

Are the Permabears Starting to Defrost?

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The last three years have been beset with issues of gravitas. A banking System that neared collapse in 2008 and the ensuing economic decline pushed the financial world to the brink. It is unsurprising that against this background many believed that this was Armageddon for the investment industry – and so it nearly was! However we have survived and the majority of investors may not have prospered as much as they would have wished but they have certainly survived to fight another day; indeed equity markets have nearly regained all the ground lost during the worst of the downturn.

If we had taken a sane man aside during the bull run up prior to 2008 and predicted that within the next three years we would have experienced several (let alone all) of the following events they would have considered us slightly deluded. If we had predicted that portfolio values would be broadly unchanged after such events they would considered us completely insane!

Banking Crisis: Some of the world largest banks will collapse (Lehman) or been close to collapse and need to be bailed out by global governments.

Recession: A swift aggressive and perceived long term recession and low growth will follow

Natural Disaster: Earthquakes and Tsunamis decimating parts of Japan resulting in a nuclear disaster that was a whisker away from being of biblical proportions.

Civil Unrest: There will be uprising and blood on the streets in London, North Africa and Arab states.

European Collapse: The bailout of several European Countries (most recently Greece) and heightened fears of contagion. The sanctity of the Euro as a global currency would come under threat.

The US losing its Triple-A rating: Hereto AAA government debt would be downgraded in a swathe initially across Europe but with the US also taking the embarrassment head on.

So has the world gone mad, or are there other forces at play?

At this point we need to put the markets in perspective. They have survived and elements of them have indeed prospered. We have not headed off into a world of barter and 1932 Depression. The "perma bears" – those who saw disaster on every corner are smarting just a little at this point – or remain in denial? What do they think now? – Have they turned a corner and are they buyers – if not who are the buyers driving the markets higher? It does not, as yet, appear to be retail investors who, it would seem, are grimly hanging on to the interest rate investment return of almost zero. They haven't been wrong as returns over these momentous years of market insecurity are around flat for market investors (give or take 5% on risk profile).

In a sense the permabears were right as 2008 was an annus horribilis and 30% falls were not unusual for investors. These losses have however been recouped.

2011 was even more bizarre in that the news was as bad as 2008 – many would have said potentially cataclysmic. Yet markets hardly went down.

My own theory as CEO of TAM is that market stress needs to be relieved and liquidity is the key component in periods of high stress. In 2008 the market stress was alleviated by outright selling and the collapse of the markets duly followed. Investors satiated their desire and liquidity was created (QE). 2011 however was potentially far worse on the news front and the forebodings of the permabears, did not result in massive sales. Why? In my opinion worried and stress ridden investors were satiated in their selling by the intense volatility that occurred during specific periods in 2011 – most notably the summer months. Sellers were able to liquidate but through it all there was equivalent buying in process. This backed by the US economic juggernaut slipping into second gear and with further liquidity pumped into the market (LTRO) meant that GDP numbers were nowhere near the low end of forecast. We trundled along with a flat(ish) GDP. Of course there were some noticeable European exceptions but the core markets, supported by China, held the global economy up by the bootstraps.

Are the real permabears beginning to defrost and is there a real "risk-on" trade to come from those with high liquidity, ultra defensive positions or balanced long/short books? Will Institutional cash and ultimately the private investor add further positive cash flow? I think it is and even the technicians (as chartists) are now beginning to consider the upside. We retain a healthy belief that cash is not as yet all dried up and that markets will make an effort to write a line under the outright trauma of 2008-2011.

However It's not over yet – there will be worries and setbacks for sure but I wanted to reflect on this unbelievable period when unless you were mad you would not have believed what has unfolded and indeed how monstrously robust the markets have been. Perma bears will step up to the plate and argue for the nastiness to come? We have all had a chance to rebuild our fortresses with and for clients without catastrophically poor returns that may have been anticipated.

The old adage is that "Bull Markets Climb Walls of Worry" – are you worried?

As a parting thought technically many indices are already in a "bull market" as a result of

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