Challenges for asset allocation

As active managers of global funds, we usually look at the world as being divided into three regions – North America, Europe, and the Pacific.

North America is dominated by the US which makes up approximately 50% of the MSCI World index we use as our benchmark. Europe takes up 33% and includes 'euro-land', UK and the Scandinavian countries. Pacific is dominated by Japan and includes 'smaller' countries like Australia, New Zealand, Hong Kong and Singapore. However, the US is the market trend-setter.

A logical way to approach asset allocation is to look at top-down factors such as valuations, or the difference between earnings yields and bond yields, monetary conditions which encompass long yields and short rates, exchange rates and earnings forecast revisions. Positive earnings outlook has been the major driving force behind the global bull market despite stretched valuations caused by rising inflation expectations and therefore rising long yields.

Equity markets tend to move a lot more when the market sentiments turn. From a fundamental point of view, it makes sense to shift some funds out of equities into bonds in a balanced portfolio when earnings growth momentum tapers off and bond yields stay high.

The new economy

However, investors who shifted funds too early in anticipation of an equity market correction may have experienced some shock as global markets continued to charge ahead, powered by the technology, media, and telecom (TMT) stocks which represent the 'new economy'.

Even though many TMT stocks are overvalued by traditional methods of valuation, investors tend to focus on the earnings growth that these companies are expected to show. Apparently the productivity gains through the use of internet in the broader economy have supported a booming US economy with little inflation being recorded.

This has been extremely equity-friendly. The trend towards more efficient and effective information exchange via the internet has spread to other parts of the world, including the emerging markets.

In asset allocation, we are increasingly being forced to look at the TMT sectors. Approximately 40% of the S&P 500 index is now made up of TMT stocks. In Germany, three heavyweight companies – Deutsche Telekom, SAP Preference, and Siemens – make up 43% of the Dax index and are among the top four performers this year. Even the FTSE 100 index is seeing a tilt towards TMT after the latest quarterly review, with 45% of the index now being in those sectors.

European markets have done well, for good fundamental reasons, and the new economy stocks dominate. The waves of mergers and acquisitions, and structural reforms in euro-land as borders disappear also tend to boost market sentiment. The danger lies in the market expecting too much too soon from Europe's TMT companies. ■

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INTERNATIONAL EQUITIES

These are a selection of issues announced recently. The details, updated to the middle of last month, were supplied by *IFR Securities Data, London* and other sources.

Issuer	Amount raised (m)	Type of issue	No shares (m)	Offer price	Pricing date	Exchange listing	Fees (%)	Bookrunner
COLT Telecom	EUR493	S	12.9	EUR38.52	6 Mar/00	London		Morgan Stanley Dean Witter
Comment: The 12m new shares were issued due to investor demand.								
Energis	GBP1001	S	30*(a)*	GBP33.80	9 Feb/00	London NASDAQ		ABN AMRO Rothschild Cazenove Dresdner Kleinwort Benson HSBC
Comment: (a) including greenshoe option of 3m shares.								
Flag Telecom	USD874*(a)*	IPO	31.68	USD24	10 Feb/00	NASDAQ London		Salomon Smith Barney
Comment: (a) post-shoe (15% of offering). (b) Pre-shoe								
Interactive Investor International (iii)	GBP94.65*(a)*	IPO	63.1 (b)	GBP1.5	17 Feb/00	London NASDAQ		Credit Suisse First Boston*(c)*
Comment: (a) post-shoe. (b) Includes 8.1m shares greenshoe. (c) Lead manager. Web-based personal financial services company.								
Psion	GBP210	S	3.2	GBP65.5	2 Mar/00	London		Credit Suisse First Boston
Comment: Proceeds will be used to develop its products, to fund acquisitions and restore cash balances.								
Riverdeep Group	USD121.66	IPO	36.5	USD20	9 Mar/00	Dublin NASDAQ		Credit Suisse First Boston*(a)*
Comment: (a) Lead manager. Provider of internet-based educational solutions.								
Ryanair Holdings	EUR176	P, S	22	EUR8	9 Mar/00	Dublin London		Morgan Stanley Dean Witter*(a)*
Comment: (a) Lead manager. Overallotment option of 3.3m shares.								

P = primary; S = secondary; IPO = initial public offering; D = demerger.