Capital Market Outlook 1st Quarter 2020

- **Our outlook for equities is positive even though we took some profits**
- **The economy seems to have hit the trough (or even passed it?)**
- **Bond markets still offer opportunities, but are hard to play**

There is no way around stocks

After years of uptrends on global stock markets, some investors now believe the valuations are starting to get expensive – especially in the US. Readings for other regions show that valuations there are still much more attractive. What is certain is that there is no way around stocks, also in the future. Bond returns are hardly attractive, especially in Europe due to interest rates, and before this backdrop, the relative valuations of stocks versus other asset classes are not at all exaggerated. Our neutral equity weighting reflects our basic optimistic assessment of stock markets. As regards the regional composition, we are a bit more cautious about the US than other regions. Stocks in North America are soaring and far ahead of other countries, and we believe there is room for catching up in other markets in the coming year. Also in this view, our fundamental optimism is evident: during correction phases, the US and the US dollar often showed strength, while in "risk-on phases", other markets often fared better. Naturally, we have reviewed our concrete positions also with respect to possible setbacks and can confirm that the risks in the portfolio are not higher.

Worry over the economy has been worse in the past

The past few months have been rather tense from an economic standpoint, but recently the situation eased a bit. The so-called "economic surprise indices" – i.e. leading indicators that link numerous macroeconomic ratios – show that Europe is on a clear recovery. These ratios are in the expansive range also in the US. Nonetheless, the sky has not cleared up yet. Topics like the global trade dispute or the relationship between Great Britain and the EU will accompany investors also in the new year and repeatedly cause fluctuations. The good news: market behaviour usually does not follow economic developments, as seen once again in the past year 2019.

Bonds and the risk-free interest rate

We expect the environment for bonds to be especially challenging in the coming year – especially in the euro area. Even though the absolute lows were seen a few months ago, investors cannot count on the "normal interest rate course" of safe bonds today. Asset managers have to search for the best possible solutions in the given environment and take desicions proactively to achieve returns. At Schoellerbank, we stand by our quality approach in this context as well, of course. Nonetheless, in the low interest rate environment, the bond trend is also moving towards corporates. In the future, we will focus more on fundamental analysis of corporate bonds and engage in buying good debtors for our portfolios. We will also increasingly look at markets outside the core euro zone, because as the past has shown: central banks have been taking firm action to prevent sovereign debt crises for years, and the willingness to protect the euro area has highest priority, also considering the alternatives. Special topics continue to play an important role for our investments: inflation-protected bonds or an admix of foreign currencies are key building blocks for achieving returns. And when the returns are good, our Investment Committee has the possibility of looking into other yield producers – but always after carefully weighing the opportunities and risks. Our motto has not changed: invest, not speculate.

Caution with the US dollar!

After the surprisingly good development, especially of the US dollar, our assessment of this foreign currency is still rather cautious: The interest rate cycle in the US is weighing on interest spreads, and there are also other indicators that make us wary. Even though we recently slightly reduced the strong underweight for tactical considerations, we are still on the safe side with a low weighting in the US dollar. In any case, our strategy remains the same. It is an absolutely good idea to add currencies from outside the euro area, not least for diversification reasons. Interest rate advantages, regional topics and also commodity upside expectations play a major role here.

Conclusion

It is not important when you invest, but rather the fact that you invest. There is always something to worry about on capital markets, and this was true for 2019 as well. Nonetheless, past market performance for almost all asset classes was among the best in a historic comparison. Many fearful investors were scared off by the negative newsflows and stood at the sidelines, i.e. in the money market – and this is precisely where assets are being obliterated over the long term. Looking back, this is of course painful. As cautious asset managers, this is why we continue to encourage investments: analyse your personal risk appetite and your financial goals, and together with your bank advisor define what you want to achieve with your investments. And then invest today.

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