

# Investing in binary times

Nervousness pervades the markets. China's restructuring and the central banks' policy dilemmas are unprecedented. But the reality is better than it appears to be.

Investors should think twice about taking an autumn break. After the rather busy months of August and September, the traditionally turbulent October is unlikely to allow investors to catch their breath. Why are markets so unsettled? Let me try to explain.

This bull market has lasted for six and a half years. Some have sought and found parallels, in terms of technical chart analysis and valuations, with the years of 2000 and 2007, when stock exchanges were also at turning points. This naturally raises the question of comparability. Does history repeat itself, or does it only rhyme?

Maybe what makes those three periods comparable is that investors each time had to face unprecedented, thus incomparable situations: In 2000 investors, who had been happy to pay triple-digit price-to-earnings ratios for internet companies, saw these valuations collapse as concerns mounted over the real economic merits of this new technology. And at the end of 2007, investors were faced with the question whether the most recent driver of growth, credit-based consumption, could ever take up that role again. Today, the big question is whether the Chinese authorities and central banks will cope with two major new challenges. On the one hand, there is a nation of over one billion people which, in current U.S.-dollar terms, has more than quadrupled its share in the global economy within the last 15 years; but which has also rapidly built up debt and now seeks to radically change its business model. On the other hand, there are the central banks which have more than tripled their balance sheets since the financial crisis and now have to work out how to run them down again. Will both China and the world's central banks manage to meet their very different objectives? Nobody can tell. Investors are faced with the dilemma of not wanting to miss any buying opportunity – and every setback since 2009

has, in a sense, been one – but not wanting to be invested either should the subsequent market fall really happen.

Just recently, the Fed dodged the start of its very own turnaround once again. Although its decision may have been well reasoned, the Fed might end up as the driven, not the driver. Also, how readily can we really wean ourselves off the easy money drug? The Fed postponement has at least served to create such negative

market sentiment that higher interest rates might even, for once, be welcomed. Wouldn't they?

Investors are currently divided on many things: Will developed economies drive emerging markets or will the latter impede

// Although some clouds may linger, the situation remains good. //

the first? Will Western consumers buy enough to compensate for globally slack levels of investment? Will consumer gains from cheaper oil compensate for the energy producers' woes? And, finally: is the actual situation better than it appears to be? These questions were on the agenda of our recent quarterly strategy meeting. In our view, the global economic recovery is intact, despite a more muted outlook for some markets. This is likely to open up a number of opportunities, just in time for the traditional year-end rally. If, of course, history chooses to repeat itself, at least in this respect.



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