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# Excellent value offshore, despite slowing growth

So far in 2019 we've seen a slowdown in global growth across the major economies and, as in the past, a central bank response of additional monetary stimulus. Although US Q1 2019 GDP growth surprised on the upside at 3.2% (q/q annualised), this was due to an improved trade surplus and higher inventories, short-term factors that masked drops in fundamentals like consumer and business spending, as well as weaker housing investment and declines in manufacturing and industrial production. In April the IMF revised its 2019 global growth forecast down to 3.3% from 3.5% previously, as the EU, Japan and China also showed fundamental slowing despite some positive data. Additionally, one of the main risks to global growth prospects (also cited by the IMF) has been the ongoing trade tensions between the US and China, which have already impacted growth (to a relatively small extent so far) but threaten to widen into a full-blown war which could further damage global expansion.

Aside from trade frictions, the slowdown is expected to be cushioned by the central bank response. The US Federal Reserve said it would pause its projected interest-hiking cycle, therefore keeping US interest rates lower for longer than investors had previously expected. The European and Chinese central banks, meanwhile, have introduced new stimulus measures and the UK and Japan have continued with their easy monetary policies. These measures all helped to lift investor sentiment, buoying equity and bond markets alike.

**Global govt bonds unattractive**

Against this backdrop of “lower interest rates for longer”, the biggest opportunity we see globally is for investors to continue to take advantage of the high risk premium available from global equities compared to bonds and cash. This remains substantially above historic norms on the back of extraordinarily low government bond yields. It makes sense for investors to avoid cash and global government bonds, especially those in the UK, EU and Japan where yields remain at exceptionally low levels. US Treasury yields are more attractive, but still not appealing compared to those from equities.

Consequently, our house view portfolios are underweight global government bonds. We are instead holding US and European investment-grade corporate bonds. These assets are slightly cheap and have the potential to deliver stronger returns going forward now that the US interest rate hiking cycle is on hold. In contrast, we have not been holding high-yield corporate bonds as they are less attractive on a risk-adjusted basis.

**Emerging market equities offer value**

Meanwhile, we are overweight global equities as a whole given the very high risk premium available. Emerging markets and currencies have underperformed developed markets, and continue to be especially well valued on many measures. As such we are overweight selected emerging markets such as South Korea, Indonesia and China. Because the US market is relatively expensive and other markets offer better value, we are underweight US equities.

We prefer the global banking sector, which has underperformed the broader market, as well as certain developed markets where equities are undervalued but fundamentals for earnings growth remain positive, including Germany and Japan. These overweight positions are financed primarily by an underweight in global bonds, as well as US equities to a lesser extent.

Finally, we would also opt to be overweight global equities compared to South African equities in portfolios where total equity exposure is constrained, such as Multi-Asset Low-Equity Funds which are limited to 40%. According to our valuation-based view, some other emerging markets are cheaper and offer better value than the local market, despite it also being valued attractively on an historic basis.

Looking ahead, global growth has good prospects for a “soft landing” thanks to the support of central banks around the world. The wild card is trade, where US-Chinese relations could deteriorate further. But investors should recognise that many global equity markets are currently priced to deliver attractive returns over the medium term, and take advantage of this opportunity rather than being discouraged by short-term factors.