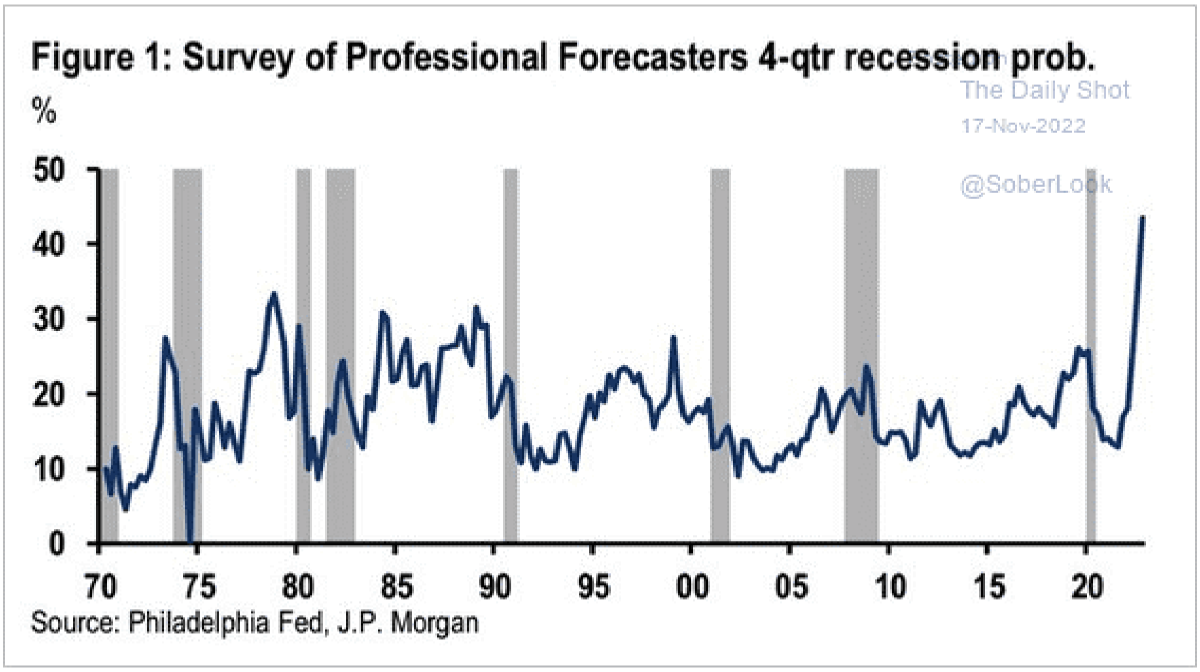
It's tough to make predictions, especially about the future.

As we near the end of a truly tumultuous year in markets, one we are certain most people will be keen to forget, we inevitably turn our attention to what the next year may have in store. Will it be a case of more of the same, or can we see grounds for increased optimism going forwards?

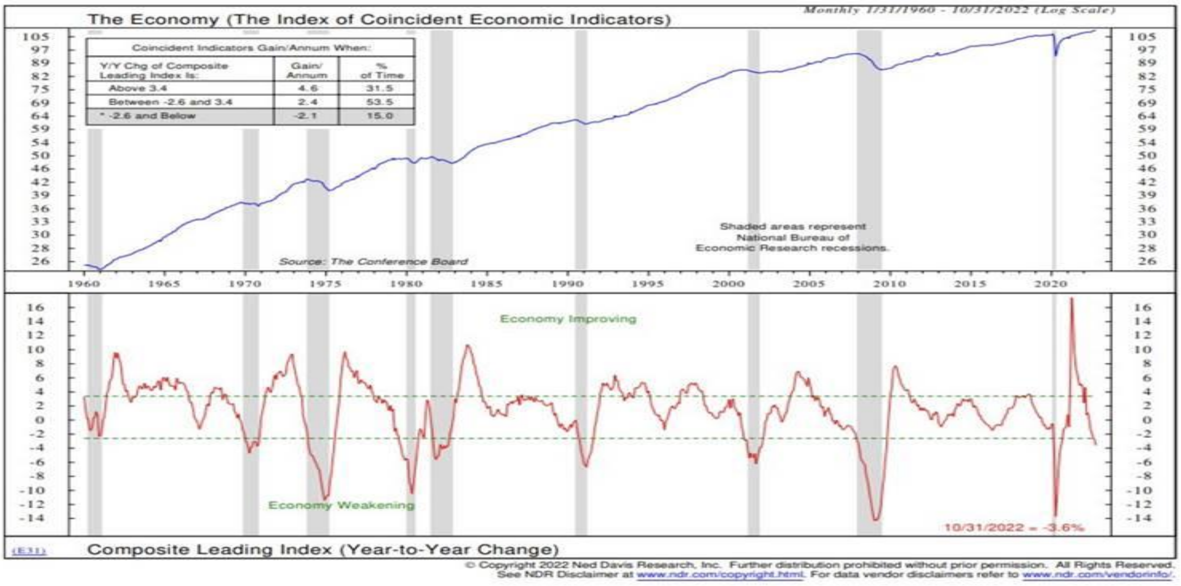
For sure, there remains a great deal of apprehension among the numerous market participants we meet daily, and with seemingly good reason. The prospect of an imminent global recession heads the worry list, although it has plenty of company from the outlook for inflation, interest rates, war, the pandemic and corporate profitability, among others.

We, of course, have no more accurate a crystal ball than anyone else. It is, after all, tough to make predictions, especially about the future! So, with that extremely large caveat in place, in this piece we offer up some interesting, to us at least, observations, and it will come as no surprise to most of our readers that we have focussed on snippets suggestive of a somewhat brighter outlook than the extremely bearish consensus we readily observe today.

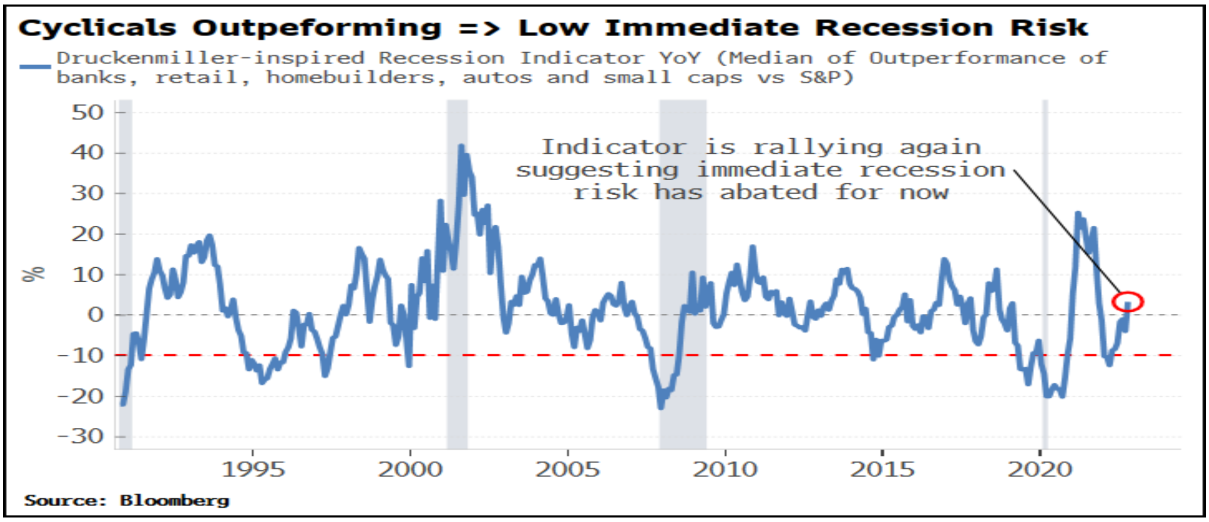


We start with the most pressing investment consideration, are we nearing recession or not? These first few charts relate specifically to the US outlook but are obviously hugely influential in a global context. A record 45% of professional economists expect a recession over the next 12 months. Could this be the most accurately anticipated recession ever? A quick glance at the chart above suggests a less than robust track record in this regard, but then again it could well be different this time.

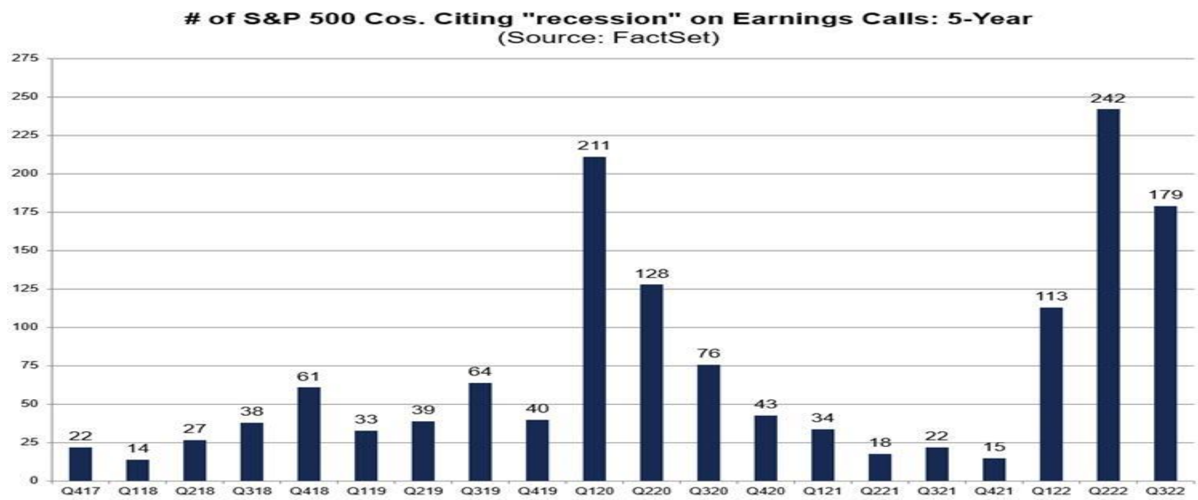
This next indicator, from Ned Davis Research, would seemingly agree with those economists and it is only fair to highlight that historically, unlike our learned friends, it has had an excellent track record in identifying recessionary environments.



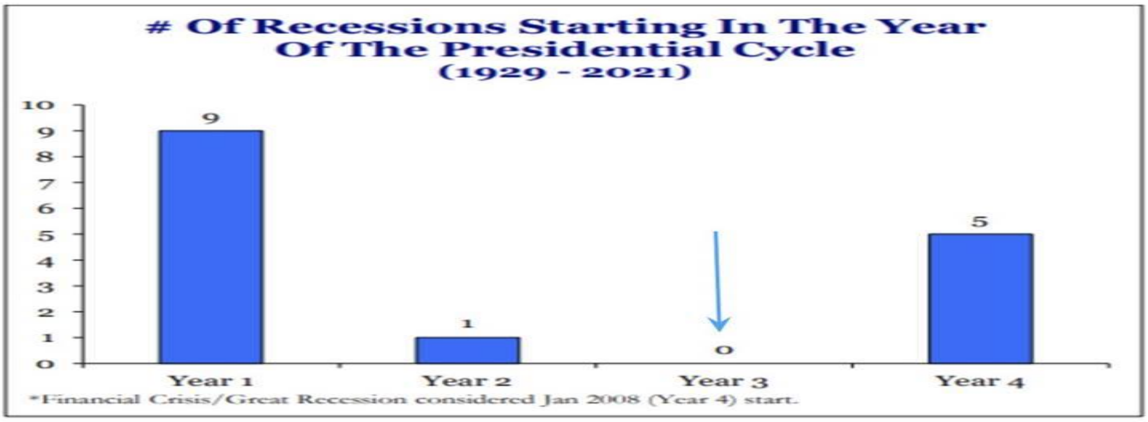
It is not entirely one way traffic though as the indicator below, inspired by legendary US investor Stan Druckenmiller, is suggestive of a significantly lower risk of recession in the immediate future.



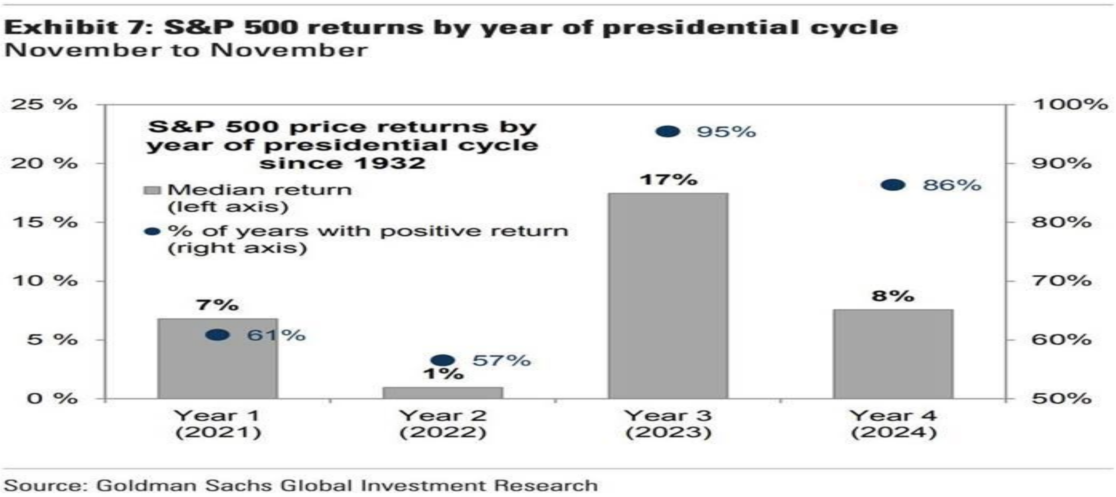
This also, perhaps, chimes with the following observation that the number of S&P 500 companies referencing ‘recession’ on their latest earnings calls, whilst still elevated, has fallen quite sharply.



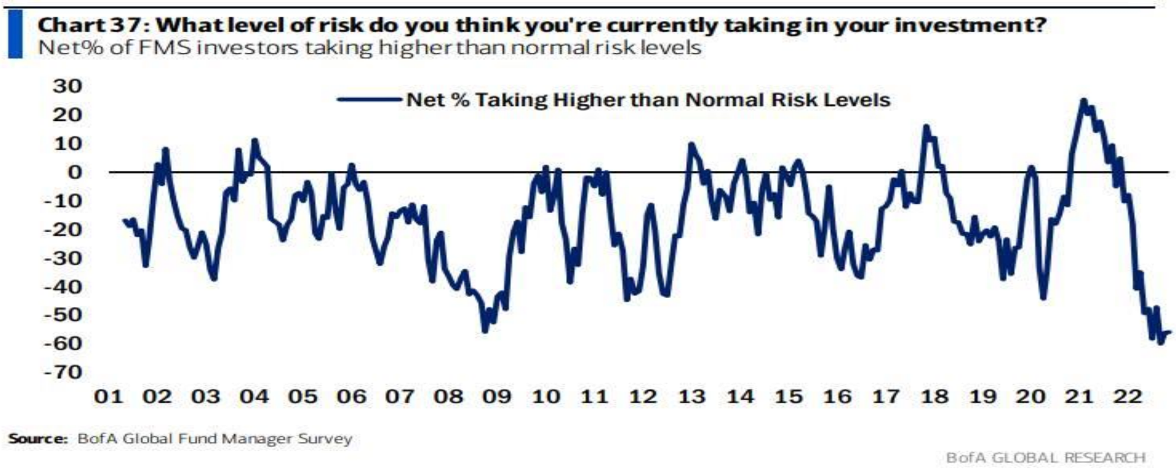
If there is to be a recession in 2023 it will notably be the only one to have started in the third year of the US presidential cycle, going all the way back to 1929.



Whilst on the subject of the presidential cycle, the chart below from Goldman Sachs highlights year 3 as the best performing year of the cycle historically, with a 95% success rate of positive returns.



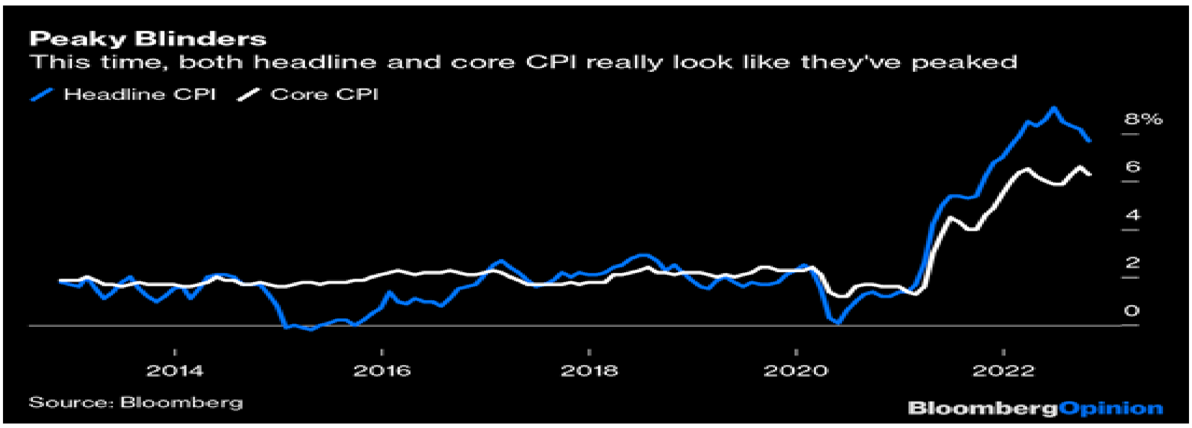
Certainly, judging by the chart below, professional investors have plenty of scope to increase risk taking in portfolios, should the environment not prove as dire next year as many fear.



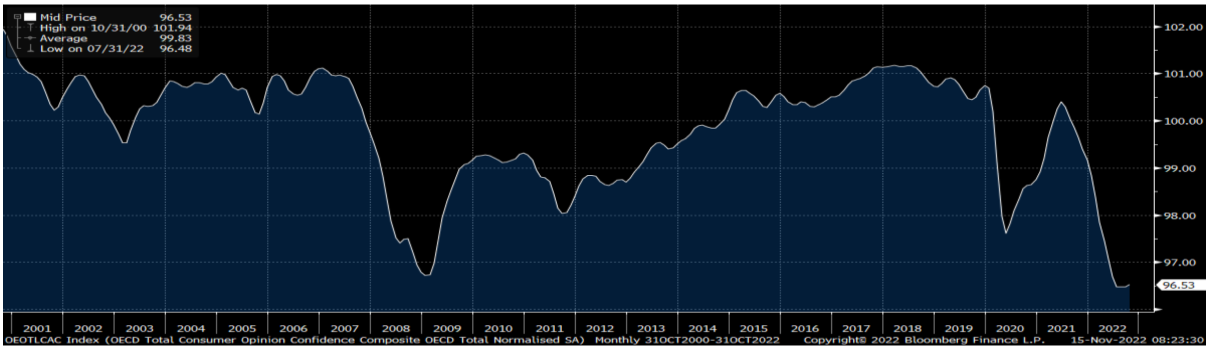
Interestingly, market moves of late, generally dismissed as 'just another bear market rally' could potentially be suggesting a more significant improvement in the investing environment. The chart below is of the MSCI World Index excluding the USA. Having fallen c.-30% between Sept 2021 and Oct 2022, the index has rallied back +19% recently – almost the definition of a new bull market - and is currently trading above the 200-day moving average. Has the downtrend been firmly broken?

Of course, one of the key issues world markets have been dealing with of late has been the relentless strength of the US Dollar against most other major currencies. But as the chart below highlights, perhaps the year-on-year rate of change has now peaked and will offer some relief in the period ahead.

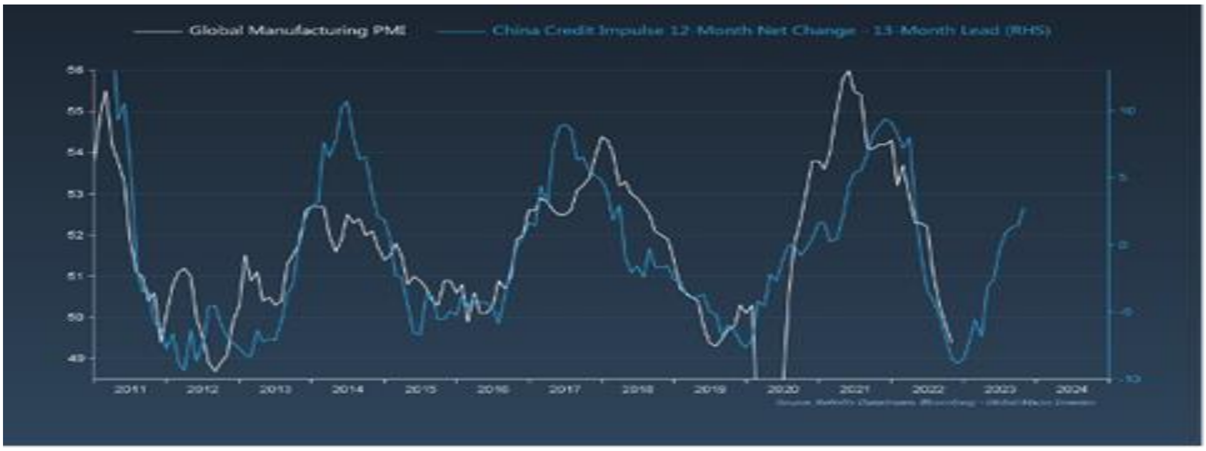
Allied to this has been the persistence of inflationary pressures globally and again, perhaps the chart below, from the US, is suggestive of a better environment as we look forward.



Finally, when thinking about two key components of the global economy, consumer spending and manufacturing, we thought the following 2 charts were worth highlighting. The first shows total OECD consumer confidence over the past 20 years. We know consumers are worried and for good reasons, but the question we ask ourselves is where is confidence most likely to head from here?



With regards to global manufacturing, the following chart again offers some reasons for optimism as we move through 2023, certainly if recent history is any guide.



We reiterate we have no better insight into the economic outlook than anyone else. However, we continue to observe a level of bearishness we have rarely experienced during nearly 25 years of stock market investing and that, naturally, makes us look for data points that might present a different conclusion. Whether they will prove correct or not, only time will tell.

Regardless of the immediate outlook, we remain resolutely focussed on building a portfolio of excellent businesses with exciting future prospects. We have been fortunate this year to acquire more of them at what we are sure will be, with the benefit of hindsight, hugely attractive prices. We look forward to our clients reaping the rewards of those opportunities in the years ahead.

Simon Murphy, Fund Manager, VT Tyndall Real Income Fund, November 29th 2022
Data source (unless otherwise stated): Bloomberg.

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