Amplia Monthly Investment Letter

June – a month without drama

June was the second-best month of the year on global stock markets, with key indices such as S&P 500 and NASDAQ rising by 6.89% and 7.42%, respectively. The parallel flow of supporting messages from politics (a G20 meeting without drama and plenty of goodwill) and the choir of central banks singing about quantitative easing meant that investors could breathe out and jump on the markets again.

Does the tranquility continue in July?

July started well, with investors still digesting the prospect of lower interest rates across continents, currencies and maturities. However, a sign of unease surfaced on Friday 5th, as the US job numbers were interpreted as “too good”, with the US creating 224’000 new jobs in June alone. Investors immediately drew a parallel between the strong labour market and interest rates not drifting any lower. Whilst we fully agree with the markets here, to us the incident especially demonstrates the degree to which markets are dependent on central bank support as the driver of continuing growth.

As more and more investors are preparing for summer holidays, we do not expect July to bring any big moves with it. We would expect the upcoming 2nd quarter earnings season, which will start on Tuesday 9th July with PepsiCo reporting, as well as the Fed meeting of 31st July to be the biggest market movers, alongside any political surprises. Given that the latter flare up the minute you least expect it, there is little one can do but to stress-test one’s holdings for murkier times and stick to one’s guns.

Our markets positioning

We remain risk on and are comfortable with our present market positioning. However, the strengthening central bank support has led us to allocate larger amounts from stock markets to fixed income and alternative income sources.

Our base case remains that an escalation of the trade war will be avoided, and the Americans and the Chinese will be able to reach a deal before the current tariffs and uncertainty wreak too much havoc on the economy.

The risks to this view remain considerable, but in the current environment we must work with scenarios. At the moment, both fundamentals and market psychology are still developing positively and thus speak for a risk-on approach when it comes to equities.

With regards to fundamental data, the afore-mentioned monetary policy remains the biggest positive cornerstone. Also consumption data are good, and valuations appealing. The only worrying tone comes from industry and service sectors, where many lead indicators such as US CEO Confidence in Economy, still point towards a cool-down.

Meanwhile, hedging demand remains high, which is a latent sign of investor nervousness. Also, the flows to risky assets have ebbed lately, although this could partially be explained by the lesser liquidity due to the approaching holiday season. Despite these phenomena, the previous weeks’ market moves were broad-based and supported by considerable volumes. In addition, economic figures have been surprising the markets nicely if compared to the expectations. All this resonates well with a risk-on view.

Asset allocation - July 2019	
Industry	↘
Consumption	↗
Monetary environment	↗
Market valuation	↗
Fundamentals total	↗
Hedging demand	↘
Economic surprises	↗
Market risk	↗
Market breadth	↗
Money flow into risky assets	↘
Risk sentiment total	↗
Equity exposure (of maximum)	**100%**

Of equity sectors, we favour health care, consumer discretionary and information technology. Especially the latter one is admittedly exposed to trade negotiation developments, and hence our overweight reflects the upside potential in case of no escalation. In exchange, we underweight communication services and listed real estate.

In the past nine months we have enjoyed strong tailwinds from a combination of lower-drifting to stable benchmark yields and – from January onwards – falling credit spreads. Whilst we do not expect any significant credit spread compression from here on, the willingness of the central banks to keep printing money is flattening the yield curve further and pressing down the benchmark rates. Simultaneously, many corporates seem to take advantage of the situation and new issuance of corporate debt remains abundant. In this situation, we keep favouring USD-denominated corporate bonds with a duration of 5 – 7 years as well as selective high-yield debt issuance in euros, primarily from Scandinavia.

As to currencies, we keep our positioning unchanged. GBP remains undervalued based on most metrics, but the risk of a hard-Brexit is weighing on its valuation. However, because Brexit is an “either-or” event, for those who believe in a sensible outcome, GBP remains attractive.

We keep our forecasts of EUR/USD (rangebound at 1.11 – 1.15) and our preference of CHF over EUR unchanged, since the Swiss Franc could see considerable inflows in case of a political fall-out or other unexpected shock rattling the markets. We are pleased to see the Swedish Krona recovering some of its losses versus the Euro from May, although SEK remains a prisoner of Riksbank’s policy mandate. Should the ongoing debate in Sweden lead to a change in Riksbank’s inflation targeting, SEK could gain against EUR and USD. The chances for this are however not huge, and thus we make use of the weak krona via Swedish equity and bond investments in the first place.

In Zurich on 9th July 2019

Yours sincerely,
Juho Kivioja

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