



Investment Insight

Friday, 2 February 2018

Hot TOPIX: Over the past couple of weeks we have started to observe some early signs of nervousness among equity investors. This is largely due to the dawning realisation of the possible consequences for corporate earnings of anticipated US interest rate rises, about which we wrote last week. While few dispute that the US market is expensive, the investor nervousness was felt in markets across the globe, not just in the US; a timely reminder of the old adage that when America sneezes the whole world catches a cold.

Notwithstanding this, in relative terms some equity markets appear to offer greater potential than others and the Japanese equity market is one of those tipped to fare better. In the **Inside Track** we get an insider's view from Fidelity's Jeremy Podger.

Full circle. Almost exactly a decade after Ireland made its (early) entry to the global financial crisis, we now hear talk of the Celtic Phoenix, the avian first-cousin of the now extinct Tiger. As a barometer of the economy's fortunes, the unemployment rate seems to confirm that we have come full-circle, nearly back at long-term norms, almost as if the past decade was a mere aberration.

Quoted...

"A 1% rise in bond yields will produce the largest bear market in bonds that we have ever seen since 1980 to 1981" – Ray Dalio (last week at Davos)

The Inside Track

Jeremy Podger manages the Fidelity Global Special Situations Fund and the Fidelity World Fund (SICAV) and has been managing global equities mandates for more than 20 years. Like many investors, he sees good opportunities currently in the Japanese equity market. The following are his recent comments.

Contrary to popular perceptions, in like currency terms, Japanese equities have kept up with global equities over recent years and there are reasons to expect the market to outperform from here. Currently, despite businesses witnessing new highs in terms of corporate profitability, the Japanese market remains well below levels seen in the 1980s. In fact, a meaningful part trades at a market value below book value and, across the market as a whole, companies have near zero debt - very unusual in an international context.

At the same time, valuations versus the rest of the world are near record lows, whilst corporate reform and increased shareholder focus continue to move in the right direction. Not only are businesses more focused on return on equity, there is a distinct change in how companies are approaching governance, with board members now needing to justify cross shareholding patterns and cash holdings on the balance sheet. After reducing holdings in 2017, it appears that international investors are now returning, and this is a good sign for the short-term, since the market's relative performance has in the past been strongly driven by foreign investor flows.

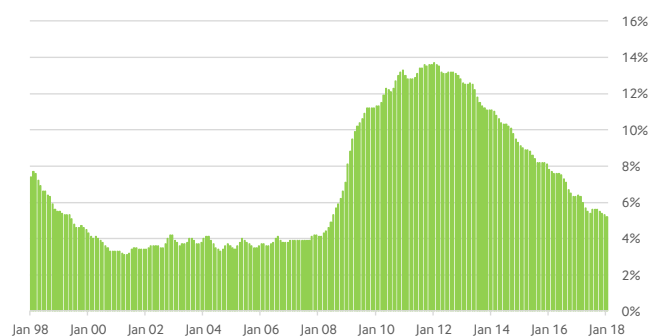
The caveat in all of this is that the Japanese market tends to be sensitive to global economic trends and there are some clear geo-political risks in the broader region. However, recent economic strength is not just the result of trade-related demand but reflects a real (some would say surprising) improvement in domestic demand conditions. In this context, we will be following developments around expected Japanese tax reform very closely in the coming period. At this point, it seems appropriate to hold a mixture of domestic and international-focused businesses with company-specific fundamental drivers.

While many investors would characterise Japan as classic value, we have been successful at identifying exceptional value, corporate change and unique (growth) businesses. As we look around the world today, while the TOPIX has broken out of its trading range recently, Japan continues to represent an area of meaningful opportunity and we will certainly be on the lookout for new names that fit our investment philosophy.

Pic of the Week

The CSO's latest seasonally adjusted unemployment figures for January 2018 showed the unemployment rate at 6.1%, its lowest level in almost a decade. While this progress is welcome, it contributes to pressures not previously felt since the Celtic Tiger era – a shortage of skilled labour, wage inflation and, perhaps most topically, accommodation price inflation. Will these pressures be handled in a manner that avoids another boom-and-bust cycle that sees the Phoenix come down in a flail of feathers? Only time will tell.

Ireland Seasonally Adjusted Unemployment rate



Market View

	Last 7 days (€)	Last 12 mths (€)	YTD (€)	5Y Ann. (€)
Global equities	-1.4%	+10.7%	+0.5%	+12.7%
US equities	-1.1%	+10.9%	+0.7%	+16.3%
European equities	-1.5%	+12.4%	+1.4%	+8.9%
EM equities	-1.3%	+20.3%	+3.7%	+6.7%
Irish equities	-2.7%	+8.9%	-1.1%	+14.4%
Commodities	-1.3%	-4.8%	-1.3%	-7.6%
Hedge funds	-1.2%	+3.1%	+0.8%	-0.5%

Currencies	Current	YTD Δ
EUR:USD	1.2457	+3.8%
EUR:GBP	0.8760	-1.5%
EUR:CNY	7.8414	+0.5%
GBP:USD	1.4217	+5.3%
Bitcoin	9,894	-31.7%

Commodities	Current	YTD Δ
Gold	1,339.83	+2.9%
Copper	7,100.00	-0.8%
Oil	68.84	+4.4%
Wheat	446.63	+4.7%

Week ahead: Key events

05/02 Japan, EU & US PMI Data
05/02 EU Retail Trade
06/02 US Retail Sales
07/02 Japan Employment & Business Conditions Data
07/02 Germany Industrial Production & US Consumer Credit
08/02 UK BOE Interest Rate Decision
08/02 US Initial Jobless Claims
09/02 UK & US Trade Data

Central Bank rates *Current*

Eurozone	0.00%
USA	1.25%
UK	0.25%

Economic indicators *Bond yields* *Inflation* *GDP YoY*

Ireland	+1.1%	+0.4%	+7.2%
Germany	+0.7%	+1.7%	+2.8%
USA	+2.7%	+2.1%	+2.5%
China	+2.1%	+1.8%	+6.8%

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