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J.P.Morgan

Global Asset Allocation
J.P. Morgan Chase Bank NA,
J.P. Morgan Securities Ltd.
Apr 27, 2012

# The J.P. Morgan View

## The paradox of austerity

- **Asset Allocation** — The shallowness of the correction in risk assets and the lack of a convincing reason to go short will likely pull investors back in, creating further upside over coming months.
- **Economics** — Data are tracking a mild deceleration of global growth in Q2, driven by excess inventories. Solid consumption data are telling us this slowdown should be temporary and are setting us up for better growth in H2.
- **Fixed Income** — Flat duration, bearish on Euro area peripherals.
- **Equities** — The reporting season is delivering significant positive surprises in both the US and Europe.
- **Credit** — We move to marketweight EM $ sovereigns overall although NEXGEM sovereigns offer a good investment opportunity.
- **Foreign exchange** — BoJ easing should keep USD/JPY in low 80s.
- **Commodities** — Central bank buying still supporting gold.

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- **Risk markets rebounded** this week on continued good US earnings, a supportive FOMC, and an OK Italian bond auction. The dollar eased modestly in line with its safe-asset image, while bonds are largely unchanged. Global equities remain about 2% below their YTD peak in March.

- Given the news flow this week, which contained a lot of political fireworks from Europe and an upside surprise on US claims, one would have expected risk markets to have traded lower this week. We like to interpret the upmove as supporting our view that the main driver of this year's rally in credit and equities will not be a surplus of good news, but a lack of enough bad news relative to the risks that already priced into markets. To put this into Finance jargon, risk is high, but risk premia are even higher.

- This strategy depends on the **Value** force which we know does not work reliably from week to week, but has to be assessed on a 3-12 month basis. A lot of more tactical players have covered their longs in risk assets recently, on event risk in Europe, and so have many of our product strategists. We understand the reasoning, but also find that most investors retain a positive medium-term view on equities and credit and will thus be looking for point to re-enter the market. Our medium-term strategy, therefore, stays long risk.

- The **prevalence of defensive positions** — in cash and safe debt — are largely due to concerns about US growth, a fiscal gridlock at year end (the so-called "fiscal cliff"), military conflict in the Middle East, the Chinese economy, and Europe. We judge that the sum total of these risks has become less acute, even as it is too much to say that they are fading away. The US continues to

The certifying analyst is indicated by an AC. See page 7 for analyst certification and important legal and regulatory disclosures.

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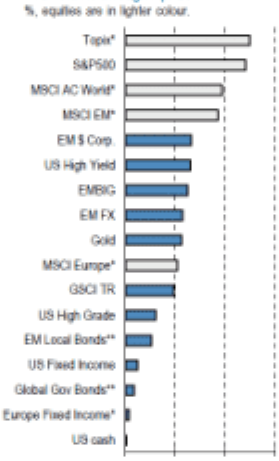
YTD returns through Apr 26
%, equities are in lighter colour.




Source: J.P. Morgan, Bloomberg. Returns in USD. *Local currency. **Hedged into USD. Euro Fixed Income is Iboxx Overall Index. US HG, HY, EMBIG and EM $ Corp are JPM indices. EM FX is ELMI+ in $.

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