Monthly Commentary 2nd February 2020

January was mostly a down month for global equity markets with falls of 2.1% for Germany's Dax, 1.1% for the S&P 500 and 0.8% for the FTSE 100. The exception was Emerging Markets (+3.7%). Bonds broadly fell about 1% and commodities were up almost 4% due to a strong gain of more than 7% in crude oil. The USD confounded most pundits and rose modestly.

Bubbles everywhere

It has been a long time since we saw so many articles on bubbles in the financial media. Indeed, the Google "stock market bubble" index has surged to an all-time high, nearly double of what it was in 2004 and 2006. Indeed, valuations in the US equity market are stretched and many sectors are extremely stretched. Many prominent market watchers are warning of an imminent crash while others like JP Morgan and Goldman Sachs are urging their clients to buy the dips if markets correct.

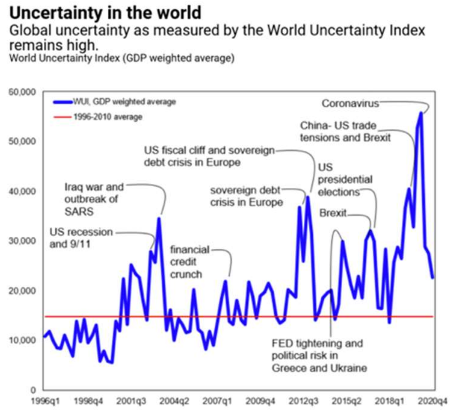
What do we think? Frankly when there is so much talk of a pending bubble pop or crash, it is rather unlikely to happen. It is probable that we get a correction of 5-15%, much as we have a few times a year in the past. Such a correction might be healthy in that it should get rid of some market froth. We also need to keep in mind that equity valuations are high but not necessarily dangerously so when compared to how low interest rates are today. If anything, bonds are in a bubble of their own.

Do we sell now and wait to buy after a correction? That would involve market timing, which rarely ends well. First we need to sell. Are we really close to a high now, or will markets head higher? No one knows. And if we do sell, when do we buy back? Difficult choice. As we are confident that our client portfolios are constructed with quality holdings that reflect their risk profile, we prefer not to attempt to time the market.

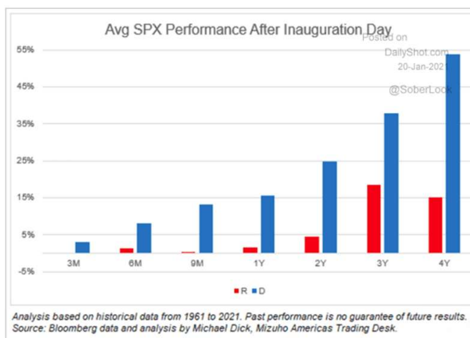
Some good news

With so much not well in the Covid world, it is good to get some good news once in a while. The following three graphics do indeed contain varying degrees of good news.

The first shows the level of uncertainty in the world. As you know, markets hate uncertainty. The sharp falls lately remove one potential headwind for markets.

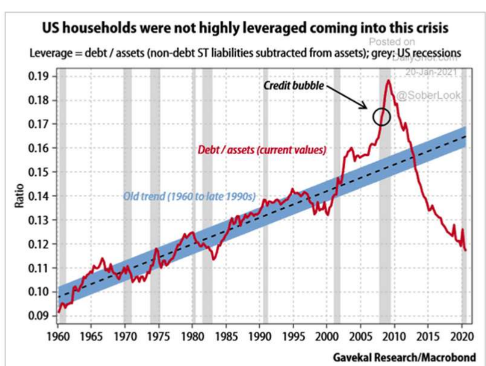


And then there is the historic market performance after inauguration of the last 60 years. As you can see below, when a Democrat is inaugurated, markets tend to perform better than when a Republican is. More potentially good news…



Source: Michael Dick, Mizuho Americas Trading Desk

Finally, with all the talk of high global debts, there is a bright spot in the ratio of debt to assets of the US consumer (the biggest consuming force in the world). It has been falling meaningfully in the last 10 years and is recently at levels not seen since the eighties. More to spend?



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