The world is a confusing place

Greg Bright | Investor Strategy News | 02 March 2015

I don't like getting up early. At my age and standing, I feel I shouldn't have to. I used to get up at 5am to start work at the *Daily Mirror* in Surry Hills in the 1970s. I got up at 5am too, when I edited *Investor Daily* whose office was near Circular Quay in the heady days of the dot-com bubble of 2000. But I still didn't like it.

The alarm goes, carefully set the night before for 6.15am so I can get a 7.30 taxi to Australian Technology Park for PortfolioConstruction Forum Markets Summit. I can't believe we're soon stalled in traffic. Who on earth else would be on route from leafy Queens Park to leafless Redfern at this hour? Heaps of people, apparently. I get there on time but there's a long queue of people trying to check in. Why are any of us doing this?

And the show begins: loud music; a touch of Hollywood. The scene is set with video. The theme, which we've all been told well in advance is: Cyclical? Secular? Structural? I even knew the differences between the three, thanks to the copious "pre-reading" I'd received in the weeks before Markets Summit. I still wonder about the word "pre-reading". When do I get the "reading"? Maybe I have to write it myself! This article could be everyone's "reading".

Pippa Malmgrem emerges from the shadows. She is a renowned big-picture thinker on global economic and investment trends. As it turns out, she is mainly concerned about the deflation/inflation question: "99% of all market observers think deflation is the principal risk. That alone makes me think I should take the other side of the trade," she said. I'm thinking 99% of all conference speakers make up their statistics - but, it was concerns about inflation that prompted the Swiss to break their currency peg, Pippa said, and there were pockets of inflation around the world such as in Russia and Dubai.

She added: "We are already in the next industrial revolution. We are on the verge of something extraordinary in the course of history." This was to be a recurring theme of Markets Summit, and it is either very exciting or very scary depending on your point of view - or, probably, psychological make-up.

What Markets Summit is, is a collection of "insights" expressed over 20 sessions of 25 minutes each, delivered by fund managers, mainly, and orchestrated by Graham within a tight framework supported by research notes and educational backgrounders, both before and after the program. But what does this year's gathering all mean? Does the artificial construct of 'Cyclical? Secular? Structural?' mean anything?

With 20 speakers, there are inevitably conflicting views of the world and attendees can be forgiven for feeling confused at the end of the day. This year, the bears outnumbered the

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bulls and the mood – probably because of Australia's own slowdown – was noticeably downbeat compared with the same time last year.

The consensus views on the day were:

- that the US was still the big positive bet in asset allocation, despite some concerns about valuations;
- that the Eurozone would remain in the doldrums for some time, whether or not it held together;
- that China would continue to slow while remaining a strong long-term proposition;
- that India was an exciting near-medium-term bet; and,
- the rest of the emerging markets may be challenged by the rising dollar but are in a much stronger position to avoid 1997-style contagion this time around.
- Views on Japan were mixed-to-positive-to-very positive.

Extreme views tend to grab people's attention and stick in their minds, as does a nice turn of phrase. Several speakers broached the Eurozone troubles and none was very optimistic. Charles Dallara, executive vice chair of Partners Group and a former US Executive Director of the IMF said the Euro "was a mistake" and bringing Greece in on it was a "profound mistake". [He's well placed to judge, given as head of the International Institute of Finance, he spent months in Athens negotiating its sovereign debt restructure back in 2010. – Ed] The Greeks hadn't paid taxes since they were ruled by the Ottomans, he said.

Bruce Campbell, the investment chairman of Pyrford International, went one further and said the break-up of the Eurozone was inevitable: "When Greece goes, watch for the rest to follow."

As with most speakers, though, regional gloom did not mean there were not selected opportunities for investors, especially in companies with international exposures.

Stock-pickers outnumber top-down allocators by at least three-to-one (that's my made-up statistic) so they don't want everyone to think they are sitting on their hands, unable to find somewhere to invest.

I always like to listen to the views of a value manager when his or her firm is upbeat on a theme. It doesn't happen very often. Value managers tend towards the pessimistic end of the spectrum. So, it's significant to hear Ron Temple, a managing director and portfolio manager at Lazard Asset Management in New York, saying that "the US has reached an inflection point and will pull even further ahead of Japan and Europe over the next three-five years". Lazard's advice is to own global equities with a "prominent" (read "overweight") position for US equities in the portfolio.

The only strong dissenter on the prospects of the US was Chris Watling, who, like Jonathan Pain, came to us via video. Watling, CEO of Longview Economics in the UK, argued there was a real risk of recession in the US in 2016, even though large-cap US equities should do well for the next nine to 12 months. "Remain nimble to switch out," he advised.

On Japan, Temple said that it offered an interesting call option because Japan had finally got things right with its quantitative easing. But, the big Japan bull at the summit was John Hock, CIO of Altrinsic Global Advisors. The main source of his firm's enthusiasm was not so much acceptance of Abenomics at the political and broad social level, but at the corporate level. He cited examples such as dividends up 20% and share buybacks up 60% in 2014. Hock said: "If I had $1 to invest globally would I put it in Japan? The answer is 'no'. I would put it in Russia. If I had $1 million to spend, I would still put $1 in Russia but I'd put the rest of the million in Japan."

But back to Pippa Malmgrem's line that the world "is on the verge of something extraordinary in the course of history". The thesis that technology is going to take us to a new place - both exciting and scary - was partially developed by BT Investment Management's Head of Fixed Income, Vimal Gor, and expanded upon by Fidelity Worldwide Investment portfolio manager, Kate Howitt.

One of two emerging trends, Gor said, was robots (the other was energy, but that story is already yesterday's news). Gor showed a photo of a robot called Baxter which could be bought for $25,000 and did the work of 10 workers in a factory in Australia. Baxter was a cut-above the sort of robots that have been used on automobile assembly lines and so much cheaper. "It may be that we won't have lower-skilled jobs any more," he said. "We may not even have middle and higher-skilled jobs. We don't know its impact. We do know it's bad for wages and bad for deflation."

Howitt had presented at Markets Summit in 2013 on the "Three Ds' of major themes: deleveraging, demographics and distortion (by government policies). This year, she added a fourth D - disruption. She analysed the three previous industrial revolutions -the harnessing of mechanical power in the late 18th century, the harnessing of electrical power in the late 19th century, and computing power in the late 20th century. The benefits of each did not come without cost and there was no strong correlation between the developments and GDP growth, she said.

The main cost, usually felt some years after the technological development which substituted capital for labour, was political unrest. For instance, in 1796 - about 40 years after the threshing machine was first introduced in England - there were riots among unemployed, given manual grain separation was the biggest single employer of labour previously. The riots resulted in four people being executed and 450 sentenced to prison terms in Australia. The second industrial revolution in the late 19th century led to a boom and bust in the stock market and a depression in some countries, such as Australia.

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"When a large percentage of the economy lose their jobs, it can take a generation for them to catch up through retraining," Howitt said. "And you get a spillover into the political economy."

For investors, the key was to look for resilient business models, such as cash cows that are broadly immune to disruption. Luckily, she said, the Australian market was cash-cow rich.

So, at the end of the long day - confused, scared and excited - I depart Eveleigh Technology Park in search of a taxi. Of course, there is none. Never, ever again... until next time.

Greg Bright is publisher of Investor Strategy News. Bright was a guest of PortfolioConstruction Forum at PortfolioConstruction Forum Markets Summit 2015.

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