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MARKET COMMENTARY – Q4 2019: Farewell trade tensions?

Financial markets were able to start breathing a sigh of relief in the last quarter of 2019, with political tensions seeming to lighten, there was a renewed sense of hope that they would be able to free themselves from the continuous drag on business sentiment and investment created by geopolitics.

Trade tensions were again at the center of investors' minds when considering their exposure to financial markets. Despite a tricky start in October, involving the blacklisting of Chinese companies ahead of negotiations held in Washington between the world's two biggest economies, incremental efforts from both side during the period pointed toward positive development. In mid-December, the United States and China announced that they finally reached an initial trade agreement. The signature was planned for January and while the details from the 80-page (approx.) document have not yet be communicated, the negotiators let the world know that no further US tariffs on Chinese goods should be expected, some will indeed be reduced by the US, and China will increase its purchase of US agriculture products.

The materialization of this trade agreement as well as its timing are difficult to separate from the approaching US elections and the increasing domestic pressure against Donald Trump. Facing an unlikely impeachment given a US senate in Republican hands, the details of the charges and the way the president is responding will no doubt have a critical impact on the 2020 US elections. Trump on the one hand, needs to deliver and multiply his accomplishments (such as getting rid of Isis's leader or more recently an Iranian general). China, on the other hand, appearing so far to be losing the trade war game, will gladly slow down tensions.

Are international trade tensions coming to an end? With an initial trade agreement also signed with Japan in October, we could be led to believe so. However, let's not forget that the US also sanctioned the EU by applying tariffs on $7.5bn worth of imports. France was targeted with a warning for more specific measures on the back of its digital tax. Germany was also on the receiving end of vitriol over the potential exclusion of Huawei as a supplier of 5G equipment. Beyond the initial deal between the US and China, several sensible negotiations are on the road map, although nobody expects them to go smoothly. In a nutshell, things have improved, but they're far from over.

The never-ending divorce of the UK and European Union saw some critical developments. Following many challenges, prime minister Boris Johnson's negotiations with Brussels resulted in an agreement (to a large extent very similar to the one proposed by his predecessor Theresa May). While the deadline of October 31st hasn't been met despite the forceful and recurring attempts to get the approval required by parliament, Boris Johnson managed to set general elections for December. Almost a year after the initial deadline and 3 years after the referendum, the gridlock was finally broken as the outcome of the election kept the current government in place and strengthened its mandate for a likely Brexit at the end of January 2020.

In addition, the significant progress made on the above two thorny topics which were the largest drivers of concern over the year, took place in a supportive context which was provided by accommodative central banks. In the US, the fed cut its key target rates for a 3rd time in October. In spite of continuous pressure from the Trump administration, Jerome Powell conveyed the message that these rate cuts should be sufficient in the current economic climate. Far from being passive, the US central bank indeed remained very active, supporting the troubled repo (repurchase agreement) market. In Europe, Mario Draghi ended his tenure at the ECB and was replaced by Christine Lagarde, who used to run the IMF. The new leader of the European central bank made it clear that the current monetary policy will remain in place, including the relaunch of the bond purchase program. The appointment of a more sharply political figure, compared to Jean Claude Trichet and Mario Draghi, both economists and former heads of central banks, says a lot about the much more politized environment we are living in.

In conclusion, a very strong year has just ended, despite the important economic slowdown leading to prices probably already reflecting the best outcome of the main challenges markets were facing. In the context of US fiscal stimuli's impact already being behind us, share buybacks slowing down, economic support being limited and Earning growth slowing down, our positioning at the beginning of the new year is slightly positive for equity, but quite cautious. We believe that emerging markets are offering interesting selective opportunities and Japanese equity remains attractive while we remain neutral on US and Europe. We also remain underweight on the bond side given the level of interest rates and credit valuation.

But the last quarter has also cast some light on the idiosyncratic drivers of investment returns, which are easily neglected in a world where headlines are focused predominantly on geopolitics. The crisis that Boeing is dealing with left the stock barely up for the year in one of the strongest stock markets since 2009. The fragility of the banking industry, swamped in heavy regulations and low interest rates, also lead some banks such as HSBC into negative territory driving valuation to potentially interesting levels. In December, we also had the biggest IPO ever with Aramco raising $25.6bn, beating Alibaba's $25bn raised in September 2014. These highlight investment opportunities, regardless of market direction which can be captured by strategies managed by seasoned specialists, which we believe we have in our portfolios.

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Markets	Indices	Q4-2019	2019
Equity World	*MSCI All Countries World Daily Total Return Net USD Index*	9.0%	26.6%
Equity Emerging Market	*MSCI Emerging Net Total Return USD Index*	11.8%	18.4%
Global Fixed Income	*Barclays Global-Aggregate Total Return Index USD*	0.5%	6.8%
Global Commodity	*S&P GSCGI Index Spot Index*	8.1%	16.5%
Hedge Funds	*Hedge Fund Research HFRX Global Hedge Fund Index*	2.6%	8.6%
EUR/USD	*Euro Dollar*	2.9%	-2.2%