. Next to the right come Sustainable funds. These not only screen out the so-called ‘sin stocks’ of tobacco and weapons, but actively engage with the management teams of the companies they hold to enhance value and the well-being of society and the planet.

The central three segments really bring us to the core of Impact Investing. Funds in this space not only avoid the stocks mentioned before, but also engage with companies and seek to invest in firms whose activities are having clear and specific societal and environmental benefits. The extent to which the risk to financial returns matters varies as you move to the right.

FIGURE 1: The Spectrum of Capital



Source: Bridges Impact+ and the Impact Management Project.

At Barclays, we offer our Multi-Impact Growth Fund which sits in the left-most of the three Impact categories. It invests in listed equity and bond funds that have a positive impact whilst also aiming to deliver a compelling return. In fact, more than two years after launch, its financial gains have beaten those of its peers. This investment takes a moderate level of risk to provide long-term growth. There's more exposure to riskier investments than Barclays' lower risk profile funds, but it's still well diversified to try to mitigate some of that risk. At this level, short-term changes in value are more likely and while you'll be invested in both bonds and shares, it'll lean more towards the latter.

The final two buckets of the spectrum are not covered by investment funds as they are philanthropic. Barclays has a service that can assist with these considerations too.

While not explicit here, one could overlay this spectrum on a timeline in the UK, starting from the left, with the Friends Provident Stewardship Fund launched back in 1984. Prior to that, all funds sat in the Traditional box. Since then, interest in ESG investing has ebbed and flowed over the intervening three decades. In the 2000s, Responsible and Sustainable funds launched and gathered attention and assets. Yet, with the advent of Impact funds in the mid-2010s, the focus on ESG investing has certainly reached new heights. The interest and weight of money has never been greater.

This is due to a variety of factors not least societal change. Young people especially have an increasing interest in the environment, and one highly effective way to prompt change for the better for the planet and society is to integrate it into investing and how investors interact with company management. By engaging with firms and, in the case of equity holders, voting appropriately, investors can have a huge positive impact without giving up financial gains.

The future

So what about the future of this space? Very soon, engaging and voting will be the minimum across all investment funds, while the amount of money in Impact Investing vehicles will continue to rise rapidly. Not only is this due to investor demands and the awakening of companies to these issues, but also the regulatory imperative, whether it's things such as the UNPRI (United Nations-supported Principles for Responsible Investment), the updated UK Stewardship Code or the SRD II (Shareholder Rights Directive).

As Peter Harrison, CEO of Europe's largest listed asset manager, Schroders, expressed in November:

“Twenty years from now we will have a much bigger discussion about the impact you have in delivering returns, what is the impact on society and climate. In my mind, our industry has been given this really deliberate purpose, which is what can you do to solve wider problems whilst also investing.”



Theme #5: Goal-based investing: a strategy to satisfy

Personal investing has always been about meeting future needs. We put money to work for our future selves, or someone we care about.

Even the word ‘assets’ has its root in this idea: it comes from the Latin ‘ad satis’, or ‘to satisfy’. So, goal-based investing is nothing new. And yet, the concept has become popular in recent years, as wealth management becomes ever more personalised – and digitised.

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New technology has enabled high-end, bespoke investment planning at a scale and a speed previously impossible. No longer are portfolios dictated by willingness to take risk alone – capacity to take it has become a vital input, alongside gauges of behaviour and preference.

Plenty of people feel that their futures are as unpredictable as stock markets. Indeed, you might not have a particular grand expenditure in mind right now. But many are increasingly looking to nest eggs to fund their family milestones.

For example, how should you invest on behalf of a loved one for their potential university fees? If they’re a new-born baby, the chances are they’ll be too busy with potty training to care about the odd stock market dump. Plus, they have time on their side to wait for a recovery.

Most importantly of all, their nascent savings are just a fraction of what they’ll be in time, if fed by regular contributions. Suppose you save £100 a month for a child – you’ll have set aside over £20,000 by the time they reach adulthood. Any losses that afflict those early few hundreds of pounds will be dwarfed by the mature portfolio. So it makes sense to seek higher returns while the consequences of losses are limited.

But when their final year exams are on the horizon, it might be wise to dial down the risk. This reduces the chances of an unpleasant lurch in value just as the invoice arrives for their first term of college.

In short, you need to think about the best portfolio you can build today, for tomorrow.

With that in mind, when should you make changes to your investments? Let’s take a look at a few common things that spring to mind.

News

We are in thrall to an always-on media that craves clicks and views. Should today’s change in the FTSE 100 price matter to your portfolio?

When we talk about investing, we mean years, not days; we mean returns including dividends, not price changes; we mean global, not local; we mean a broad selection of assets, not just stocks.

Even in a crisis, we have to remain focused on the long-term prospects, not knee-jerk reactions. Remember too that while politicians like to portray themselves as stewards of the economy, they could more accurately be described as hostages.

However grave the headlines, it’s hard to think of a world in which owning a share of future company profits wouldn’t still be expected to beat the interest on a deposit. Tune out the noise.

¹ <https://www.etymonline.com/word/assets>

Age

As we get older, our portfolios mature with us, as in the example above. In most cases, this will mean a diminished capacity to recoup any losses, and fewer contributions yet to accumulate.

Therefore, it usually makes sense to slowly reduce the risk of your investments over time.

Performance

Bad performance can be maddening. But when does it signal time for a change? Some styles of investing can get stuck in a rut for months or even years before they come good. Even the best fund has a rough patch.

If poor returns come with a reasonable explanation, and are not expected to last, then it might not make sense to incur

trading costs purely to shake things up for the sake of it. But if a manager starts to act as if they've had an overnight change of philosophy, or if even a strong performer's prospects start to dim, don't be afraid to realign your assets accordingly.

Plans

If your life suddenly turns upside down, it could mean anything for your investments. New member of the family? Time to think ahead. Win the lottery? Don't let the jackpot languish in cash.

Investing wisely can improve the chances of achieving your goals. No matter how uncertain things may be, having a plan and staying on track is the best way to satisfy your future self.



The View from the Asset Allocation Forum

Rising optimism – Our TAA positioning

A lot of attention has been given to the recent weakness in manufacturing survey data, but the broader US economy has so far remained resilient to spillovers from weakness in the manufacturing sector.

The latest batch of activity data shows tentative signs of a stabilisation in the economic slowdown. Alongside the declining risk of a no-deal Brexit and a more conciliatory tone in US-China trade tensions, investors have become more optimistic.

Cash & Short-Maturity Bonds: **Overweight**

- In their effort to stem the global economic slowdown, central banks across the globe have reduced interest rates. However, some are signalling they are done with cutting rates for now.
- Our overweight to this asset class is a function of underweights in others. We are looking to deploy cash when opportunities arise.

Developed Markets Equities: **Overweight**

- Better news flow along with stabilising economic data has helped fuel a strong rally in Developed Markets Equities.
- Although recent returns have been strong, we think sentiment can still improve from here and so remain overweight.

Emerging Markets Equities: **Neutral**

- Emerging Markets Equities have rallied following a more conciliatory tone from US-China trade tensions and investors becoming less pessimistic over the growth outlook.
- While we think sentiment has room to run for equities, we prefer to take our exposure within developed markets, so remain neutral for now.

Alternative Trading Strategies: **Neutral**

- This is a heterogeneous asset class with little tactical appeal at the moment.
- We typically use this asset class as an alternative source of funding.

High Yield & Emerging Market Bonds: **Overweight**

- High yield credit spreads continue to tighten despite weakening fundamentals, such as leverage and interest coverage ratios. Given rich valuations relative to history, we remain underweight.
- Broadly speaking, EM countries have healthier fundamentals today, while inflationary trends remain well-behaved. We are currently overweight emerging market (EM) local debt.

Here, we explain our current thinking behind our Tactical Asset Allocation (TAA). Please refer to the glossary below for an explanation of the terminology.

This is our view but it's important to appreciate that predictions of future investment conditions are always uncertain. Outcomes may differ from those that we expect. Circumstances might change or we could be wrong. We don't give personal investment advice. You make your own decisions. If you're unsure, seek independent personal advice.

We maintain a long-term Strategic Asset Allocation (SAA) for five risk profiles, based on our outlook for each asset class. We also make tactical adjustments to our portfolio, mainly based on our shorter term (three-to-six month) outlook.

Real Estate: Underweight

- We are underweight as part of our relative view versus Developed Markets Equities. Our previous research has shown that relative returns are negatively related to higher bond yields.
- While economic data has indeed continued to mostly disappoint, a lot of monetary policy easing and bad news has already been priced into the bond market. In our view, this leaves risks skewed to the upside for bond yields, which would be supportive for relative returns.

Investment Grade Bonds: Underweight

- Investment grade bonds were mixed last quarter, with rising yields offset by a narrowing in credit spreads.
- Although leading economic indicators point to a stabilisation in the deteriorating growth outlook, current valuations look expensive.

Developed Government Bonds: Underweight

- Yields have moved higher as some of the pessimism priced into bond markets earlier in the year has unwound, with economic data showing some signs of stabilising.
- Despite this, the compensation for assuming interest rate risk still remains low. This means global Treasuries look expensive and have an unattractive risk/reward profile from a tactical standpoint.

Commodities: Neutral

- Tactically, commodities remain an area of low conviction for us.

Glossary

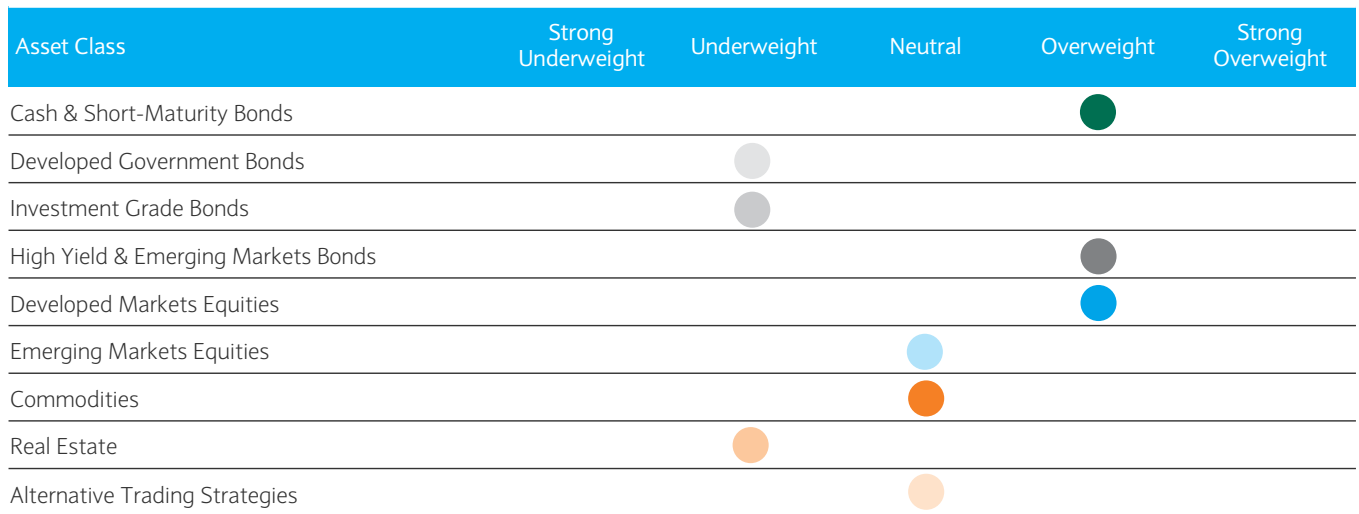
Strategic Asset Allocation (SAA): the long-term view based on our outlook for each asset class

Tactical Asset Allocation (TAA): tactical adjustments relative to our SAA, mainly based on our shorter term (three-to-six month) outlook

Overweight: tactical exposure to a particular asset class which is in excess of our long-term allocation (SAA)

Underweight: tactical exposure to a particular asset class which is less than our long-term allocation (SAA)

FIGURE 1: Tactical asset allocation (as at 29 November 2019)



Fixed Income

- Underweight global Treasuries as a lot of monetary policy easing and bad news has already been priced into the bond market.
- Underweight IG as we see bond yields rising and heightened credit risks at this point.
- Overweight EM bonds as we see healthy fundamentals and an attractive risk-reward profile. Underweight HY as we think valuations are expensive.

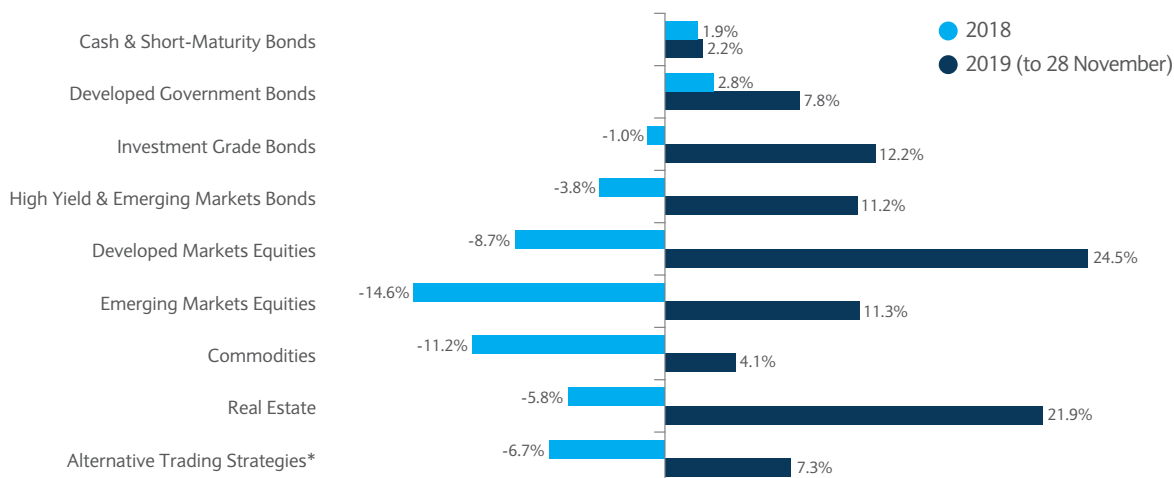
Equities

- Overweight DM equities as data shows tentative signs of a stabilisation in growth, monetary policy remains supportive, and sentiment has room to improve further.
- We are currently neutral on EM equities.

Alternatives

- Underweight Real Estate as a function of our relative view versus Developed Markets Equities. Our research shows relative returns are negatively related to higher bond yields.
- Commodities remain an area of low conviction for us.

FIGURE 2: Total returns across key asset classes

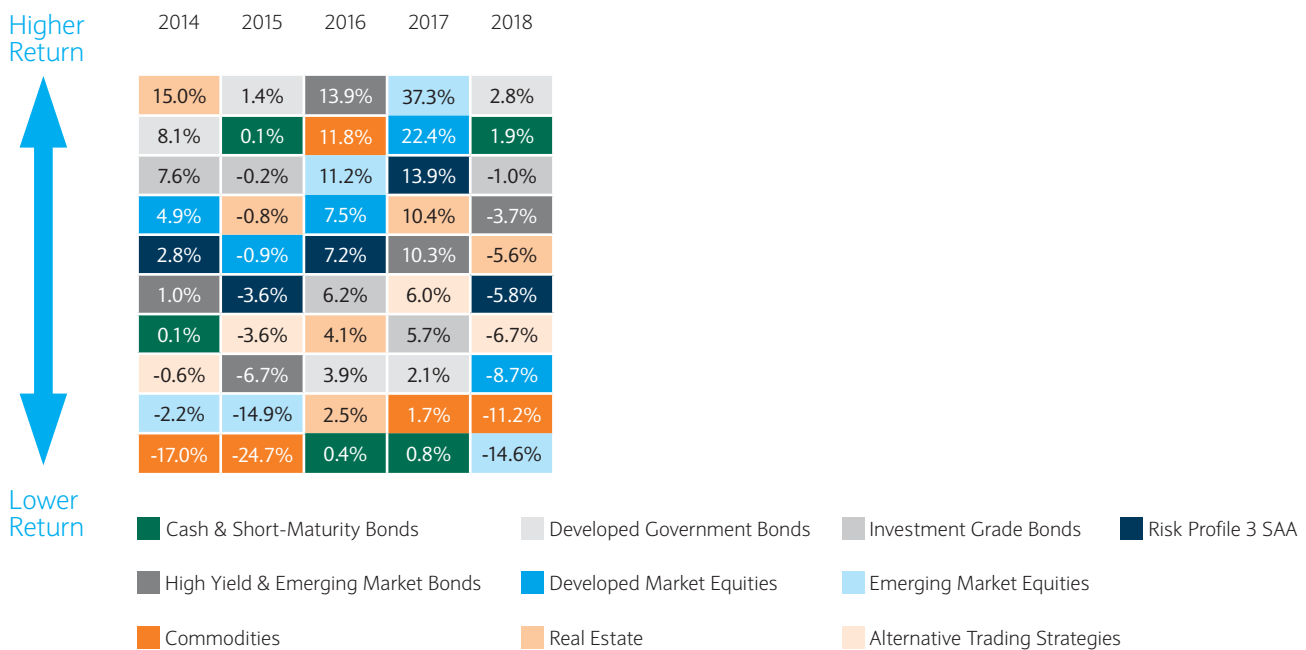


Source: FactSet, Barclays, as at 28 November 2019 (*ATS as at 27 November 2019). Asset classes in USD. For the asset class indices and a table of historical discrete annual performance, please see the [Appendix](#).

Past performance does not guarantee future results.

Appendix

FIGURE 1: Asset class annual returns, 2014-2018



Asset classes in USD and represented by the following indices: Cash & Short Maturity-Bonds, Bloomberg Barclays US Treasury Bills; Developed Government Bonds, Bloomberg Barclays Global Treasury Hgd; Investment Grade Bonds, Bloomberg Barclays Global Agg Corp Hdg; High Yield and Emerging Markets Bonds, ICE BoAML US HY Master II Constrnd (40%), JPM EMBI Global Diversified (30%), JPM GBI-EM Global Diversified (30%) from 1 August 2016, ICE BoAML US HY Master II Constrnd (50%), JPM EMBI Global Diversified (20%), JPM GBI-EM Global Diversified (30%) from 15 January 2018; Developed Markets Equities, MSCI World NR; Emerging Markets Equities, MSCI EM NR; Commodities, Bloomberg Commodity; Real Estate, FTSE EPRA/NAREIT Developed NR; Alternative Trading Strategies (ATS), HFRX Global Hedge Fund. Source: Bloomberg, FactSet, as at 31 December 2018.

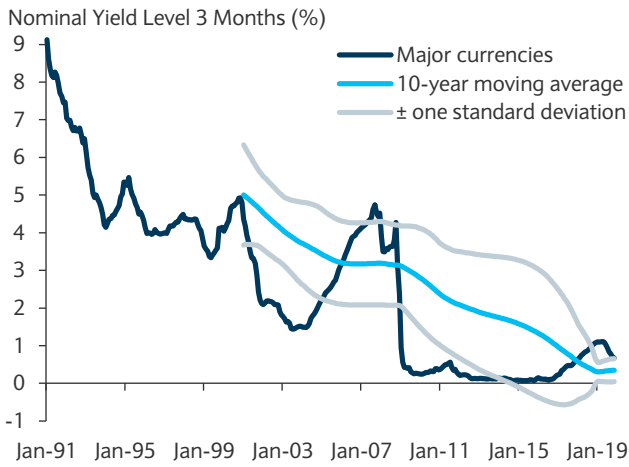
FIGURE 2: MSCI Word Momentum Index

Year	12 Month return
2018	-2.4 %
2017	32.6%
2016	4.8%
2015	4.5%
2014	7.0%

Source: MSCI. Returns in USD.

Interest rates, bond yields, and commodity and equity prices in context*

FIGURE 1: Short-term interest rates



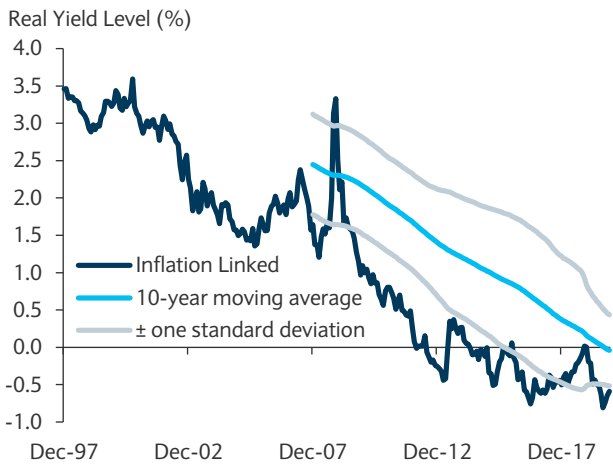
Source: FactSet, Barclays

FIGURE 2: Government bond yields (global)



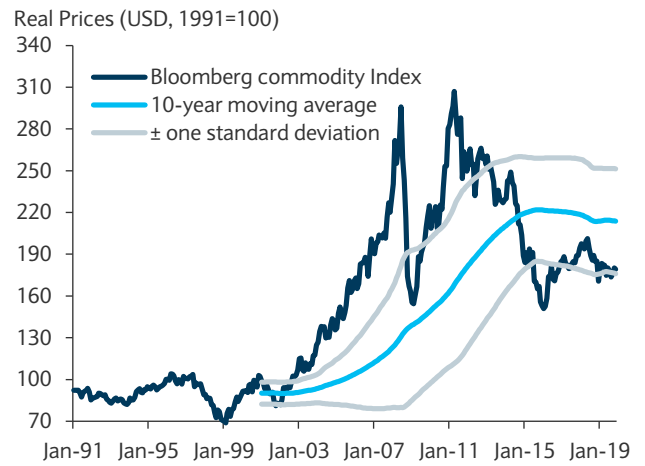
Source: FactSet, Barclays

FIGURE 3: Inflation-linked real bond yields (global)



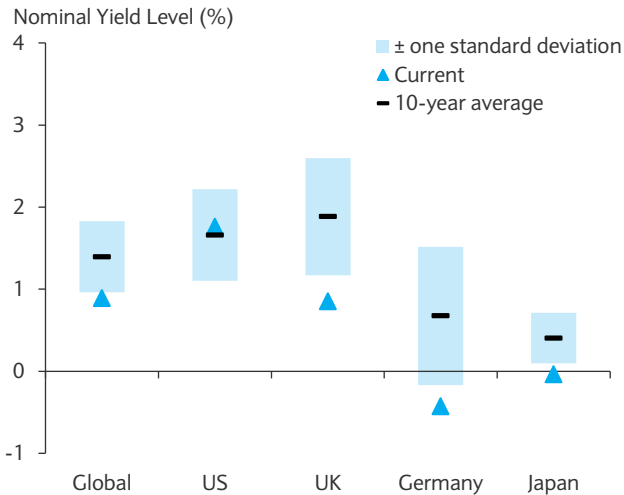
Source: Bank of America Merrill Lynch, FactSet, Barclays

FIGURE 4: Inflation-adjusted spot commodity prices



Source: FactSet, Barclays

FIGURE 5: Government bond yields: selected markets



Source for Figures 5-6: FactSet, Barclays

*Monthly data with final data point as of 28 November 2019.

Past performance does not guarantee future results.

FIGURE 6: Global credit and emerging market yields

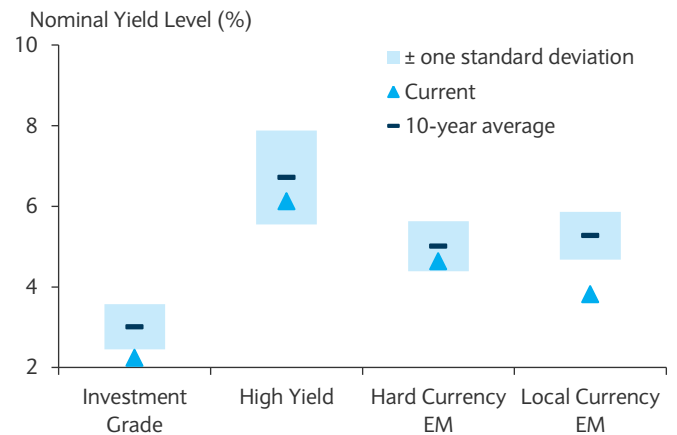


FIGURE 7: Developed stock market, forward PE ratio



FIGURE 8: Emerging stock market, forward PE ratio

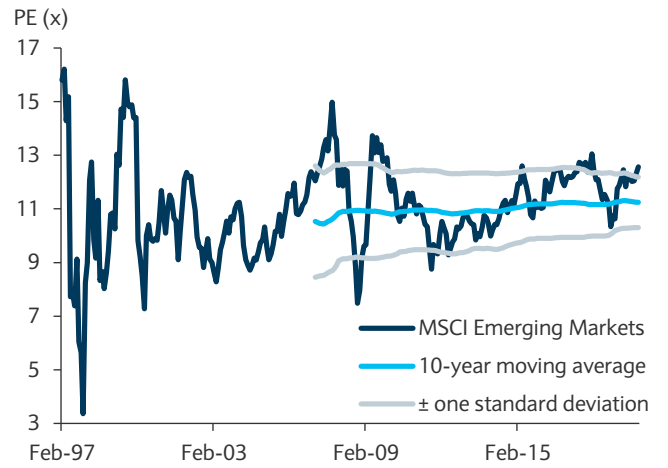


FIGURE 9: Developed world dividend and credit yields

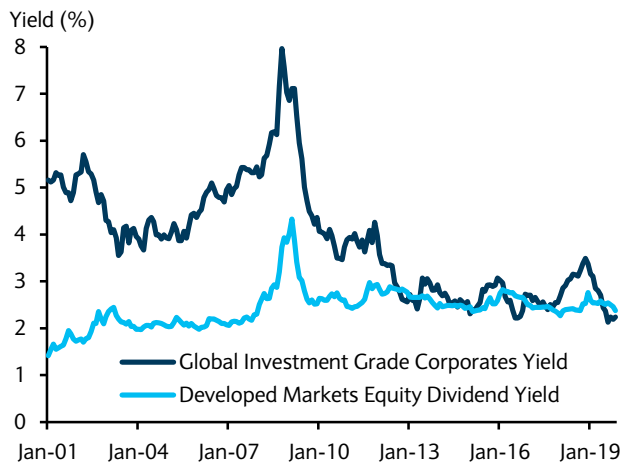


FIGURE 10: Regional quoted-sector profitability

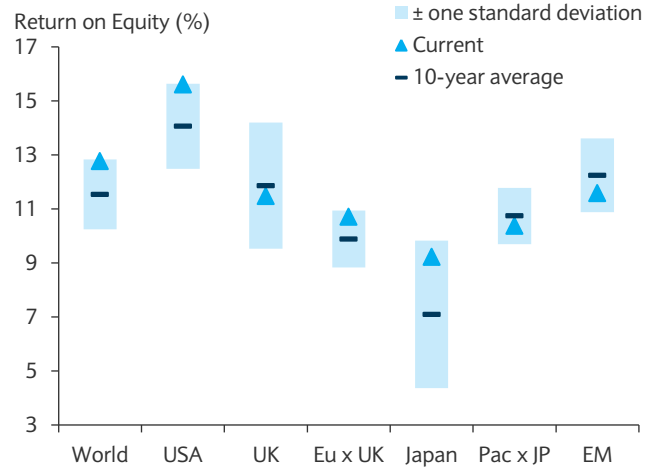


FIGURE 11: Global stock markets: forward PE ratios

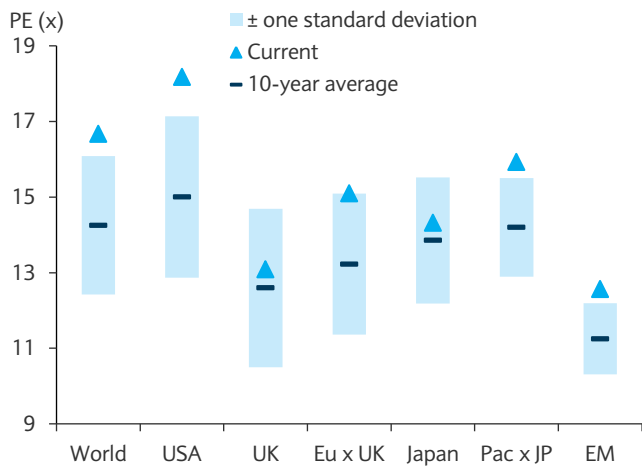
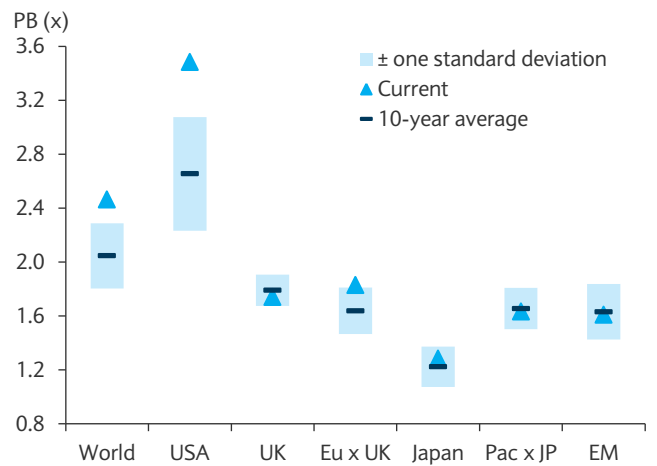


FIGURE 12: Global stock markets: price/book value ratios



All sources on this page: MSCI, FactSet, Barclays.

Past performance does not guarantee future results.

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