From: US GIO <[redacted]>
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Attachments: JPM_View_07.20.2012-pdf.zip
Inline-Images: image003.png

The J.P. Morgan View

Stay short cash

- **Asset Allocation** — Stay short cash. Cash pays near zero; the world is long; central banks are only printing more and are moving towards negative rates. Asset price inflation rules. Cash is the one asset you should underweight.
- **Economics** — US growth lowered again to 1.4% in Q2 and 1.5% in Q3.
- **Fixed Income** — Meager return on cash favors carry trades.
- **Equities** — Next week's flash PMIs will be crucial in assessing our Cyclical vs. Defensive equity sector call. Stay UW for the moment.
- **Credit** — Greater policy room-to-maneuver keeps EM credit attractive.
- **Foreign exchange** — EUR remains the better funding currency.
- **Commodities** — Supply concerns are pushing up oil prices while demand for base metals remains subdued. Stay OW energy vs. base metals.

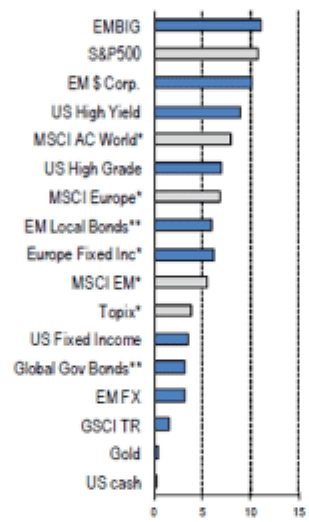
- **Equities are up on the week,** but so are most all asset classes in beating cash despite weak economic activity data. We lowered Q3 growth for the US to 1.5% and world GDP to 1.6% in Q2. Softer data are boosting hopes for more monetary stimulus across the world, reinforcing the **asset price reflation** force that we have been relying on for much of our strategy.
- **Being underweight cash and investing in better-yielding assets remains the best investment strategy.** End investors and corporates remain quite long cash, while continued monetary and easing, through rate cuts and QE, will only add to the world's stock of cash. Clearly cash pays close to nothing in most markets and we now find that some central banks are moving towards paying negative interest rates on reserves. Our economists expect the ECB to make this switch by October (see today's *GDW*), but do not see this Fed moving this far.
- The **overall theme behind our strategy** remains below-trend economic growth pushing inflation lower, restraining profit growth, and inducing further policy easing through QE type actions in DM, and rate cuts in EM. This is a great environment for fixed income, and especially for better yielding bond markets such as EM and credit. Equities benefit from asset reflation also, but in a much less reliable and more volatile fashion. We thus focus our long risk exposures versus cash in EM and credit bond and FX. We have almost no country preferences.
- **Being outright long spread product versus cash** has been the best trade in recent weeks, but runs into the argument that UST and HG yields have again reached new historic lows. The half-life of mean reversion in nominal yields has to be measured in decades, though (chart p. 2). More anecdotally, the lead author of this piece has seen new lows in UST yields at least once every three years in his 25 years at JPMorgan and has learned painfully to pay more attention to momentum than mean reversion in assessing future bond returns. Economic conditions remain good for well-yielding bond markets. Stay long.

See page 7 for analyst certification and important disclosures.

Global Asset Allocation

[redacted]

YTD returns through Jul 19
%, equities are in lighter color.



Source: J.P. Morgan, Bloomberg. See blue box on page 2 for description.