L&G Mixed Investment Funds

MONTH IN FOCUS

THE HEADLINES

- **Global presidential club: 'one in one out'?**
- **What will June bring for May?**
- **OPEC extends the cuts but oil slips away**

MARKET OVERVIEW

May showed us that the global presidential club seems to be operating a 'one in one out' policy at the moment. The 'i' was certainly the letter of the month and the markets discussed both 'inauguration' and 'impeachment' with equal enthusiasm.

With Emmanuel Macron sworn in as the new French President, investors' attention soon shifted to the Americas. Up north, President Trump fell into trouble with the FBI as the probe into Russia's involvement in the US elections continued. Down south, corruption allegations in Brazil put Michel Temer's presidency in question.

In the UK, May was on everyone's lips. The Prime Minister began the month by striding confidently along the campaign trail before the opinion polls hinted at a gradual closing of the gap between Conservatives and Labour.

Nevertheless the markets responded with a certain degree of poise. Investors seem to be more used to political jitters by now, considering the drama that played out on the political scene over last 12 months. As a result, May was another kind and benevolent month for market participants. Most bond markets saw small gains with the European periphery, in particular Portugal, being the standout performer. As some of European political risks receded, the most notable currency change was the strength in the euro. The pound fell slightly against the US dollar reflecting a softer tone to UK data and more uncertainty around the prospects of the ruling party in the June election. In local terms, most equity markets were somewhat higher, emerging markets outperformed developed markets and defensive sectors (e.g. utilities) were ahead of cyclicals.

Oil ended up lower despite the OPEC extension of the supply cuts for another nine months. Investors will undoubtedly watch their next decisions very carefully to assess their efficacy in terms of supporting the oil price.

FUND PERFORMANCE REVIEW

Funds recorded positive returns in May. Weaker sterling, in particular against euro, supported returns on large-cap UK equities that generate a portion of their overseas earnings in Europe. The Mixed Investment Funds have had a positive bias to sterling since early October when the currency level constituted an interesting entry point on valuation grounds. As it moved back up in April (see the Chart of the Month below), we then lowered our sterling overweight in the funds. Higher exposure to overseas currencies was a positive contribution to the funds when they ended the month relatively stronger.

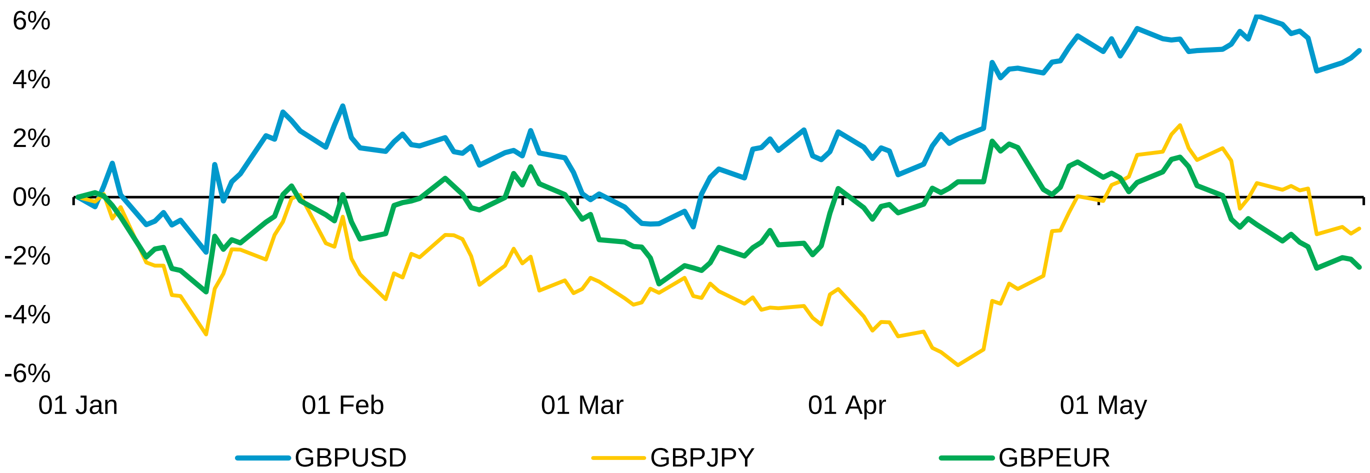
In terms of underlying investments, all major asset classes added to the overall fund performance with only energy stocks detracting from the overall fund return in May. Higher risk funds outperformed lower risk funds as investors' appetite continued to support returns on riskier assets in our portfolios such as equities and emerging market debt.

RECENT PORTFOLIO CHANGES

↑ US DOLLAR

↓ POUND STERLING

CHART OF THE MONTH – 2017: CURRENCY MOVE IN THE LIGHT OF POLITICAL RISK



Source: Bloomberg L.P. LGIM

Legal & General INVESTMENT MANAGEMENT

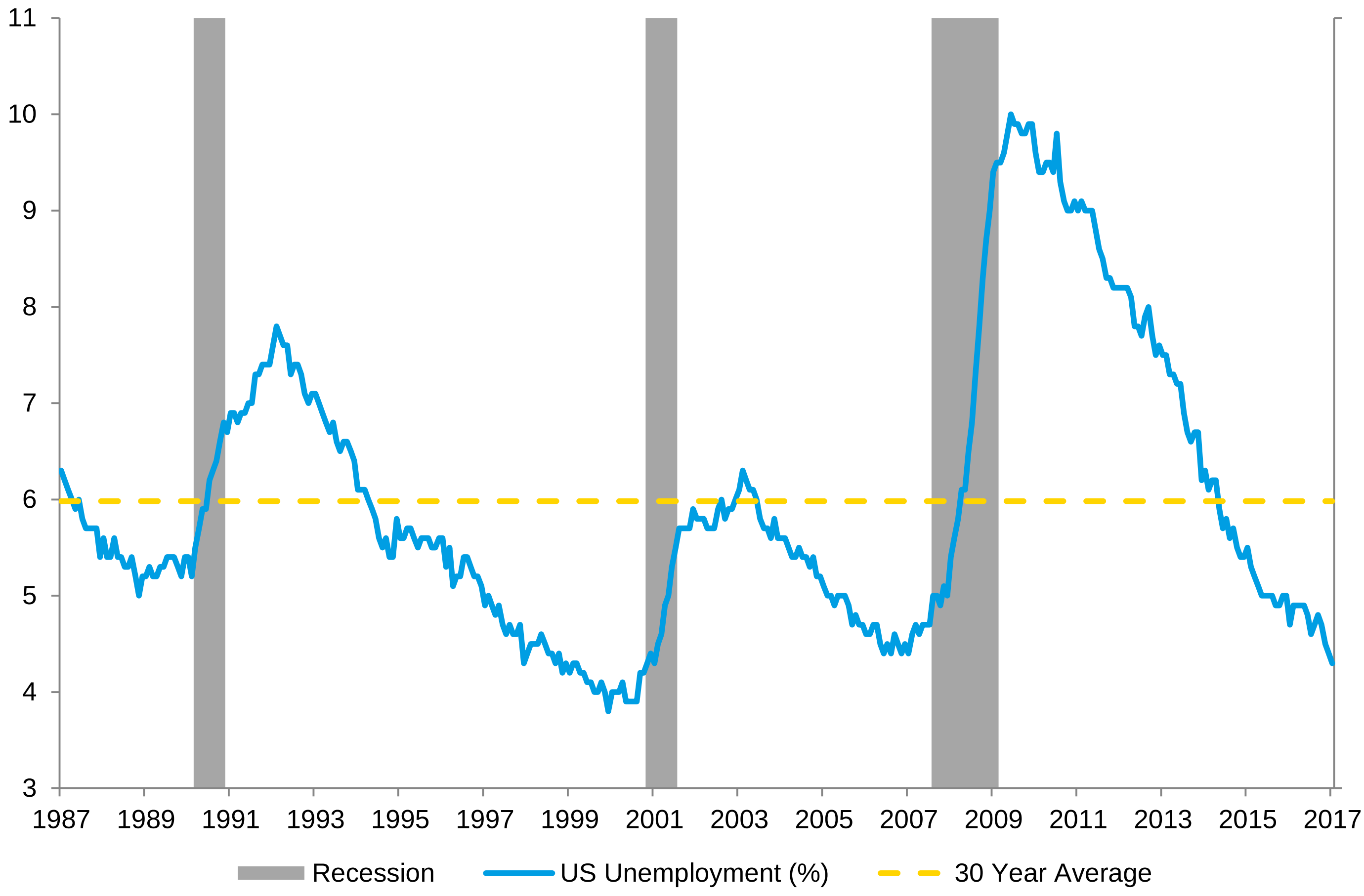
MARKET OUTLOOK

We have a positive view on global growth and this typically should provide a tailwind to the performance of risk assets over the year ahead. However, we are wary that markets haven't fully considered the medium-term headwinds to growth, or to the risks. The market enthusiasm behind President Trump's proposed policies may run out of steam if he can't deliver, or indeed if he does deliver what the market believes to be the wrong policies. Furthermore, we have material political and economic risks to be wary of, including European politics in the medium term (as risks in France diminished, the situation in Italy and Greece is still far from certain) and Chinese debt levels over the longer term. We have therefore taken a more cautious view on certain asset classes whose recent performance has been exceptionally strong, in particular high yield debt and some of the more cyclical sectors. In our view, sectors which have lost favour amongst investors, such as energy and infrastructure, offer better opportunities.

THE LONG TERM VIEW – JOBS APLENTY BUT WHERE'S THE WAGE GROWTH?

The unemployment level in the US continues to fall. The latest data shows unemployment under 4.5%, the lowest level in the current economic cycle and only eclipsed by the lows of 1999-2001 in the past 30 years. This data is consistent with the idea that we are approaching the later phase of the US economic cycle. But while labour markets are starting to look a bit tight in some ways, there is a part of the picture missing. One of the biggest macroeconomic puzzles today is the lack of wage growth despite an apparent return to full employment in a number of countries. While wage growth has picked up from a low base, wages are clearly running at a weaker pace than many would have forecast a couple of years ago. There are a number of plausible explanations out there, such as demographics changes, a slowdown in productivity, or maybe globalisation, but none are conclusive. There is some uncertainty about how long the puzzle will persist, but we believe that lower unemployment will ultimately result in higher wage growth.

US UNEMPLOYMENT RATE (%)



Source: Bloomberg L.P. LGIM

Important notice