Virginie Maisonneuve
Chief Investment Officer
Eastspring Investments

A member of Prudential plc (UK)

BACK TO THE FUTURE

To date, the liquidity environment created by regulators and Central Banks following the Global Financial Crisis has been very supportive of capital markets.

But while ample liquidity continues to provide a "tame" backdrop to the investment landscape, investors must watch for trends that indicate increased risk of "tail events" – infrequently occurring events that have a large negative impact on portfolio returns.

Such events should not deter investors from staying invested. But they should put event risk at the core of portfolio strategies mindset and construction.

"ECONOMICS VS POLITICS": ARE POLITICAL PARTIES OUTDATED?

The theme of "Economics vs Politics" is still running strong given the cycle of elections under way, but we believe markets have not adjusted yet to the realities of the new leadership styles in place.

Although elections in France took a "rational path", over recent months, we have seen citizens in the UK, the US, the Netherlands, Austria and Turkey vote for nationalistic agendas aimed at restoring jobs to the middle class, and reducing migrants and the size of government. Much of this support for a nationalist agenda is being exacerbated by growing income inequality, as measured by the Gini coefficient.

Are voters being driven to extremes in their electoral choices because of a structural disconnection between traditional political parties and the economic realities?

If so, the "unconventional" electoral campaigns we are seeing may have a meaningful impact. We need to understand whether we are looking at a structural, long-lasting rise in populism that could turn into a wider, global movement.

Alternatively, will the populist tide turn in the wake of the likely voter disappointment from the failed promises of their newly elected leaders? If global growth remains tame, will we see further extremes or will sentiment subside?

Interestingly, at the same time another trend is taking shape in the geopolitical arena: a "post post-cold war" world order is emerging, with further long-term ramifications.

THIS NEW "POST POST-COLD WAR" ENVIRONMENT IS REDEFINING GEOPOLITICS AND WORLD MARGINAL POWER

The post-cold war world order of globalisation and increasing trade and cultural interaction among nations is breaking up. This new post post-cold war era is being caused by dramatic shifts in several groups of countries:

1. Brazil, Turkey, Greece and Italy have become economically or politically disaffected by the consequences of crisis.

2. Russia, the Middle East and Scandinavia have been severely affected by the impact of technology disruption, especially related to the economics of the energy sector.

3. China has seen its marginal power increase dramatically as it has gained share of world growth in a declining growth world and a vacuum.

4. The US and UK are choosing to become more isolationist, which may impact their ability to function well in transition moments.

5. North Korea and some large-scale terrorist groups with claims to nationhood have arisen as "rogue" powers.

This mosaic of trends is shaping a new world map, creating a potentially more volatile, fragmented environment with little room for turning back from a structural standpoint.

This fragmentation will ultimately lead to rising tail risks. Yet so far the markets supported by liquidity, have mostly ignored this.

DECODING A SHIFTING MAP

We need to understand how these shifting themes impact world competitiveness and economic opportunities for companies. Some of the trends impacting the geo political re-design will continue to offer investment opportunities. They include:

- **The maturation process of China and India, the resulting impact on the global economy as well as demand and supply chain**

- **Technical innovation, especially in energy, artificial intelligence and health care**

- **Sources of disruptions, including digital warfare and the changing security landscape**

Finally, investors should keep an eye on the impact of major demographic changes. The "millennial switch" will shape demand as the new generation assumes control of the largest wealth transfer in the past 150 years, while healthcare and retirement living needs of the older generation escalate.

WHAT DOES IT MEAN FOR OUR INVESTMENT PORTFOLIOS?

Structure is key. In this transitive world, we recommend anchoring portfolios with active products, such as low volatility equities.

These should be complemented by well-established sources of alpha, through applying investment styles, asset classes as well as regional, sectorial and thematic considerations.

This will help investors to navigate the air pockets emanating from the rising risk of tail events in the "Back to the Future" landscape.

Disclaimer

This document is produced by Eastspring Investments (Singapore) Limited and issued in:

Singapore and Australia (for wholesale clients only) by Eastspring Investments (Singapore) Limited (UEN: 199407631H), which is incorporated in Singapore, is exempt from the requirement to hold an Australian financial services licence and is licensed and regulated by the Monetary Authority of Singapore under Singapore laws which differ from Australian laws.

Hong Kong by Eastspring Investments (Hong Kong) Limited and has not been reviewed by the Securities and Futures Commission of Hong Kong.

Indonesia by PT Eastspring Investments Indonesia, an investment manager that is licensed, registered and supervised by the Indonesia Financial Services Authority (OJK).

United States of America (for institutional clients only) by Eastspring Investments (Singapore) Limited (UEN: 199407631H), which is incorporated in Singapore and is registered with the U.S Securities and Exchange Commission as a registered investment adviser.

European Economic Area (for professional clients only) and Switzerland (for qualified investors only) by Eastspring Investments (Luxembourg) S.A., 26, Boulevard Royal, 2449 Luxembourg, Grand-Duchy of Luxembourg, registered with the Registre de Commerce et des Sociétés (Luxembourg), Register No B 173737.

United Kingdom (for professional clients only) by Eastspring Investments (Luxembourg) S.A. - UK Branch, 125 Old Broad Street, London EC2N 1AR.

Chile (for institutional clients only) by Eastspring Investments (Singapore) Limited (UEN: 199407631H), which is incorporated in Singapore and is licensed and regulated by the Monetary Authority of Singapore under Singapore laws which differ from Chilean laws.

The afore-mentioned entities are hereinafter collectively referred to as **Eastspring Investments**.

This document is solely for information purposes and does not have any regard to the specific investment objective, financial situation and/or particular needs of any specific persons who may receive this document. This document is not intended as an offer, a solicitation of offer or a recommendation, to deal in shares of securities or any financial instruments. It may not be published, circulated, reproduced or distributed without the prior written consent of Eastspring Investments.

Investment involves risk. Past performance and the predictions, projections, or forecasts on the economy, securities markets or the economic trends of the markets are not necessarily indicative of the future or likely performance of Eastspring Investments or any of the funds managed by Eastspring Investments.

Information herein is believed to be reliable at time of publication. Where lawfully permitted, Eastspring Investments does not warrant its completeness or accuracy and is not responsible for error of facts or opinion nor shall be liable for damages arising out of any person's reliance upon this information. Any opinion or estimate contained in this document may subject to change without notice.

Eastspring Investments (excluding JV companies) companies are ultimately wholly-owned/indirect subsidiaries/associate of Prudential plc of the United Kingdom. Eastspring Investments companies (including JV's) and Prudential plc are not affiliated in any manner with Prudential Financial, Inc., a company whose principal place of business is in the United States of America.

eastspring investments

A member of Prudential plc (UK)