29th July 2016

Our Ref: MK/RD/Q22016

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Dear xxxxxxxxx

Re: MPL Portfolio Valuation – xxxxxx.xxxx

Your current risk profile is xxxxxxx, Should you wish to discuss further then please don't hesitate to contact your adviser.

The Decided

On 23rd June 2016, the UK voting public decided to leave the European Union and despite a few days of volatility in global financial markets, the initial pullback was perceived by many as a short term buying opportunity.

Why?

Various reasons can be given for this, the most unconstructive of which was the thought that whilst the UK has voted to leave the EU, there is no automatic triggering of Article 50 of the Lisbon Treaty, which article initiates the exit process. The quick succession to Tory party leader and prime ministership of Theresa May has put paid to any idea of an early commencement of this process, kicking the exit negotiation question into 2017 and thereby restoring some immediate stability to financial markets as political risk has subsided.

Other reasons for this current market stability include the uncertainty of the result being removed, and also the fact that companies within the FTSE 100 and 250 Indices that have exposure to US Dollar and other overseas 'hard currency' earnings stand to benefit from the fall in Sterling which was the immediate response to the Brexit vote. A further reason of at least equal importance was the statement by bank of England Governor Mark Carney on the day following the historic vote, and to the effect that the Bank stands to do basically 'whatever it takes' to protect the UK economy from negative fallout from the vote to leave the EU. Carney's statement has huge gravitas and thereby perhaps the most importance when determining why the UK markets have stabilised following the vote, precisely because of the potential future impact of further monetary easing by the Bank of England Monetary Policy Committee (MPC).

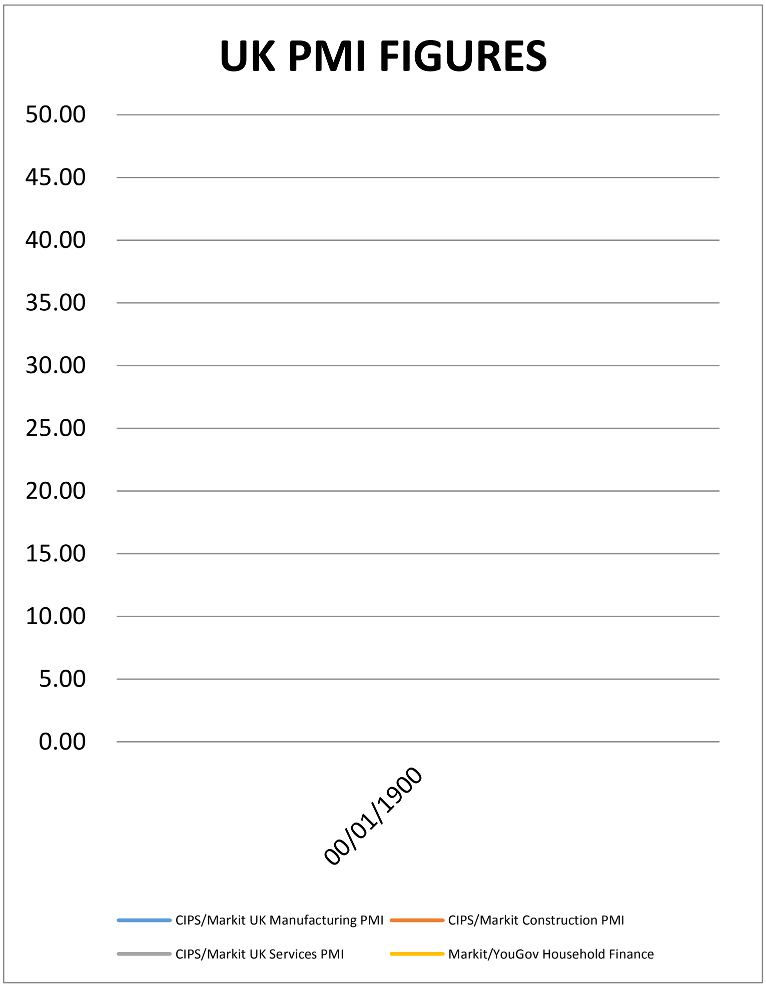
The UK economy

In short and due to the reasons outlined above, nothing particular will happen to the UK economy and markets overnight, however there remains the distinct potential that the UK economy will fall into recession at some point over the coming three quarters. We have had in the latter part of July some Purchasing Managers Index (PMI) figures for June which give us some cause for concern, these figures effectively indicating that the economy is starting to falter as a direct result of the Brexit vote. Whilst the most recently announced GDP figures for Q2 of this year were slightly better at +0.6% rather than the 0.4-0.5% growth widely expected, this positivity reflected the run-up period to the referendum when the likelihood of a Remain vote was the more widely-held perception, whereas the forward-looking PMI figure gives an indication of what future conditions are likely to be.

The UK economy as measured by Gross Domestic Product (GDP) is a function amongst other things of: the Personal Consumption Expenditure; Gross Private Domestic Expenditure; Exports and Imports of Goods and Services; and Government Consumption Expenditures and Gross Investment.

As GDP figures are only produced once every three months, leading indicators such as the PMIs – which are monthly economic surveys of many companies and government organisations in many different segments within the UK economy - help to give us some indication of what to expect going forward, and it is these PMIs which currently give us cause for concern about the UK economy.

UK PMIs for Construction, Manufacturing, Services, Government Expenditure and Household Finances for the month of June 2016.



Source: Bloomberg

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.

A PMI reading of 50 or higher generally indicates that an industry is expanding; if the manufacturing sector for example is expanding, then the general economy should be doing likewise. Over the past two years however, the rate of expansion in the manufacturing, construction and services industries has been quite gradually falling towards a rate of contraction. Within the last three months, the Construction sector's output fell at a faster pace, recording its weakest level of performance in seven years.

June PMI data signalled a steep decline in residential building and a reduction in commercial work, this downturn in business activity being linked to uncertainty ahead of the EU referendum.

Lower levels of intended activity were reflected in deteriorating order books and a corresponding lack of new contracts to replace completed projects. A number of firms noted a reluctance among clients to commence new contracts in the run-up to the EU referendum, alongside uncertainty about the wider economic outlook.

Construction firms in particular have responded to the deterioration in client demand by cutting back on materials input buying, and exercising greater caution in terms of staff recruitment. Consequently, it may be that the result of the EU referendum will hit construction spending decisions for some time to come. Similar issues are being reported in the services sector, where uncertainty linked to the EU referendum has led to postponed decision-making and /or cancelled orders from customers.

The Manufacturing sector has bucked this trend however, as production and new order volumes increased ahead of the referendum result, buoyed by a pick-up in the UK's export business based on the new competitiveness of Sterling on the global stage. However, there is a clear risk that ongoing uncertainty regarding the UK's future trading relationships will have at least some short term negative impact on the manufacturing sector.

All of these factors point towards less favourable UK GDP readings going forward, no doubt with the prospect of recession being mentioned in relation to these readings. But the EU referendum outcome and any negative GDP readings flowing from that may well prompt the Bank of England to act later at some point in the year; one should not attribute the Bank's failure to decrease base rates in July to any degree of complacency on the part of Carney and the MPC – rather they were more likely retaining what monetary ammunition they do have available for when it is most likely to be needed, later this year. All of this leaves us with an interesting investment scenario.

<u>Market Review - Equities</u>

Just prior to the EU referendum, the MPL investment team increased client holdings of UK equities and corporate bonds, in tandem with a reduction in international equity holdings. Whilst the EU referendum result was largely unexpected, UK equity markets have rallied significantly since the initial volatility experienced in the aftermath of the referendum result.

The outlook for the UK economy is not rosy at present, and in normal cyclical conditions we would hold more defensive equity positions. However, tactically over the next month or so, we will hold our current positions in UK equities as the prospect of further monetary easing from the Bank of England should benefit UK equity markets in general. We note in this regard that the sole 'hawk' on the MPC has now joined the 'doves' in calling for easier monetary conditions, meaning that the MPC will likely be unanimous when it calls for lower rates and / or more quantitative easing (QE).

Not only will an interest rate cut and /or more (QE) make certain equity dividend yields more attractive, the pound may weaken even further against the US Dollar thereby enhancing the earnings of UK companies with US Dollar and other overseas revenues. These two factors should give a further boost to UK equity valuations.

Fixed Interest

As above, whilst we face the prospect of further intervention from the Bank of England, we also have to consider the US Presidential election taking place in November. US equity markets are now considered fairly valued (taking into account expected US corporate earnings for 2016), and will be volatile in the run-up to the election. Considering all of these factors, US sovereign and US corporate bonds may benefit UK investors in this short term period.

As the US dollar may well strengthen against sterling in light of any action from the Bank of England to ease policy, and volatility in US equity markets may trigger a flight of capital to the safety of US bonds in this period, we will shortly be allocating client funds into these areas to take advantage of these factors.

With kind regards

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*figures courtesy of Bloomberg