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Market outlook November 2019

Growth stories

Once you look at economic markets during the last months you will find that the world seems to have gone crazy. On the one hand there is generalized slowing growth in all developed economies, the drums of recession are wagering and fear of the upcoming is all around. On the other hand the markets seem to be not hearing it. The S&P index is up 4% in the last 30 days, DAX rises by 4.2% same period. Looking at fixed income markets it seems to be the same paradox. Global Public debt markets are up in 2019 by more than 9% in Euro terms, European Corporate debt is up in the same period 5.2%, Emerging markets debt shot up by over 15.5% in the year.

What on earth is happening?

Well, why not use the old good economic tools those of us who studied economics (or are interested in such dry topics) had to study in the textbooks.

So, lets go by Microeconomic components such as saving, investment and consumption.

In times of quantitative easing of money in terms of supply by Central Banks there are various angles to it:

If you are a good standing customer (other way to put it is wealthy) – I will not distinguish between corporations or businesses versus private person for the reason that wealth at the end is always in the hands of someone – you are able to borrow extremely cheap given the negative interest rate commercial banks are receiving from Central Bank overnight deposits. Should you wish to deposit money as such customer the bank will pay you nothing or even charge you for keeping your money. So, the logical optimal choice in this situation is to invest in something that has a recurrent return with low risk such as rental businesses etc. in other words something yielding or in case your investment horizon allows it to invest in opportunistic investment with higher risk, but more than compensated by excess return. That explains why private lenders are willing to invest in yielding opportunities at low rates of interest returned such as 3 to 7% and command in excess of 15 to 25% for opportunistic investment.

Just keeping the money is not an option given inflation is still being in positive territory and "eating" the wealth and as silly as it may sound, the lack of appropriate storage opportunities. Just to note: the marginal propensity of consumption of well off people is extremely stable – they do not need the extra money for spending!

Now, the normal Joe case: Your wealth is likely to be composed by fixed assets such as your house you are living, the amount of money you generate from your job and the savings you are holding. Normal Joe´s ability to finance through bank are very limited given that the fixed asset – the place where she or he lives has likely a mortgage and so has already eaten a significant part of the credit score. You may note that someone who holds no fixed asset is better off, but that is unfortunately not the case. The fixed asset serves in two ways: it's a collateral for borrowing money and so leverages your wealth and may, if rightly chosen, experience a price increase over time – thus generate extra saving.

So, if saving is what you do not consume, in times of zero interest return on the already generated savings and at the same time a growing tendency for stagnating or lower income due to lower economic growth will lead to less consumption at constant savings (the reason for the constant savings is linked to concepts such as Permanent Income Hypothesis or Life Cycle Hypotheses, but that goes far beyond the scope of this article).

For our purpose it reveals the reasons for increasing savings on both sides of the economic spectrum: the rich save by investing and the less rich save through less consumption hoping to be able to compensate for less income and less interest return on existing savings.

Now, what has all this to do with the aforementioned paradox of financial markets? Simple, more money is flowing to markets, where the recipients face a difficult situation: With less growth and higher uncertainty the expected return of investment is declining through the bench and will undoubtedly lead to surprises and corrections in the course of the investment cycle.

Adding uncertainty to all this mess is the new technologies pounding the walls of traditional business models and "old" Tech companies. Especially sectors like Banking and Finance will have to cope additionally with new kids on the block – FINTECH. The whole banking model is changed by companies such as Wirecard, N26 et al and leading to a completely new cost/transaction model. Biotech is on the verge of being shaken up by new developments in the speed of genetical engineering through new methods including for example CRISPR - whole new world.

What to do now? Invest in markets, companies? Yes, but with caution and always with a longer term investment horizon. The other way is to mimic the Rich. Get involved in yielding businesses that take advantage on the changing needs of people. Non-animal food products for example such as Beyond Meat and others, have a market where demand outgrows supple by far. Early stage companies, but keep in mind where Amazon was at the beginning and look now at the company value.
Intelligent rental projects yielding good return with less risk than the traditional buy to rent models could be another idea.

We are happy to help finding the right investment angle for you, so, if this feels interesting please contact us!