MERRION INVESTMENT MANAGERS

CANTOR Fitzgerald

Strategy & Outlook MARKET UPDATE

February 2020

Outlook

An acceleration in growth was priced into equity markets in the first half of 2019, with economic acceleration expected first in H2 2019. When this acceleration didn't materialise, it was pushed out to Q1 2020. It appears to us that these growth acceleration hopes are likely to be pushed out again due to the corona-virus.

With that consensus expectation for a rapid and sustained improvement in economic growth comes the consensus outlook for a rapid rebound in earnings. Earnings growth of approximately 10% is expected for 2020, and looks too optimistic. In the current earnings season, ex some market-exposed financials and technology, results for industrials and cyclicals have been mixed at best with outlooks that can be described as hopeful with second-half-weighted recoveries. In absolute terms, earnings have declined over the last year, leaving the entire gain in equities since end 2018 down to multiple expansion.

As noted above, one of the key drivers in our view of the most recent move higher in equities was the provision of liquidity by the Federal Reserve. Whilst the Federal Reserve is likely to keep its balance sheet large, reliance on repo is likely to fade, the balance sheet will not expand continuously, yet equity markets appear to have priced an ever-expanding balance sheet.

Ultimately, we are in a low growth, low/zero rate, high risk but highly liquid environment, which means portfolios should be focused on factors such as high quality, sustainable structural growth, positive earnings momentum, strong and growing dividends, regulatory tailwinds not headwinds, and insulation from geopolitical risks. These are the factors which will continue to add value to portfolios over time.

Positioning

We remain close to the lower end of our asset allocation ranges, as concerns about economic growth, elevated valuations and technically stretched markets encourage a defensive posture. Within our equity holdings, we sold the residual holdings we had in the oil sector, moving from underweight to zero. Regulatory headwinds continue to increase for carbon emitters and even despite the supply shortages from Libya crude is unable to rally. Given how stretched stocks and sectors we like have become we also reduced our holdings in technology space (back more towards neutral), adding to some of our holdings in global stock exchanges and to renewable energy holdings in Europe as the regularity tailwind for this sector continues to grow with the latest iteration of the European's Green ambitions.

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