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A year-end review of global markets and economies - December 2019

The UK General Election results are in and it has been a resounding victory for the Conservatives. Brexit details still need to be hammered out, but Boris Johnson's comfortable majority has given the UK market a boost. As global investors it is important to keep some perspective despite the noise of domestic issues. The average international investor normally has about 5% of their portfolio in UK assets, although Brexit uncertainty has driven this closer to 0%. Speculation about the details of the UK's future relationship with our European and global trade partners will continue but the election result is likely be a catalyst for global investors to reassess the relative attractiveness of many UK assets which currently trade at significant discounts to their international peers.

Despite the negative news flow about Trump trade deals, recession fears and Brexit 2019 has been decent year for most asset classes. We had a strong rally at the beginning of 2019, but markets spent the second half of the fretting about geo-political issues and the threat of economic slowdown. According to some analysts 2020 was supposed to be the year of recession. However recent economic data seems to have blunted the twin threats of an escalation of the US/China trade war and an overtightening of monetary policy, especially by the US Federal Reserve.

So, we look forward to the Christmas festivities with slightly more optimism and can look back on what has been a good year. Central banks continued to be the key players in 2019 starting the year by promising to stop tightening policy and ending up actually cutting interest rates further. That accounted for the strong rally that took us through the spring. The summer can be viewed as a "muddle through" period, when growth expectations remained under pressure and threats of trade war escalation continued but liquidity support remained strong, limiting the downside for equities.

Overnight news has fed optimism that Presidents Trump and Xi have tentatively reached a "phase one" trade deal. This should help global trade and corporate investment to recover. There is also hope that some of the big drags on Germany's economy are fading, and also that a loosening of policy in China is beginning to have a positive effect.

Finally, there is the prospect of increased fiscal spending as politicians (egged on by voters) pledge an end to austerity. Consumer confidence supported by strong employment figures and low inflation have prevented most major economies from slipping into recession, however the global manufacturing sector has not been so lucky. So, it's not surprising that commentators are closely watching the Global Manufacturing Purchasing Managers Index, a key indicator of the health of the manufacturing sector. Although still in contractionary territory, this index has now risen for three consecutive months. It's early days and this fragile rebound could be derailed by a poorly timed tweet from the White House, but could this indicate a brighter 2020 for manufacturers?

The threat of recession seems to have receded, but to build on 2019 gains equity markets still need Central Banks to be supportive. And even with those positive macro-economic tailwinds' investors need to be more discerning as they assess investment opportunities. Certain markets/sectors/stocks look expensive at current levels so investors will need to keep a close eye on corporate earnings.

The recent problems faced by investors in the Woodford funds and more recently some commercial property funds demonstrate that liquidity concerns can apply to individual funds as well as global economies. Those funds experienced problems because a period of poor performance lead to investors withdrawing money which put pressure on cash reserves. This in turn exposed the illiquid nature of the underlying assets. Commercial properties are by their nature illiquid, it can take months to buy/sell a single property, so it is important to have plentiful cash reserves to address the day to day dealing of an open-ended fund. However, in a low interest rate world funds don't want to have too much cash, earning next to nothing as, this will dilute the performance of the overall fund reducing the dividend/interest/rental yields/capital returns.

The question of how much cash to hold poses similar dilemmas for investors as it does for fund managers. Interest rates are likely to stay lower for longer so after the effects of inflation cash investors are likely to see their savings being eroded over time. Historically equities, bonds and property assets have given investors protection against inflation, but this comes with associated risks. The risk assessment process provides a vital insight into an investor's tolerance to the ups and downs of the investment journey. Our asset allocation models often include a cash element which helps with the efficient management of the portfolio and reduces volatility. However, this should be regarded as separate to any short-term cash requirements you may have. Investors, particularly those with immediate income requirements should keep enough in cash for the unexpected, for emergencies and for peace of mind.

If you have any questions or would like to discuss any issues raised in this review, please contact Anderson Sinclair.

We wish you and your family a happy and healthy Christmas and look forward to seeing you in 2020.

Kind Regards

Ross Anderson ACSI　　　Gavin Anderson CeMAP MIFS DipFA　　　December 2019