CORUM AG investment policy for Q3 2019

Recession in sight? Central banks abort normalisation process

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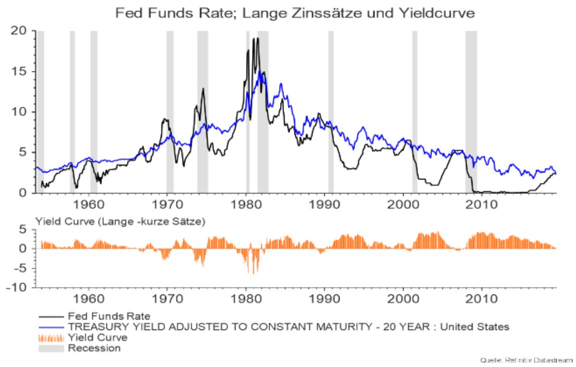
Global growth indicators also weakened further in the 2nd quarter. The discussion about a possible recession has become accentuated. Fears of inflation, which were still germinating last year and led to fears of cooling measures from the American central bank, have disappeared into the distance again. Long-term interest rates slid dramatically in the 2nd quarter, to such an extent that we have an inverse interest curve again for the first time since 2009. Some commentators see this as an unmistakeable sign of the next recession. Historically, it is actually the case that nine times out of ten a rise in short-term interest rates above long-term interest rates has been followed by a recession after, at the latest, one year (see graphic).



However, it has to be taken into account that the current situation cannot be compared with historical cycles. Past inverse interest rate curves were almost exclusively caused by active cooling measures by the central banks. Inflationary tendencies were to be curbed by restrictive monetary policy. This was not possible without restraining investments and exports. Today, however, there cannot be any talk of inflationary developments, even in the USA. Despite record lows in unemployment, wages are still developing below productivity. No, the central bank was merely concerned with slowly reducing the central bank money supply, which had been expanded over the course of a decade and could easily have become a mortgage in a growth downturn. This has little to do with restrictive monetary policy. The term normalisation of monetary policy fits better under these circumstances. In addition, the American central bank still has considerable scope to cut interest rates again. It will probably do so as early as the July meeting. Another quarter-point could follow in autumn. The markets have already priced in three to four further cuts in the Fed Funds Rate for 2020. In view of the political pressure from the White House we believe this is realistic, but not urgent, economically. In our forecast we are assuming a stabilisation of the world economy at the beginning of next year, so that an expansive monetary policy could quickly trigger stability policy problems.

This all the more so because we expect Trump-style fireworks, with which he wants to secure his re-election in autumn 2020. In particular, we expect the build-up of the threatening backdrop in trade, which he will ultimately dismantle in good time with new trade deals and populist rhetoric in the style of “America First” slogans. Further initiatives in the areas of migration and armaments can be expected. The dilapidated infrastructure also offers numerous points of reference for “great ideas”. Indebtedness? It has never been a problem for the Republicans. Quite the contrary: it should rise as high as possible so the Democrats have as little leeway as possible for an expenditure and redistribution programme at the election after next.

If the thesis of the resolution of the trade disputes is confirmed, the signs of weak growth in Europe will also gradually be resolved. With regard to Brexit, despite the change in leadership at the top of the Conservative Party, hardly any new impetus can be expected. The country remains deeply divided, whether with or without the Withdrawal Agreement. A general election would also change little about this situation.

Greece is another trouble spot that has caused great problems for the euro in the past. Under pressure from Europe and the IMF, Alexis Tsipras forced through an austerity programme over several years which lead to an unprecedented collapse in economic output, namely of about 30%. Usually only a left-wing government can survive something like this without violence. But now it has been punished for this in a manner similar to what happened to the German Social Democrats under Gerhard Schröder's leadership with his Hartz IV model at the beginning of the noughties. The new government under Kyriakos Mitsotakis has good chances of raising Greece up from the rubble. It will be important to retain the reformed legal, competition and taxation system so that the trust of investors returns again.

However, if entrepreneur friendliness is confused with privileges for the old dynasties, the inflow of foreign capital will be a long time coming. There are also risks if redistribution from below upwards happens too abruptly, or if social unrest is triggered by extensive privatisation programmes and lay-offs. Overall, however, we assess the opportunities for reconstruction to be greater than the risks. This is also a positive signal for Europe, which will no doubt grant the new government additional leeway for growth.

The situation in Turkey, where Erdogan has trampled on the independence of the central bank by dismissing its head with the justification that he had not cut interest rates in the way he had demanded, is less pleasing. "With high interest rates inflation will rise even further." We expect that the successor will follow orders, capital will flow out, the currency will devalue even further and imported inflation will begin to rise again. And that is when it will become really dangerous for equities.

However, we can identify that investment policy prospects can be assessed to be more positive, despite signs of weak growth. The greatest weight comes from the USA, where the election is casting its shadow. Trump will not shrink from doing everything in his power. The price cannot be high enough. In terms of investment policy, it will be important to take these circumstances into account in good time. The risks of this course of action are not inconsiderable but not yet latent.

In summary, it seems to us that, despite the higher valuations, it makes sense to keep the equity quota neutral and to go overweighted in American investments to the disadvantage of Europe, and to slightly increase them at the expense of Switzerland. Bonds remain underweighted, but we have slightly reduced the underweighting. Parts of the euro and recently also the US$ have been hedged.

You can take the details of the asset allocation for the third quarter of the year from the following table.

Strategic and tactical Asset Allocation for the 3rd Quarter 2019

	Reference Currency CHF			Reference Currency EUR		
	Investment strategy Balanced			Investment strategy Balanced		
	SA	IC	C	SA	IC	C
Investment categories						
Money market	**5**	**4**	**-2**	**5**	**7**	**-2**
Bonds	**40**	**38**	**+2**	**40**	**34**	**+2**
Home Country	24	23	+1	30	25	+1
Rest of Europe	8	7		5	2	
USA	4	3		5	6	
Rest of World	4	4	+1	0	1	+1
Stocks and shares	**45**	**45**		**45**	**46**	
Home Country	9	8		15	14	
Rest of Europe	11	9	-1	10	4	-1
USA	12	14		10	15	
Rest of World	13	14	+1	10	13	+1
Alternative investments	**10**	**13**		**10**	**13**	
Commodities	4	5		5	5	
Various	6	8		5	8	
Total	**100**	**100**		**100**	**100**	

SA = Strategic Asset Allocation IC= Investment Committee C = Change