Prime Partners
SINCE 1998

MARKET INSIGHT

APRIL 2019

CITYWIRE TOP 50
INDEPENDENT ASSET MANAGER

Market Analysis

April 2019

Liquidity alone will not be enough

After two strong months for risky assets, the situation was patchier in March. Although the equity volatility remains low, there was some pressure at the end of the month in the wake of economic figures, which do not yet provide any indication of an upturn in the global economy.

In many respects, the marked easing of bond yields only confirmed the growing doubts as to the economy's ability to bounce back. It is true that the excellent performance of bonds has been facilitated by the U-turn performed by central bankers over the last few weeks. Clearly the most abrupt turnaround came from the US Federal Reserve, which may postpone any additional rate hike. Confirmation of an end to the Fed's balance sheet reduction programme also stoked the feeling that monetary policymakers are worried by sluggish growth and the risk factors affecting it, such as Brexit, various elections, the geopolitical situation and the trade tensions.

In the same vein, the European Central Bank's decision to implement a new round of preferential financing for banking institutions (TLTRO) is an indication of a lack of confidence in the economic outlook.

So it is not surprising that investors have become cautious of fuelling stock market rise. Liquidity alone will not be sufficient to justify price rises for risky assets – especially as valuations are no longer so attractive, particularly for US securities.

In our opinion, a consolidation in equity markets in the short run is a healthy assumption to make, given how swift the rise has been since the beginning of the year. If part of the recent rally is directly linked to the excessive correction in the last quarter of 2018, we cannot ignore the marked expansion in P/E multiples since January. This expansion has been all the greater as downwards revisions to earnings growth forecasts have been significant over the last few months.

Some are countering the valuation argument on the back of a major assumption: the so-called goldilocks scenario is back in the news thanks to the resolute action of central banks.

For several months, we have been counting on a kind of soft landing for the global economy, in what remains the late phase of the cycle; our investment policy is therefore built around the idea that the conditions for a stabilisation in global growth should materialise from the second quarter of 2019 onwards.

In light of disappointing statistics, there is no reason to question our view that a soft landing is the most optimistic scenario for the coming months.

Consequently, just as we found forecasts of imminent recession prevalent at the end of 2018 to be excessive, we believe it is unreasonable to bet on a goldilocks scenario today.

The recent change in stance for monetary policy is first and foremost a means of taking all possible action to avoid a more pronounced downturn in the economy, whatever the cost.

Whilst this may please some people, one thing should be remembered: abrupt changes in the handling of monetary policy may lead to a loss of credibility for policymakers in the medium term. In a world where many reference points have been called into question, the central bankers have acquired the status of the long-term navigators of troubled economic and financial waters.

"Growing scepticism regarding the ability of central bankers to predict economic cycles should not be taken lightly",

FRANÇOIS SAVARY, CHIEF INVESTMENT OFFICER, PRIME PARTNERS

Against this background, growing scepticism regarding the ability of central banks to predict economic cycles better than most market participants is something that should not be taken lightly!

In practical terms, we have not changed the course of our investment policy in March. It is still based around two major axes: to manage the global risks of portfolios and the need to show great flexibility in our decisions.

As explained last month, we believed that the conditions for profit-taking had been fulfilled after the solid performance of our allocations since the beginning of the year. Our view has not changed. Accordingly, we have further reduced our risky assets' exposure over the course of the last month.

We set up new protection on our equity holdings at the end of the period. Similarly, we have somewhat reduced our exposure to emerging equities. This is not intended to call into question our positive view on securities in these regions, particularly in Asia, in the medium term; it fits in the overall framework of our tactical choice to limit risk, having reduced our holdings in developed markets in February.

As the vast majority of our investments has posted positive performances since the beginning of the year, we have solda long / short equities strategy that has proved disappointing over recent quarters. This decision does not alter our call to keep a broad exposure to liquid alternative strategies. In this regard, we must highlight that the other products in this investment bucket have made a positive contribution to the performance since January.

Whilst visibility on the economic cycle is limited, we believe it remains appropriate to hold uncorrelated assets in the portfolios.

Our fixed income strategy did not change in March, with the exception of a reduction in some convertible bond holdings.

Given the rise in fixed income asset prices in March, we back our decision to underweight this asset class. Considering the significant fall in yields, we believe that favouring tactical products to gain e+xposure to bond risk is all the more justified. In addition, taking profits in the highest-risk segments must be considered, given that we continue to believe that we have entered the final stage of the economic and financial cycle.

In conclusion, we backed up our words with actions during the last month.

As we see no reason to change our global scenario, in light of the economic data, we did not reconsider the decision to reduce risk – on the contrary.

This may possibly have led us to reduce risk a little early and, accordingly, to limit the returns on our investment policy. We are not overly worried by this, given the high-quality returns generated by our tactical choices since January.

At the end of a first quarter that was favourable to risk taking, the question of economic and political uncertainties is far from having diminished. Managing these issues will remain key in our approach. In this respect, we believe that assumptions of a consolidation in the stock market gains may gather strength over the coming weeks. As a consequence, we will keep our defensive tactical bias until we see more attractive investment opportunities.

Geneva, 27 March 2019

Prime Partners SA
Rue des Alpes 15
P.O. Box 1987
1211 Geneva 1

www.prime-partners.com

CONTACTS

François Savary
Chief Investment Officer

Jérome Schupp
Equity Analyst

Julien Serbit
Portfolio Manager

Tel +41 22 595 09 97
fsavary@prime-partners.com
jserbit@prime-partners.com