MONETARY EASING SAVES WORLD STOCKS IN 2019

For equity markets, liquidity has beaten geopolitical uncertainty this year

Equity markets globally have delivered investment returns in 2019 that few would have predicted back in January when trade wars and worries about recession dominated.

In the absence of a complete meltdown over the next few weeks, we have seen excellent returns in global equity markets this year. In round numbers, China is up 30%, the US 25%, the EU 23%, Japan 17%, the UK 9% and South Africa 7%.

"This outcome was not obvious back in January, when investors were preparing for some combination of a recession and trade war," said Mario Fisher, chief data scientist and portfolio manager at Prescient Investment Management.

"It's interesting that market performance has not been driven by massive economic growth or a boost in corporate earnings. While the recent easing in trade tensions has contributed, what has really saved equity markets is what has worked repeatedly during this economic cycle: monetary easing."

Fisher said the struggle between geopolitical uncertainty and easier financial conditions was at a peak in the third quarter. Since then global stocks are up approximately 6%. The year-to-date performance for emerging markets is 11%, and for developed markets, 24%.

He states that better liquidity will likely continue supporting risky assets.

"I would substantiate that scenario on the basis of some easing of geopolitical risk, accelerating liquidity on the back of expanding central bank balance sheets, and the view that better liquidity will lead to economic stabilisation," he said.

Fisher added that, for now, geopolitical uncertainty is receding from its mid-year peak. Global liquidity is improving, with central banks having resumed buying assets. The European Central Bank (ECB) has restarted its quantitative easing programme and the Federal Reserve is expanding its balance sheet again.

The collective balance sheet of the Fed, ECB, Bank of Japan and Bank of England is growing for the first time since 2017. The resultant improvement in global liquidity should lead to improving, or at least more stable, growth.

"This dynamic could change if central banks turn more hawkish or if there's an increase in political uncertainty. However, for uncertainty to have a material impact it will need to dramatically reduce business and consumer confidence. For now, unemployment is low and consumers continue to spend. In this regime, greater liquidity should offset intermittent cases of geopolitical fear," said Fisher.

When it comes to stock selection, he added that greater liquidity and stable growth imply lower cross-sectional volatility. Under these conditions, stock selection is less important as the potential for single stocks to perform way above average is low.

The converse also holds true, in times of low liquidity, high uncertainty and high cross-sectional volatility, stock selection becomes more important.

"That implies selecting the right stocks, at the right time and having a consistent, risk managed view on how these stocks are selected. At Prescient we follow a pragmatic, risk-controlled approach that ensures we can navigate through all market conditions and plot a course that generates consistent returns," said Fisher.

Ends

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