moneywise FIRST 50 FUNDS

WHAT DOES 2020 HOLD FOR INVESTORS?

With trade wars, Brexit and anaemic economic growth, this year has proved tricky for investors. But will things improve in 2020? We ask *Moneywise* First 50 Fund managers for their views

BY STEPHEN LITTLE

There is no doubt that 2019 has been a mixed bag for investors. The stock market rallied at the beginning of the year following the plunge on Christmas Eve, with the S&P 500 and Nasdaq both reaching record highs.

However, this streak of strong earnings failed to last as global growth slowed, in part a result of the growing trade spat between the US and China.

Other factors affecting the slowdown include flagging growth in Europe and a slowdown in the Chinese economy.

With economic expectations for most countries slipping, some experts are predicting a global recession.

BREXIT

Brexit continues to be a concern for the UK economy, with uncertainty hampering business investment. In the event of a no-deal Brexit, UK shares could stumble by as much as 15%, according to a forecast from the index provider MSCI.

However, with no deal looking less likely, experts are more confident that 2020 will be a good year for equities.

Richard Watts, manager of Merian UK Mid Cap Fund, says once Brexit uncertainty lifts there will renewed interest in British companies.

He says: "UK equities, in general, have attractive valuations in comparison to other advanced economies. In particular, the UK mid-cap market looks cheap relative to long-term averages.

"The primary reason for the mid-cap market being cheaper is that it is particularly sensitive to the political backdrop and the effect of sterling weakness.

"Despite the Brexit malaise, the UK economy is in good shape. Wage inflation is over 3% and headline inflation is at 2%. Job creation is healthy, which means there is a strong labour market and, to top it off, all political parties are promising to boost government spending after the election.

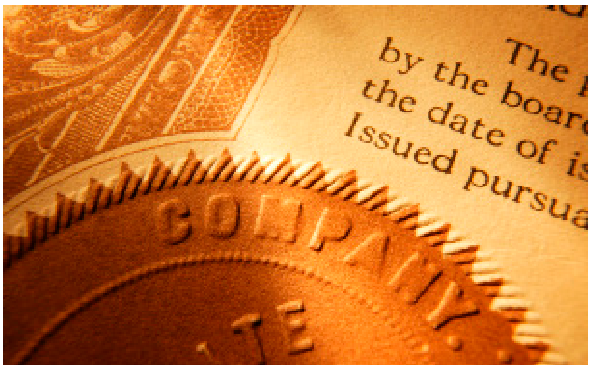
"With the chances of a hard Brexit diminishing, we will likely see a bounce in sterling, which will push down inflation, perhaps to less than 1% if sterling appreciation is very strong. As a consequence, the income available for discretionary spending should grow at double-digit rates. This would be a considerable tailwind for UK-focused sectors, such as house builders."

BOND MARKETS

As pessimism about the world economy grows, bonds are increasingly seen as a safe-haven for investor cash.

Noelle Cazalis, fixed income fund manager at Rathbones, says the corporate and high yield bond markets are likely to be important themes in 2020 as investors assess where we are in the credit cycle.

"Returns this year in bond markets have been strong – European government bonds for example have returned over 10% since the start of 2019," she says.



"High yield has grown as an asset class as investors have searched for precious yield, but if the market environment deteriorates some of these companies may struggle to repay their debt. Some sectors, such as retail, are also facing structural challenges.

"Economic numbers have been weak, and markets are likely to continue to watch for any soft patches – so it looks like caution is here to stay next year. The political agenda will also be in focus in Europe, with many investors hoping for a boost from Germany and other European countries."

TRADE WAR CONCERNS

The US and China have been locked a trade war for over a year, imposing tariffs on billions of dollars on each other's goods.

US president Donald Trump has accused China of unfair trade practices and intellectual property theft.

Negotiations between the world's two largest economies have continue to struggle, with neither side able to find common ground.

The uncertainty regarding the trade tensions is hitting businesses and hurting global growth.

Andrew Bell, chief executive of Witan Investment Trust, says the US economy remains important for investors.

"The trade war has been like a wet blanket on economic growth, but with the election in 2020 Trump needs the economy to be booming," he explains.

"If the economy is either stagnant or in a recession as a result of the trade dispute, Trump could lose the election, so I believe he very much wants to do a deal. It could also help him shrug off the political impact of all the sort of noise about impeachment.

"I expect there will be a deal within three or six months, which will be good for economic growth and lead to a degree of relief in equity markets."

> "A trade deal within three or six months will be a relief in for equity markets"

IGNORE SHORT-TERM VOLATILITY

Martin Bamford, chartered financial planner at Informed Choice, says that clients who ignore short-term volatility often see the best returns.

He says: "Investment is always going to be risky and there will always be headwinds such as Brexit or the trade war between the US and China.

"The level of caution you have as an investor depends on what you want to achieve with your money. The difficulty with being cautious is you tend to miss out on the returns when they come along unexpectedly.

"We often see clients missing out on growth opportunities because they see volatility and sell. The important thing is to try to ignore the roller coaster volatility in the short-term, because it is the people who stay invested that get the best returns."

moneywise FIRST 50 FUNDS

Moneywise First 50 is our list of 50 funds we recommend for novice investors wishing to start their own portfolio. The list includes active and passive options as well as investment trusts. **Moneywise.co.uk/first-50-funds**

DIVERSIFY YOUR PORTFOLIO

Jason Witcombe, chartered financial planner at Progeny Wealth, says investors worried about headwinds should diversify their portfolios.

"The mixture between asset classes, such as cash, equities, bonds and property, will help determine what your investment journey looks like and so it makes sense to have a coherent strategy around this.

"Most long-term investors will have a balance of those asset classes and then, ideally, will have significant diversification within each asset class too.

"For example, if you were to pick a UK FTSE All Share Tracker Fund for some or all of your UK equity exposure, this one fund might give you access to around 600 UK companies, all for a very low cost.

"If you follow that same philosophy for overseas equities as well as the other asset classes, you can give yourself significant diversification."

GLOBAL RECESSION

With weaker growth and the ongoing trade war, there are fears there could be a global recession.

Global economic growth is currently 3%, down from 3.6% last year, according to the IMF.

Two in five (38%) investors expect a recession over the next year, the highest response since August 2009, according to September's Bank of America Merrill Lynch survey.

Geoff Hitchin, manager of the Marlborough Global Bond Fund, says that while investors can expect economic volatility in 2020, the likelihood of global recession remains less clear.

"It's probably more likely we'll have a continuation of the slowdown in growth. Europe is one of the regions facing a heightened risk of recession, in part because growth is so low already. Whether that includes the UK depends on political developments here," says Mr Hitchin.

"Europe also has limited scope to counter recessionary pressures, because the eurozone, Switzerland, Denmark and Sweden already have negative interest rates. The US on the other hand still has scope to cut rates to stimulate its economy.

"While the investment outlook is complex, recessionary environments have historically proved positive for higher-quality bonds. That's partly because investors are seeking 'safer' assets and because lower interest rates are positive for bond prices.

> "We're likely to to see growth continue to slow down"

"For governments, there is an argument that those with solid credit ratings should take advantage of low interest rates to borrow and stimulate the economy through investment. However, there is a point at which markets will get nervous about government debt levels. So while it's a possible answer to recessionary pressures, it's not without risk," he adds.

US INTEREST RATES

The US Federal Reserve cut interest rates three times in 2019 to meet a target borrowing rate of between 1.5% and 1.75%, with the aim of shoring up the economy in response to the slowdown in economic growth.

Job creation has also slowed, and wage growth remains subdued while inflation has fallen. Analysts are also predicting further cuts in US interest rates to fuel economic growth.

This is likely to boost equity valuations, according to Colin Morton, manager of Franklin UK Equity Income Fund. He says: "The current expectations that US interest rates continue to fall over the next 12 to 18 months, should provide an element of support for equity valuations.

"Lower interest rates in the US will help consumers and businesses borrow more cheaply, which will encourage spending. Interest rates for a lot of countries in the world are based off the US interest rate. In particular, those in Far East and emerging economies will potentially benefit from lower rates. Hopefully, things will start to improve economically for these countries, which have faced a very tough time." mw