

A NEW AGE

Our View on Financial Markets

October 1st, 2014

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As co-founder and co-owner of Albin Kistler AG, André Kistler regularly publishes views and expectations on financial market developments.

The periodically appearing views on financial markets are also available on Albin Kistler's website as downloadable PDF.

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A Curious Situation

Over the last few months growth forecasts for the western world have been taking an increasingly gloomy turn. The expansive phase of an economic cycle has never been as weak as it is now.

Whilst the monetary floodgates remain open, inflation has been at record lows for years. This gaping divergence is absolutely without historical precedent.

Where is all the Growth gone?

Since the financial crisis the world has fundamentally changed. Is everything different this time, and do we have to jettison all we have learned over past decades? No, but might be living in a new age.

In the EU, unfavourable demographics, vertiginous amounts of debt and unresolved structural and competitiveness issues have brought about a crisis of confidence and caused capex to fall. This is a relatively new situation, but one that will stay with us for some time.

The steady decline in global inflation is directly related to neo-globalisation and a sharp rise in competition everywhere. Never in the past have the different parts of the world been as closely interconnected as they are today.

Knowledge, products and services for billions of people are being created, shared and exchanged at breathtaking speed. Free enterprise – the source of all lasting economic success – is being spread irresistibly and at high speed by the internet and modern technology.

Looking back over the past hundred years, the world has never been as free, flexible or interconnected as it is today. “The forces of spontaneous order” (Friedrich August von Hayek) have created astonishing economic progress in recent times, giving rise to increased prosperity all over the world. Masses of people will relentlessly continue to ascend into the middle class for decades to come.

Summary

Over the last few months growth Successful investors need to look beyond forecasting index levels. What matters is whether in the years to come governments will continue to offer a friendly environment for free enterprise.

Although the current economic upturn is relatively weak, it will continue for some time. The world's leading companies have years ahead of them in which they will be able to build on their outstanding profitability. With inflation remaining low, an earnings yield of around 6 % means equity valuations remain attractive.

Geopolitical and cyclical risks are merely temporary dangers, and any cash holdings should be used to lower average purchase prices. Low bond yields reflect the fact that inflationary pressure is low. Particular caution is appropriate for banks that have inflated their balance sheets with government bond holdings.