25th January 2016

Our Ref: MK/RD/Q415

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Dear xxxxxxxxx

Re: MPL Portfolio Valuation – xxxxxx.xxxx

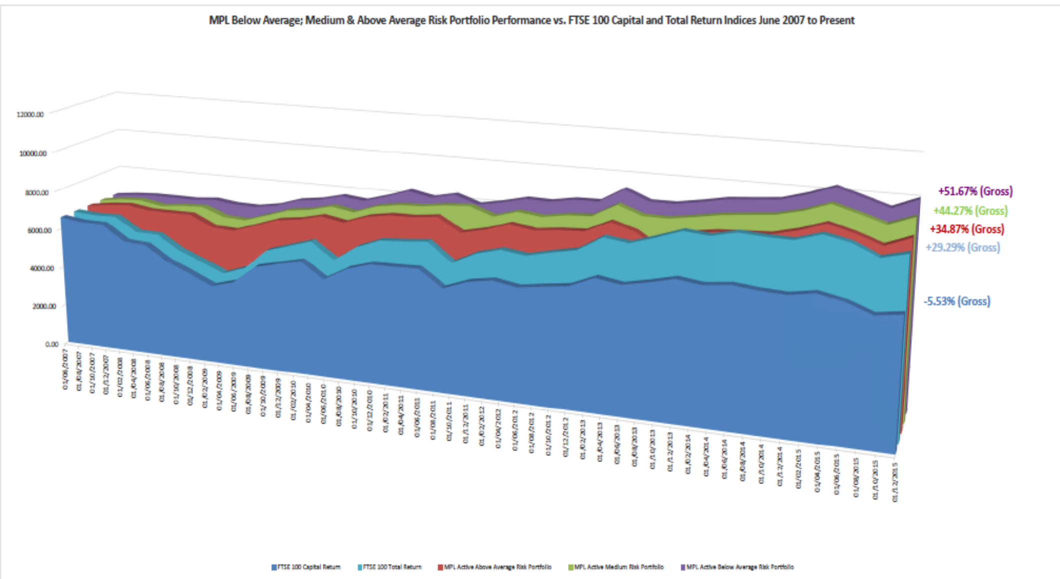
<u>Findings</u>

In the period from 1st October 2015 to 31st December 2015, the portfolio has risen x.xx% in comparison to an increase of 2.98% in the FTSE 100 Index* and a fall in the UK Gilt All Stocks Index* of 1.69%.

In the period from 1st January 2015 to the 31st December 2015, the portfolio has risen x.xx% in comparison to a fall in the FTSE 100 Index* of 4.93% and an increase in the UK Gilt All Stocks Index* of 0.66%.

Your current risk profile is xxxxxxx, and we would be grateful if you would complete the attached questionnaire and return in the enclosed pre-paid envelope at your earliest convenience, to ensure that your portfolio continues to be managed in line with your risk requirements. Should you wish to discuss further then please don't hesitate to contact your adviser.

Whilst the positive return in quarter four of 2015 enabled portfolios to recover from the negative period experienced in quarters two and three, it has been a rather benign 2015 characterised by a high level of volatility in financial markets, and a rather flat return in our client portfolios versus a negative return in UK equity markets.

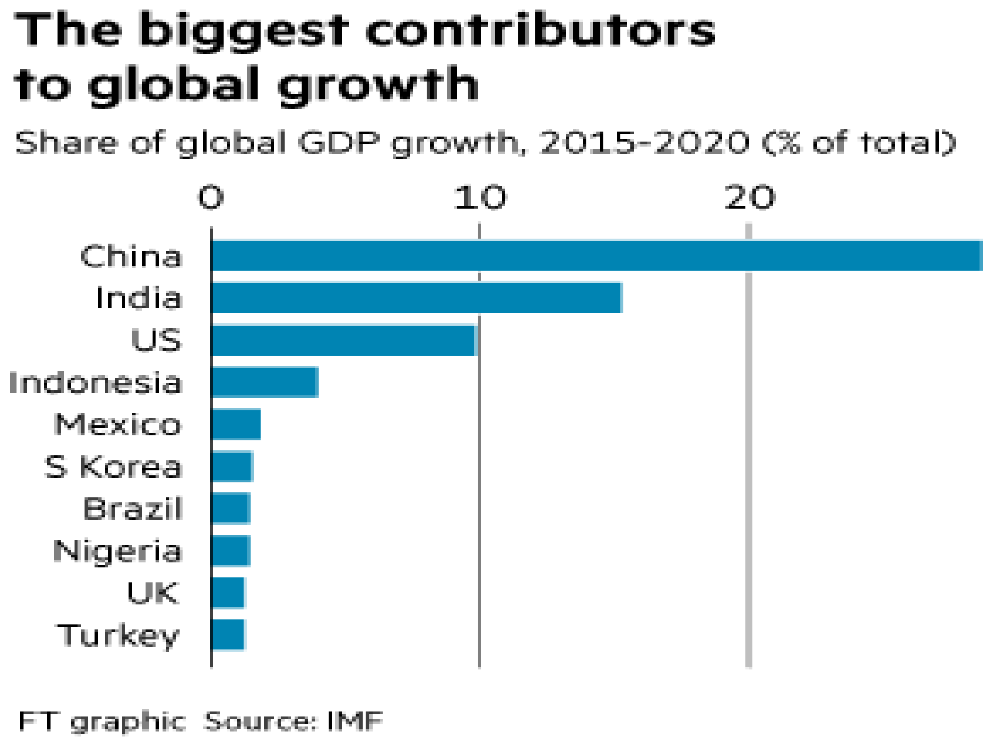


The value of investments and any income will fluctuate (this may partly be the result of foreign exchange rate fluctuations), and investors may not get back the full amount invested. Past performance is not a guide to future returns.

2016 appears to have picked up where we left off at the end of quarter three of 2015, with China, oil and US rates at the forefront of investor concern, with the European economy and the British referendum on continued EU membership in the background for now.

Why the fuss about China?

After three decades of super-charged growth, China recently accounted for 16 per cent of world output and almost 30 per cent of expected global growth last year, up from 13 percent a decade earlier, according to the World Bank. "The key risk to global growth is a larger-than-expected slowdown in China," according to the Organisation for Economic Co-operation and Development in a recent statement.



By last October China's economic growth dipped to 6.9% annually from July through September, while 2015 quarter 4 growth came in at 6.8% - its slowest pace in more than six years, although these are still growth levels most industrialised states and indeed many developing states can merely aspire to.

Growth in China's gross domestic product has decelerated for four straight years and will likely keep slowing through 2017, according to the International Monetary Fund (IMF). However, one has to bear in mind the size of China's economy at circa $10 trillion and the difficulty of both sustaining and managing high growth rates within the world's second-largest economy without triggering inflation, supply chain issues and other ills. China's year-end and Party-directed Central Economic Work Conference at the end of 2015 agreed an implicit 6.5% economic growth target, facilitated and supported by ongoing accommodative fiscal and monetary policies – this is a pragmatic growth target although many dispute the official Chinese GDP figures in any event.

In July 2015, the IMF stated that "China's deceleration is having a bigger-than-expected impact on the global economy". This is one reason the IMF lowered its forecast for global growth in 2015 to 3.1%, which would be the weakest rate since the recession year of 2009 and down from a previous estimate of 3.3%.

The devaluation of the Chinese Currency "the Yuan"

In recent days Chinese policy makers have allowed the Yuan to weaken a further 0.8% against the US dollar, which is the largest slide over such a period since August 2015, when the authorities first started to devalue the currency and triggered a global market sell-off. Devaluation may be seen as a distress signal from Beijing policymakers that the world's second-largest economy may be far weaker than the 7% a year growth that official figures have suggested. However it can also be argued that the Yuan had to be devalued against the very strong Dollar (to which it had in fact been pegged) in order for the Chinese currency to retain some competitiveness on the global stage. Furthermore, it could be considered a natural step in order to commence the process of transitioning the Yuan into a truly convertible currency, given it was awarded in late 2015 the status of a currency now recognised as a reserve currency and a member of the IMF's SDR (Special Drawing Rights) basket of reserve currencies.

A negative point that needs to be made is that a weaker Yuan is feared to drive the global economy closer to recession, as the purchasing power on the global stage of the world's second largest economy deteriorates every time the currency is devalued.

Currency Wars?

Beijing's move to devalue was ostensibly offered as part of measures to open up its financial system to the world, and allow foreign exchange markets more say over the value of the Yuan – something America has long demanded as evidence that China is genuinely open to financial reform. Whilst the move was welcomed by the IMF, Republican Senator and former US trade representative Rob Portman accused China of trying to gain an unfair trade advantage over America through the oft-made charge of "currency manipulation" – just as the US was negotiating an important trade agreement, the Trans-Pacific Partnership, with a number of China's rivals, including Japan.

Chinese Debt

Private, non-financial debt reached 160% of gross domestic product in the US in 2007 and almost 200% in the UK before households and companies tightened their belts. China has already surpassed these levels, according to data from the Bank for International Settlements. Since 2008-9, the growth in Chinese private, non-financial debt has risen from approximately 100% to 250% of gross domestic product (or GDP which is the monetary value of all finished goods and services produced within a country's borders in a specific time period).

With growth slowing and perhaps more rapidly than official Chinese statistics show, the nation's ability to service and sustain such debt can be called in to question. Defaults and huge losses could conceivably follow, sparking a vicious circle of fragility and bankruptcy in the financial sector, a squeeze on credit and yet weaker economic prospects. Whilst the rest of the world would not be able to ignore such a crisis, given China's size, trade links and financial connections with other countries, it does also appear that Beijing has a plan to deal with debt issues, especially at local government level - here many of the outstanding debts will be securitised and delivered into the nation's savings markets. Additionally China has vast reserves available to it, but it is lingering uncertainty over the country's debts and growth rates that has led to investor nervousness.

Interest Rates

Central bankers in the US and the UK have been issuing warnings for months that with growth strengthening they are preparing to start normalising interest rates – reversing the emergency cuts made in the global credit crunch. However, if the cheaper Yuan going forward continues to cut the price of imports and possibly even import deflation into the West, then this will further undermine inflationary forces and thereby delay rate rises. This was likely a key reason behind Mark Carney’s recent backtracking on the prospects for UK base rates rising any time soon – we now anticipate that UK rates may only rise for the first time either late in 2016, or more likely not until 2017.

Disinflation

In the short to medium term therefore, these lower-than-expected borrowing costs will benefit indebted Western consumers, including Britain’s mortgage-holders. But some analysts continue to fear that China’s decision to devalue is evidence of a deep-seated lack of demand in the global economy, which will unleash deflation or at least disinflation. Whilst this is possible, we believe that China suffers from a simple excess in industrial and manufacturing capacity following its rapid economic growth and urbanisation rates of recent decades, and what must now be viewed as a partial slowing and maturing of its now very large economy.

Natural Resources

As its economy surged in those decades, China consumed disproportionate amounts of the world's resources. Nearly half the copper, 54% of aluminium, 50% of nickel and 45% of steel went into increasing Chinese GDP, according to the World Economic Forum. China’s apparently insatiable demand for natural resources has been a key factor supporting the price of oil and other commodities in recent years, thus fears that China’s economy is in trouble tend to undermine oil prices at a time when fall-out amongst feuding OPEC members, and the advent of US shale production are already leading to an excess in supply. The plus-side of this is reduced energy costs for consumers across the globe, and this in effect is equivalent to further extensive tax cuts or monetary loosening, and should work to the distinct advantage of consumers and the global economy.

US Interest Rates

The US as the world’s most important economy increased interest rates for the first time in a decade, in December 2015. This reflects the maturity of its economic recovery and its success in generating employment growth, with US unemployment rates now having fallen to historically normal levels. Janet Yellen as Federal Reserve chairperson has now made it clear that she sees strong prospects when she looks at the US economy, as do her colleagues on the Federal Open Market Committee (FOMC), which sets interest rates.

Yellen has explained that the decision not to raise rates in September last year reflected increased uncertainty in the global economy at that time, and was not a sign of perceived weakness within the US economy. She stated in September 2015 that FOMC members anticipated that achieving the conditions of maximum employment and stable inflation would likely entail “an initial increase in the federal funds rate later this year, followed by a gradual pace of tightening.” Subsequent to these comments, in December 2015 the FOMC raised short-term interest rates with FOMC officials citing that the US economy was strong enough to keep growing with a little less help from the Federal Reserve.

The key point here is that the FOMC, having now commenced the rate normalisation process, is committed to merely a gentle pace of tightening from this point.

Europe

In Europe many economic indicators are now looking more positive than at any time since the Eurozone crisis started in 2011. Greece and probably none of the other Euro-peripheral nations any longer have the power to derail the rest of the single currency area, and European consumers are enjoying a rare increase in their net incomes following the decline in commodity prices across the world. Furthermore, additional monetary and fiscal policy measures are available to react to slower global growth prospects, with further stimulus likely to be effected in coming months.

The UK's EU Referendum

Touching briefly for now on this situation, a significant factor to be considered in determining the outlook for future UK investment is the government's decision to hold a referendum on EU membership. This does constitute some risk to growth, as the uncertainty that the referendum will create will make companies reluctant to invest more into the UK until the result of the referendum is known. It is encouraging that David Cameron seems determined to get the referendum out of the way sooner rather than later, with June of this year now touted as a potential date.

Hence market participants will no doubt begin to discount the prospect of this forthcoming uncertainty into the value of all UK asset classes reliant upon a stable UK economic environment, with this likely to have already proved a factor in pricing UK equities in recent weeks, and also probably of the Pound Sterling.

We will continue to keep an eye on earnings and credit expectations for companies in the current climate, as we believe that those which are directly related to the European, UK and US consumer will benefit from a mixture of low borrowing, energy and oil costs, increased consumer wages and an improved employment outlook, which together should lead to improved margins and hence higher earnings through 2016.

With kind regards

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*figures courtesy of Bloomberg