INVESTMENT OUTLOOK August 2019

OUR INVESTMENT OUTLOOK

We expect global growth in 2019 to continue at around the average 3.5% level we've seen since the 2008 financial crisis, which should be supportive for the price of shares. However, we are seeing a return to more normal levels of volatility (ups and downs), meaning investors will need to remember to be patient and ride out the bad times.

Across the globe, most major companies' shares are cheap or fairly priced. There's one exception though. In the US, companies' shares are more expensive. In Developed Markets, the US and UK with record low unemployment, are still growing at a steady rate. Brexit continues to be the main concern for the UK; whereas in the US, the focus is on whether the strong growth experienced recently will continue. Share prices there have had a good run and as a result, they look expensive compared to their historical average. The Eurozone saw a difficult end to 2018, with Germany and Italy failing to grow in the second halves of the year, however, France and Spain's consistent growth softened the blow. We see recent Eurozone weakness as a temporary wobble, with employment growing steadily. Japan is still trying to achieve consistent long-term growth, something that hasn't happened since the bubble in Japan property, and shares burst in the late 80s.

Emerging Markets, on the whole, are benefiting from long term improvements to laws, regulations, and policies, combined with favourable demographics. Another positive to take away; ahead of any weakness in the global economy, governments of emerging countries have a much sharper set of tools, like higher interest rates and a greater amount of cash, to alleviate any discomfort that may arise, compared to developed nations.

With interest rates near all-time lows, bond holders are getting smaller interest payments for lending to companies and governments than ever before, as they can borrow so cheaply from banks and other institutions. This makes shares in companies that have been historically cheap look even better, when compared to bonds.

If you have any questions on our investment outlook, why not get in touch with our friendly customer support team, who can provide you with more information.

WATCHLIST

When we manage your money, there are key events and risks that need to be closely monitored. Here are some events we're keeping a close eye on.

B is for...

The Brexit process remains the UK's biggest unknown. It could have far reaching implications for the UK and Europe, but we see little risk of global contagion. The outcome set is so wide; from a "no deal" to a complete reversal, giving UK investments a high level of uncertainty.

US Central Bank

Concerns of higher interest rates have now disappeared. Forecasters are now expecting multiple interest rate cuts by the end of the year. We believe we won't see as many interest rate cuts as expected by the stock markets, unless the US economy gets hit by a strong shock.

Rising political turmoil

Current political unrest across many parts of the globe seems to have minimal economic impact outside of local pain-pockets. However, this can change quickly, and particularly in major economies, contagion is always a concern.

Oil

An escalation of Middle East unrest could drive oil prices significantly higher, which would likely only be positive for energy companies.

Rapid wage growth

A rise in employment levels and easy access to borrowing has boosted consumer spending. However, wages have not been going up. If wages do catch up and grow rapidly (wage inflation), it could trigger action from Government banks, which would hurt bond and share prices.

INVESTMENT	OUTLOOK	WHAT WE THINK
EQUITIES		
UK	=	Pessimism around Brexit weighs heavily on UK shares, despite a large percentage of revenue and earnings being generated elsewhere globally. Should the Brexit process be smoother than expected, a rapid rise in confidence could support UK shares.
US	−	US shares remain expensive compared to other developed markets. We believe there's scope for more interest rate hikes than most market experts are forecasting, and there's also potential for greater wage inflation, both of which will likely have a negative impact on US shares.
Europe (excluding UK)	=	Growth remains above trend and employment is drifting higher, but the region is still struggling to grow. A US and China trade war would likely impact growth in Europe further. Crucially, EU shares' strong performance in the first six months of the year has reduced its attractiveness. The combination of these factors has seen our outlook lowered to neutral.
Japan	+	Japanese shares remain attractive compared to their historical value, and relative to other global stock markets. A pivotal pillar of this view is strong government support, accompanied by robust corporate health. However, if the global growth falters, it'll likely affect Japan's important export market.
Emerging Markets	+	On a country by country basis, results are varying, however, collectively we expect continuation of steady Emerging Markets growth. The bright spots include two of the bigger nations, China and India. US-China trade tensions remain an overriding concern for the region and financial markets globally.
Asia Pacific	+	Attractive prices, with strong expected returns, are complimented by a high dividend yield offered by share in Asia Pacific. The main risks remain a trade war or a slowdown in global growth.
BONDS		
Government Bond		
UK	=	UK government bonds have benefited from continued Brexit uncertainty, as bonds typically favour well when there is uncertainty, or volatility. The main risk is a significant growth shock to the UK economy coupled with high inflation.
US	=	The US Central Bank (Federal Reserve) is now expected to leave interest rates on hold through 2019. This has pushed up bond prices making them expensive. We see wage growth as the main risk, as it would force the central bank to raise interest rates, which is normally bad for bonds.
Europe ex UK	−	European Central Bank (ECB) bonds are dramatically overvalued due to the central bank buying its own bonds, also known as Quantitative Easing (QE). The end of the ECB buying these bonds is likely to ignite a decline in value as one of the biggest buyers' steps away from the market.
Japan	−	Japan bonds are extremely expensive due to Japan's Central Bank (BoJ) buying its own bonds, to force prices up and returns on bonds down. There's little expectation for near to medium term change to this programme. Shares are the attractive way to capture Japan's economic improvement.
Emerging Market	+	Emerging Market (EM) government bonds continue to offer an attractive return compared to developed market bonds. EM Central Banks are in strong shape, with high foreign currency reserves. The main risk is if US government bonds start offering improved returns, investors may sell higher risk EM bonds.
Corporate Bonds		
UK	=	UK corporate bonds issued by companies since the start of 2018 are starting to look more attractive than they have for some time. Low default rates and global diversification of UK companies leave us more optimistic than most investors. However, Brexit forces us to temper our optimism.
US	=	US corporate bonds don't offer much more return than US government bonds, but they come with more risk, making them unattractive. However, recession risk remains low in our opinion which is key.
Europe ex UK	−	Similar to European Central Bank (ECB) bonds, European corporate bonds are unattractive due to the central bank pushing up bond prices, making them expensive with little returns available. Despite low default rates, these bonds are uncompelling, particularly compared to shares.
Japan	−	Similar to Japanese government bonds, Japanese corporate bonds are expensive due to the central bank pushing up bond prices. We prefer shares.
ALTERNATIVES & THEMATIC		
Commodities	=	Global growth concerns have seen a volatile recent period for commodities. Oil's outlook remains uncertain given the nimbleness of shale oil. Global demand remains crucial for commodities overall expectations are overly downbeat in our estimations.
Global Property	=	Globally property remains appealing given the time it takes to build new properties, and how difficult it is to borrow money compared to previous periods. It also offers diversification against shares and bonds. However, property has had a very strong start to the year and now appears expensive. We have reduced our holding.
Private Equity	=	Public shares remain expensive, which increases appetite for private shares where investors are hoping for much higher returns, coupled with higher risk. There is also a record level of investment chasing those opportunities.
Gender Equality	+	Academic research has shown that companies with greater diversity show strong long-term productivity, return on equity, and dividend growth.