RATHBONES | Incorporating Investec Wealth & Investment (UK)

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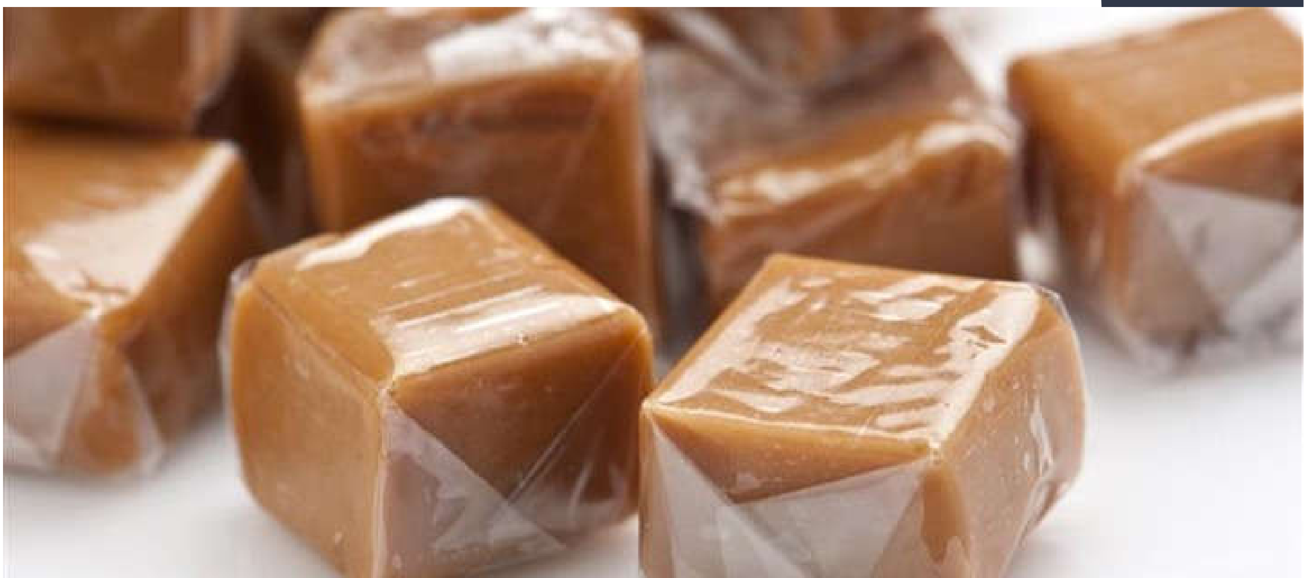
# If You Know Your History



John Wyn-Evans
Head of Investment Strategy

I have to admit that History was not a strong point for me at school. It might have had something to do with the fact that I was never taught about anything that occurred after the early eighteenth century, and most of it was confined to events that happened within our shores (apart from the odd, glorious victories in battle on the Continent – I can still remember the Duke of Marlborough's "phone number": BROM 4689!). It was difficult for me to find any relevance to current events. However, these days I often find myself looking at past events, especially those in financial markets, and trying to work out how they might be used to inform the present.

A phrase attributed to the philosopher George Santayana is that "Those who cannot remember the past are condemned to repeat it". Reuters used to do an annual survey of financial market participants and one of the questions posed to respondents was "How long have you been working in financial markets?" When the answers were totted up, it regularly turned out that around half of the current industry had been involved for less than a decade, a finding that always surprised me given that I worked with quite a few old lags (amongst whom I must now count myself).

Even if the reality is somewhat longer than that, though, it does suggest that there is some sort of limit to what we could describe as "market memory". Let's say it's more like fifteen years. In that case, the majority of people involved in making financial decisions today have no professional memory of the Global Financial Crisis (2008); even fewer of the Technology Boom and Bust (1998-2002); and the numbers shrink further as we regress through events such as the failure of the hedge fund LTCM (1998), "Black Wednesday" in the UK (when we left the European Exchange Rate Mechanism in 1992) and "Black Monday" when stock markets crashed in 1987. Neither lines on charts nor the best writing can properly evoke the reality of living through such periods.

All that might suggest that one should let one's money be looked after by the oldest manager they can find. But of course, that doesn't work either. A manager schooled in a time of financial crisis might waste the rest of his career trying to avoid the next one that never comes. Plenty of those who struggled to survive the inflation of the 1970s and 1980s just could not see the disinflationary shift that followed. A certain type of value investor has continued to lag a growth investor for years now as new technology platforms have been in the ascendant and as current business models require less capital.

Indeed, another phrase, this one generally attributed to Mark Twain, is probably more apposite: "History does not repeat, but often rhymes". What pointers can we take from the past today? Let's start with the most positive one, which is that equities markets tend to rise. That's easy to forget during periods of market disruption or recessions. Yes, individual companies go bust and whole country markets have come close to disappearing entirely in the past. One example is the Vienna Stock Market in the 1870s. Interestingly, experience and the study of the boom and bust which characterised that period became the basis of what is known as "Austrian Economics" as popularised by Ludwig von Mises and, more recently, Friedrich Hayek. It might not surprise you to know that adherents of that school of thought have been forecasting nasty things for financial markets for what feels like most of my career. Sometimes they have been right, but most equity markets are still trading at around all-time highs.

Having said that, it's clear that the raw material for market setbacks is often detectable well before the penny drops. It can take time to turn a supertanker around, during which period it actually goes even further in the direction it was originally travelling. Investment careers have been destroyed by reaching the right conclusion... but too early. Some of those who push financial assets to excess are willful participants, riding the wave as far as they dare; some are "locked in" by reference to their investment mandates and benchmarks; and some just never see it coming.

There is usually some sort of "tipping point". A couple of weeks ago, we had the DeepSeek-induced panic. That company's latest Large Language Model had been released a month earlier and I have subsequently seen various blog posts warning of disruptive potential that were written months earlier than that. It seems that the warning signs were there.

Five years ago, we were still grappling with the potential risk of the Covid virus. It's sobering to look back through my diary for the period between the declaration of an international global health emergency by the World Health Organisation (30th January 2020) and when I finally took to my sickbed with a temperature of 102o (13th March). I undertook a full marketing tour of the UK and Channel Islands; attended three investment conferences; two major sporting events; two trips to the theatre; three concerts; had one weekend away; went out for dinner five times and played two football matches. It looks as though I even managed to sneak in a final round of golf after my (thankfully speedy) recovery but before the first lockdown! I guess my behaviour fell somewhere between "willful" and "ignorant", given that I was getting plenty of information about the virus risk but had never actually experienced anything like it.

Anyone who has read The Big Short or seen the film will know that some clever folk saw the financial crisis coming a mile off. But in that case and in those above, it was impossible to predict the moment at which markets would tip. As Chuck Prince, the CEO of Citigroup, famously said not long before the financial crisis erupted: "When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing."

Some other long-term charts I am observing closely at the moment concern bond markets. I have written in previous commentaries about the rising "term premium", or the higher yield demanded by investors to compensate for the uncertainty of holding longer-dated bonds. The term premium last peaked in the early 1980s and then spent forty years falling, finally bottoming out in negative territory (meaning that you earned less for taking on more duration risk). Those four decades were a golden era for investors given the very attractive starting valuations and the subsequent collapse in the discount rate. I struggle to see how it can be replicated, especially if, as we believe, inflation is set to remain higher and more volatile than we have been used to. This means that those saving for the future will, sadly, have to save harder. An alternative course, which is no doubt being adopted by some, is to take massive investment risk in highly speculative instruments and to utilise leverage. That's not a strategy we could recommend, given that it risks the total loss of capital.

But "history" can also give us opportunities. As I have observed in the past, much of the trading in financial markets today is done by computers reliant on algorithms that are informed by historical price movements. Clever as they are, it's not clear to me that they always "understand" the present context in which they are operating. This can lead to overreactions, both positive and negative, of which we might be able to take advantage.

The key thing is that we should never stop learning about the factors that drive markets in the short term because they evolve continually. But in the long run, a bias towards high quality investments is something that we believe has proved to be a winning formula.

As for today's title, when it comes to football clubs, they should perhaps come with a disclaimer that "Past performance is no guarantee of future success". But there are some pursuits in life where you have to leave cold logic at home, hope for the best and ride the emotions. I have rarely been happier in my life than I was at around 9.28pm last Wednesday. If you know your history, it's enough to make your heart go – woh, oh, oh, oh!

# Economic Commentary

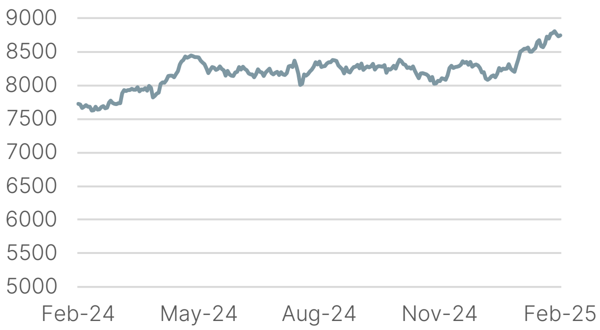
## FTSE 100 weekly winners

| | |
|---|---|
| Flutter Entertainment Plc | 9.8% |
| Prudential plc | 9.5% |
| BP p.l.c. | 8.0% |
| Rentokil Initial plc | 7.7% |
| Pershing Square Holdings, Ltd. Public Class USD Accum.Shs | 5.9% |
| Croda International Plc | 5.6% |
| Intertek Group plc | 5.5% |

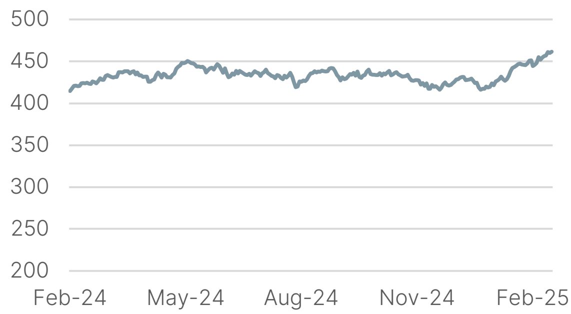
## FTSE 100 weekly losers

| | |
|---|---|
| British American Tobacco p.l.c. | -7.7% |
| International Consolidated Airlines Group SA | -7.6% |
| Unilever PLC | -6.4% |
| Ocado Group PLC | -3.8% |
| Whitbread PLC | -3.8% |
| NatWest Group Plc | -3.6% |
| Vodafone Group Plc | -3.5% |

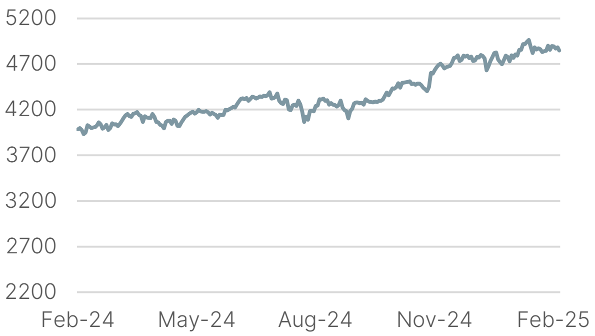
FTSE 100 index, past 12 months




EuroStoxx 600 index, past 12 months




S&P 500 index, past 12 months




All data shown in GBP.



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