BLACKWOOD
ASSET MANAGEMENT

INVESTMENT COMMENTARY - FEBRUARY 2019

Last month we described how difficult the final quarter of 2018 was for investors.

In fact for the U.S. equity market it was the worst December since 1931 amid the great depression.

To absolutely prove the dangers of extrapolating a trend, January has turned out to be the best since 1987. Equity markets were oversold in the very short term and due a bounce but volatility is likely to persist.

The recovery in equity markets was mainly in response to the Federal Reserve indicating that it may put its withdrawal of liquidity (i.e. quantitative tightening) on hold rather than it being on autopilot. This, combined with the emerging view that they may also be near the end of the interest rate cycle, sent shares higher in the U.S. and elsewhere.

Perversely, the number of fund managers who are overweight cash during this sharp rebound hit levels not seen since the financial crisis in 2009. Selling after significant declines in prices and then sitting on cash as markets recover is standard behaviour for "the experts".

Major financial institutions remain disengaged with markets in a form of "buyers strike" meaning that liquidity remains limited in many asset classes and this is leading to continued sharp movements in prices.

Evidence of this is not hard to find; December 26th saw the biggest one day points rise in the history of the Dow Jones and we have also seen a mini flash crash of the Swiss Franc in the past couple of days.

It is worth noting that equities are defined as liquid, which means you can sell equities usually instantly and have access to your capital within hours. The value of this liquidity is hard to gauge and varies over time, but it is our contention that it is materially undervalued by investors. In most investment calculations liquidity is deemed to have no value…until assets become illiquid and then it becomes like gold dust. Ask investors who couldn't sell property assets for six months after the Brexit vote (unless at a major discount) how much they valued liquidity?

We recognise and protect the liquidity of our clients' assets. We continue to believe that equities remain (broadly) cheap but that volatility will remain higher than we grew accustomed to in 2018. We will endeavour to remain light on our feet throughout 2019.

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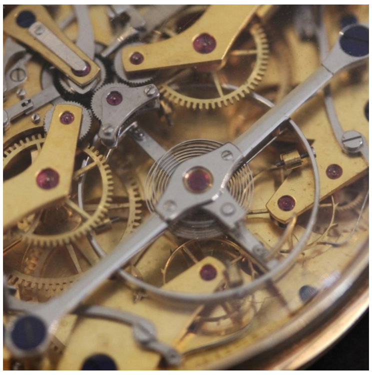

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