

# 2019

## The Macro Challenges and Opportunities

ANDREW COLE

---

13 June 2019

Leeds

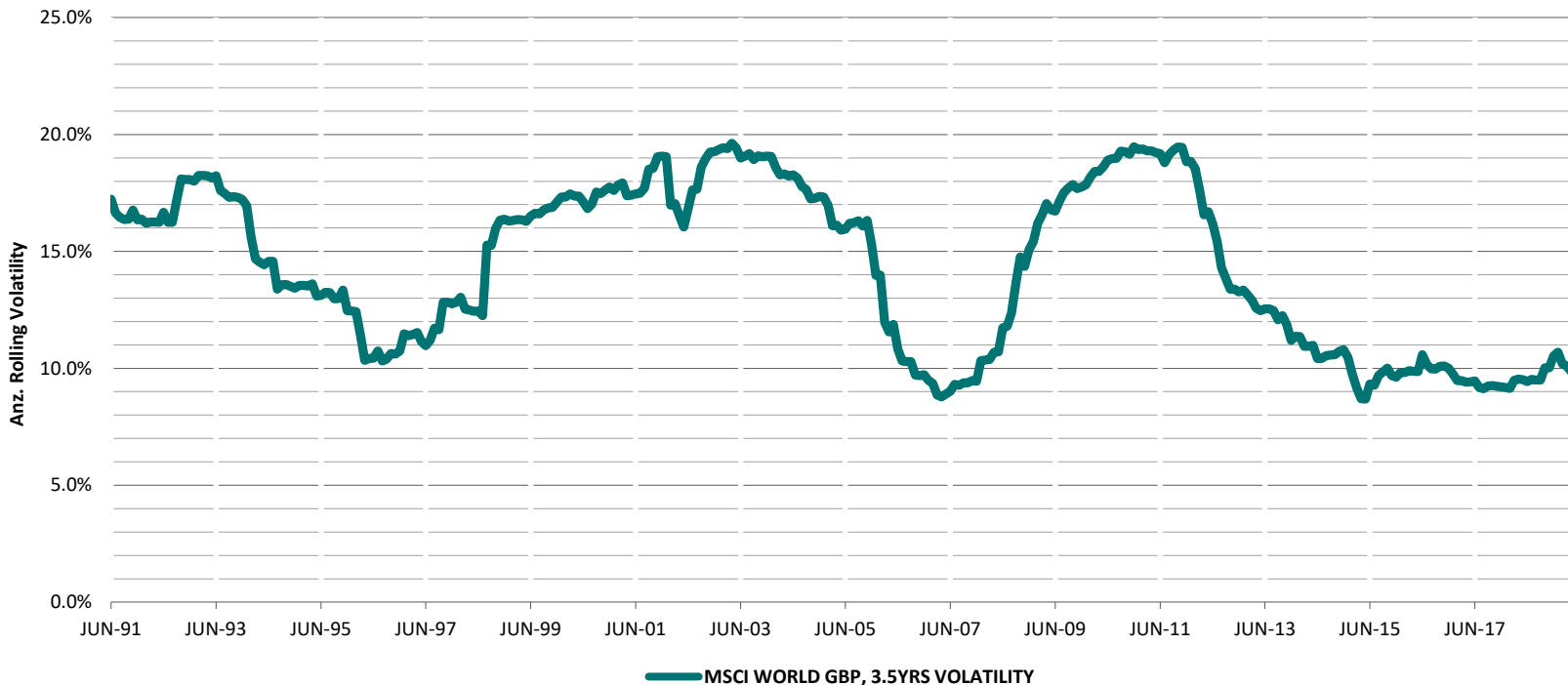


**From doom to boom?  
Perhaps not.**



# IT MIGHT BE AN UNCERTAIN WORLD BUT IT'S NOT BEEN VOLATILE

## Rolling volatility of Global Equities

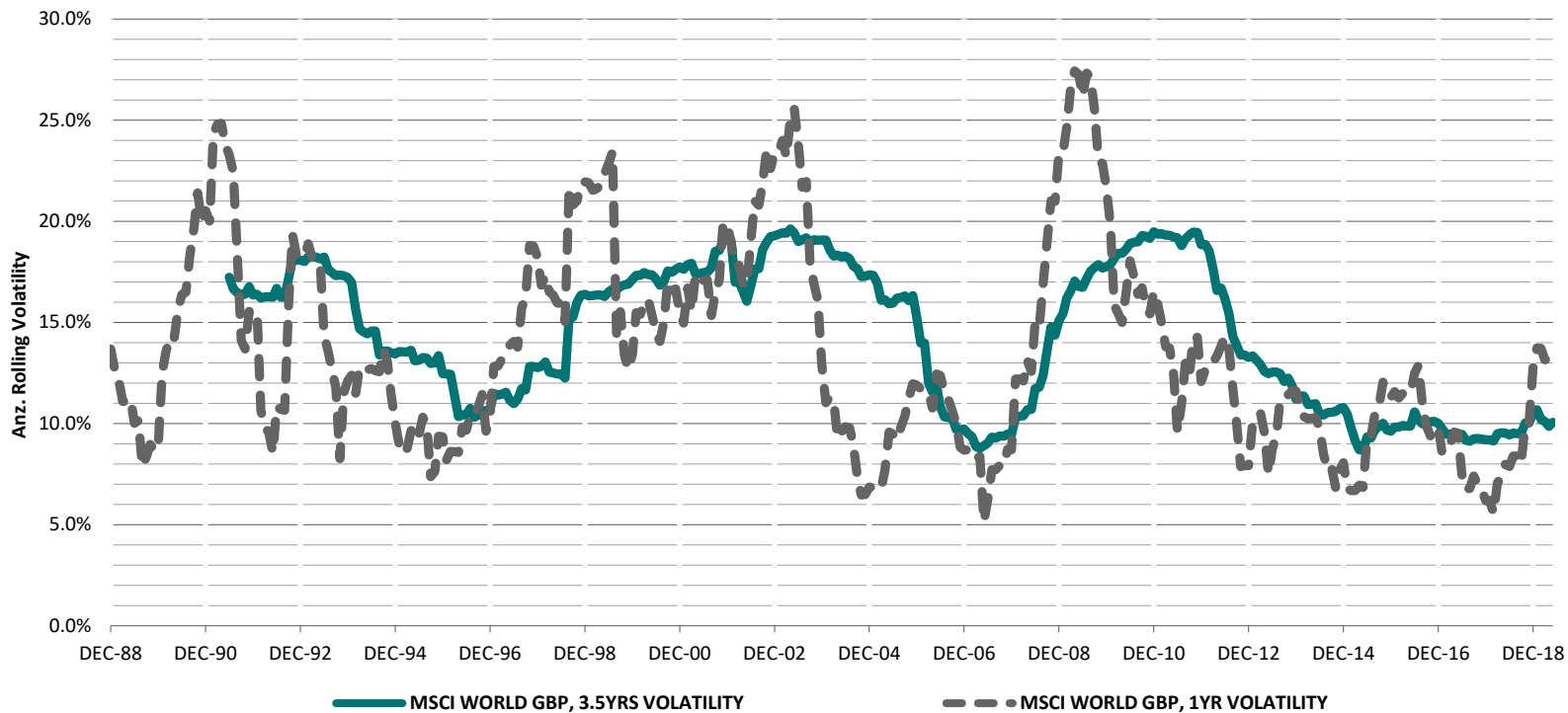


Source: Pictet Asset Management, Bloomberg



# GLOBAL EQUITY VOLATILITY

## Rolling volatility of Global Equities

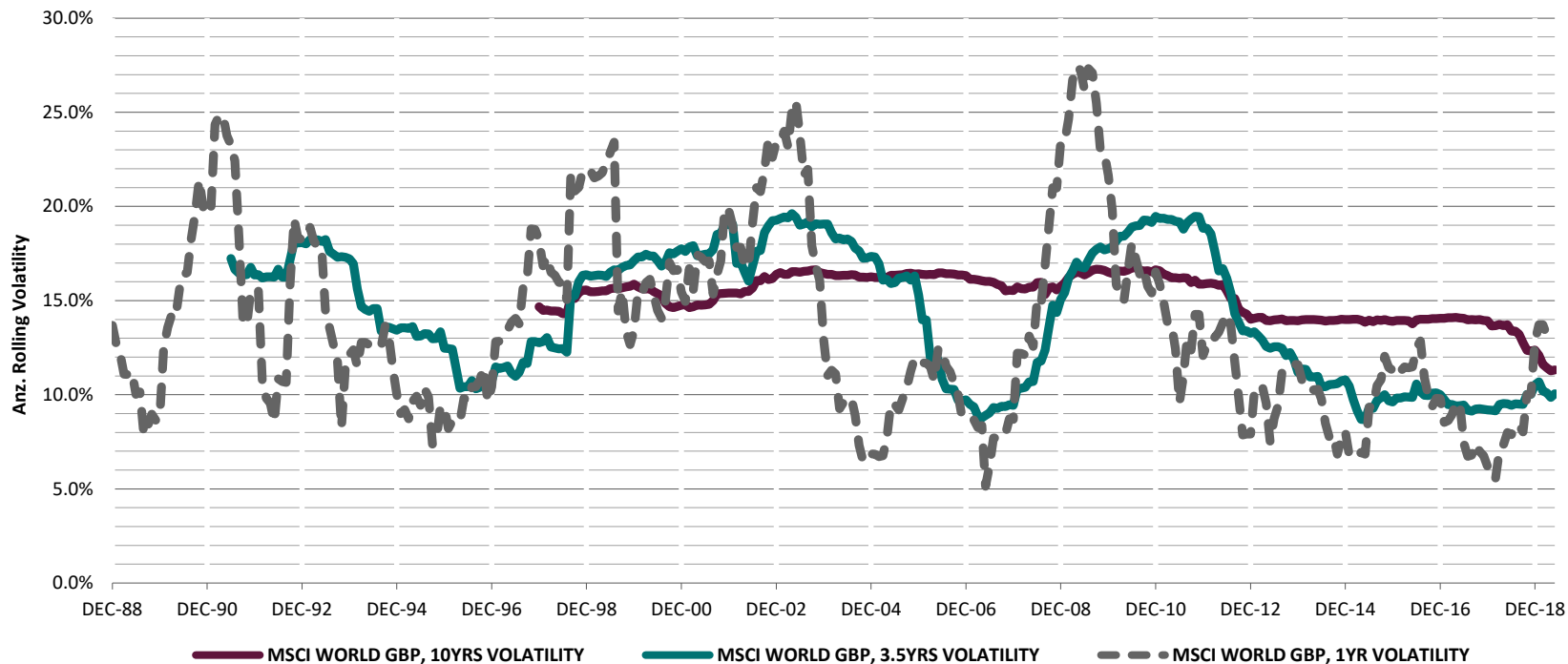


Source: Pictet Asset Management, Bloomberg



# GLOBAL EQUITY VOLATILITY

## Rolling volatility of Global Equities

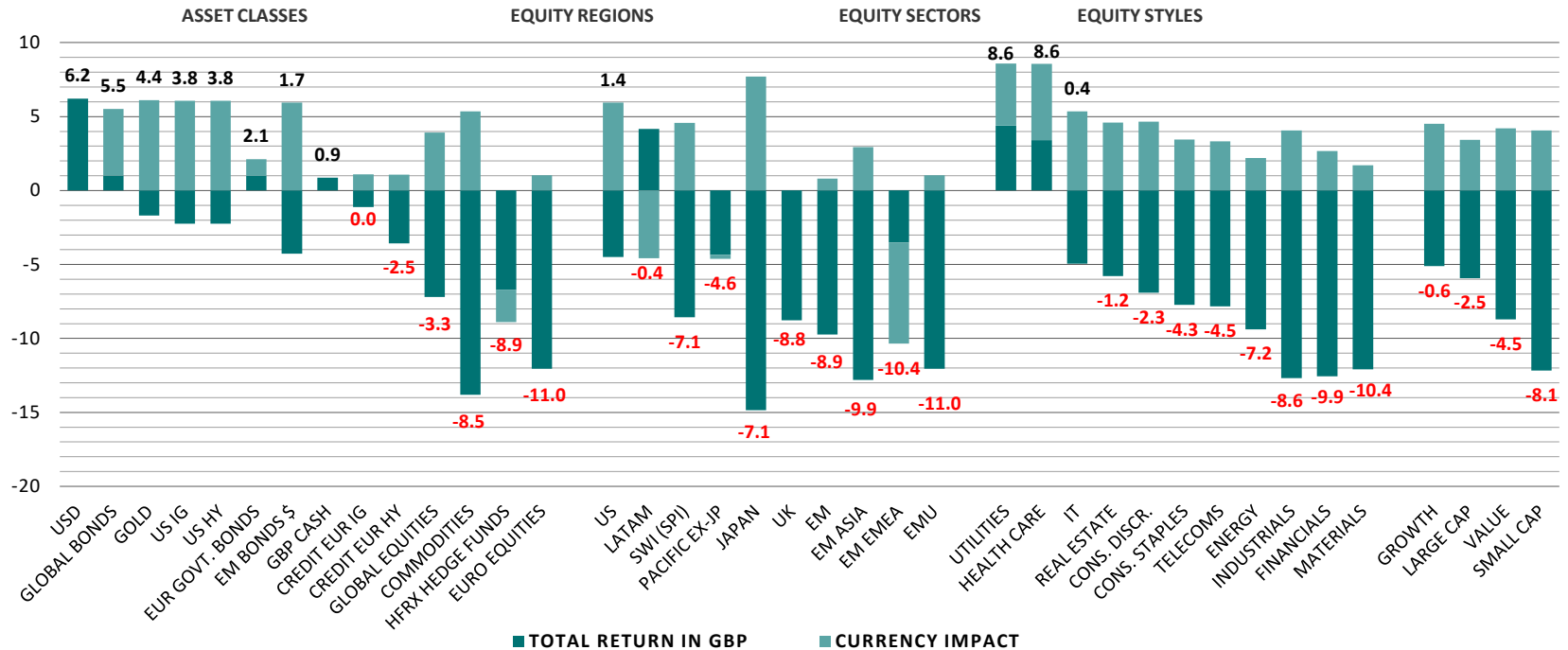


Source: Pictet Asset Management, Bloomberg



# VERY FEW PLACES TO HIDE IN FOR INVESTORS IN 2018

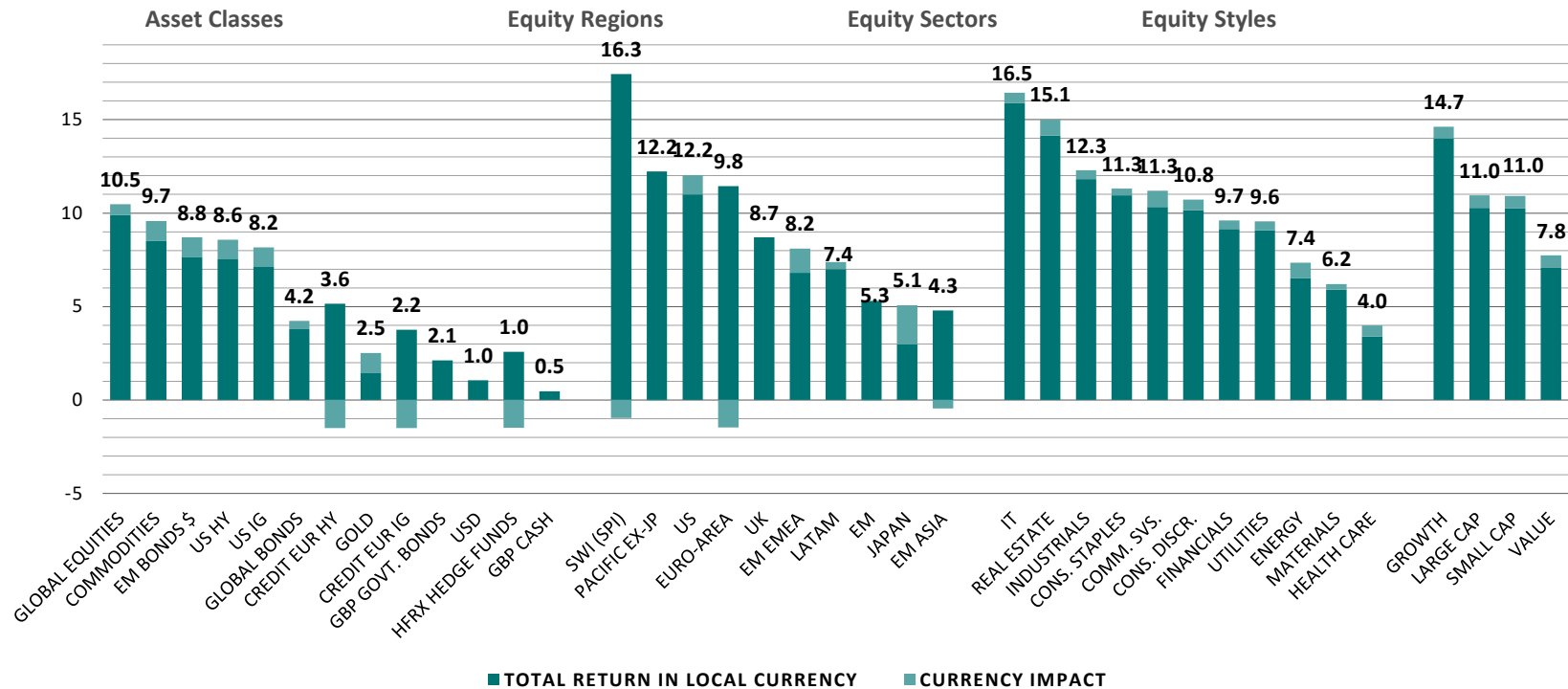
## Full year performance for selected asset classes, equity regions, sectors and styles, in local currency and GBP



Source: Datastream, Pictet Asset Management. Currency impact equals the appreciation / depreciation of the local currency vs. GBP Performance Jan – Dec 2018. The returns listed in black/red are the total returns of the asset classes in GBP including the currency impact in 2018

## ASSET CLASS RETURNS – THE YEAR SO FAR

YTD performance for selected asset classes, equity markets, sectors and styles, in local currency and GBP



Source: Datastream, Pictet Asset Management. Currency impact equals the appreciation / depreciation of the local currency vs. GBP. Data as of 31<sup>st</sup> of May 2019

## SO WHAT NOW?

---

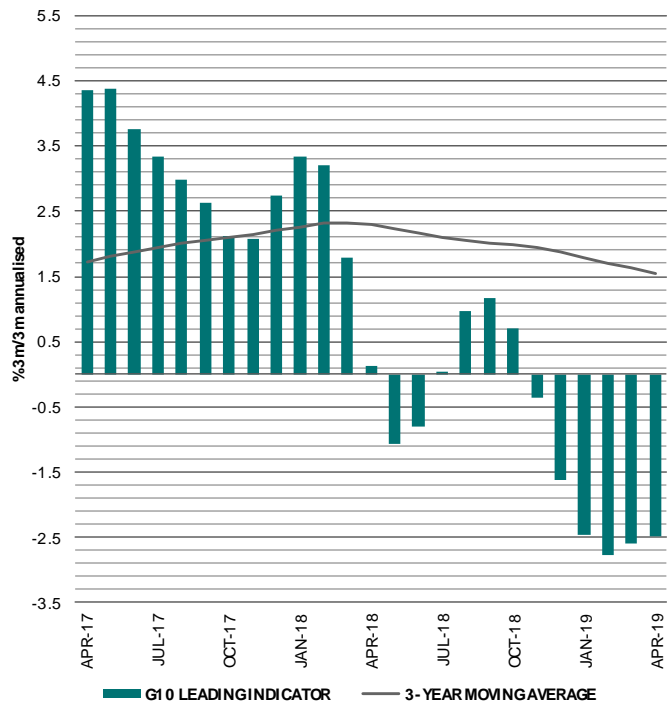
- › Developed market equity recovery liquidity driven, with macro backdrop still mixed
- › Emerging Markets: Real yields and earnings growth with favourable value
- › Trade war will have direct and indirect impacts via global value chains
- › US election uncertainty a threat to CAPEX and consumer expenditures
- › Europe sidelined and increasingly dependant on generating domestic demand
- › Defensive quality preferred in developed markets
- › Who's providing the credit how do they respond to defaults?



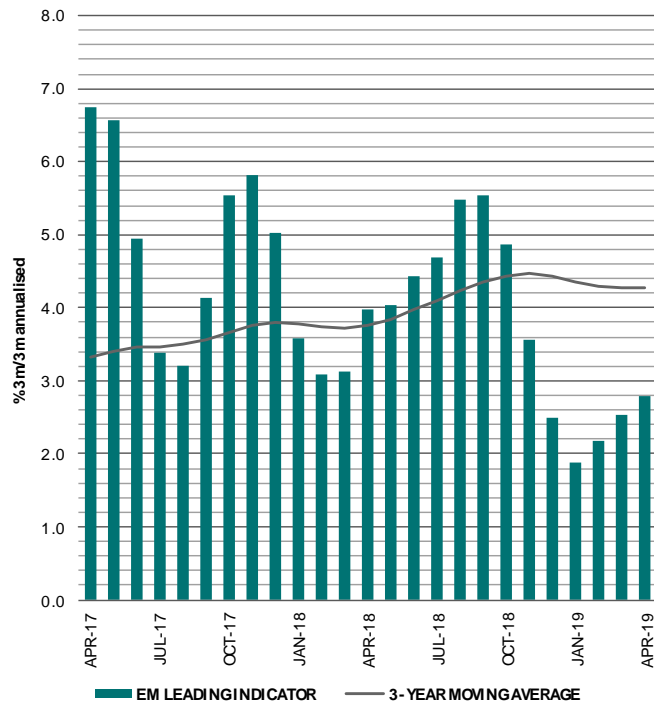


# EM ACTIVITY HAS RECOVERED WHILE DM MACRO BACKDROP REMAINS MIXED

## DM leading indicator (3m/3m growth)



## EM leading indicator (3m/3m growth)



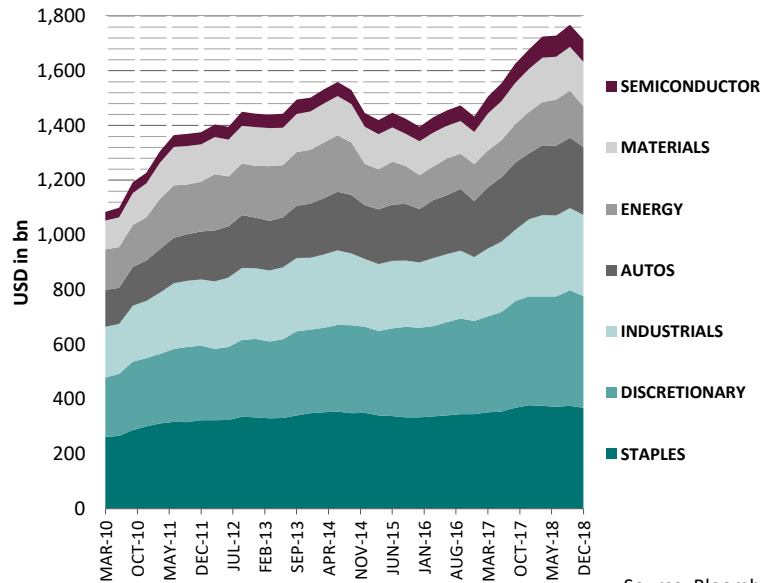
Weighted average of 10 countries (in DM) and 24 countries (in EM) leading indicators.

Source: Pictet Asset Management, BIS, CEIC, Datastream.

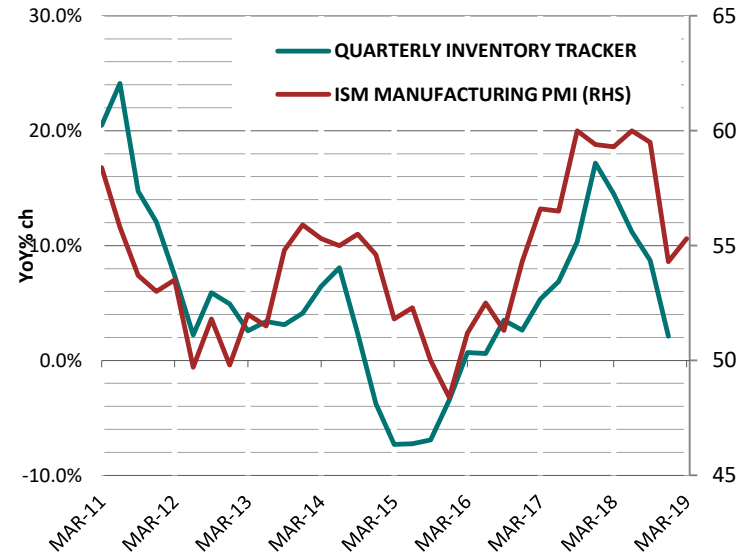
# GLOBAL INVENTORY: DESTOCKING IS AN OVERHANG FOR MACRO

- › Quarterly inventory of the biggest cyclical companies showed severe stock build ahead of the trade dispute.
- › Restocking momentum peaked at the beginning of 2018 and preceded the deterioration in the ISM.
- › The current destocking cycle has lasted for more than 4 quarters, suggesting a bottom in industrial activities is near.

Quarterly Inventory Tracker (Aggregate value by target industries)



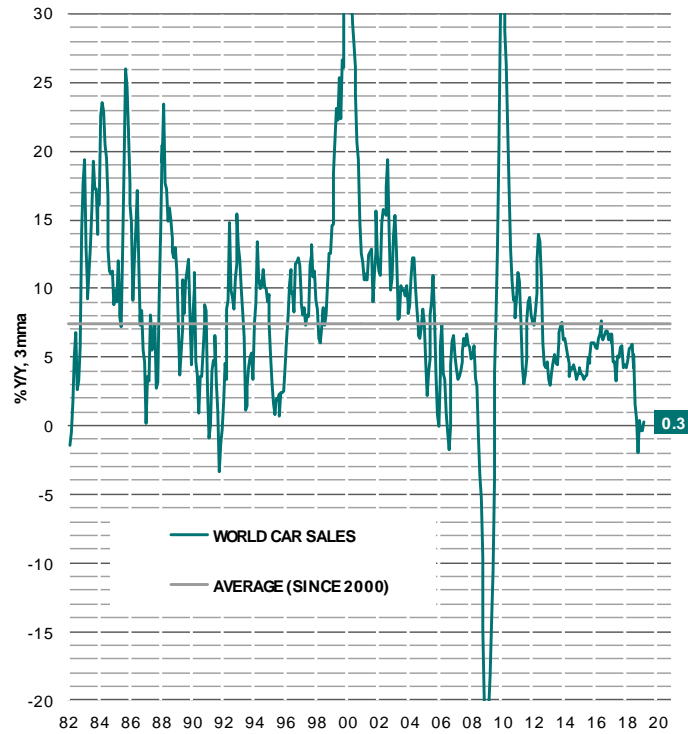
Quarterly Inventory Tracker (YoY % change)



Source: Bloomberg, Pictet Asset Management.

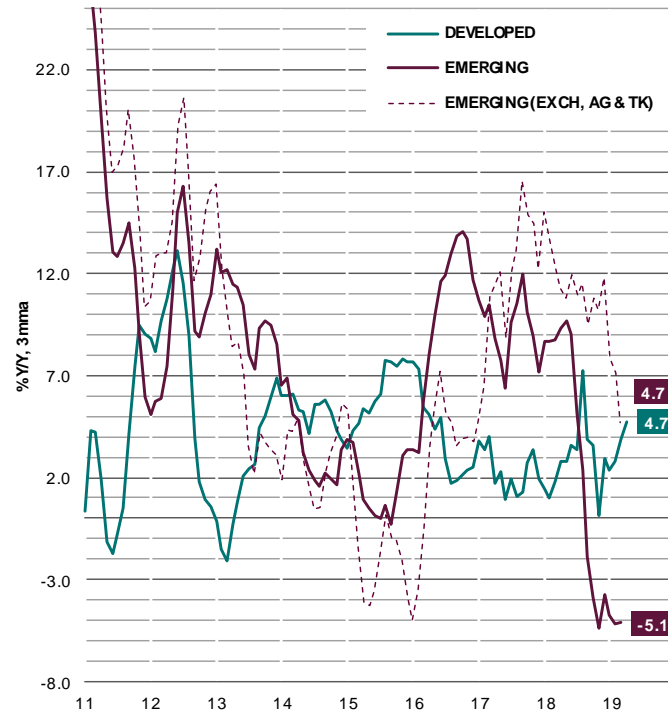
# WORLD CAR SALES

## World car sales (volume, %Y/Y, 3mma)



Source: Pictet Asset Management, BIS, CEIC, Datastream

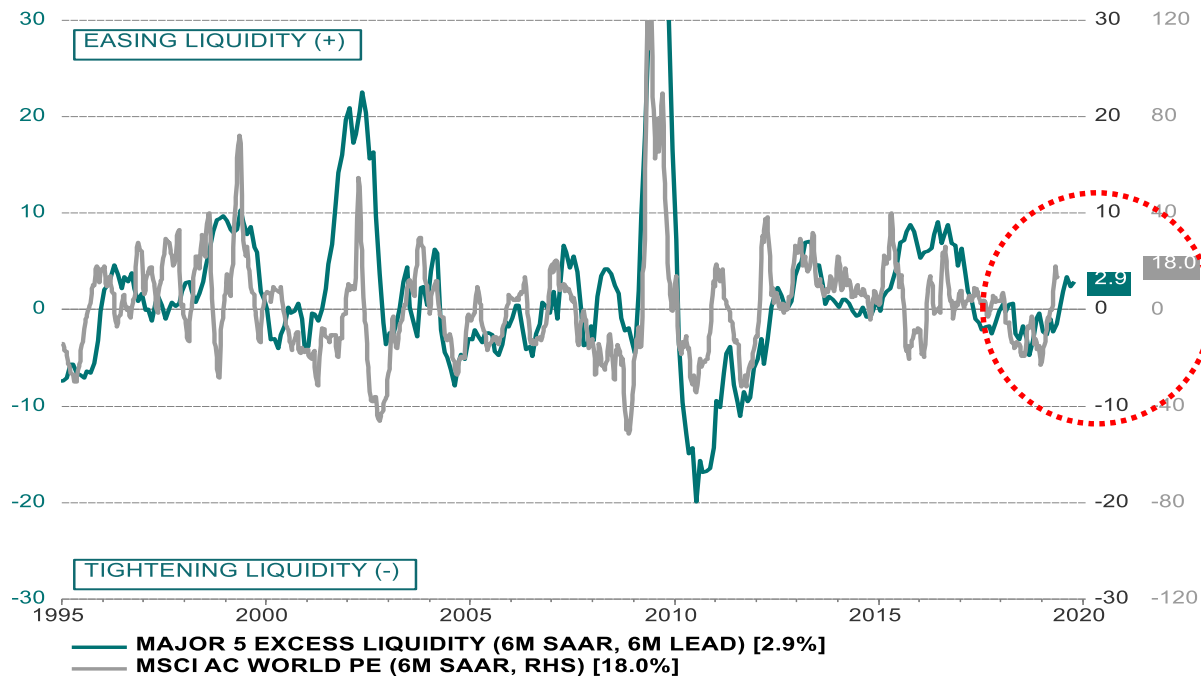
## World, DM & EM car sales (volume, %Y/Y, 3mma)





# MARKET VALUATIONS HAVE OVER-DISCOUNTED EXCESS LIQUIDITY

## Major 5 – Excess Liquidity (6-Month SAAR)

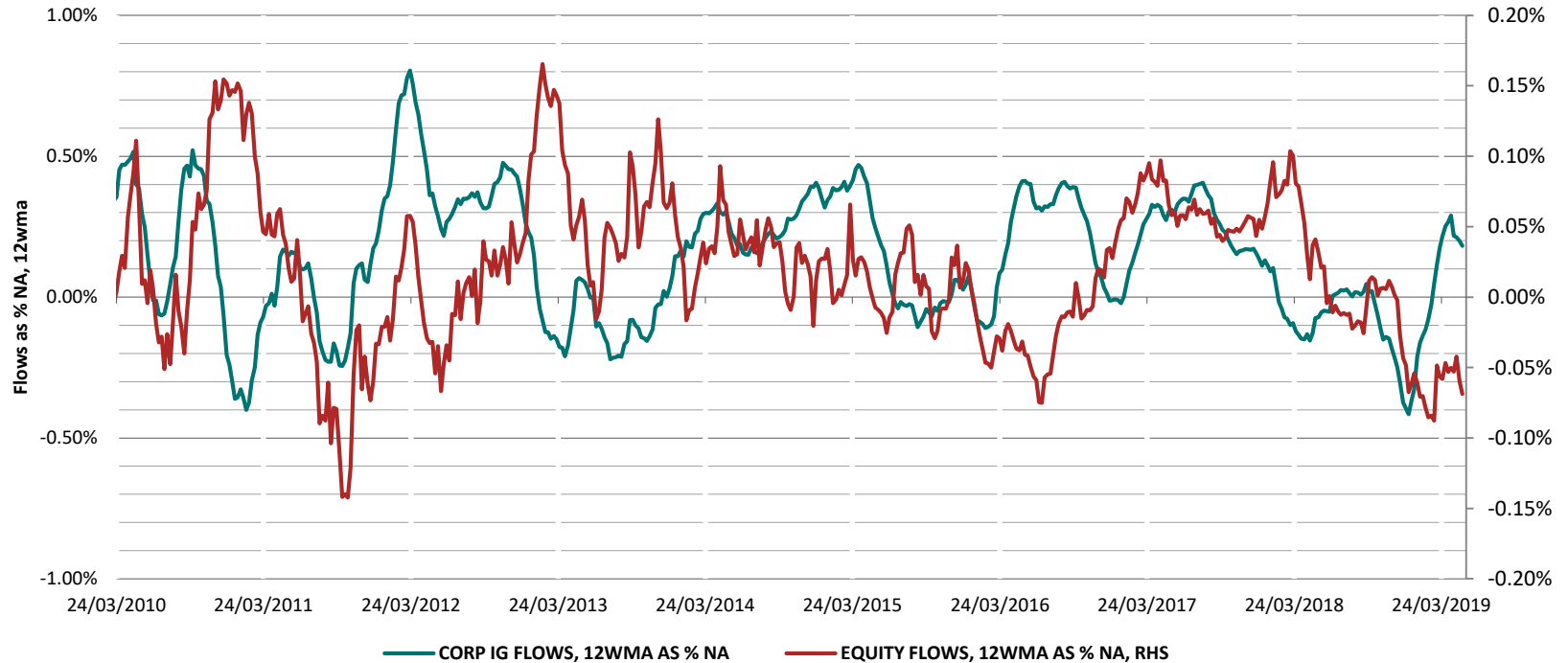


Source: Datastream, Thompson Reuters, Pictet Asset Management



# DIVERGENCE BETWEEN CREDIT AND EQUITY FLOWS

## Global Corporate Credit and Equity Flows, 12w MA as % Net Assets

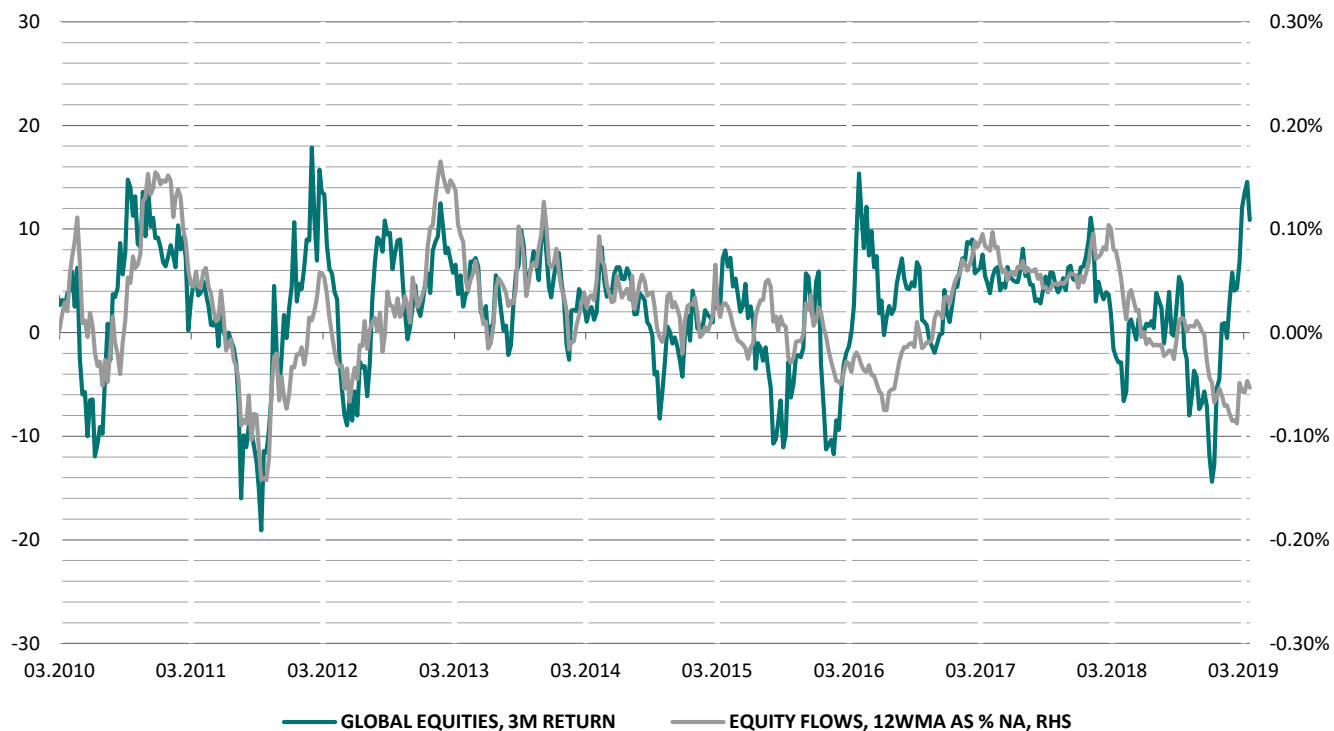


Source: EPFR



# BIG EQUITY GAINS DESPITE LOW FLOWS

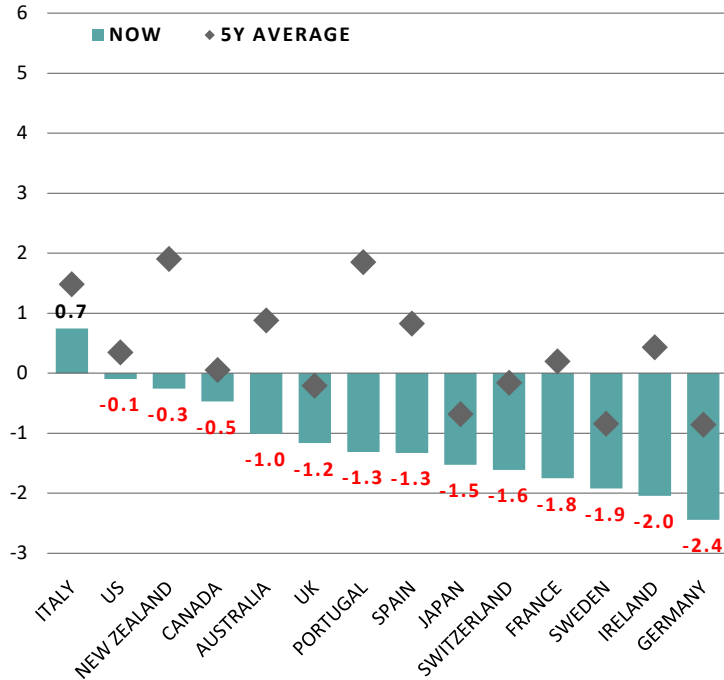
## Global Equity flows vs. 3m equity return



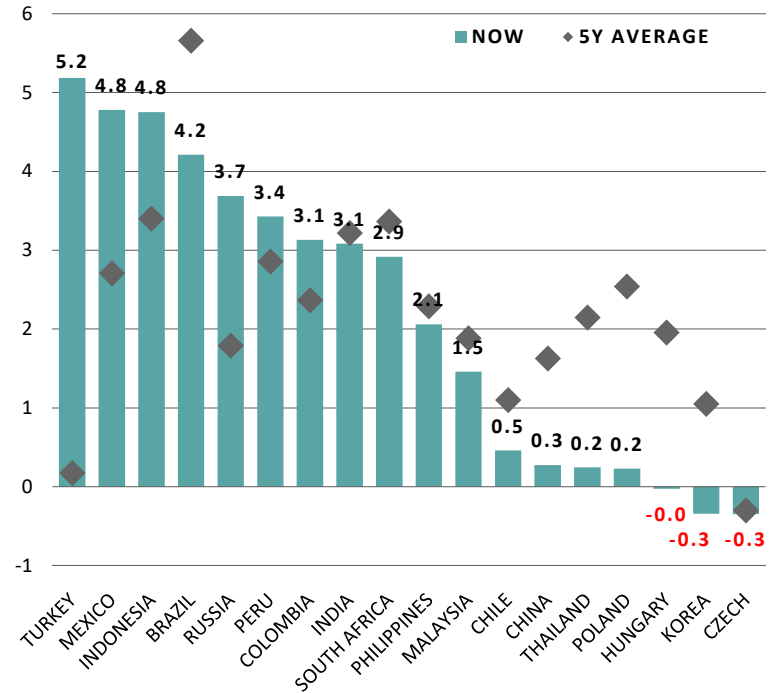
Source: Datastream, EPFR

# POCKETS OF VALUE IN SOME GOVERNMENT BOND MARKETS

## DM real bond yield\*



## EM real bond yield\*

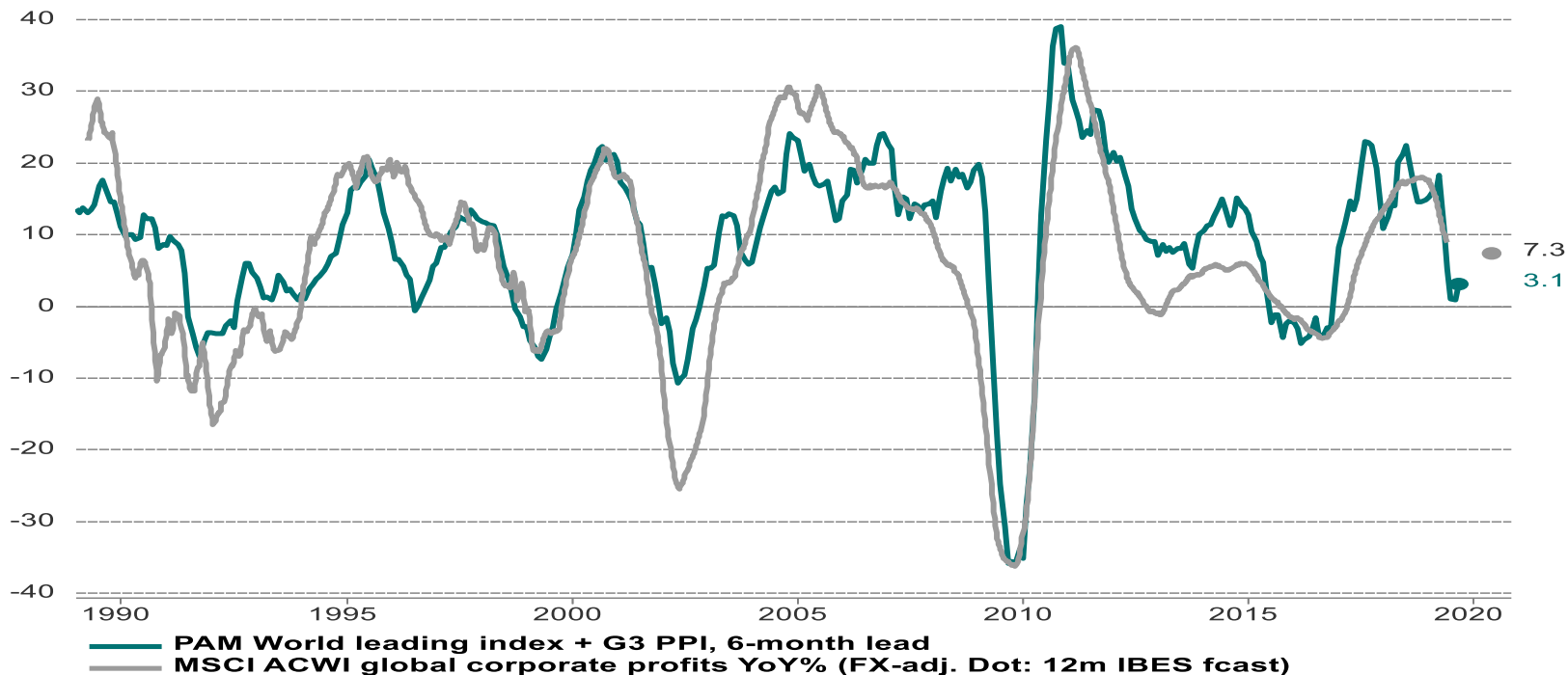


\*Real yield based on 10Y local currency government bond yield (9Y for Peru) minus trend headline inflation (using IMF forecast over next 5 years as a proxy). Source: Datastream, IMF, Pictet Asset Management. As of 11th June 2019



## CORPORATE PROFIT CYCLE PEAKED IN 2018

Pam World leading index + G3 PPI and corporate profits



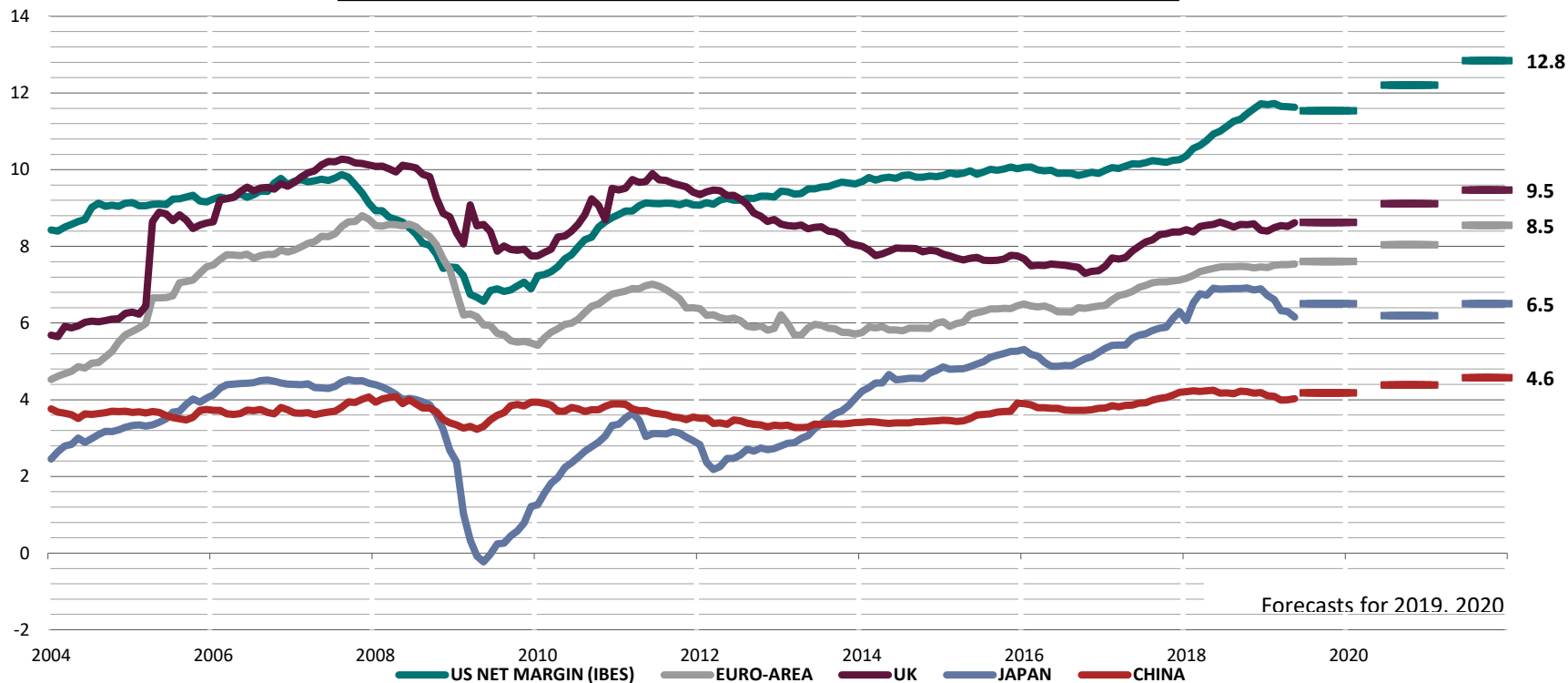
Source: Pictet Asset Management, Datastream





# CONSENSUS EXPECTATIONS FOR CORPORATE MARGINS ARE OVERBLOWN

## Net margin consensus forecasts (IBES) for 2019, 2020 and 2021

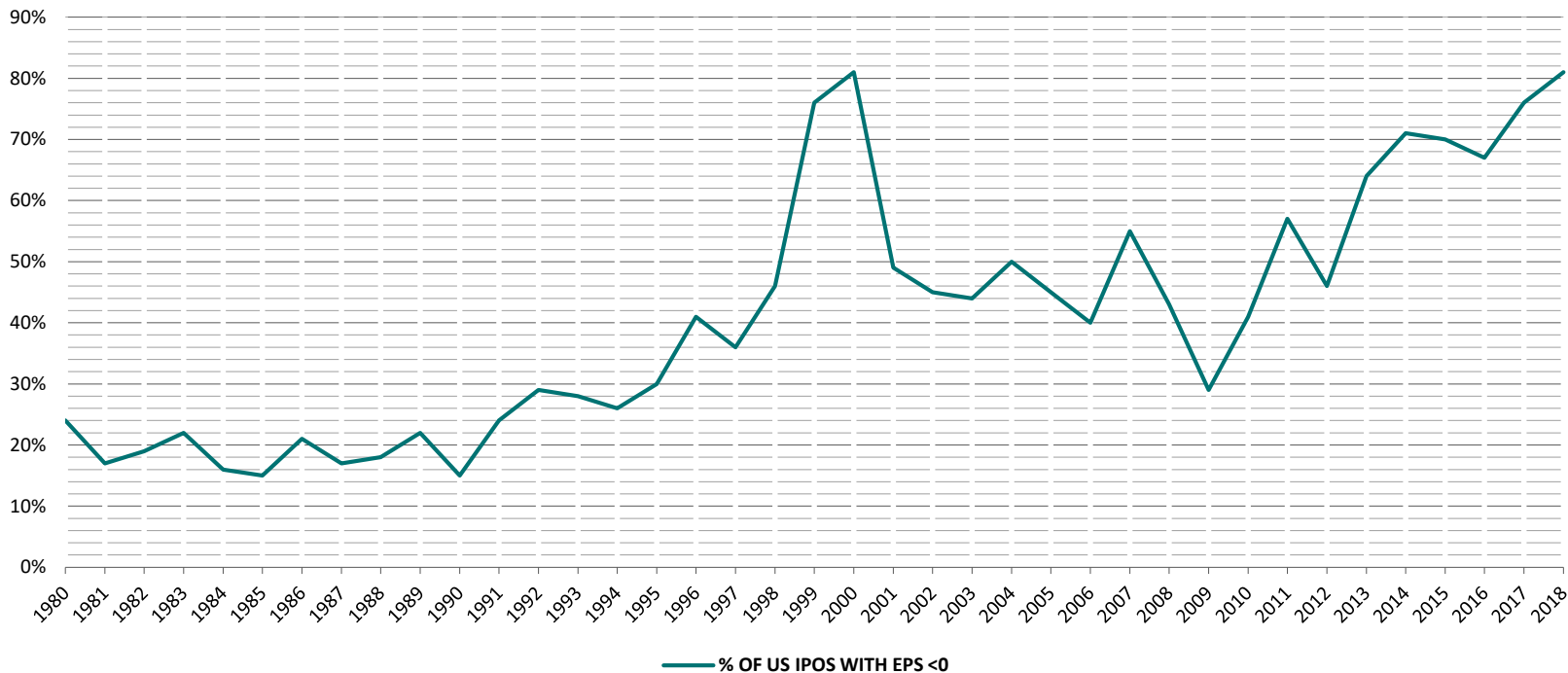


Source: Datastream, IBES



# UNPROFITABLE COMPANIES LISTING

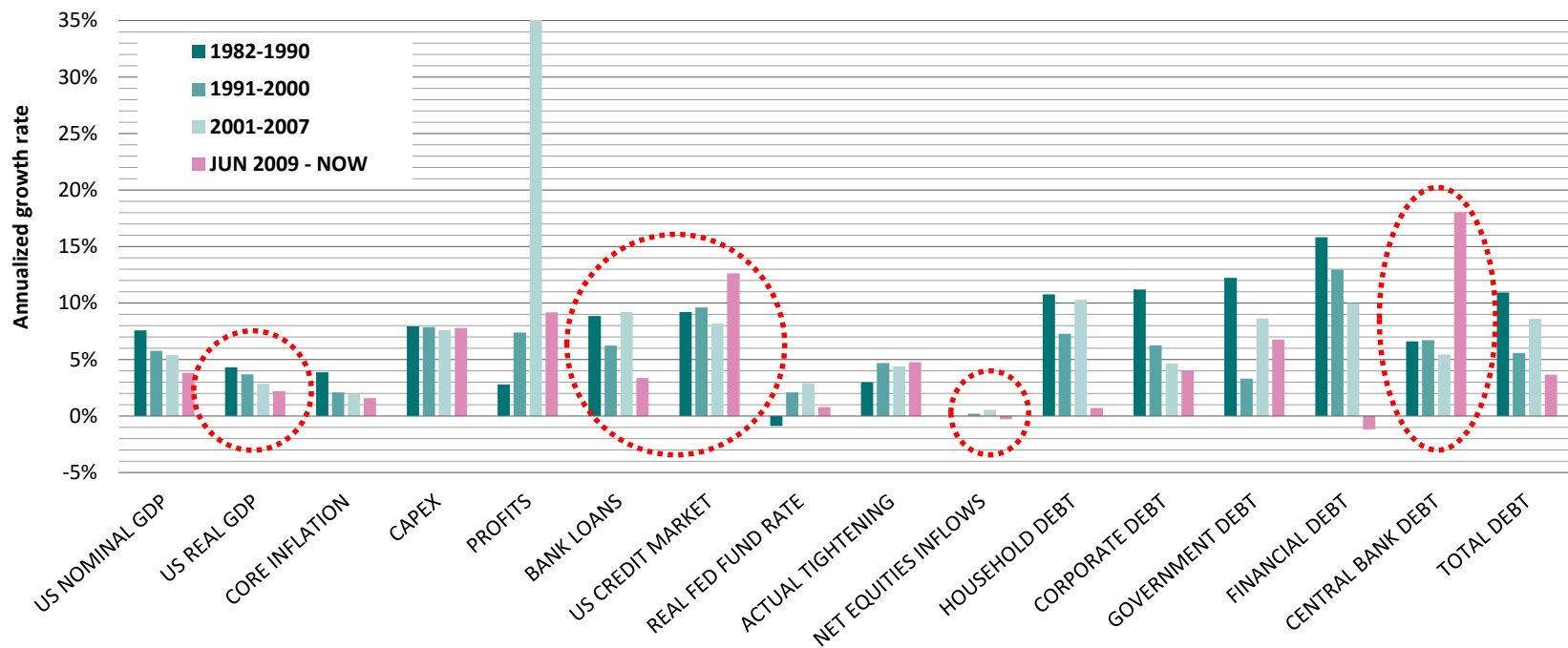
## Percentage of unprofitable IPOs in the US



Source: Jay Ritter, University of Florida. Includes operating companies going public in the us.

# IT HAS BEEN A LONG CYCLE

## Macro and financial variables in the last 4 business & market cycles\*

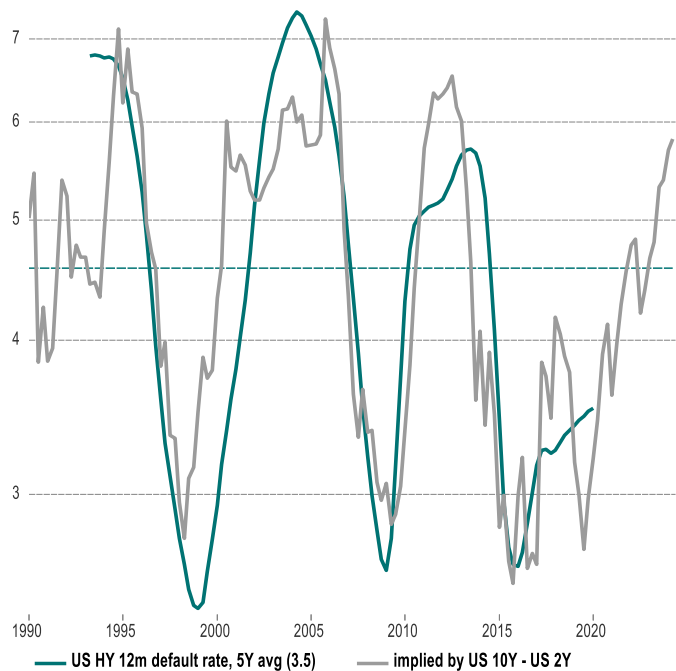


Source: Datastream. \*annualized growth since start of recovery (bull market for equities).  
 Cumulative change for real fed fund rate and (actual tightening: including "shadow rate") for net equities inflows as % of market cap.



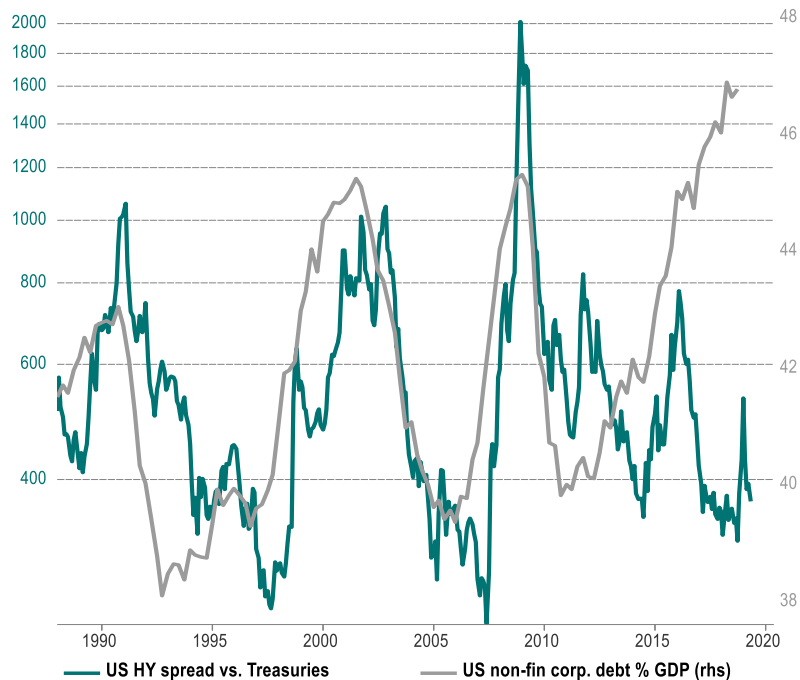
# CORPORATE BONDS VERY VULNERABLE AS CREDIT QUALITY SET TO DETERIORATE

### US yield curve and high-yield default rate (average over 5 years)



Source: Datastream, Moody's, Pictet Asset Management, as of 30<sup>th</sup> April 2019

### US high-yield spread vs US Treasuries and corporate leverage

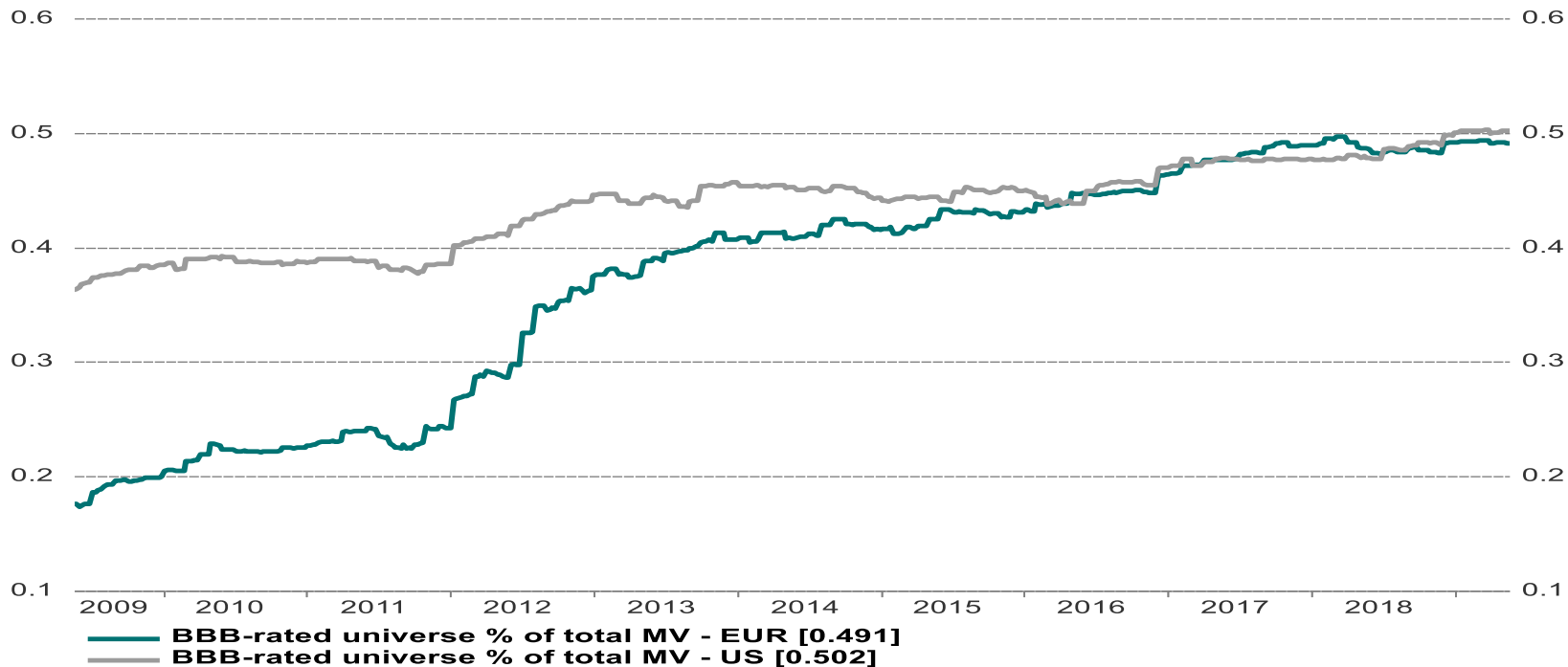


Source: Datastream, Pictet Asset Management, as of 31<sup>st</sup> March 2019



# WIDESPREAD FINANCIAL ENGINEERING

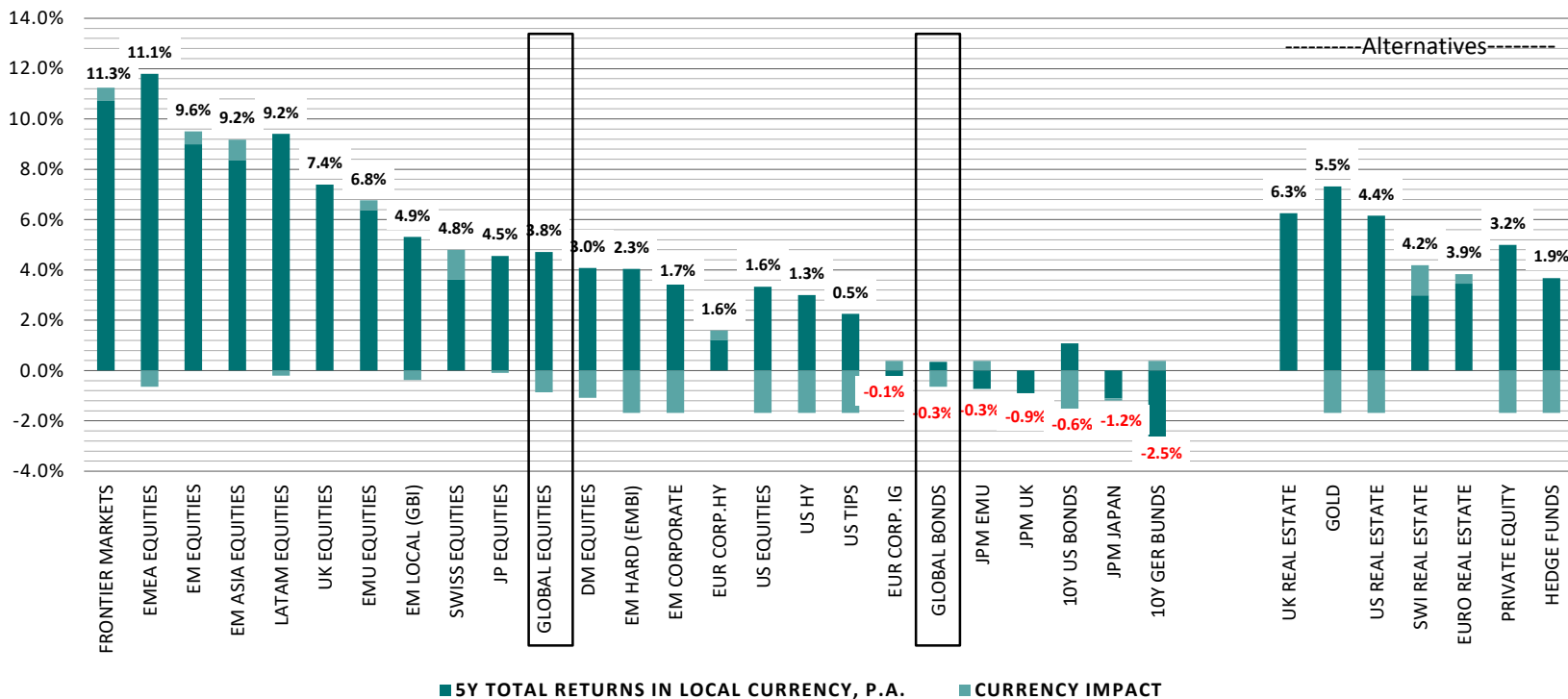
## US and Europe: BBB-rated corporate universe as % of total



Source: Bloomberg, Includes

# LONG-TERM ASSET CLASSES RETURN FORECASTS

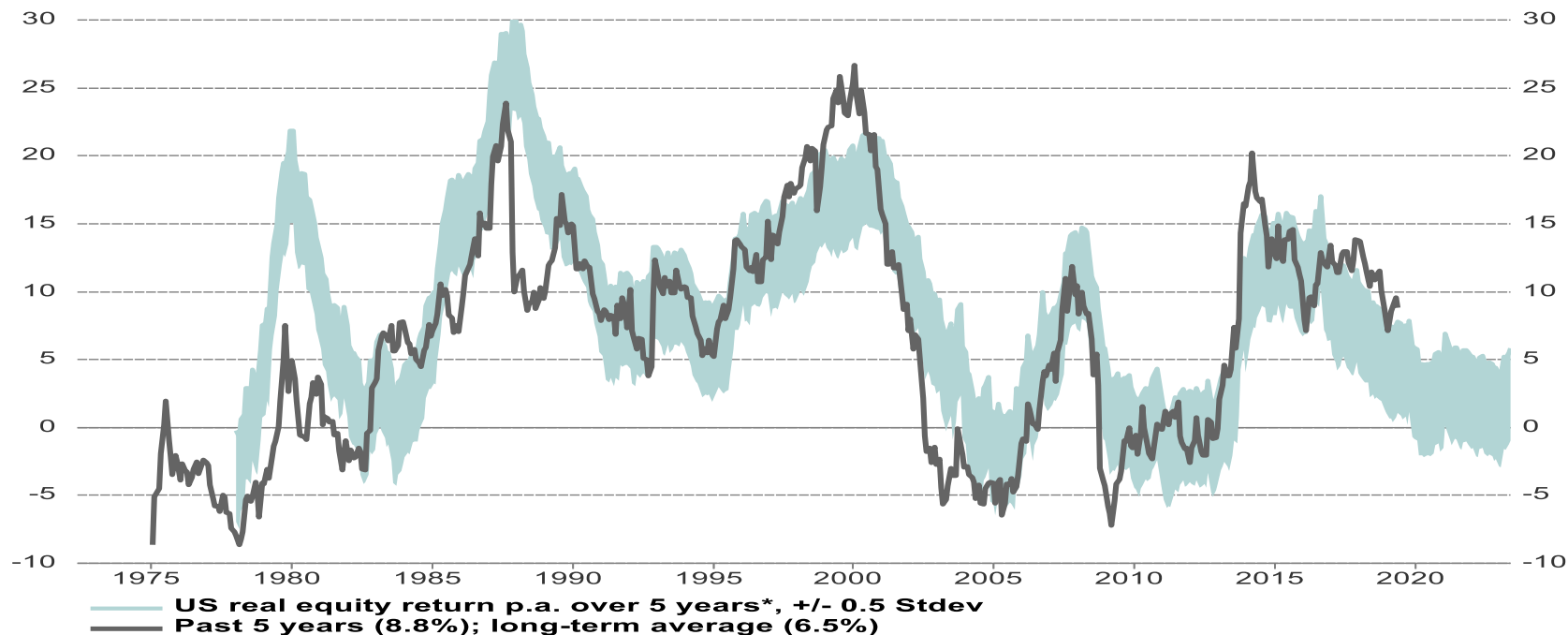
## Asset classes 5Y return forecasts in GBP, p.a.



Source: Datastream, Pictet Asset Management, as of 31<sup>st</sup> March 2019. Frontier markets include Kuwait, Vietnam, Morocco, Nigeria, Kenya, Sri Lanka and others.

# EQUITY RETURNS TO BE WELL BELOW AVERAGE IN THE NEXT 5 YEARS

## Expected real return of US equities over the next 5 years\* (p.a. in %)



\*Model based on based on trend and deviation from trend of US real GDP growth, price/earnings ratio and CBO forecasts of US bond yields in 5 years' time.

Source: Datastream, Pictet Asset Management, as of 30<sup>th</sup> April 2019.



## AN OPPORTUNITY WITH VOLATILITY LOW



Source: Bloomberg. Data as at 18.04.2019





## OUR PORTFOLIO: WHAT WE FAVOUR

---

### Equities

- › Asian equities: domestic demand, national champions whose growth is under-priced
- › Developed market equities: low leverage, high quality growth, US centric

### Bonds

- › Treasury Inflation Protected Securities (TIPs): Declining real yields
- › Emerging Markets local currency bond & hard currency bonds: Financial conditions improved
- › Australian government bonds: slower credit & economic growth, and RBA adopting a more accommodative stance

### Alternatives

- › Gold/gold mining stocks and transportation asset leasing
- › Volatility is low so upside optionality (Convertibles)

*Current risk profile below average.*

*Dry powder, ie cash,  
available for meaningful and timely changes to portfolio in the event of market volatility.*