



The Invisible Band

Travis, 2001

For a decade, we have enjoyed a period of central bank activism, bolstering financial markets in a way almost equivalent to the credit-led investment cycle of the 90s. Ten years is a long time and we have become progressively accustomed to a very particular mindset that many refer to as: "bad news is good news". Since 2008, central banks have responded to periods of macro deceleration by supporting the economy and financial markets in innovative ways by historical standards. However, today, the world cycle is slowing down in a way never seen over that period. The Eurozone was the only zone slowing in 2011, as was China in 2015. This time, the US, China and the Eurozone are showing simultaneous signs of slowing macro momentum. If this lasts, bad news will become actual bad news as weaker earnings drag down equity valuations. To us, the key question now is: where is the invisible band that separates a world that can avoid slowdowns using QE from a world in recession, over which central banks can only have limited control? Crossing this invisible band will turn bad news into bad news.

WHAT'S NEXT?

From bad news is good news...

The Fed was the first to provide extraordinary monetary stimulus in 2009 and, since then, most of the developed world's central banks have followed suit. Since the Great Financial Crisis, when a macro deceleration began in a given region, the reaction of its central bank was almost always the same, to give more support to financial markets in an attempt to bolster the economy. In our view, central bankers around the world demonstrated an impressive capacity for innovation over the period. From lower rates, negative rates, direct bonds purchases, equity purchases to direct currency control, they employed an extensive list of new and creative monetary policy techniques to try to help the world heal the deep economic wounds created by the 2008 economic crisis.

Living under this intense liquidity medication is, however, having a significant side effect in our opinion, leading to the rise of a new phraseology to qualify their actions: "bad news is good news". This very simple wording implies a lot in terms of market participants' behaviour: any degradation in economic indicators opened the door to a new round of interventions in markets. The Fed's U-turn between December 2018 and January 2019 is the perfect example of that. The US macro situation remains positive, as indicated by our growth nowcaster for the zone: it is indeed decelerating (it has been since November 2018) but the US should still be printing positive growth for a couple more quarters, a view supported by Fed rhetoric in its December FOMC meeting. The formation of a recession expectation across equity markets in December was nonetheless enough to lead the Fed to change its wording significantly in January, moving from a hawkish to a dovish stance – echoing the now decade-long tradition of Greenspan's "Fed put". In January, markets rallied significantly on the back of this new communication line. The 2015 Chinese slowdown had a similar impact on the Fed. Bad news is good news indeed, you just need to twist the central bank's arm by selling stocks.

... until bad news becomes bad news for good

When we say markets formed recession expectations, we obviously mean equity markets. And of course these days, all eyes are on the Fed in spite of the fact that most of the macro deceleration is currently happening east of the Atlantic Ocean. We have been communicating about the

deceleration that we are currently witnessing in our indicators for a while: the Eurozone started deteriorating in February 2018, China remains in a sub-potential growth situation but is steady while the US started decelerating in November 2018. The question that currently weighs on our minds concerns the invisible band that draws the line between a situation that can be patched up with more stimulation (slow growth with limited inflation) from a situation in which patching would no longer work. Over every recession period of the past 100 years, no central bank has ever been in a position to get control over it. During recession periods, a coordinated effort between governments and central banks can help alleviate some of its damage on the economy and on markets but, overall, history shows that a recession is unavoidable when it starts. In addition, there are good reasons for that: as economic growth falls into negative territory, earnings start to fall all the more as costs – such as wages – react in a lagged way. Higher costs and slower sales growth create a scissoring effect on earnings.

What to watch from now on?

In the US, there are clouds gathering right now that are typical recession tells. First, the US housing market is likely to post negative growth figures for the first time in a long time, as per our US growth nowcaster. Second, investment intentions are receding and only 8% of the data used in the investment component of our nowcaster is improving; a good example of that is the capacity utilisation rate in the US, which printed its first drop since its 2015 recovery. The Fed is likely to pay a lot of attention to it. Deteriorating long-run decision-making indicators are historically the first sign of an upcoming recession. For the moment, these are the only severe signs around and there are a handful of figures telling a very different story, such as the US ISM Manufacturing index. The transition from a slowdown to an actual recession can take time. Reaching that point will likely be a slow process, making investment cases more and more difficult as growth remains positive and central banks use their arsenal while deceleration becomes increasingly obvious. But when we cross that invisible band, bad news will become bad news again. Until then, we remain on the cautious side.

Listen to: [The Invisible Band by Travis](#)

STRATEGY BEHAVIOUR

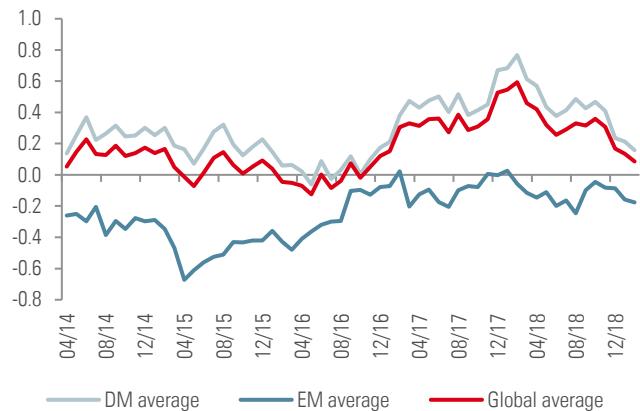
Our medium-term views remain cautious, so we are complementing a more positive pro-growth stance with tactical underweights in credit indices and making use of options to protect the portfolio in the case of equity drawdown.

PERFORMANCE REVIEW

Year to date, the Uni-Global – Cross Asset Navigator fund has returned 3.65% versus 9.60% for the MSCI AC World index, while the Barclays Global Aggregate (USD hedged) index is up 1.25%.

UNIGESTION NOWCASTING

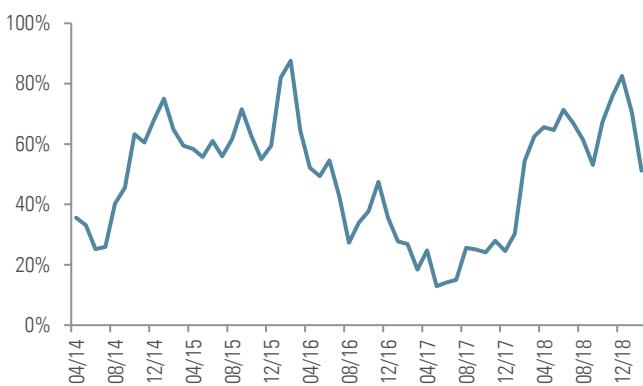
World Growth Nowcaster



World Inflation Nowcaster



Market Stress Nowcaster



Summary of the week

- ▶ Our Growth nowcaster receded further last week, following another batch of decelerating data releases. The largest negative change sits in India and Canada. All countries but China showed weaker data over the week.
- ▶ Our Inflation nowcaster continues to decline in an almost synchronous way across developed economies.
- ▶ Market stress decreased marginally again. Volatilities are currently giving the weakest stress signal.

Sources: Bloomberg, Unigestion as of 18 February 2019

NAVIGATOR FUND PERFORMANCE

Performance, net of fees	2018	2017	2016	2015
Navigator (inception 15.12.2014)	-3.6%	10.6%	4.4%	-2.2%

Past performance is no guide to the future, the value of investments can fall as well as rise, there is no guarantee that your initial investment will be returned.

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