

MARKET INSIGHT



Feathering the throttle

Anyone ever watched a stage of the world rally championship? The only thing more impressive than watching the rally cars drift around impossibly tight corners at breakneck speed is the skill at which it takes the rally driver to achieve this without coming a cropper.

'Feathering the throttle' is a technique used to apply the lightest touch to the accelerator propelling the car around the corner with the perfect balance of speed and control without overshooting and crashing. As with everything that requires skill, it's hard to do and prone to going wrong.

The driver's fine line between perfection and failure chimed with a question I had been asking myself. With 2019 being one of the best years for capital markets since the 2008 crash, what does the market need to do from here to keep the party going? Well, safe to say a stock market version of feathering the throttle comes pretty close.

To illustrate the type of enthusiasm we saw in 2019, just one ETF provider in the final three months of the year saw \$37 billion move into its equity ETF products. That's at a rate of \$12 billion a month for one ETF provider, of which there are quite a few. Fixed income also traded in a rich vein of performance, leaving almost all fixed income fund managers in agreement that investors should not expect another 2019 year in 2020. Most agree that another year like 2019 risks overheating an already expensive market and driving the market in the proverbial ditch... AKA a serious stock market correction.

Risks in 2020 will centre around a few pivots:

- Too much growth and we risk overheating the whole mechanism, with investors continuing to pile billions into an increasingly expensive market risking a steep pull back.
- Too little growth and central banks will likely use their last ounce of dry powder to lower rates leaving them rudderless when the global economy really does hit the skids. This could end up spooking markets into giving up the gains we made last year and TAM certainly does not want to do that.
- 2019 was a year where TAM's investment portfolios not only outperformed their benchmarks (with markedly lower risk, I might add) but also returned more in absolute terms than they have in the past 5 years, and that's a story worth fighting to protect.

So, what is 2020's version of 'feathering the throttle' to avoid the above? With the S&P 500 in 2019 gaining circa 30% in dollar terms, the global economy now needs to deliver some concrete growth numbers to back up this front-loaded positivity. For us, 2019's performance extolled the age-old adage of "buy the rumour, sell the fact" – 2020 now needs to deliver on that rumour.

If the market can see a recovery and pin it on the benefits of the "phase one" US-China trade deal, then there is every chance the equity market will grind higher as corporate growth and earnings begin to catch up with the high stock prices from the 2019 rally. If we can achieve this without central bank intervention, that could well cap off a healthy, high single-digit gain in 2020.

Sadly, we don't live in a perfect world and it doesn't take Warren Buffett to see that the above scenario is so fraught with ifs and buts just waiting to steer the rally off course. Nothing underscores this uncertainty than Trump ordering, out of left field, the killing of an Iranian general sending oil and safe havens rocketing up along with the VIX index in an eerie reminder of January 2018 volatility spikes.

Unsurprisingly the best approach for this type of see-saw market is to spread risk and cast your opportunity net far and wide. Should markets give back the gains of 2019, then it's going to be safe havens like government debt, gold, silver and mega cap equities which will protect your capital.

Should we thread the 2020 market correctly, then it's going to be cyclical value opportunities, emerging and Asian equity and debt, and perhaps European assets which should power your gains onto new levels.

Active management, especially within a fund of fund capacity, thrives in this environment because it provides investors with a highly diversified vehicle offering all of these components in both risk-on and risk-off investments under one roof. This avoids following the investment herd into one specific corner of the market on the hope of equity markets delivering investors more 2019 like gains.

Keeping our clients' portfolios nimble, reactive and highly diversified into some high-quality investments will be the best approach in 2020. Afterall, as the saying goes, follow the herd for long enough and you're bound to step in s**t.

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