# INVESTOR INSIGHT

Winter 2019/20

A look at the markets by RSMR

## Welcome

Welcome to the latest edition of our 'Investor Insight' which provides high-level commentary on the global markets and how these might be affecting your investments.

We hope you find this useful.

**Ken Rayner**
**Investment Director**
**RSMR**

## The global economy: What's going on?

**Benign economic policy U-turn fosters investor optimism**

In spite of concerns about slowing global growth due to the US-China trade dispute, UK political Brexit deadlock, and a European manufacturing contraction, 2019 saw markets recover after a poor previous 12 months.

Most equity holders will be pleased with 2019's performance, which saw a 29.8% return for US dollar investors after a more supportive economic policy was introduced, including three US Federal Reserve (Fed) interest rate cuts.

Since Trump's January 2018 announcement at the Davos World Economic Forum that trade tariffs were imminent, world growth has fallen from 3.8% in 2017 to a likely 2.9% for 2019.

The most exposed sectors, such as manufacturing, have come closest to contraction and many people have feared a global recession was imminent. This has faded recently but little growth improvement is expected in spite of central bank support.

The US interest rate U-turn also helped bond markets where longer-term assets delivered strong returns. The European Central Bank (ECB) followed the US in stimulating the economy and we should see evidence of this in 2020.

Generally, investors have ignored most negative political and trade upheaval and relied on the optimism generated by central bank support, and consumer spending which was resilient in spite of low wage growth.

> "Most equity holders will be pleased with 2019's performance"

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## The asset classes – a quick update

### EQUITIES

Overall, 2019 was a strong year for equity markets in spite of gloomy economic data.

International trade disputes and tottering political stability made investors nervous about company profits and earnings but this was mostly overtaken by optimism which increased valuations, even after negative economic or company news.

Consumer-led, and technology, sectors were strongest, with growth stocks – those with potential to outperform the market – leading the way until towards the year end when there was a rally in some value stocks which usually trade below their true worth but can generate superior returns.

The most consistently positive markets, in local currency terms, were in developed economies. The US posted a 29.8% return compared to -20.5%, in Chile, while Russia was top with 39.8%.

The reversal of the Fed's interest rate raises bolstered markets after a poor final quarter in 2018. A more accommodative approach, in the US and Europe, gave investors confidence and boosted chances of avoiding, or delaying, a recession.

Many investors will be relieved that that there is now more political clarity about Brexit and a potential timetable for leaving the EU.

### FIXED INTEREST

The Fed's interest rates U-turn was a factor in the 2019 bond markets' rally.

A strong source of return has been government bonds with longer duration assets performing best.

Slowing economic growth does not yet mean recession, and although there has been market volatility during the last three years, investors have enjoyed significant gains and most markets remain positive.

Negative bond returns probably mean low global economic growth and very low inflation for some time.

Investors also face new challenges in assessing how bonds fit into traditional portfolios.

Traditionally, they have been 'a safe haven' but, with rates already very low, it may be impossible for a bond portfolio to balance equity risk as before.

Very low, or negative, returns in a variety of government bonds in Europe and Japan have made high-quality corporate debt more attractive, if only for the small positive return.

Fed interest rate cuts have shown that, perhaps for the first time, it is more focused on global events than just the US economy.

## PROPERTY

Property, where changes are slower, provided mixed fortunes during the last quarter.

Most property investors will have seen slightly negative returns as Brexit uncertainty continued to dampen the market, along with worries about traditional ‘high street’ retailing, which had its most difficult year since records started.

An interesting feature for commercial property in the UK and continental Europe is that some sectors are moving in opposite directions. UK warehouse capital values rose by 5% during the 12 months to September 2019 while retail capital values fell by 13%.

The office market is fragmenting: as the value of city centre premises rises, that of many out-of-town office parks is falling. The Brexit political stalemate also hindered investor and occupier decisions.

Online sales growth at the cost of shops is a key factor in retail’s varying fortunes and warehouse capital values.

While traditional retail is re-pricing, the current 7%-8% return could disappear as leases expire and more retailers fall into insolvency.

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## Global round-up

- US retail sales grew by 3.4% between 1st November and Christmas Eve, mostly online.
- European manufacturing activity contracted for the 11th successive month in December.
- While China’s growth has slowed to 6%, domestic consumption remains strong.
- Japan has announced a USD 120bn spending package to boost its economy.
- Argentina, Ecuador and Lebanon are having problems keeping up with debt repayments.
- Brazil carries much of the hope for South America through the new president’s pro-business policies.
- UK 2019 economic growth is expected to be 1.2% – the worst annual performance for a decade.
- The continuing US-China trade war has reduced capital spending in China.
- UK pay growth peaked at 3.9% in the summer, the highest for 11 years.

“UK 2019 economic growth is expected to be 1.2% – the worst annual performance for a decade.”


# So, what's next?

**An expected average global economic growth rate around 2-3 % in 2019 is far lower than recently and, in several economies, close to recession.**

While central banks have helped, boosting investor confidence, this may create problems later.

Slow economic growth and modest wage rises are likely to continue in 2020 but may build inflationary pressures and greater volatility.

If this happens, dips in economic growth could affect investor confidence more significantly.

The slowdown in economic growth has already made investors more cautious and companies delay investment in a more uncertain future

Economists now believe that monetary policy, control of interest rates and money supply, has fewer options with interest rates already very low and that governments must introduce more fiscal – tax and spending initiatives – to drive expansion and increase global demand.

Most forecasters don't see a recession coming soon but the position remains fragile.

As long as recession is avoided in 2020, and corporate earnings show some recovery, equities still look likely to deliver better than other asset classes, although, after a long period of a rising market, investors are jittery.

This means that, when they happen, market setbacks are likely to be sharp and sudden as in 2019.

> "The type of deal that is negotiated, and whether it represents a hard, or soft, Brexit, will continue to influence the UK equity market throughout 2020."

## About RSMR

**Independent specialist research.**

**RSMR was formed in 2004 to meet a growing demand from financial advisers for specialist and impartial investment research.**

The RSMR team is made up of individuals with expertise from across all areas of the financial industry – from asset management, strategy and fund research through to business development, strategic planning and market research.

We are best known within the financial industry for our 'R' fund ratings – this rating is given to investment funds that meet our stringent research criteria. We don't limit ourselves to just looking at performance – we also look carefully at the people, processes and capabilities that are required to make effective investment decisions.

We work in partnership with your financial adviser, providing the benefit of our broad industry insight and rigorous research. This quarterly market summary is designed as a 'snapshot' of the more thorough and lengthy commentary that we provide to your adviser on a quarterly basis.

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