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J.P.Morgan

The J.P. Morgan View

Can the risk rally last?

- **Asset allocation** — Following our re-entry into long US equities vs cash last week, we have further upgraded our risk exposure by being long both equities and credit versus cash and government debt. Given the overnight announcement of Chinese infrastructure spending, even if not all new, we cover our underweight in Chinese equities and in industrial metals and reverse the short in commodity FX.
 - **Economics** — World growth is in a bottoming process, but at well below potential with a return to trend only projected by the middle of next year. Policy easing is restarting in the US, UK, Euro area with monetary policy, and in China with both monetary and fiscal policy.
 - **Fixed Income** — Position on ECB policy though Spanish curve flattens, and Fed QE3 through long end Treasury steepeners.
 - **Equities** — We take profit on our BRIC underweight within EM.
 - **Credit** — We go further up in yield and down in quality in our credit portfolio.
 - **Currencies** — Close defensive trades and go long commodity FX vs Europe.
 - **Commodities** — The newly announced Chinese stimulus makes us take profits on our OW energy vs. base metals trade. We stay long energy on Middle East risk.
- ECB President Mario Draghi's promise yesterday to provide a backstop to EMU members with funding problems, by using Outright Monetary Transactions (OMTs) to keep risk premia low, induced a massive rally in periphery bonds and global equities. Even a weak US jobs report could not rain on this parade. And all this without him actually spending any money as no country yet meets his conditions cleanly. Both US and German equity indices reached new cycle highs. While consistent with our long-risk strategy, these new highs do force us to ask whether the good times for risk assets can last.
- We think the positive environment for risk assets can and will last over the next 3-6 months. And this is not because of a strong economy, as we foresee below potential global growth over the next year and are below consensus expectations. Overall, we continue to see data that signal that world growth is in a bottoming process. With most countries having now reported, global GDP looks to have expanded at a tepid 1.9% pace in 2Q12, 1.3%-point below what would simply be trend. On the back of weak gains in consumer and business spending at mid-year, global IP growth has come to a stand-still. And while things appear to have bottomed with some signals of improvement in consumer spending in July, the soft trajectory of both spending and production through June is expected to hold global GDP growth to another tepid quarter of just 2%.

See page 7 for analyst certification and important disclosures.

Global Asset Allocation
07 September 2012

Global Asset Allocation

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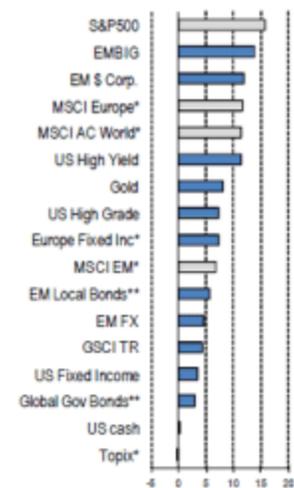
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YTD returns through Sep 6 %, equities are in lighter color.



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

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