From: US GIO <[redacted]>
To: Undisclosed recipients:;
Subject: JPM View 09.21.2012
Date: Fri, 21 Sep 2012 21:21:09 +0000
Attachments: JPM_View_09.21.2012-pdf.zip
Inline-Images: image003.png

J.P.Morgan

Global Asset Allocation
21 September 2012

The J.P. Morgan View

Weak economy vs. strong liquidity. Who wins?

- **Asset allocation** — Strong liquidity, heavy supply of safe assets, high risk premia, defensive positioning by end investors, and a QE focus on reducing downside risk are not technicals but are true fundamental drivers of the risk rally that trump weak economic growth, in our view.
- **Economics** — Q3 global growth remains as soft as Q2, confirming bottoming process, but not yet a rebound. Only rising order/inventory ratios and rallying markets hint at rebound into Q4, we believe. We nudge up 2013 Euro area growth from 0.2% to 0.3% on improved financial conditions.
- **Fixed Income** —Position on wider swap spreads in Treasuries, Bunds and UK.
- **Equities** — Stay long value stocks in Europe, commodity sectors globally, US-housing-sensitive sectors within the US, and US against EM.
- **Credit** — Stay long credit spreads across the US HY and EM sovereigns and corporates and we expect further spread compression.
- **Currencies** — New FX forecasts, with weaker dollar into year-end.
- **Commodities** — We think agriculture prices have peaked and will move lower from here. Open a short in the GSCI agriculture index.

- **Markets took a breather this week, after last week's fireworks,** with equities and credit largely flat, and bonds yields and commodities down. It was a quiet week for data, but what we got was on the softer side. We continue to think global growth is bottoming, but the evidence so far confirms only that growth has come down and that Q3 seems equally soft as Q2. There seems no real evidence yet of a rebound in growth. All we have is a rise in orders relative to inventories in flash PMIs, a rise in confidence, & surging financial asset prices.
- The weak economic data of the past two years and rising asset prices have created a conundrum to investors on what they should really follow -- **the weak fundamentals or the good "technicals"**? We have argued here frequently that liquidity driven asset reflation in a market with high risk premia and defensive positions trumps weak economic growth, as long as the latter does not deteriorate into recession. Hence, we have chosen to remain long risk assets despite repeated downgrades to economic growth projections. We like to make clear though, that these so-called technicals are to us very fundamental and are not as short term in nature as many would suspect. And this for three reasons.
- For one, the **relative supply and demand** for financial assets is not a mere short-term technical but is based on the first fundamental law of economics, which is that of supply and demand. Government supply of government debt and cash is many times the supply (net issuance) of corporate debt and equities. Hence the latter, scarcer corporate securities should rise in price against the much more abundant supply of government liabilities (high-powered money and government debt). This force is not a short-term technical impact, but in fact works more slowly and profoundly.

Global Asset Allocation

Jan Loeys AC
(1-212) 834-5874
[redacted]
JPMorgan Chase Bank NA

John Normand
[redacted]
J.P. Morgan Securities plc

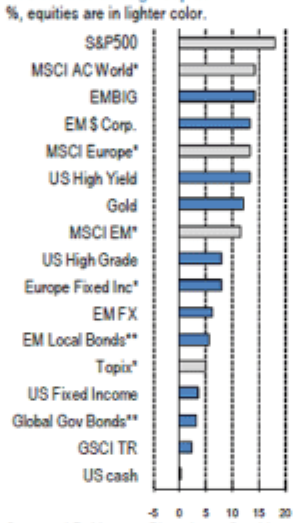
Nikolaos Panigirtzoglou
[redacted]
J.P. Morgan Securities plc

Seamus Mac Gorain
[redacted]
J.P. Morgan Securities plc

Matthew Lehmann
[redacted]
J.P. Morgan Securities plc

Leo Evans
[redacted]
J.P. Morgan Securities plc

YTD returns through Sep 20
%, equities are in lighter color.



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

See page 7 for analyst certification and important disclosures.