Prime Partners

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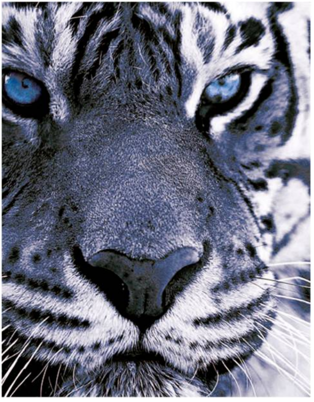
MARKET INSIGHT

OCTOBER 2019

CITYWIRE TOP 50
INDEPENDENT ASSET MANAGER



Market analysis

October 2019

Central bankers have done their job. What next?

Whether coordinated or uncoordinated, central banks took stronger action in September. This was due to an uncertain economic cycle, too-weak inflation despite low unemployment rates and strong trade frictions.

The attacks on oil sites in Saudi Arabia came too late in the month to influence recent monetary decisions. However, the resultant supply and geopolitical uncertainties will in turn affect economic policy management in the coming months.

Pending greater visibility on the duration and extent of the disruptions that the abovementioned attacks imply, monetary policymakers will be inclined to maintain a very accommodating monetary stance.

Already struggling to show signs of stabilisation, the last thing the global economy needed was tensions in the Persian Gulf. In this respect, the OECD's revised growth forecasts have attracted a lot of attention. Now, projected growth in 2019 is less than 3% (2.9%). It is clearly no longer possible to downplay the risks of a global recession; we had increased the probability of such a possibility last month (to 30%).

As it is too early to draw conclusions on the effects of the damage to certain production sites in Saudi Arabia, we are not revising our view of the global economic situation at this time.

We maintain our baseline forecast that activity will stabilise over the medium term, while growing increasingly convinced each month that strong growth is not a realistic proposition. This stance has not been altered by the generous monetary policies implemented.

“The cat-and-mouse game between Washington and Beijing needs to be halted.”

FRANÇOIS SAVARY, CHIEF INVESTMENT OFFICER, PRIME PARTNERS

It is therefore important that labour markets continue on a positive growth trajectory, so that domestic demand remains a major buttress for the global economy.

Above all, the cat-and-mouse game between Washington and Beijing needs to be halted. The downward pressure on investment, which has been fuelled by the trade dispute of the past eighteen months, can only be reversed if both sides reach an agreement, even a partial one, quickly. Against this backdrop, the forthcoming US presidential campaign gives us hope that recent signs of more moderate stances will lead to a “deal”; a ceasefire in the absence of an unlikely lasting return to trade peace.

The situation cannot continue as it is without increasing the risk of a recession in 2020. The coming weeks will be crucial, especially as market participants have given the idea of an agreement a chance, judging by the performance of assets in September.

Be it a question of pressure on yields or the recovery of stock markets, all the signs are that there is still hope despite the uncertain geo/political context.

Dashed hopes have very pernicious effects on the economy. Indeed, the “asset effect” should not be overlooked, especially at the end of the cycle. A sharp decline in risky assets in the wake of negative news on the trade front could worsen the sentiment of economic actors and dampen demand; in other words, the vicious cycle of recession could definitely begin, with a decline in everyone's financial wealth fostering fatally cautious behaviour.

As we have been saying for several months, an injection

of liquidity alone will not be able to prolong the economic cycle indefinitely. The fundamentals must take over from "free money" at some point. In this respect, the earnings season will also be a test for investors. They will not be able to accept a widening gap between risky asset prices and fundamentals indefinitely!

Conducting an investment policy has never been an easy task, but it is even less so under the current conditions. As we move further away from 2008, the feeling that it is clear that things will not return to the pre-financial crisis "normality" is becoming a more prevalent reality.

It is almost enough to make people nostalgic about insufficiently controlled inflation, unfettered globalisation or Cold-War-era frozen geopolitical risk!

In a world where yesterday's economic and political certainties have been shattered, we must be flexible and not hesitate to question the assumptions underlying an investment strategy.

In recent months, we have encouraged you to move in this direction. Our recent decisions are completely in line with the content of this monthly bulletin.

Accordingly, after increasing our convertible bond position at the end of August, we have reduced equity market hedges in recent weeks. By doing so, we have grasped the opportunities thrown up by the excessive correction of risky assets during the summer.

Similarly, and in line with our vision which rejects the idea that a type of "Japanisation" of the world economy is inevitable, we have resisted the lure of government debt, believing its summer advance was overblown. The steps taken by central banks lead us to believe that monetary policies are resolutely anti-deflationary; in other words, price stability is no longer a primary objective of central bankers.

The above paragraphs may give the impression that our world view is very pessimistic. This is not the case! We try to observe the facts and draw the most accurate conclusions possible.

In this context, sound risk management, which is a priority in view of the performance of our allocations this year, leads us to continue to recommend not to overweight risky assets. While we have moved closer to what we consider to be a "neutral point" in terms of equities, we should not forget that we have reduced our credit risk since early 2019.

Similarly, the idea of maintaining a defensive sector stance in relation to equities is not called into question, despite signs that market players are "warming up" in respect of the most cyclical and / or value segments of the stock market.

We remain convinced that it is not the right time to accumulate "all" risks in a diversified portfolio. In the current context, we remain committed to visible growth rather than making "bets" on cyclicality!

Our choices on our preferred emerging assets remain the same. Recent monetary decisions and a continuing cautious view of the US currency underpin this decision.

Similarly, we are very consistent in our positive recommendations in terms of gold bullion and liquid alternative products, even though the latter's performances in September were sometimes mixed.

More than ever, the world today must foster an enquiring mindset.

We will be reassessing the situation on a daily basis in the coming weeks, in order to steer the investment policy that we believe is the most appropriate. Remaining vigilant in the face of risk and the pursuit of opportunities is what best characterises our approach in 2019!

Geneva, 25 September 2019

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