

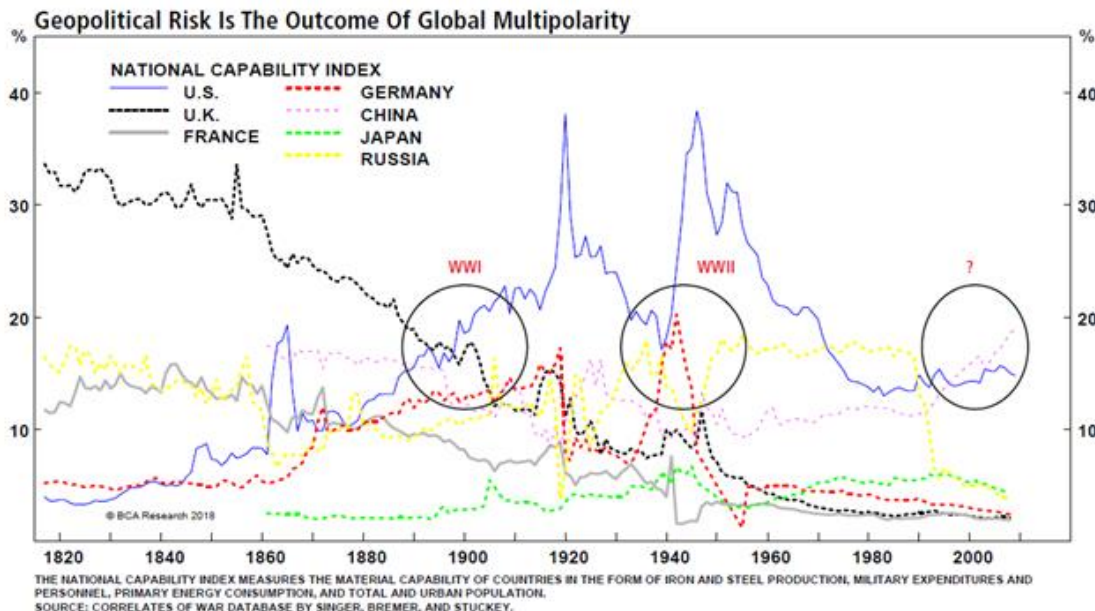
SKERRITT'S VIEW - DECEMBER 2018

If You Believe In Climate Change...:

There seems to be fairly strong consensus that the world is experiencing a phase of climate change. Its causes and consequences are more vociferously challenged depending on personal beliefs, but generally speaking, change is acknowledged and there is an acceptance that things will not be the same as they have been in the coming years.

We would argue that there is another climate change occurring, and that its consequences will have a material impact on what we've perceived as our normal over the past three or four decades or so. This change is occurring in the climate of the geopolitical world order.

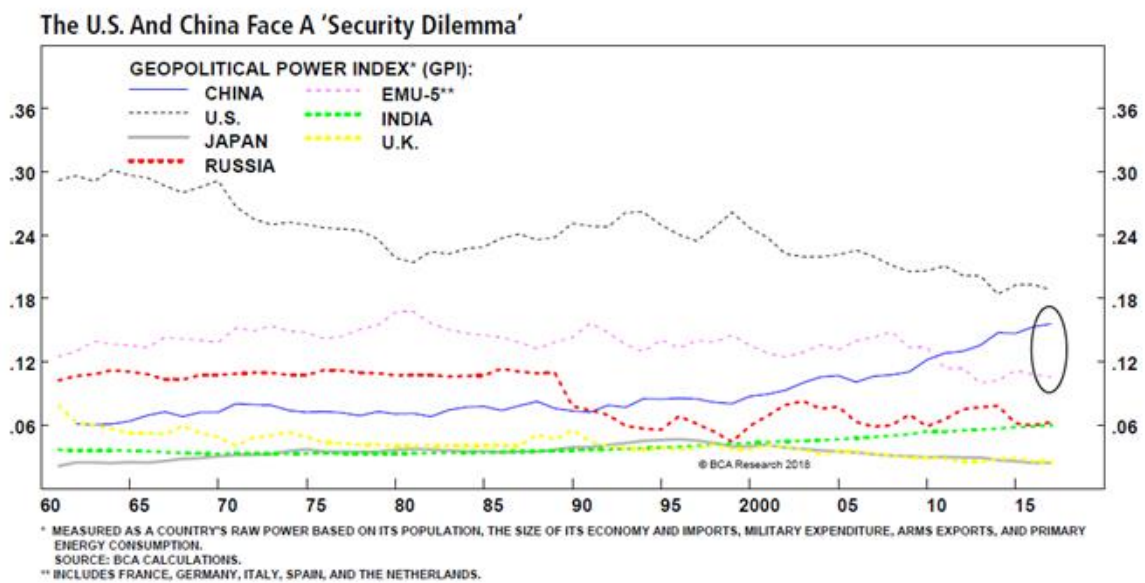
Most people that we talk to are familiar with the idea that all is not well with the world. Their concerns centre mainly around Brexit (although if one travels outside Europe this is viewed more as a curiosity rather than a major issue) and Trump. There is also a vague realisation that one of the issues involving Trump has to do with a trade war with China, but most UK observers focus more on other aspects surrounding the US President. Virtually no one that we speak to is aware of the more fundamental changes that are going on, and which are leading to so many of the headlines that we see daily.



The world is coming out of a time of stability, even though it didn't always feel stable at the time. The US was the global hegemon and stood alone as the world's police force in a way. In recent years though, we've seen the rise of China, the withdrawal from the Middle East of the United States and the re-emergence of Russian nationalism, as well as a migrant crisis across Europe which has cost the

German Chancellor her job and seen Eurosceptic political parties gaining traction across the Continent. We are in an era of multipolarity.

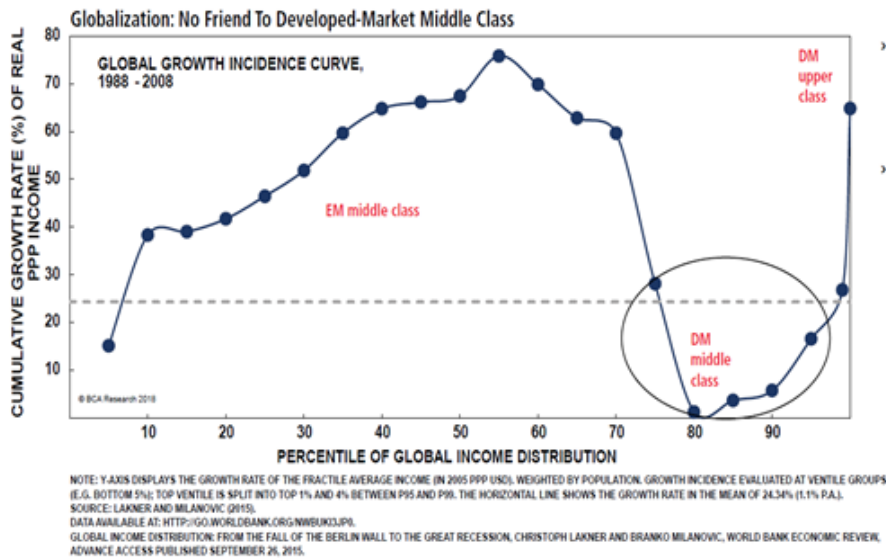
It is a situation that is illustrated clearly in the chart above. It is also quite clear to see that such periods lead to the kind of instability that we are witnessing at present. We can also see from the chart below that the Geopolitical Power Index is shifting, measured as it is on a country's population, the size of its economy and imports, military expenditure, arms exports and primary energy consumption.



Much of the cause behind the situation today is globalisation, that word that has been synonymous with the 20 years leading up to the 2008 Great Recession. We think that we are witnessing the end of globalisation, as populism has reared its head in the US, in the shape of an "America First" President who is pursuing a protectionist policy (which, by the way saw the Democrats gain seats in the recent Mid Term elections, scotching any thoughts that the American electorate are any lovers of free trade) as well as, of course, in the UK in the shape of Brexit. Italy is the most recent example of the electorate declaring that they've had enough of the status quo. The chart below illustrates the point being made here quite succinctly.

It is likely that, whatever platitudes may have emerged from the G20 Summit in Argentina, the trade war between China and the US is not going away – although it may die down a bit for a while. Why?

No American President has been re-elected since 1860 when there has been an election in the same year as a recession. The next election in the States is 2020. Will President Trump risk a full blown trade war through 2019 which could lead to a possible recession? We doubt it. Will he be more likely to ease back, but then up the ante again going into 2020 to demonstrate his toughness and adherence to the America First principle prior to the election, with the likely consequent recession appearing *after* the election has taken place? Well, we think it's worthy of consideration. So what are the investment implications?



- > Globalization was very good for emerging and frontier markets, where the cumulative growth rate of real incomes skyrocketed.
- > But developed markets experienced little income growth during the same period of intense globalization (1988-2008), excepting among the educated "elite."

Investment Implications:

What appears to be quite a bleak outlook could actually be positive, or at least we believe that our strategy has the best chance of being so. We repeat over and over again that we prefer to invest in themes that have a multi-year probability of recurring. Importantly, in a world that looks as though it's going to be more divided, these themes are global and are in the best interest of all parties. So, cyber security, robotics, AI, digitalisation, healthcare innovation....all of these form a core of our equity exposure and, while they can take short term hits in value, their longer term sustainability appears to us to be obvious.

But in a world that is increasingly uncertain, flexibility of investment ideas is crucial, and we will pursue tactical positions as and when opportunities arise outside our core themes.

And as any follower of sport understands, success is built upon a sound defence, and so our defensive tactics will be as important in achieving longer term returns above the average as our more positive strategies will be.

If the political climate is changing along with the natural climate, we need to adapt. We think that by thinking about the problems that lie ahead, and meeting them head on, we have more chance of navigating the choppy waters that lay ahead.

These are our views and are for professional use only