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[INTRODUCTION]
Juliet Schooling Latter (JSL): Hi, I'm Juliet Schooling Latter, research director at FundCalibre, and I'm here with managing director, Darius McDermott, looking ahead to 2020.

After a worrying end to 2018, 2019 turned out to be a good year for stock markets. Amidst a backdrop of a global economic slowdown and trade wars rumbling on, the US central bank took action: it paused its interest rate rises, then subsequently cut rates. Europe and the UK followed, as did the central banks of many other countries and stock markets rose.

But what does 2020 hold in store for investors?

Today we're going to review what some of the Elite Rated fund managers we have interviewed recently had to say about the outlook for various markets, but first: Darius, what are your thoughts going into 2020?

[INTERVIEW]
[0:50]

Darius McDermott (DM): 2020 looks to be a really interesting year. The major thing happening in the US is the presidential election and I think that will probably be the dominant factor in markets globally. In the UK, unfortunately we will still be talking about Brexit. At least post election, we have some clarity of which way we're heading, but actually getting the trade deal and everything done will still be an overhanging issue for 2020.

I'm hopeful for another reasonable year for equities, but I do expect bond markets to be a bit more difficult. In the UK we've already seen the stock market breathe a sigh of relief and a rally on the back of that general election result. If global fund managers believe that the outlook for the UK is

now more positive, they may reallocate to UK equities even if that goes back to a neutral position that buy/sell demand on should push stock markets higher. Recently we had an investment trust dinner and we were lucky enough to be joined by Job Curtis who is the manager of the City of London Investment Trust and he agrees that there is value in UK equities.

> **Job Curtis:** Well I think there's some great value on offer. In particular the stock market yields slightly over 4% that means the dividend yield is over 4%. So when you compare, you know interest rates are still incredibly low in the UK, only 0.75% back in the base rate, or what you get in a cash ISA or you get in fixed interest. I think that dividend yield is attractive and we've got some great companies. I've got some real global leaders and I think, you know, if some of those domestic issues are a bit more certain, I mean we could see a sort of strong bounce of some of the domestic stocks within the UK stock market. So I'm pretty positive going forward actually.

[2:34]

JSL: In the US, Donald Trump has managed to both tie his presidential success to the US stock market, and influence its direction. In his quest for a second term, we believe he will do everything in his power to both avoid recession and keep the stock market climbing higher.

Investors can take some comfort from the historical performance of the US stock market in the run-up to a presidential election: A study of election cycles between 1952 and 2000 showed an investor holding a portfolio of stocks that mirrored the S&P 500 in the 27 months preceding a US election saw significant returns anywhere between 16% and 70% depending on the election year.

However, as a useful counterpoint, the same study found bear markets - defined as a decline of 15% or more in the value of the S&P 500 - historically tend to happen in the first and second years of presidential terms – so 2021 might not be as good.

Peter Ewins, manager of BMO Global Smaller Companies Investment Trust also believes the US election will become more significant for stock markets as the year unfolds.

> **Peter Ewins (PE):** I think we're all starting to think about the election in America. I mean we were talking about it in the office today and ultimately we're still not clear who the two candidates are running will actually be. The agendas of the Democrats and Republican side could be quite different. Um, and so we are conscious of some parts of the market being potentially vulnerable to a change of administration. So you know, companies that maybe

operate private prisons would be vulnerable, some aspects of the healthcare system could be changed, but ultimately, it seems, you know, it's really too early to judge who's going to win that election. But we are conscious that, you know, that it is coming closer to something that we need to be conscious of at the moment.

[4:29]

DM: Brexit has also left European equities and companies under a bit of a cloud. In fact, even though they did have a strong rally in the second half of this year, but now there is a clear mandate following the general election, will the outlook be more positive for Europe too? Here's what Graham Clapp manager of the RWC Continental European fund had to say.

Graham Clapp: I think the outlook for European equities in 2020 is pretty good. I mean you might think that with the European equities up over 20% this year that maybe they're a little bit extended, but you have to remember that they did fall 10% or so in 2018. So valuations on average look pretty attractive. Obviously the range of valuations has expanded and one of the things about that is that in next year we see a very good environment for stock picking whereas certainly the first half of 2019 was all about valuation changes. In 2020, we think the market and share prices are going to be driven by a fundamental performance of companies and that's a great environment for stock picks, stock pickers such as ourselves.

[5:40]

JSL: Meanwhile, in Asia, trade wars have been taking their toll. But it’s not all doom and gloom, as Mark Hammonds and Edmund Harriss, co-managers of Guinness Asian Equity Income fund told us recently.

Edmund Harriss (EH): I think the first point I would say is that Asia still is a growth story, but it has developed substantially over the last 15-20 years, so it’s moved beyond just being about growth from a low base. But you now have a landscape where there are many more economic participants, so consumers are present and a big part of the economy now. The industries and the businesses that serve this consumer base are by and large now cash generative, well established businesses and quite mature and, as a consequence, they’re not having to reinvest at the same rates that they were. They’re generating cash now, generating enough to reinvest and enough to distribute.

Mark Hammonds: And I think just to add to that is one of the things the trade war has sort of highlighted is just how entrenched some of the supply chains are in China and we've seen certainly in the short term quite a big uptick in activity in Vietnam as manufacturers try and relocate outside of China but actually you start to see other problems that that causes such as a shortness in the labour markets and manufacturers struggling because not all of the components can be produced in the country where as in China you've got a much more integrated supply chain. So if anything it does tend to highlight the key role that China plays in global trade.

EH: And the result of a trade dispute may mean that Chinese companies will need to establish factories in other parts of the region and supply chains will have to adjust and they almost certainly will although we haven't seen a lot of evidence of that happening just yet but that is clearly a trend.

[7:44]

JSL: And Matthew Dobbs manager of Schroder Asian Alpha Plus, thinks that the trade tariffs and political issues have resulted in pent-up demand.

Matthew Dobbs: I think the one big swing factor that I think people are kind of not so focused on as a general thing, so we've got things whether it's politics or environment and carbon or whether it's tariffs, is that actually we live in a world where it's very difficult to make long term planning. And if that was resolved, and that's an issue of tarrifs, it's an issue of politics, it's an issue of the whole existential issues facing some industries, whether it's energy or autos. But as that gets a bit clearer, I think particularly in Asia, there's a lot of pent-up demand from the sort of capital spending side, whether that's automation or expansion or moving production out of China to Vietnam or elsewhere in the region. And I think once sort of businesses have got more clarity in which they can actually plan because at the moment they don't. If they get that, then I think we might be surprised by the inflection point.

JSL: Within Asia, India has long been a firm favourite of ours at FundCalibre, as demographics – with its young and entrepreneurial, and increasingly educated population – coupled with the pro-business reforms of Prime Minister Modi, make it appealing over the long term. Here's what Anup Maheshwari, Chief Investment Officer of IIFL Asset Management, had to say about the outlook.

Anup Maheshwari: I think India is coming out of a bit of a broad bump as far as growth is concerned. Last year has been fairly slow and I think we're looking at a reversion back up

over the course of next year. The important thing though for markets is profits of companies. Finally, that's what drives market returns. And interestingly enough after a batch of about seven years of fairly low growth in corporate earnings in India, we are actually looking for a fairly sharp pick up in the coming year. That's also been partly helped by the fact that the government has cut taxes just like we've seen in the US some time ago. And that is given an additional fill up one time to earnings. So the next year's earnings outlook looks a lot brighter for India. That should be driven largely by the financial services sector, which is becoming an increasingly larger part of India and the stock market as well.

So the key to investing in India, which I must emphasise is to give it time. You know, you shouldn't, people tend to see emerging markets and India particularly sometimes there's a bit of a flavour of the season market, but we have enough statistics that we've done on the past and analysis that suggests to us that the optimal timeframe for investing in India is normally a five year cycle and very rarely if at all in a five year period would you have negative returns from the Indian market. So to that extent I think that's the time dimension, which people should have in mind when you're coming to a market like India, but the returns can be fairly good. And I think, as I mentioned, a 12% to 14% sort of return expectation in dollar terms would be quite reasonable at this point in time given where growth is heading over the course of the next year.

[12:20]

DM: Japan is another market we currently like at FundCalibre. The stock market is still reasonable value and Prime Minister Abe’s economic reforms are really starting to make a difference after decades of stagnant growth. Peter Ewins likes the markets too.

PE: At the moment, we think the Japan offers is a relatively attractive place, relatively safe in terms of politics. Obviously impacted by China and the US sort of trade, but ultimately relatively stable. We think corporate governance is inching forward. We're seeing, you know, better return target, return on equity targets for companies in Japan now being set out. So we think that there is some attraction to Japan at the moment.

[13:04]

JSL: Of course, equities aren’t the only investment in town. What about bonds? Can the 35 year-plus bull market continue? When more than $13 trillion worth of global bonds have a negative yield, it suggests care needs to be taken. Here’s what Jim Leaviss, manager of M&G Global Macro Bond had to say.

Jim Leaviss: I think if you look at all the bond asset classes, it's hard to see huge amounts of value in government bonds for the reasons we just talked about. You may make a little bit as a result of capital appreciation, corporate bonds we do have in the portfolio and I think there are certain areas and sectors where you still get yields that overcompensate you for the risks that you take. And again, European central banks going to come in and buy these things again and maybe other central banks in the future.

I think the areas that we should be looking at when you try and find absolute value now though are probably emerging markets. Where else can you get yields of 7%, 8%, 9% in Dollar or Euro or Sterling bonds issued by emerging markets. And I think some of the fundamentals are looking more attractive for emerging market debt, but still lots of landmines. We saw over the summer Argentina get into big difficulties, bond price halved. So it's not without its risks, but if you're looking for absolute value, I'm thinking that's an area I should have more of in the portfolio over the next year or so. It may not be quite time yet, but in a world of zero yields, I think improving fundamentals in EMD, emerging market debt, probably make some sense.

DM: Bruce Stout, manager of Murray International Investment Trust, agrees that emerging market bonds – although riskier – look more attractive than their developed market counterparts.

Bruce Stout: And at this particular point we see some very attractive opportunities in emerging market bonds. Now the reason for that is the emerging world, particularly Asia and Latin America is really the only part of the world that has been following economic orthodoxy in the last 5 or 10 years compared to the developed world where they've been flooding the markets with debt and yields have fallen to zero. So it's possible to analyse emerging market debt and therefore it's possible to value them as being looking very attractive at the moment.

JSL: So there you have it. A mixed bag, but a relatively positive one, as we head into 2020. All of us at FundCalibre would like to wish you a very happy – and hopefully prosperous – New Year. And if you like to hear more of our podcasts, please subscribe to FundCalibre.