Amplia Monthly Investment Letter

The end game

For more than a year, the same topics have dominated the macroeconomic – and especially political – discussion, up to a point where investors have started to turn numb and tired of it. Trump administration's tariff twists with their Chinese counterparts and Brexit negotiations have taken ever-new turns, moving markets along as news have broken.

Last week's agreement between the US and China, no matter whether one interprets it as a truce or peace treaty, combined with positive tones from Brexit, almost raise our hopes that we could finally leave these concerns behind us. Whilst the tone of argumentation has – especially in the case of Brexit debate in the House of Commons – at least occasionally born an uncanny resemblance to a stage play of Shakespeare, the themes start to be gradually worn out. Based on this, we remain hopeful that both political issues could be set aside for the next months. We remain hopeful that investors, consumers and corporates could plan their future with more visibility on the future and focus on more mundane decisions and matters at hand.

It's all about the sentiment

The trade truce could prove a welcome development for the investor and corporate sentiment. In particular Europe is highly dependant on global trade flows, and thus a pause in tariffs could help the manufacturing to bottom out on both sides of the Atlantic. Whilst manufacturing only accounted for 11.6% of US GDP in 2018, and somewhat more in the Eurozone (15%), it has an important role for the overall consumer sentiment in Europe. It is also well interlinked with the services sector in countries like Germany.

Given the global slow-down in inflation and persisting weakness in both services and manufacturing data, a concentrated effort of fiscal stimulus and central bank easing is prepared in many leading economies across the globe. In the US, we believe Trump administration to stay on the select course and not introduce any further measures, as the biggest ones (tax law overhauls, corporate overseas cash repatriation, infrastructure spending programs) have already taken effect, and hence the responsibility of demand stimulation lies at the Fed. This is also commensurate, given the steepening Federal budget deficit (-4.4% of GDP as of August) and the still-positive treasury yields (whose long end has recently luckily corrected upwards), speak for expansion of monetary instead of fiscal policy.

In Europe, the mantra should be that those countries stimulate who can afford it. This primarily applies to the Northern European states with AA or AAA credit ratings. This is also currently happening in Germany where the government is embarking on a massive infrastructure and green energy stimulus.

Meanwhile in Asia, Chinese government's U-turn from reigning shadow banking and credit growth to implicitly fostering them will help alleviate the drop in GDP growth that is forecast to land at 6.1% for Q3. In Japan, PM Abe is ready to act if "downside risks were to materialise". The US-Japan trade pact has removed the immediate threat of additional tariffs on Japanese exports.

In Emerging markets, the situation should be brighter than a year ago in Russia, Brazil, Iran and Turkey, although the latter's situation may change as the Syrian situation evolves.

To conclude, the global growth is slowing: a view that is shared by many observers such as IMF which revised its 2019 global growth forecast to 3.0%, lowest since the financial crisis of 2009. This *should* still be enough to avoid a recession in any of the important economic blocks.

In the meanwhile, our focus lies on the ongoing third-quarter earnings season and – as previously argued – Trump's tweets and central bank communication.

Our markets positioning

Asset allocation - October 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%**

We favour health care, energy and financials (the latter two mostly due to the valuations and income yield). We remove real estate from the preferences, following the strong performance of the recent two months. We underweight utilities, as we give more space to cyclicals amid the more positive macro outlook.

On the fixed income side, the picture remains good. Credit spreads remain at very low levels. There is practically no upwards pressure in benchmark rates in any developed markets' currencies. We continue to favour low investment grade issuers and high (BB+ to BBB-) high yield notes, with maturity of 5 – 12 years in USD. For euro investors, Nordic, non-rated and variable-rate debt with adequate covenants and debt metrics is still our preference.

With regards to currencies, we would gradually consider EUR attractive vs. USD at levels of 1.10 and below. Monetary policy and trade flows development should result in slight strengthening of the euro. The pound Sterling, in its turn, may have reached the zenith of its short-term cap at the current GBP/USD levels around 1.29. We still consider the SEK attractive vs. EUR, and remain SEK buyers, with target levels at 10.60. Gold is worth buying at today's levels ($ 1480) only as a hedge against falling stock prices.

In Zurich on 17th October 2019

Yours sincerely,
Juho Kivioja

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