The one factor that matters

"Five things they don't tell you about economics:

1. 95% of economics is common sense
2. Economics is not a science
3. Economics is politics
4. Never trust an economist
5. Economics is too important to be left to the experts"

– From *Economics: The User's Guide* by Ha-Joon Chang.

Quick quiz. Who said the following ?

"We are living, once again, in an era of strident nationalism and xenophobia. The hopes of a brave new world of progress, harmony and democracy, raised by the market opening of the 1980s and the collapse of Soviet communism between 1989 and 1991, have turned into ashes."

Answer: Martin Wolf, last week, in a typically miserabilist piece ('The long and painful journey to world disorder') for the *Financial Times*. Apparently the UK's vote to leave the EU has triggered global armageddon.

But somebody at the FT has a puckish sense of humour. No sooner had the FT's chief economics commentator had his say than Yuval Noah Harari, author of the excellent 'Sapiens' and 'Homo Deus', popped up in the very same pages to repudiate all of Martin Wolf's more ridiculous claims. The title of Harari's piece says it all:

'At last, liberals are waking from a long dream'.

Harari was the perfect antidote to Wolfish existential despair:

"The first step is to tone down the prophecies of doom, and swap panic for bewilderment. Panic is a form of hubris. It comes from the feeling that one knows exactly where the world is heading. Bewilderment is more humble and therefore more clear-sighted. If you feel tempted to declare that the apocalypse is upon us, try telling yourself instead: "The truth is, I just don't understand what's going on in the world."

It may not even be that difficult to understand. The liberal elites have simply lost the plot.

Speaking of liberal elites, Brexit hit the FT hard in 2016, as it should have done, since almost all of its columnists were backing Remain. Some of them clearly still do, as if the referendum never actually occurred. Martin Wolf is the very definition of what the philosopher John Gray was describing when he made the best analysis of the Brexit vote that anyone has yet penned:

"Predictably, there is speculation that Brexit will not happen. If Britain can vote for Brexit, it is being argued, surely anything is possible. But those who think the vote can be overturned or ignored are telling us more about their own state of mind than developments in the real world. Like bedraggled courtiers fleeing Versailles after the French Revolution, they are unable to process the reversal that has occurred. Locked in a psychology of despair, anger and denial, they cannot help believing there will be a restoration of an order they believed was unshakeable."

And then we had Trump. For any millennial snowflake who was just clinging on after Brexit, this was the last straw.

But the market response to both events was surprisingly sanguine. After an extremely quick admission of shock, stock markets rallied hard. UK stocks by and large benefited from the sudden devaluation of sterling, making it appear suspiciously as if Brexit had managed to achieve what eight years of increasingly desperate-looking QE had singularly failed to do. And US stocks took off into the wide blue yonder on the back of a euphoric anticipation of tax cuts, infrastructure spending and wholesale deregulation of the financial sector under the incoming Trump administration. It was left to the bond market to play the ghost at the feast.

For anyone with a ghoulish wish to roll back the clock and enjoy 2016 all over again, Dave Collum's year in review remains the definitive summary of what by any stretch was a genuinely historic 12 months. It contains this gem:

"If you pay well above the historical mean for assets, you will get returns well below the historical mean."

But what about the year to come ?

This commentator spent Christmas re-reading Edwin Lefèvre's classic 'Reminiscences of a Stock Operator', the thinly disguised biography of the infamous financial speculator Jesse Livermore. What leaps out from the pages of this outstanding encylopedia of trading advice is the primacy of just one factor when it comes to investment: ***price***. Everything else is secondary. This matters regardless of whether one is making a calculated long term investment or whether one is trading momentum over the short run. Benjamin Graham's definition of both strategies is as good as any:

"An investment operation is one which, upon thorough analysis, promises safety of principal and a satisfactory return. Operations not meeting these requirements are speculative."

The problem with QE and the litany of associated stimuli that have followed in its wake is that they have floated more or less all boats, such that most equity markets now have more than a whiff of overvaluation about them. In Benjamin Graham's words, they have lost any "margin of safety". QE, in other words, has made most supposed investments uncomfortably speculative.

Most, but not all.

Bonds still feel as if their 30+ year bull market ended last summer. If the long bull run really is dead, the key question is whether the monetary authorities can keep yields contained (the printing press is still on their side), or whether rising yields start to strip the gloss off stocks into the bargain. Alternatively, we could see a huge rotation from weakening debt markets into equities, extending the bull run in the latter. We think the pragmatic response as well as the path of least resistance is to avoid bonds and favour the pockets of genuine value still on offer from among the world's stock markets instead. (Japan and Vietnam still constitute our favourites.)

Much of the euro zone goes to the polls this year. Lacking a crystal ball as to the outcomes, from a holistic perspective we would complement our equity exposure with some outright portfolio insurance, by means of holdings in trend-following funds and gold. Martin Wolf might not approve, but Jesse Livermore probably would.

Tim Price is co-manager of the VT Price Value Portfolio and author of 'Investing through the Looking Glass: a rational guide to irrational financial markets'.

"There are.. historical gems and anecdotes galore. Read this book. Be entertained. Be educated. And then act on Tim's advice.."

- *John Butler, Head of Wealth Services for Goldmoney, Inc.*