



# ASSET ALLOCATION STRATEGY

## MARKET ANALYSIS AND PRINCIPAL INVESTMENT THEMES

SEPTEMBER 2019

### IT IS TIME FOR CAUTION

► We recall that we had already reduced the European equity exposure in our portfolios on 2 August because of the Fed's return to a more neutral and less proactive stance, as well as mounting political risks linked to a hard Brexit and new elections in Italy.



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We sold more equities because:

- the US yield curve inversion is worrying as the curve should have returned to normal after the FOMC, in a particular way when we look at the short end of the curve. It is unreasonable for markets still to expect a 100bp rate cut now that the Fed is delivering practically neutral signals. The yield curve inversion has always been a reliable advanced indicator of an economic downturn.
- the latest Chinese and German data suggest the economic situation is deteriorating. The slowdown is not surprising as Beijing has already reduced growth forecasts to 6%. Given imbalances stemming from previous stimulus plans, Beijing is now accompanying the slowdown and is prevented from adopting a more expansionist policy or is at least holding back some ammunition in case growth suffers a bigger knock. A stimulus plan could also be on the cards in Germany where GDP contracted in the second quarter. Berlin certainly has substantial leeway to act but, there again, political pressures mean we should not expect anything more radical than measures designed to accompany or limit the slowdown.

So far this year, equity markets generally posted the sort of returns that would normally be unthinkable amid an earnings slowdown, an increasingly fragile economic cycle and a political environment that has become so risky that global corporate confidence levels have been eroded.

In our view, these solid returns are entirely due to central banks going sharply into reverse between the fourth quarter of 2018 and the latest FOMC.

Bear in mind that the Fed is now trying to be less pro-active and more reactive, i.e. more neutral. It is also worth noting that monetary policy often has a very big impact on markets at turning points and then tends to fade. We believe that we have already seen most of the market advance orchestrated by central banks and that the environment is now deteriorating. **It is time for profit taking and extreme caution.**

We decided to cut US Equities after the August 13 rebound, upping our equity underweight by one notch.

#### KEY POINTS

A neutral stance from the Fed

We remain invested with extreme caution

We are underweight on US equities by a notch



## NEXT HEADLINE EVENTS

Next ECB meeting: September 12

Next FED meeting: September 17&18

Brexit date?: October 31

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