Investec
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Preparing for cyclical change

The world is changing and investors will need to make significant changes to the portfolios to exploit those changes, said Philip Saunders of Investec Asset Management.

While consensus has been about secular stagnation and low growth, there has been significant change in underlying cyclical conditions. "In 2017, barring any significant shock, we should see synchronised global growth," predicted Philip Saunders, co-head of multi-asset growth at Investec Asset Management, at the Investec Global Insights Asia forum in Hong Kong in late 2016.

The evidence is mounting. And market data across regions shows that since July 2016, there has been a significant rotation away from interest rate-sensitive and defensive equities towards more cyclical exposure.

Commodity prices started to bottom-out late last year, although oil prices remained a lagging indicator. Investor sentiment on commodities and metals was still highly negative back then but as history frequently shows, that is often associated with a turning point. "Gold mining stocks, which took off in remarkable fashion as we entered this year, was the first indicator that cyclical change was underway," said Saunders.

There is also now growing debate about the continuation of ultra-easy monetary policies, which, while much needed in the aftermath of the global financial crisis, seems to have reached its limits. One indication of that is Japan moving away from QE to QQE – focusing on the yield curve.

That is because too much easing has contributed to asset price bubbles, capital misallocation and depressed productivity growth. "Asset price inflation has also had social, economic and political impact, most visibly in the rise of populism around the world," he said. In addition, the typical indicators suggest the risk of recession is receding.

It's a similar story in China, where the narrative has been all about a potential hard landing and the use of excessive debt to create growth. But the truth is, economic picture has improved and it has an impact from a cyclical perspective.

Yet investors have failed to pay attention to these significant changes. "In financial markets, we seems to be misdirected, obsessing over things that are not important," said Saunders.

So what are the implications of a Trump presidency? "We have a pro-growth president and Republicans controlling both houses, which is typically good for markets. Unlike politicians, Trump is also a businessman, which means he can get things done. But what he gets done, we still have to wait and see."

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Currently, markets have been too heavily and unusually influenced by macro factors. But it is beginning to change and it will only be a matter of time before the cyclical growth trend gathers momentum. ■

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