L&G Mixed Investment Funds

MONTH IN FOCUS

THE HEADLINES

- **"Mirror, mirror on the wall…**
- **…who's the best Chair of them all?"**
- **Trump finally finds his answer**

MARKET OVERVIEW

President Trump has mastered the art of dominating news headlines around the world and his search for the new Chairman of the Federal Reserve was no different. Although it concluded two days after the month's end, the candidates were dancing in and out of the White House in the game of musical Fed chairs throughout October, keeping investors on their toes.

The final choice (spoiler alert) of current Fed Governor and trained lawyer Jerome Powell provided sufficient perception of policy continuity to calm markets. With the top position filled, we continue to monitor future board appointments to decipher who may drive the economic debate in the bank.

Behind all the flashing headlines, global markets have progressively moved to price in a scenario of above-trend economic growth and below-trend inflation. This trend towards a 'goldilocks' environment gave equity investors more reasons to celebrate in October. In particular, those investing in Japanese equities, which gained over 5% in local terms, were heartened by signs of global growth and the re-election of the government of the current Prime Minister Shinzo Abe.

The rest of Asia-Pacific and emerging markets were not far behind. The push by the Catalan government towards independence had little impact on markets. Instead, it was overshadowed by the growing optimism about the progress towards tax cuts in the US, keeping US equity returns in the positive territory for the twelfth month in a row.

FUND PERFORMANCE REVIEW

All funds recorded positive returns in October with higher risk funds outperforming the lower risk funds which are more fixed income-heavy. Year-to-date performance also follows the same pattern as equity markets have been the best performing assets over the past ten months.

Returns across equity markets were broad based over the month with all markets contributing positively. Real Estate Investment Trusts (REITs) also gained over the month, but the year-to-date performance has been disappointing, with returns much lower than would be expected in an environment where equity markets have done particularly well.

We maintain our position in Indian equities that we introduced in early 2017. This was one of the top performers in October as stocks surged on the back of the bank recapitalisation program announced by the government

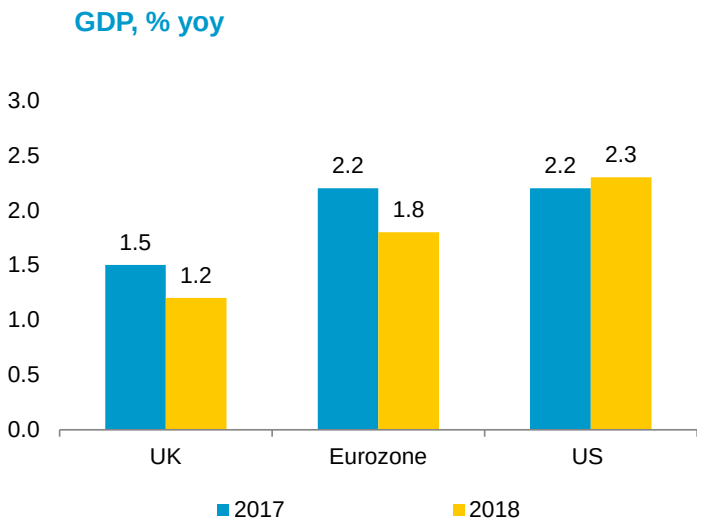
High yield and investment grade corporate bonds also helped fund performance in October as spreads narrowed slightly, but emerging market debt was a drag on performance. Finally, bonds issued by peripheral EU markets like Spain, Italy and Portugal, which we hold in the funds, performed well as ratings agencies upgraded their view on these economies.

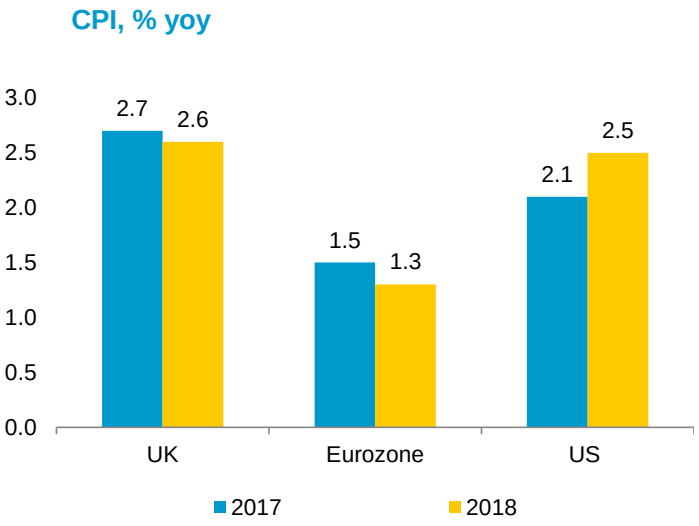
RECENT PORTFOLIO CHANGES

↑ EMERGING MARKET LOCAL CURRENCY DEBT

↓ INVESTMENT GRADE CORPORATE BONDS

CHART OF THE MONTH – "GOLDILOCKS": LGIM GROWTH AND INFLATION FORECASTS





Source: LGIM

Legal & General
INVESTMENT MANAGEMENT

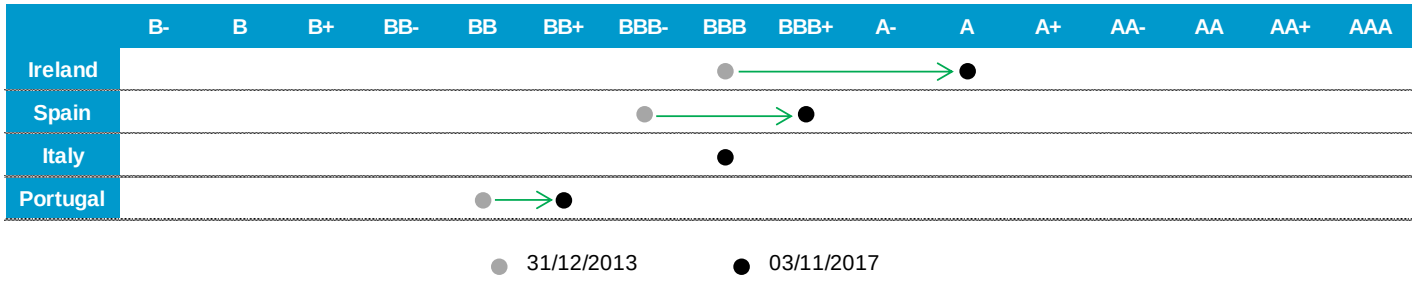
MARKET OUTLOOK

As a result of upgrading our medium-tem view on equities from cautious to neutral, we are looking to increase risk across the board through additions to our equity exposure where we see value. We believe the level of systemic risk has slightly improved. Despite the ever-present short-term risks that bring uncertainty, we think it seems unlikely for any of them to escalate into a disaster at the moment or that these are at least appropriately priced into markets. Such risks include, for example, the US debt ceiling, geopolitical tensions with North Korea and the Chinese economy. Whilst we remain negative on emerging market equities relative to developed markets, we have upgraded our view on local currency-denominated emerging market debt and local currencies on the basis of the favourable economic backdrop and limited recession probability. We retain our positive view on emerging hard currency-denominated debt. In contrast, we are still negative on the prospects for investment grade debt and high yield given the tightness of credit spreads. We have downgraded our general outlook on global fixed income and remain positioned for strength in the US dollar.

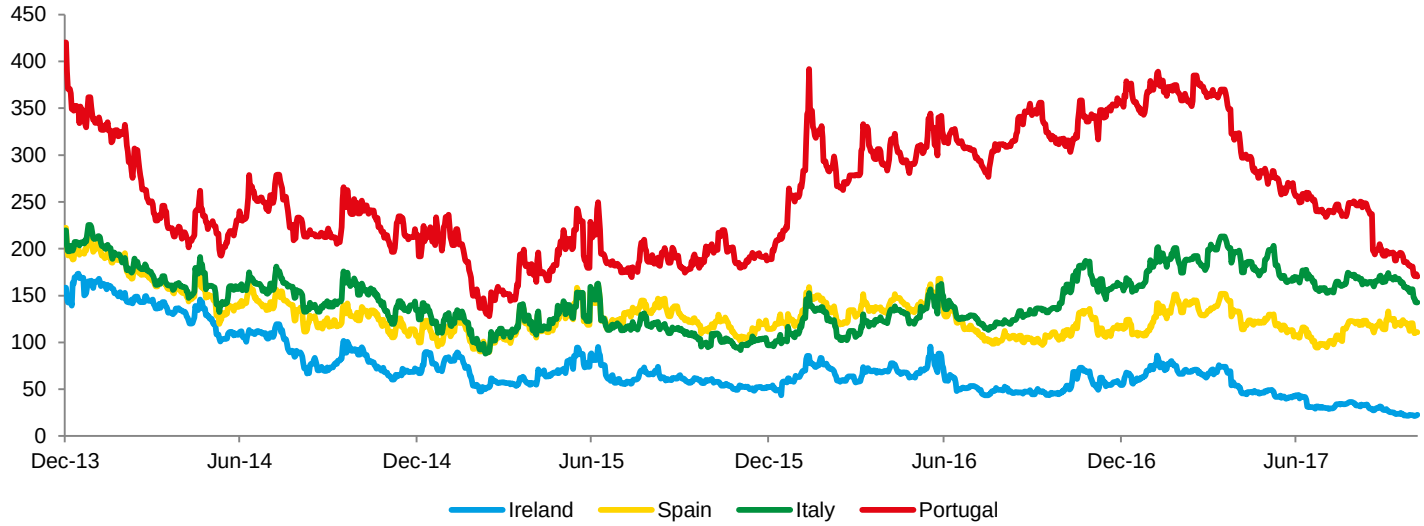
DEBT CHECK: EUROPEAN PERIPHERAL DEBT

In the years that followed the great financial crisis of 2008/2009, Europe entered its own sovereign debt crisis, with many countries in Europe suffering from collapsing financial institutions, rising government debt and downgraded ratings by agencies like Moody's, S&P and Fitch. As a result they saw rising costs for governments issuing new debt relative to safer neighbours like Germany. This translates to a higher spread on their bonds. More recently, we are seeing a renaissance for these economies after years of austerity and high unemployment, growth is returning and the ratings agencies have been back starting to upgrade their assessments. Most recently, Portugal was upgraded to investment grade status (BBB- or better) by S&P, with other agencies likely to follow over time, triggering a significant uptick in the value of its bonds, or a decrease in its spread. The Mixed Investment Funds are benefiting from these upgrades through their tactical holdings of peripheral debt, especially in the lower risk, more fixed income heavy portfolios which have a higher allocation than high risk, more equity dominated funds.

EU PERIPHERAL DEBT RATINGS – AVERAGE OF MOODY'S, S&P AND FITCH.



EU PERIPHERAL DEBT SPREADS OVER GERMAN BUNDS, 10 YEAR BONDS



Source: Bloomberg L.P. LGIM