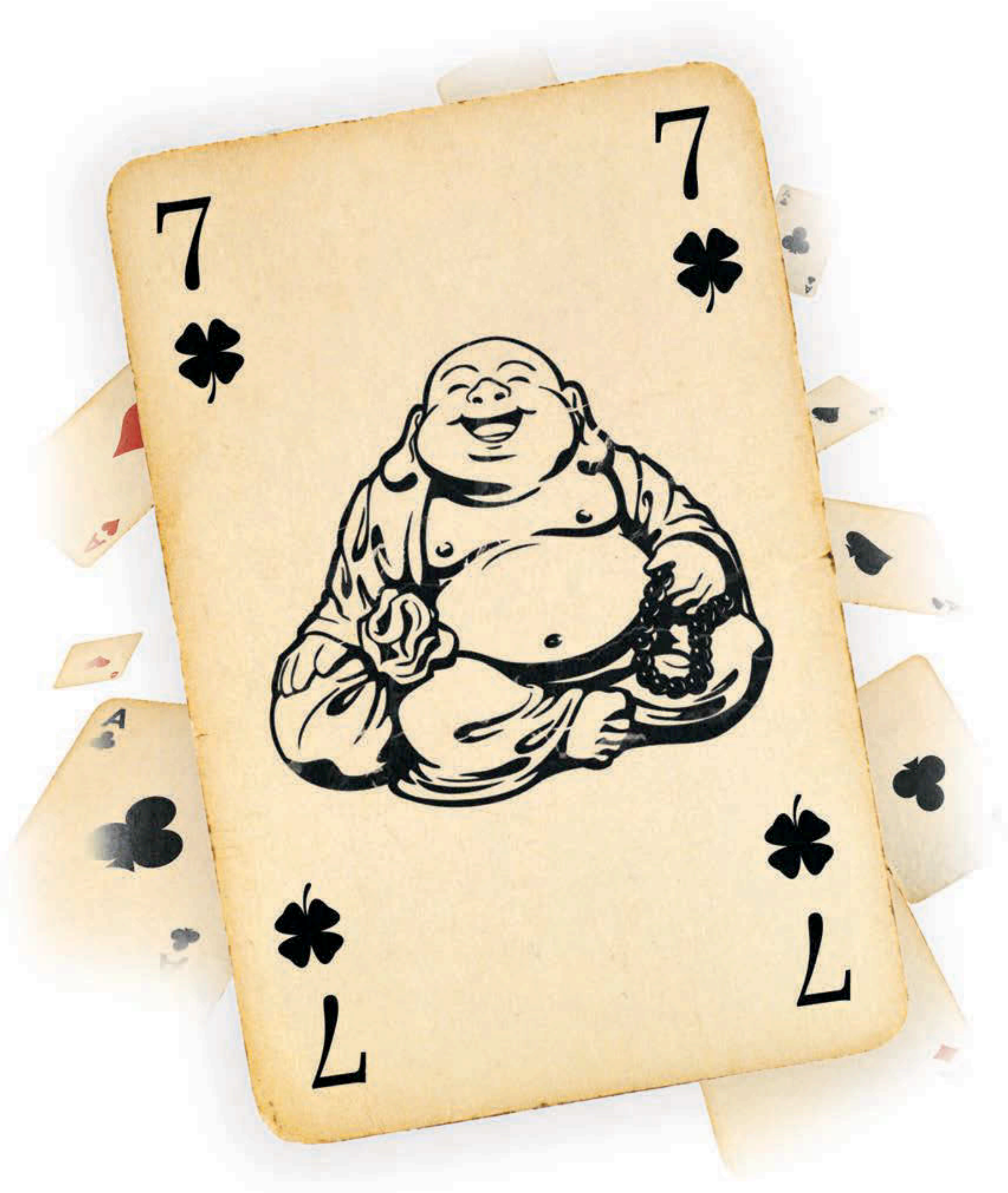

Feeling Lucky?

You don't have to be superstitious to be worried about what 2013 will bring. **Rebecca Jones** asks a panel of experts for their outlook and recommendations for the 12 months ahead

It may not feel like it, but most stock markets haven't done at all badly over the past 12 months. The FTSE 100, the S&P 500 and the MSCI World have all returned between 9 and 10 per cent in sterling since 1 January 2012.

Emerging markets are just slightly behind, at 8.8 per cent. The main laggard is Japan, which has seen a relative upturn over the past month (see page 32).

But despite all this, investors are still jittery, living in fear of bogeymen like the Eurozone crisis, war in the Middle East, the slowdown in China and the US 'fiscal cliff' (a mixture of tax rises and spending cuts).

The bulls have enough strength to prevent markets crashing, but the bears hold them back from reaching new heights with their persistently doom-laden forecasts.

In this uncertain environment, it's tough for investors to know where to turn, so we've turned to six experts with very different predictions for how things are going to turn out. And after hearing from them, we've tried to make sense of it all and answer that all-important question: where do I put my money in 2013? ◆

'The main obsessions of 2012 are going to persist – US government finances, Chinese growth and the European sovereign debt crisis'

Andrew Goldberg, executive director and global market strategist, JP Morgan

We'll see more of the same in 2013. That means more uncertainty and low volume (not a lot of people trading). Investors don't have a ton of conviction, with many just sitting on the sidelines. The main obsessions of 2012 are going to persist – US government finances, Chinese growth and the European sovereign debt crisis.

Winners

Markets dramatically overreacted to China slowing, and when people find out that growth is going to stabilise and maybe even tick back up, they will look back to now undervalued emerging market equities. Also, if income is your problem, the answer is multi-asset class. It doesn't matter whether you're a billionaire or you've scraped together savings your whole life, you need income from a variety of assets such as equities and bonds.

Losers

A major wildcard for 2013 is oil. If the conflict between Israel and Iran spreads, Iran may threaten to close the Strait of Hormuz, which is how the world gets most of its oil from Saudi Arabia. That will create a major spike in oil prices: a shock that recovering markets are very susceptible to. Also, cash is trash. Most central banks are trying to create inflation, which is going to eat away at the value of cash. It's a guaranteed way to lose money. The gold party is set to end too.

Buy

As the global economy is going to accelerate in 2013, cyclical stocks like technology will do well. Companies have massively underspent on things like new equipment, which means they have almost no choice but to spend to keep up with clients' needs. Also, financial stocks around the world have been beaten up too hard. As the global economy finds a more solid footing you'll see more lending, and with that more profit for banks.

Jonathan Davis, economist and wealth manager

My outlook for 2013 is very bearish. Firstly, the stock market is between 80 and 110 per cent up on the lows of 2009, and in an investment cycle that's already toppy. Second, by my definition 80 per cent of the planet is in recession, including China, whatever the politburo tells us, and global trade is turning negative year-on-year for the first time since 2008.

Winners

I am short-term bullish on the US dollar and US treasuries because there is quite a high inverse correlation between these and stocks. The US dollar is the reserve currency, and when global trade is going up the US dollar tends to go down and vice versa – *ipso facto*.

Losers

All risk assets such as bank and mining stocks have peaked in the past year, so those parts of portfolios that are 'risk on' are rapidly moving to 'risk off.' Oil will also fare badly due to the rise of the US dollar and the fall in global trade. I expect oil prices to take out the 2012 low of $70 a barrel, which will reflect in big oil share prices. Most currencies will also perform very badly against the US dollar, particularly the Australian dollar due to a fall in exports to China and cuts to interest rates that the reserve bank has already embarked upon.

Buy

During 2013, people should be looking to preserve their wealth rather than grow it, so they should be reducing risk exposure markedly. I would recommend the TLT ETF, which is buying into 20-year US treasury bills. A holding in an ETF that shorts the stock market would also be good. The Deutsche Bank db x-trackers ETF that shorts the S&P 500 gives extra benefit to sterling investors, who would also gain from a weakening sterling against a strengthening dollar.

> 'A major conflict in the Middle East would have a negative impact on oil prices, the global community and the global economy generally'

James de Sausmarez, director and head of investment trusts, Henderson

For 2013, it's a case of 'steady as you go.' I think investor enthusiasm for income will continue, but for long-term investors there's more value in growth-style stocks. Currently, we're in the sort of market where the strength of individual companies is going to come through rather than particular regions or sectors. It's never been a better time to be a bottom-up stockpicker.

Winners

The best-performing market in the year to date is Germany, which shows that Europe is ticking along despite all this uncertainty. I think the bad news is priced in: there's been no progress in Europe all year, and if there's no progress next year then it's par for the course. There are some very good companies in Europe, and those companies are operating internationally. Generally, companies are in much better shape than countries.

Losers

Everyone's talking about the US fiscal cliff and the lack of a solution in Europe, but I think the big risk in 2013 is a serious escalation in Middle East tensions. A major outbreak of hostilities in the Middle East would have a negative impact on oil prices, the global community and the global economy generally. This seems to me to be the area of high risk that's not yet priced into the market.

Buy

Equities really are the place to be. For a long-term, slightly more adventurous investor, something with a small-cap nature could do quite well. Small companies are in a good position to grow: they're undervalued and I think we'll see some recognition of that next year, especially in Europe. However, if you're a slightly more cautious investor, go for the mainstream City of London investment trusts, which have never let anyone down.

Colin Chapman, lecturer in finance at Birmingham City University

Investment returns in 2013 are likely to be pretty flat. I think private investors still haven't regained their appetite for risk, and are looking for a major upturn before they re-enter the markets. They'll be waiting for institutional investors such as pension funds to move out of bonds and into equities.

Winners

In my view, there is going to be a continued demand for income-producing, high-dividend-paying stocks. Areas such as Central and South America are also attractive as consumer spending is set to increase due to higher wages. I'd look particularly at consumer staples such as food and drink manufacturers, possibly Ambev in Brazil and Semsa in Mexico. Also, the time has probably come back for UK and US banks. As they have started to recover, their debt is trading at a higher level. Both financial preference shares and bonds offer attractive returns, which may tempt back investors who think we're out of the worst.

Losers

Anything to do with Europe. Even if the EU comes to some sort of agreement about Spanish and Greek debt, problems are going to keep occurring as the austerity measures required won't be accepted by the man on the street. The sovereign debt bubble is also set to burst as people move into equities, and the government bonds that have been bought by central banks will have to be sold again at some point.

Buy

Income-producing shares from big players such as GlaxoSmithKline and National Grid, which may be acceptable replacements for low-yielding bonds. I would also look at telecoms companies like BT, TalkTalk and Vodafone, especially as the latter pays such high dividends. For a more left-field option, look at successful smaller companies such as brewer and pub chain Greene King, which is starting to add premium options alongside its cheaper outlets.

'Emerging market equities are the best asset class because of the decent growth backdrop'

Tim Drayson, senior economist, Legal & General Investment Management

We don't think global growth will exceed 2.5 per cent in 2013, which is below the 3 per cent consensus. The main reason is the US, where we anticipate expansion of just 1 per cent due to the 2 per cent fiscal tightening we expect to see. Europe is also an area of concern for us. This is due mainly to Spain and Italy, both of which we believe will go into recession in 2013. However, we're optimistic on emerging markets, which we think will grow in line with consensus due to domestic demand and inter-regional trade.

Winners

Emerging market equities are the best asset class because of the decent growth backdrop. China we think will have a soft landing because it has loosened monetary and fiscal policy, while Brazil has cut interest rates quite aggressively, which is supporting growth. We're also reasonably positive on commodities. Even though growth is slow and there's more supply coming on stream, commodities will still be supported by the exceptionally loose monetary policies being conducted in the West.

Losers

For developed market equities it's going to be quite volatile. We think US equities are going to struggle next year because of the weak growth environment, and it will still be quite choppy in Europe, though equities will finish the year higher. The most risky investment going into 2013 is core government bond markets, where there is a bigger danger that you'll lose money than in equities.

Buy

Gold. Central banks are going to be very slow to stop money-printing, and then when they do stop it, they'll be slow to raise interest rates, so with negative interest rates gold prices should continue to do well. Property, particularly US residential, also looks attractive on a multi-year basis as the housing market is bottoming.

Andy Gadd, financial adviser, MHA Macintyre Hudson

I think the FTSE 100 will break through the 6,000 mark in 2013. Although growth in the UK will be low, the markets will be looking ahead at better prospects for 2014 and beyond. You'll continue to have a tale of two halves in Europe in which northern countries like Germany and France will do relatively well while southern countries will continue to suffer, but it won't collapse. The growth rate in China also has to fall as workers' wages rise.

Winners

I like equities, especially those that produce a good dividend yield. In the UK, it's the first time since the 1950s that the yield on stocks is higher than the bond market, so the UK looks good value. I would also look at property selectively. While I don't think you're going to get massive capital growth, the yield, typically 5 per cent, has attractions in a low-growth, low-inflation environment.

Losers

I would avoid fixed interest, particularly sovereign debt. Government policy, both in the UK and US, seems to be quantitative easing, the definite result of which is going to be inflation. Sadly, trying to manage an economy is like trying to drive a car while looking out of the back window and with only an accelerator and a brick; as soon as inflation starts to rise, it's too late to put the brakes on.

Buy

I like the Thames River Distribution fund as I like companies that produce cash. It means that you've got support against 'unknown unknowns' like a major earthquake in California or a spike in oil prices because war breaks out in the Middle East. For the higher-risk end of the market I'd go for M&G Recovery, while for a defensive play I'd go for Artemis Strategic Assets, which is an absolute return fund managed by William Littlewood.

What Investment's view

We boil down the experts' views and try to find a consensus

So, are we any closer to answering that fundamental question of where to put your money? Well, our experts' opinions are divided along surprisingly sharp lines. While some claim European equities are undervalued, others wouldn't touch them with a very long barge pole. For one, the US will be the main culprit behind a drop in global growth, for another, the prime place to invest.

This is reflected by the fact that no single asset scored above 39 out of 60 in our unscientific straw poll (see table below). However, there are some general trends.

First, almost all the equity classes did better than bonds, property, gold and cash, with the exception of Japan equities (see page 32). The consensus is clear – the time has come to take on risk and return to the stock market. Only one expert preferred bonds to shares: Jonathan Davis, who correctly predicted the property crash of 2007. His bearish outlook is a reminder that there are still strong headwinds facing global corporations; the stock market investor should take a multi-year view. James de Sausmarez reckons that 'the strength of individual companies', not whole markets, will be a theme of 2013, giving the best active managers an excellent hunting ground.

Apart from Japan, there is no great variation in how different global markets are viewed. UK equities top the table, but only one point ahead of US shares, with emerging markets and UK small-caps close behind. There is slightly less enthusiasm for Europe.

> 'The consensus is clear – the time has come to take on risk and return to the stock market'

But the best argument for equities may be a negative one: the almost non-existent returns being offered on bonds and cash. All of our experts believe the bond bubble is set to burst to some extent, while persistent inflation and falling interest rates are making cash a viable alternative to fire lighters this winter. Andy Gadd makes the interesting point that yields on bonds have now fallen below those on equities for the first time in decades. For the first half of the 20th century, this was regarded as the natural order of things: equities paid out more to compensate investors for the additional risk. A return to the status quo could mean investors needing income would be advised not to ignore the stock market.

The big theme of the past couple of years has been a flight away from perceived 'risky' assets and towards 'safe' ones – so from equities into bonds, emerging markets into developed, growth companies into blue-chips, everything into cash. Sooner or later, the tide will turn. No-one can guarantee that will happen in 2013, but for those with a medium- to long-term investment horizon, it could be time to be greedy while others remain fearful. ◆

Where should I invest in 2013?

	Andrew Goldberg	Jonathan Davis	James de Sausmarez	Colin Chapman	Tim Drayson	Andy Gadd	Total optimism rating
UK equities	5	2	8	8	7	9	39
US equities	5	3	8	9	6	7	38
Global emerging markets	7	1	8	8	8	5	37
UK small-caps	6	1	8	8	6	7	36
Euro ex UK equities	8	2	8	4	6	4	32
Corporate bonds	6	4	7	5	3	7	32
UK property	6	2	5	5	5	5	28
Japan equities	4	0	7	6	6	4	27
Gold	1	4	4	4	8	5	26
Cash	1	8	2	2	4	2	19
Government bonds (UK/US)	1	7	3	3	2	1	17

What the table shows: We asked our experts to rank the prospects for each asset class in 2013 on a scale of 0 to 10. The final column represents the total out of a possible 60