

## CHAPTER 11



# BLACK SWANS 2020

*With fear of recession in the air, ongoing uncertainty surrounding the upcoming US election cycle, and heightened tensions in the Middle East, the year ahead is fraught with danger. By Eleanor Mahmoud*

## GARETH DEAGON, PORTFOLIO MANAGER, BLACKFINCH INVESTMENTS



To attempt to pick out a potential black swan event that may have global implications in 2020, it is difficult to look beyond the US.

With so many potential candidates still in the running for the Democratic presidential candidacy, I believe that the emergence of a far-left candidate taking on president Trump and winning come November 2020, has the potential to cause a shock to global markets. While any Democratic candidate considered to be 'far-left' is substantially less extreme than many of their global counterparts, the impact on large corporates could be significant.

Of course, in the interim there is always the potential of a controversial tweet from the current incumbent causing a market meltdown, although we can but hope that he may put a little more thought into some of the statements that he makes so publicly, for fear of damaging the economy and harming his re-election chances.

## ANNALAN ANNALINGAM, CO-HEAD OF MULTI ASSET INVESTMENTS, SIGNIA WEALTH



By definition a black swan is an unpredictable event, so I would like to focus on two risks: dollar funding and US inflation. In September last year no one was really sure what confluence of factors caused the scramble for dollar

liquidity, and this year we could see a similar event. The Fed can pump in liquidity, but it's not necessarily the case this will be passed on. A major funding squeeze at the beginning of 2020 could trigger major market panic.

Inflation has now been widely written off, but when one considers how close personal consumption is to the Fed's target and where it's been as recently as August, it's not difficult to see how continued reduction in unemployment, wage increases and solid growth could see inflation increase. Accompanied by the Fed having to raise rates, this could result in a 2018 Q4 scenario.

## TIM SHARP, MANAGING DIRECTOR, POTTINGER INVESTMENT MANAGEMENT



Our house view is that the economy is late cycle, while almost everyone else seems to think and be positioned as though it is mid-cycle. If we are correct and there is a global recession in H2 2020, this would have enormous implications for global markets. A recession

alone does not always constitute a black swan event, of course, but a recession in the second half of this year would be unexpected and markets are not at all positioned for it.

We think that other 'grey swans' for 2020 include the election of Elizabeth Warren as president of the USA (and to a lesser extent Bernie Sanders, whose economic policies are more radical but whose potential election is less likely than that of Warren), the UK leaving the EU with a 'no-deal' or hard Brexit on 31 December 2020, the successful impeachment and removal of Donald Trump from office and the imposition of heavier-than-expected tariffs between the US and Europe.

## MATTHEW HOGGARTH, HEAD OF RESEARCH, THEISIS ASSET MANAGEMENT



Most internet encryption relies on mathematical chicanery such as it being easy to multiply two large numbers together, but difficult to deduce the two numbers if you only know the

result. Nobody has yet devised a simple method to solve this factorisation problem, but there is no proof that it is impossible. Advances by academic mathematicians, or a breakthrough in practical quantum computing, could potentially render most internet communication insecure.

Secure online transactions have become so pervasive that it would be quite a wrench to lose them. Imagine client communication going back to post, fax and phone, and airline bookings via a trip to the travel agent.

Some companies' business models would be disrupted instantly, such as Amazon, Easyjet and Direct Line. High street businesses might not benefit however, as many will be dependent on payment networks for processing card transactions and electronic communication for managing their supply chains.

## SIMON EVAN-COOK, SENIOR INVESTMENT MANAGER – MULTI ASSET FUNDS, PREMIER MITON INVESTORS



I am irritatingly pedantic about the term black swan. This is one of the few things that makes me confront the horrific truth that I am gradually turning into my father (the others being bad jokes and tuneless whistling).

The term specifically refers to an event that is impossible to predict. So the mere act of predicting it here would instantly rule it out as a black swan. So events for 2020, such as an inflation spike or a serious, rapid escalation in US/China tension would be lower-probability, high-shock events for markets, but they wouldn't be technically black swans.

The truest significant examples in recent living memory were the terror attacks of 2011, which no-one saw coming and had severe, far-reaching effects. An example for 2020 would be Mother Nature throwing a disastrous spanner into a tight, fragile global supply chain. Such random events are why it pays to always be cautious; and not just when 'the macro' outlook is dodgy.

## WILL DICKSON, CHIEF INVESTMENT OFFICER, P1 INVESTMENT MANAGEMENT



While 2020 may be too early to predict such a series of events, we have considered the scenario where a string of severe natural disasters, brought on by climate change (eg. hurricanes, flooding, wildfires), cause a significant policy shift from governments and companies.

Such a stark realisation that the economy needs to adapt to solve this global issue may lead to the anticipation of extreme taxes on fossil fuels, lessening extractors' profitability and leaving stranded assets. Debt owed by these companies may also become valueless.

While such a scenario may be required to meet the needs of the environment, financial markets, pension funds and banks would be hit hard by such losses. The dramatic shift between industries would also undoubtedly lead to extreme winners and losers.



## DAVID SENWENS, HEAD OF INVESTMENT STRATEGY, WEALTHIFY



People typically focus on negative black swans, but as an optimist, I wanted to highlight three market positive grey swans that would extend the cycle well beyond its current expected expiration date.

Firstly, half-way through 2020 China and the US reach a deal, quite possibly the greatest deal mankind ever saw, restoring global manufacturing activity and business confidence across the globe.

Secondly, low interest rates and infrastructure needs finally inspire the G-20 to put political differences aside for a grand spending plan that supports growth, delivers a long-term investment plan and even lifts inflation in the eurozone.

Finally, with his Brexit mandate secured, Boris Johnson quickly agrees a FTA agreement with the EU and multiple other trade partners covering services, security and goods. All in less time than many people take to plan a wedding. Pent up demand sees UK equity markets and the economy go on to become the top 2020 performers.

## OLIVER FOGHLER, CEO AND MANAGING PARTNER, STONE MOUNTAIN CAPITAL



Black swan events could hit several markets during 2020. The US equity market rose strongly in 2019, driven mainly by increased P/E ratios, and could be a prime candidate for a black swan due to the

presidential impeachment proceedings, upcoming presidential election, potential upsets in China/US trade deals and the Federal Reserve, which could start a rate increase cycle due to the accommodative policy since the great financial crisis.

Rates rises could be a surprise in the case of one of the US, UK, Japan or China trading with a credit premium. The broader debt market due to low interest rates of major central banks could implode due to rating migration. Fixed income ETFs could face a liquidity event in 2020.

Leveraged loans, CLOs and the broader corporate credit markets have seen Ebitda multiples surpass pre-crash levels. Peer-to-peer and marketplace lending could see rises in default rates.

The tech sector could also face regulatory and privacy action and could be split up. Cryptocurrencies, specifically Bitcoin, Ethereum and Libra are also subject to regulation actions in 2020.



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