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WEALTH MANAGEMENT

The Inside Track

JANUARY 2018

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- 2018 begins with a **marked dissonance between improving economics and deteriorating politics** - the greatest risk to the global economy. The current, almost perfectly synchronized, economic upswing is impressive but won't last forever. When it comes to an end, policymakers will have little or no room to respond by cutting interest rates, reducing taxes and upping transfers for the casualties of the downturn. This will exacerbate the drift to authoritarian leadership and populism.

- **Dollar weakness is a bit of a puzzle.** Since Trump took office a year ago, the greenback has fallen almost 15% against the EUR (up to 1.25 at one point) and by 10% against a basket composed of 6 of the world's major currencies. With an economy boosted by tax cuts and rising interest rates, the $ should be going in the opposite direction. A possible explanation has more to do with politics than economics: the fear that **Trump policies constitute a threat** to America's global stance and **to the $ as the world's reserve currency**.

- **It is in trade that US retrenchment is most visible.** Several comments recently made by US officials (Treasury secretary Mnuchin sees an acceleration of US trade measures this year while Commerce secretary Ross believes a trade war is already under way) raise concerns about rising protectionism. This said, the potentially devastating impact of a full-blown trade and currency war guards against it. Meanwhile, the world is moving on without the US: 35 new bilateral and regional trade pacts are under consideration. In 2018**, trade skirmishes will unnerve investors,** leading to an increase in risk premium and volatility, **but they won't translate into full-blown conflicts.**

- **The "global rules – based order"** (often a metaphor for US domination) **is crumbling.** As a result, economic openness, multilateral institutions and security co-operation are under threat. In particular, the "systemic dissonance" between China and the West is ever more apparent, shattering once and for all the illusion that China would one day converge with the West. One of the most notable investment implications of this coming disorder is that **foreign ownership will become increasingly constrained.** New Zealand banning foreign ownership of real estate is a taste of things to come.

- More policy-makers and business leaders recognize that our **fixation on GDP growth is misleading** because it doesn't account for wellbeing and living standards. To understand where a country is heading, market participants are much better off using alternative measures like the WEF "Inclusive Development Index" or the UN "Human Development Index". Tellingly, pioneering academic research shows that **changes in population wellbeing are more predictive of election outcomes and populist voting than traditional economic indicators** such as GDP growth and unemployment.

- Davos has settled the debate between techno-optimists versus techno-pessimists and how the 4th industrial revolution will impact our lives. **In the short-term, it will make most people nervous and less secure about their future.** A flurry of comments made by top CEOs from different industries (including big tech) showed that job losses will be consequential and the adjustment painful. Take it from the horses' mouth! Jack Ma, Alibaba's CEO, even said that the angst provoked by job losses could lead to conflicts…

- Big tech has every reason to be concerned about the coming regulatory and taxation backlash. Nowadays, there is nobody to defend the Faangs, accused of stifling innovation, promoting state surveillance, impacting our mental health, destroying jobs, supporting authoritarianism, encouraging abuse and pornography. The list is long and consequential… **A social issue now poses a threat to share price.** Two investors who between themselves own about $2bn of Apple's stock just launched a campaign concerning technology addiction. Others will follow – **the honeymoon with big tech stocks will soon be over.**

- Globally, **2017 recorded the highest number of extreme weather events** – now ranked as global risk no.1 by the WEF global risk network in terms of severity of impact and likelihood of occurrence. Global warming and rising sea levels are swelling the claims of insurance companies to the point that certain assets will soon be too risky to underwrite. For long-term investors, **many coastal areas will become uninvestible,** while the fear of stranded assets will increasingly compel investors to divest from fossil fuels (700 large investors have already done so). Iran epitomizes the dramatic and far-reaching implications of acute and repeated extreme weather events. The recent protests were in part triggered by the water crisis (partly due to environmental corruption) - a ticking time bomb that threatens the country's stability.

- With a global elite now so preoccupied by inequality and the dangers that come with it, **corporate social activism is about to rise decisively** – bringing far-reaching negative implications for companies that do not behave and conform as 'good citizens'. Private and institutional investors (including the world's largest: Blackrock and its $6tr of AUM) are increasingly demanding that companies think longer-term and address the issue of their net contribution to society.

- In 2018, the overwhelming presence of men in the upper echelons of business and gender pay divergence will become an increasingly sensitive issue, negatively impacting companies that do not walk the talk in terms of diversity and pay policy. This is much more than a moral issue. As new research demonstrates, the absence of gender diversity affects profitability, while pay inequity affects reputation, which in turn affects the P&L. Simply put: **diversity generates higher profits**. Investors: take note!

- In Q1 2018, top **"must-watch" issues include**: (1) Whether the global bond market sell-off continues, possibly igniting a broad market correction; (2) Whether Trump will cause a significant deterioration in US-China trade and/or global trade relations; (3) Whether China will be able to deleverage without sacrificing too much growth; (4) The direction of the USD: it impacts everything and everybody (5) How the Italian elections on March 4 will affect the strong resurgence of Europe and its animal spirits.