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Investment Strategy Quarterly Conference

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We held our quarterly investment conference this week where we take the time to review the evolving economic data around the world and to consider the implications for our investment strategies.

The OECD and the IMF have recently downgraded their estimates for global growth in 2019/20 by 20bps to 3.4%. Recent Sino-US trade conflict has had a negative impact and trade volumes are 7 percentage points below the Dec 2017 peak.

Weakness is most evident in Continental Europe where excess German savings continue to generate damaging intra-Eurozone financial imbalances. The OECD strongly recommends that countries with so-called “fiscal space” should increase domestic spending and investment to boost growth prospects. Germany is in the strongest position to do this but won’t. Italy, though possessed of the weakest public finances in Europe will, and has embarked on a modest fiscal expansion with the introduction of a “universal basic income.” This will be a fascinating “real-time” natural experiment in social and fiscal policy.

Growth in the UK has been impacted by the vacillation and equivocation over Brexit. It is estimated that the cost to the UK is already about 0.7% of GDP or £18bn. But, importantly, the UK is one of the least liked markets in the world largely because of the uncertainty surrounding Brexit and Sterling. Unlike many other developed markets UK listed assets do not trade at a premium to GDP. Unloved and uninvested, the UK market is one of the cheapest developed markets and the consensus around our table was very much that almost any “deal” would provide clarity around which businesses could plan and moreover begin to attract foreign investors back into “cheap” UK listed assets.

One of the emerging themes of the last quarter has been the simmering hostility between Donald Trump and the Federal Reserve. Possibly as a result, Jerome Powell, Trump’s appointee at the Federal Reserve, has become markedly less hawkish in his assessment of the path of future US interest rates. This is despite the fact that the US economy is in robust good health.

Absent from the global data is any real hint of inflation anywhere in the developed world. This is supportive of a softer path, not just of US interest rates, but of rates elsewhere as well. Nonetheless, a softening in the US rates outlook does suggest that we may have passed “peak dollar.”

If the USD has peaked, and both fundamental and technical analysis suggests that it has, then it will open the door for a sunnier outlook for Emerging Markets. Rising US interest rates tend to tighten policy in the EM world as many currencies are formally or implicitly tied to the US currency. If USD strength goes into reverse, Emerging Markets in Asia and Latin America are likely to benefit.

China is a more difficult conundrum; the sheer scale of the economy raises the prospect of geopolitical tension between it and the US. Nonetheless, the authorities have relaxed policy somewhat over the quarter and whilst growth has been revised down from 6.5% to 6%, the focus is on the “quality” of that growth and on curbing excess leverage. In sum, China is still a net positive for global demand.

As we have noted previously, we expected a long and slow recovery from the excesses of 2008. This is indeed, what we are seeing. Yet with the absence of inflation we see no incentive for central banks led by the Federal Reserve to tighten aggressively and “end the cycle.”

Recent volatility, we believe was a mid-cycle correction and as clarity emerges on trade, Brexit and Sino-US relations we expect to see bond yields stabilise and equity markets make further progress.

Of course, it remains essential that your portfolio reflects your tolerance for risk and that you maintain the correct balance of stabilisers and growth assets in your portfolio to meet your personal investment objectives.

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