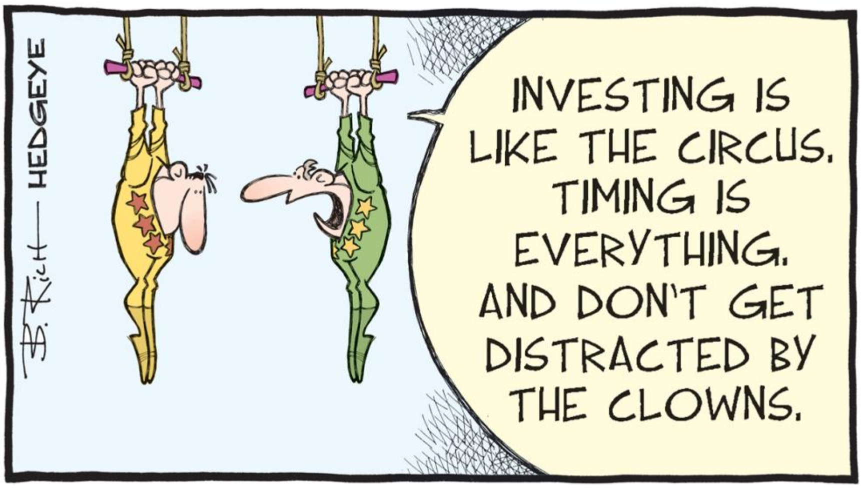
Market Review End of April 2018



Sell in May and go away? Looking at this year's returns, this song may not sound too compelling. Unless you had bought barrels of oil last fall and kept them until now, very few asset classes have produced positive outcome so far. So shall you hang on to your holdings and hope for better days? Buy and hold does not longer seem to be the right strategy either.
Timing a shift in sentiment, a change in asset allocation has been the winning recipe so far this year. Don't get distracted by the surrounding noise of short term variation, keep an eye on the horizon and you will see major trends unfolding.

Market moves at the end of April

	Equities in Local Currencies							
End of April	MSCI World	S&P 500	EuroStoxx	CAC	Spain	Switzerland	UK	Hong Kong
Perf 1 Month	1.02%	0.27%	5.21%	6.84%	3.96%	1.66%	6.42%	2.38%
Perf 3 Month	-5.73%	-6.22%	-2.02%	0.70%	-4.51%	-4.81%	-0.32%	-6.32%
Perf YTD	-0.81%	-0.96%	0.93%	3.91%	-0.63%	-5.28%	-2.32%	2.97%

	Commodities			Currencies vs EUR			
End of April	WTI Oil	Gold	Copper	USD	JPY	GBP	CHF
Perf 1 Month	5.59%	-0.77%	1.39%	1.56%	-0.95%	-0.24%	-1.75%
Perf 3 Month	5.93%	-2.22%	-4.37%	2.59%	-2.75%	-0.42%	3.38%
Perf YTD	13.49%	0.94%	-6.07%	-0.79%	2.45%	1.04%	-2.25%

	Bloomberg Indices Bonds Total returns					
End of April	Global Aggregate	US Aggregate	Euro Aggregate	US 10 Year	German 10 Year	Emerging Sovereign USD
Perf 1 Month	-1.61%	-0.74%	-0.26%	-1.25%	-1.08%	-1.02%
Perf 3 Month	-1.44%	-1.05%	0.93%	-0.95%	1.58%	-2.31%
Perf YTD	-0.26%	-2.19%	0.47%	-3.13%	0.02%	-2.48%

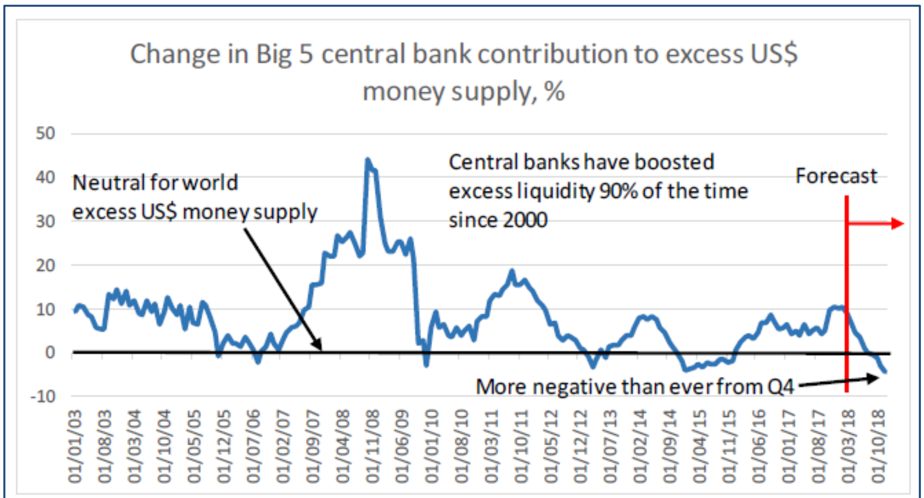
Source Bloomberg 30/04/17

The consensus in the market so far was that we are in an inflationary environment; Trump's late cycle fiscal stimulus, the rising twin deficits, protectionism, sanctions, and China's move to a renminbi-based oil contract are all contributing to the view.
And as a result, the market was short USD, short bonds, long emerging markets as well as commodities and leveraged long risk assets in general.

But recently markets had a change of heart. What if we are entering a deflationary phase for global markets characterised by a strong dollar, a sustained downturn in equities and other leveraged risk assets, a sell-off in commodities and in due course a return of the bond bull market?

As we have said in a recent note, we think we are at a cross-road for financial markets. It is still too early to tell which option will prevail.

Here’s a quote from Macrostrategy Partnership:
“If nothing else changes, from US bank loan growth to net US capital flows, then the Fed’s accelerating balance sheet reduction programme will be highly deflationary for the US by the end of the year. We will likely see significant net flow of capital back to the US (from repatriation, reduced ‘risk-on’ outflows from the US and increased ‘risk-off’ inflows). The net effect will be that all global markets will likely deflate, the US$ will rally, and that liquidity will likely tighten faster offshore than onshore.
This has the potential to become self-reinforcing just like the reflation from February 2016, but in reverse. As deflationary pressure hits the offshore US$ economy hardest, the pressure to ease policy from Beijing to Brussels will increase faster than in the US, rallying the US$ further and reinforcing the deflationary trend.”



Source; The MacroStrategy Partnership, the Big five central banks

These are serious questions to consider for your asset allocation. With rising interest rates in USA and a tighter money supply, some Emerging markets are already feeling the pain (debt in USD and capital outflows). Should markets become more volatile, will Central bankers blink and postpone the normalisation of their monetary policies as they have done since 2008? Kicking the can down the road is obviously the option which was chosen so far. One day though, we will have to face reality and deal with this global debt problem.

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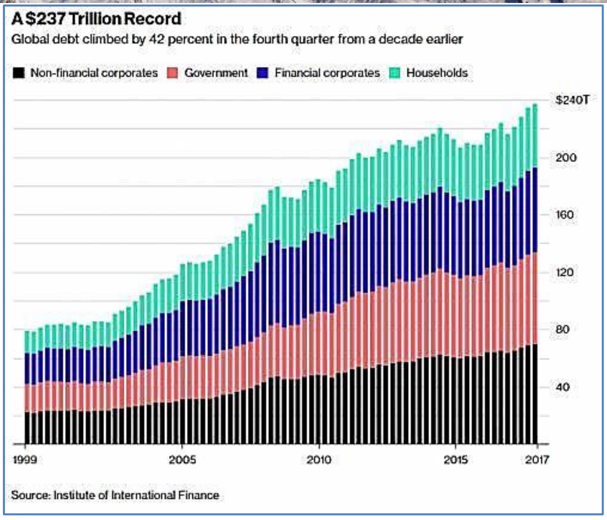
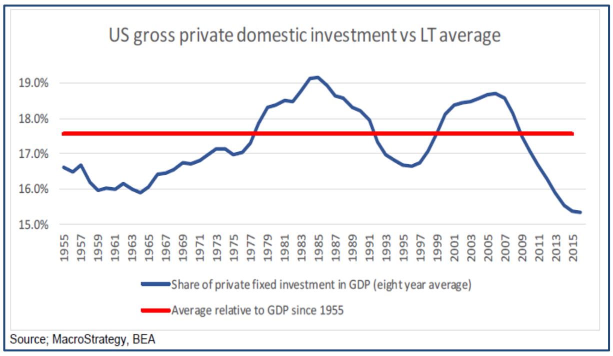
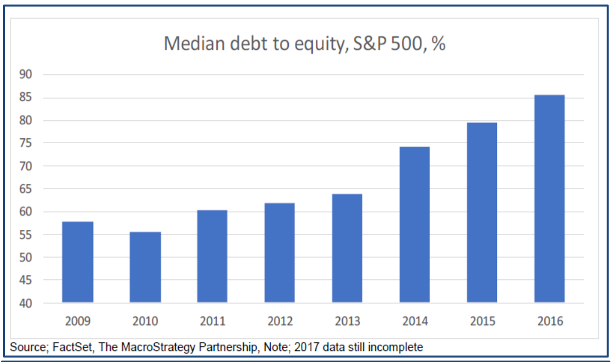
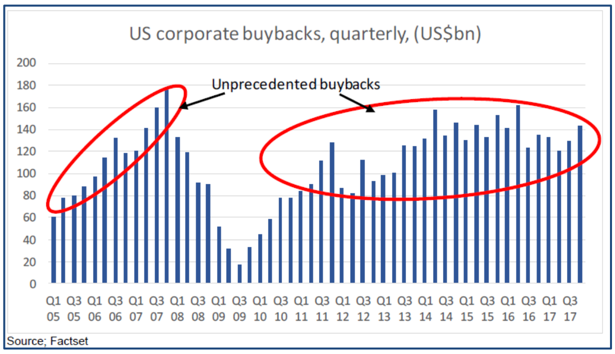
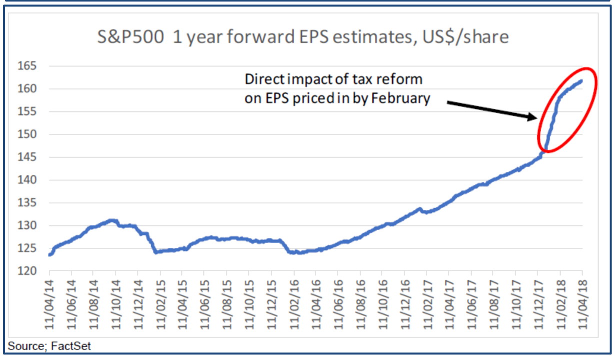


Extremely accommodative monetary policies are having perverse addictive side effects. Companies have not invested. Record low interest rates have enticed corporations to borrow more. Thanks to low cost of capital and lower capex, they raised dividend payments and made earnings cosmetically more appealing with large share buy-backs programmes.

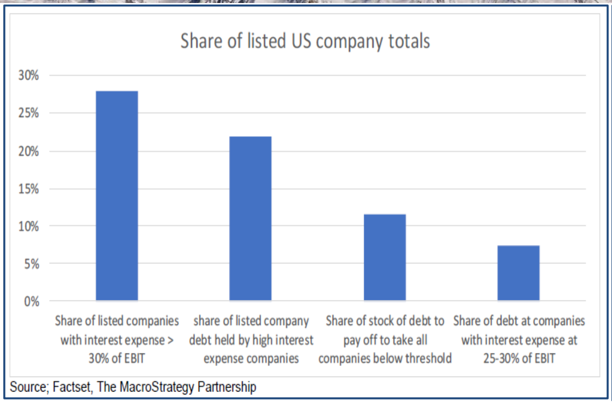


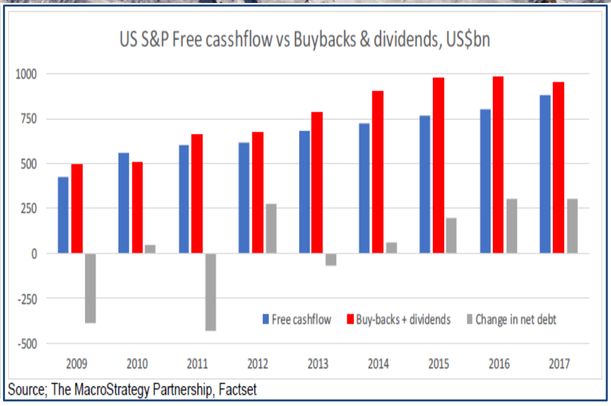






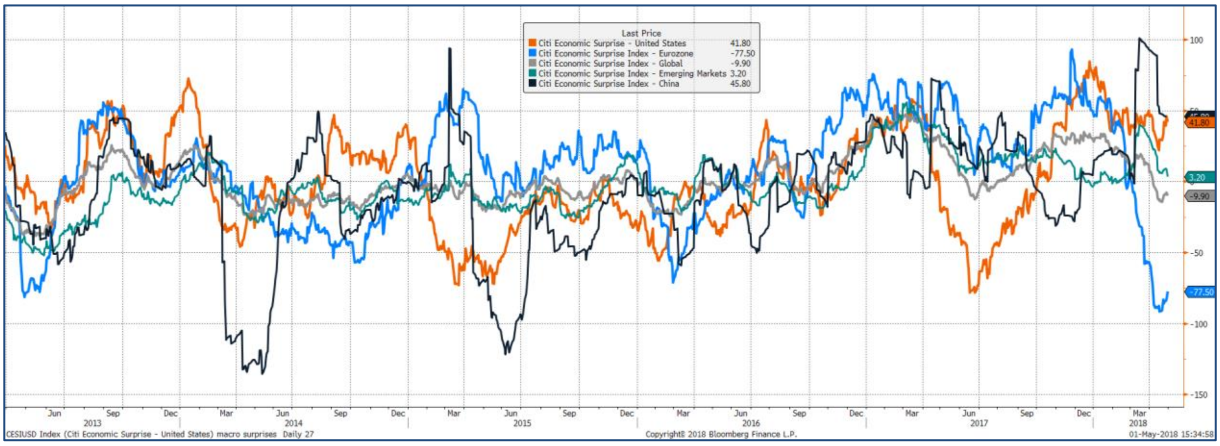
Buybacks plus dividend payments have outpaced free cash flow generation. Higher debt loads have filled this gap. Needless to say that rising interest rates will make debt refinancing more difficult, cash flows will shrink and buybacks will vanish.



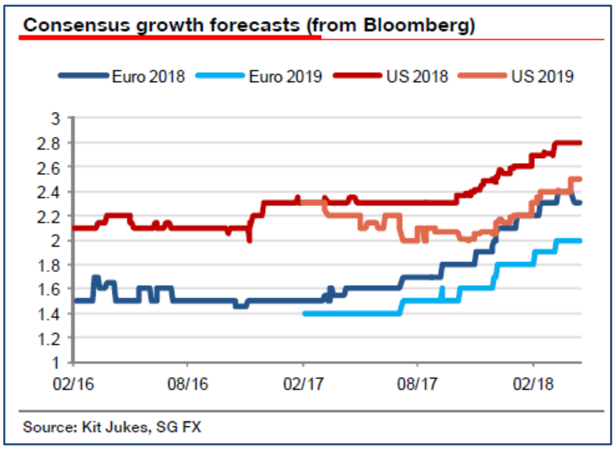


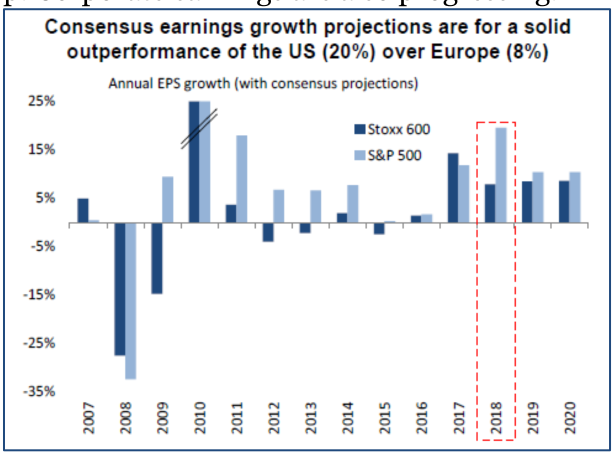
Central bankers know very well that tighter monetary policies could crash the markets. So the timing and pace of implementation are key.

Meanwhile leading indicators have rolled over sharply in Europe. A strong Euro was probably one explanation. The latest USD strength may be a relief for the European area, indicating a bottoming process.



Western economies are still growing at a healthy clip. Corporate earnings are also progressing.





Market volatility offers investment opportunities. But watch Central Banks actions and wording carefully.

We invite you to read our monthly investment committee publication for more details on our strategy and outlook.

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