

Are you suffering from FOMO?

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Whilst there is no formal recognition that FOMO exists in the professional world, if you asked any investor, they would certainly agree that stock market participants share the same fear of missing out as that of their children. In stock market terms, think of the clamour to jump on hottest performing stock or asset (recall the urge to jump on the tech bandwagon, despite warnings of a bubble, or more recently the rush to invest in Bitcoin and other cryptos as the market rallied higher and higher). Unfortunately, this often irrational 'fear of missing out' leads investors to switch off the logic side of their brain and jump on the band wagon with little regard for underlying valuations or indeed any intrinsic knowledge of the asset,

and ultimately we know how the story ends.

Usually, FOMO occurs within one asset class at a time but right now, with almost every market rallying, it seems investors have gotten universal FOMO as they rush to buy up everything for fear of missing out on a rally.

If you had listened to as many stock market commentaries as we have over the last 6 months, you would have heard talk about 2019's markets being broadly positive but with much higher levels of volatility. Essentially this was the economists equivalent of a pilot switching on the "fasten seat belts" sign.

Let's just quickly touch on the (now dated) theory that in good times, equity markets receive a wall of money coming out of the fixed income or the "debt" market as investors push the equity risk peddle to the floor. As with anything that's suddenly in sharp demand, the price rises to meet it which is why the equity market then rallies and completes the self-fulfilling cycle coined the "great rotation".

Now, with global equity markets up 16% in 2019, one would expect to see outflows from fixed income markets to fund the subsequent equity splurge. Apparently not - fixed income investment for the year has risen from $147billion to $185billion which is a 4.6% rise in assets being managed and has pushed debt prices to near record highs.

Bringing up the rear is gold, a staunch asset class which investors historically retreat to in times of uncertainty. Since the renewed volatility coming from the US / China trade war, the precious metal has staged a 9% rally and is currently trading near a five-year high. Gold equity stocks have also returned near 20% in one month.

So, equities are up which signals a positive view, fixed income is up which signals a more cautious view, and investors are flocking to gold which is an asset class that thrives on panic. This is the stock market's version of "FOMO".

It seems investors are starting to fret about the state of the global economy, evidenced by the money going into gold and fixed income, but at the same time they don't want to miss out on the odds of a relief equity rally and so are keeping hold of their equities.

Let's try and unpick this convoluted mix of signals. Despite a gain of 16% from global equities, equity funds have seen a total of $52billion coming out of the market this year. This tells us that investors are taking this 16% rally as an opportunity to take profits from ten years of equity returns and recommit them to the fixed income market. This move chimes nicely with investors listening to economists' forecasts of heightened volatility and the call to fasten our seat belts.

June's 2019 fund manager survey by Bank of America Merrill Lynch has yielded some more telling observations about the way global investors are currently positioned. Highlights from the report show us that global investors are currently holding not only the largest overweight position to fixed income since 2011, but also their largest holding of pure cash since 2011.

On the equity side, the same report indicates the largest underweight position to global equities since the financial crash. Holistically this type of long fixed income and short equities approach to markets is reserved for times of pessimism surrounding economic performance, as well as fear about where we are in the cycle which ultimately produces the tell tail dive for safety assets that we are currently seeing.

So, readers, this poses somewhat of a conundrum for investment mangers which goes something like this - with global government debt rallying into record territory, gold putting on nearly 10% in eight weeks and the dollar keeping a lot of its strength, managers wanting to buy some defensive firepower in these uncertain times are either forced to pay top dollar for it or sit in straight cash!

Now, managers always strive to invest as much of a client's assets as possible, but how many managers in the peak of 2018's Q4 sell off, or indeed 2008, would have given their right arm to own cash rather than equities? There is, on occasion, a benefit to owning an asset which delivers you 0% when equities are dropping like a stone, and traditional safe havens like gold and government debt are looking very expensive. So, don't be surprised to see your portfolios with larger than average cash positions and dwindling equity allocations as safety becomes the prime concern.

TAM has, since the middle of last year, been building its defensive positioning in the market whilst taking profits on some of its more satellite investments which traditionally yield the best returns in good times and fall fastest in the bad. Indeed, this massive rally in gold has been welcomed at TAM because our clients were invested into the precious metal when it was trading at historic lows in the Autumn of last year.

TAM remains on the hunt for the best combination of cash and defensive investments (which we don't have to pay the earth for) to see our clients though any bouts of volatility. And yes, we too are concerned about the equity market, but we don't believe it's time to throw the baby out with the bath water and wash our hands of the equity market altogether. We will be keeping the best and most defensive investments running to ensure, if we do get a rally into the back end of the year, our clients will still be making money.

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