MVAM
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ASSET MANAGEMENT

Monthly Newsletter

'Cash is King?' September 2019

Cash is King, Long live the King. Oh, sorry My Lord, but the King is dead.

This is not the script from a Monty Python film, but the reality developing across Europe in 2019. Danish and Swiss banks are leading the way and introducing a charge on deposits. The flip side is that Scandinavian banks are offering a negative interest rate of 0.5% on a mortgage. This is not fake news. Danish banks are paying you to take out a mortgage. Imagine receiving a payment each month to have a mortgage! In this brave new world, cash savers will end up with very little, as the combination of inflation and deposit charges destroy the value of their money, while the borrowers end up with a house, indirectly paid for by those cautious savers. Crazy world….

The heart of the problem is a moribund European economy, with the German export driven model caught up in the US/China trade war and inflation remaining stubbornly below the European Central Banks target level. Recession and deflation are the front of mind fears of investors across the world. Against this background, many government bonds are offering a negative yield. If you invest in them and hold them until expiry you are guaranteed to lose money!! Large companies have joined this party more recently, Airbus, Nestle, Sanofi and Walmart are all being paid by investors to borrow. These negative yields imply investors see virtually no chance of positive returns anywhere…

Another red flag highlighting the prevailing high level of investor fear is the price of gold, which has jumped by 20% in 2019 and is standing at a six-year high. This is a commodity which yields nothing and has little intrinsic value. As legendary investor Warren Buffett said, "gold gets dug out of the ground in Africa…then we melt it down, bury it again and pay people to guard it. Anyone watching from Mars would be scratching their head".

Against this background of weak investor sentiment and low returns, the UK stock market yield was 4.8% in 2018, approaching a 30-year high, compared to a long-term average of 3.5%, while inflation is only 2%. Special dividends, especially from the mining and housebuilding sector have inflated the number, but there is also the strong recovery from the banks, as they emerge at long last from the financial crisis. For investors a key question is the sustainability of this positive dividend trend, against the background of a slowing global economy. Certainly, several weaker companies facing structural and regulatory issues have cut dividends, such as M&S and Centrica. However, modest dividend growth is still forecast for the overall market for the next 12 months. If this proves to be correct, then the dividend pay-out level and yield should support the market during these uncertain times. A mooted European fiscal stimulus, led by Germany and the UK, would be the icing on the cake.

This all leaves UK investors with interesting and sharply contrasting investment choices in these uncertain times - stock market, bonds, cash or gold. Only one is offering a high yield, which doesn't feel like a bad choice if we are close to the darkest hour. Sadly, Churchill is nowhere to be seen.

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