# The thin line between investment and speculation

Weekly Digest

30 April 2018

– *Lorenzo La Posta*

The financial industry's history is ancient and strongly linked with the development of human society. It first started as barters and grain-money more than 10 thousand years ago; it evolved through the introduction of rudimental record-keeping systems and the issuance of the first seed-grain loans about four thousand years ago; and it reached a more modern structure when the Greeks and the Romans laid the foundations of today's banking system that finally matured during the Italian Renaissance.

Today's financial industry is very far from where it started, as society's needs have grown and diversified. Thanks to globalisation, industrialisation and developments in technology, nowadays it is a system accessible from virtually every corner of the globe. Who is that system composed of? The types, locations and dimensions of market participants are countless. Here I will focus on two kinds: investors and speculators.

To highlight the differences (for the sake of simplicity, we will focus on the stock market only), it is better to start with the common aspects. Both groups participate in the financial markets by buying and selling securities, providing and consuming liquidity and they ultimately hope to increase their wealth through these transactions. Apart from that, though, the two categories approach the financial markets from very different perspectives.

An investor conducts research on a specific company and evaluates a set of characteristics in its business, such as its future risk, profitability, growth, sustainability and many others. They will invest in this company's stock in exchange for a share of the company's future cash flows taking into consideration the associated risks. In addition, they will allocate their capital efficiently across many different companies and will effectively participate in their growth over time. They will ultimately increase wealth as the whole economy grows through a series of claims on these companies' earnings and assets. The time horizon of an investor is often long, mainly because a company requires time for its capital to work and create value.

A speculator buys a stock with the sole objective of selling it at a higher price. They seek to profit from short-term market fluctuations by betting on the direction a certain stock price will move. In the short-term, businesses (hence, financial markets) have no time to create value and increase overall wealth, thus the only harvestable profit is found in moments of irrationality and inefficiency. Such a speculative approach is not far from gambling: a profitable trade is the one where one speculator correctly guesses how others will react to the same short-term dynamics.

Despite these evidently different approaches, drawing a neat line between these two categories is not an easy task; rather, a blurred border between the two is a more realistic description of the reality. All market participants are positioned on a continuous spectrum, being either a pure investor or a pure speculator; furthermore, the same entity might even shift behaviour through time as different opportunities and needs arise. Here at Momentum we aim to create long term wealth for all our clients, by continuously and thoroughly analysing all our investment decisions and never falling into the trap of speculation or short-termism.

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## The **Marketplace**

- UK Q1 GDP growth disappoints
- Kim Jong-un steps foot in South Korea
- UK Home Secretary Amber Rudd resigns
- 10 year US Treasuries hit milestone 3% yield

## Market **Focus**

### US

- Q1 2018 GDP growth beat expectations at 2.3% annualised versus a consensus of 2.0%. Despite this, the reading is the lowest in a year and down from 2.9% growth in Q4 2017.
- With S&P 500 earnings season underway, of the 268 companies that have so far reported, 78% beat estimates on earnings per share, the highest level since 2010. A further 147 companies are due to report this week.
- US equities flat-lined during the week, while Treasuries rose 0.1%. 10 year Treasury yields hit 3.0% on Tuesday for the first time since 2014, although failed to maintain this level, ending the week at 2.96%.

### UK

- UK GDP growth missed expectations in the first quarter of 2018, at 0.1% versus a market expectation of 0.3%. This marks the slowest growth rate since Q4 2012.
- On a trade weighted basis Sterling fell 2.2% on Friday following the weak GDP growth reading while 10 year gilt yields fell 59 basis points as investors readjusted their rate hike expectations.
- The budget deficit beat expectations, falling to GBP 42.6 billion in the 12 months to March versus estimates of GBP 45.2 billion and down from GBP 46.2 billion in the previous year.
- In politics, Home Secretary Amber Rudd resigned amidst scrutiny surrounding current and previous handling of the 'Windrush generation' migrant scandal.
- UK equities ended the week up 1.9% in Sterling terms, boosted in part by the 1.9% fall in Sterling versus the US Dollar. UK Gilts rose 0.5% over the week.

### Europe

- The Eurozone composite PMI reading for April stood at 55.2, unchanged from March and remaining at a 14 month low. Despite this, the reading marginally beat expectations of 54.9.
- The European Central Bank kept its monetary policy unchanged and provided no information about plans for the future of its quantitative easing program.
- Continental European equities advanced 0.7% in Euro terms during the week.

### Asia

- In a historic moment, Kim Jong-un became the first North Korean leader to step foot in South Korea since the Korean War, as he met with South Korea's President Moon Jae-in. The leaders pledged to work on a common goal of denuclearisation across the peninsula and announced the Korean War would end this year.
- The Bank of Japan voted 8-1 to keep monetary policy unchanged. In a surprise move, the policy setting committee removed its timeline for achieving 2% inflation.

***Past performance is not indicative of future returns.***

*Source: Bloomberg. Returns in local currency unless otherwise stated.*

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| Asset Class/Region | Currency | Currency returns | | | |
|---|---|---|---|---|---|
| | | Week ending 27 April 2018 | Month to date | YTD 2018 | 12 months |
| **Developed Market Equities** | | | | | |
| United States | USD | 0.0% | 1.2% | 0.3% | 13.3% |
| United Kingdom | GBP | 1.9% | 6.7% | -1.1% | 7.3% |
| Continental Europe | EUR | 0.7% | 3.5% | -0.2% | 1.6% |
| Japan | JPY | 1.5% | 3.6% | -1.3% | 18.1% |
| Asia Pacific (ex Japan) | USD | -0.6% | -0.1% | -0.6% | 18.6% |
| Australia | AUD | 1.5% | 3.4% | -0.6% | 5.0% |
| Global | USD | -0.1% | 1.6% | 0.3% | 13.6% |
| **Emerging markets equities** | | | | | |
| Emerging Europe | USD | 0.1% | -3.8% | -1.8% | 12.7% |
| Emerging Asia | USD | -0.9% | -1.0% | -0.2% | 22.7% |
| Emerging Latin America | USD | -0.6% | -0.5% | 7.5% | 18.9% |
| BRICs | USD | -0.2% | -1.1% | 1.1% | 25.9% |
| MENA countries | USD | -0.2% | 3.0% | 10.0% | 12.4% |
| South Africa | USD | -3.4% | -1.9% | -6.0% | 16.1% |
| India | USD | 0.5% | 3.3% | -2.3% | 11.6% |
| Global emerging markets | USD | -1.0% | -1.1% | 0.3% | 20.6% |
| **Bonds** | | | | | |
| US Treasuries | USD | 0.1% | -1.0% | -2.2% | -1.1% |
| US Treasuries (inflation protected) | USD | 0.1% | -0.3% | -1.2% | 0.4% |
| US Corporate (investment grade) | USD | -0.1% | -1.0% | -3.3% | 0.7% |
| US High Yield | USD | -0.4% | 0.6% | -0.2% | 3.4% |
| UK Gilts | GBP | 0.5% | -1.4% | -1.2% | -1.1% |
| UK Corporate (investment grade) | GBP | 0.3% | -0.3% | -1.8% | 0.5% |
| Euro Government Bonds | EUR | 0.2% | -0.3% | 1.1% | 2.2% |
| Euro Corporate (investment grade) | EUR | 0.1% | 0.0% | -0.4% | 1.2% |
| Euro High Yield | EUR | 0.0% | 0.6% | 0.1% | 4.0% |
| Japanese Government | JPY | 0.0% | -0.1% | 0.4% | 0.6% |
| Australian Government | AUD | 0.0% | -1.0% | 0.1% | 1.8% |
| Global Government Bonds | USD | -0.7% | -1.8% | 0.4% | 4.4% |
| Global Bonds | USD | -0.7% | -1.5% | -0.3% | 4.5% |
| Global Convertible Bonds | USD | -0.9% | -0.5% | 1.2% | 5.3% |
| Emerging Market Bonds | USD | -0.7% | -1.4% | -3.4% | -1.0% |

*Source: Bloomberg. Past performance is not indicative of future returns*

| Asset Class/Region | Currency | Currency returns | | | |
|---|---|---|---|---|---|
| | | Week ending 27 April 2018 | Month to date | YTD 2018 | 12 months |
| **Property** | | | | | |
| US Property Securities | USD | 3.7% | 1.8% | -6.8% | -5.0% |
| Australian Property Securities | AUD | 2.2% | 2.6% | -4.9% | -6.2% |
| Asia Property Securities | USD | 0.6% | 1.1% | 1.7% | 15.4% |
| Global Property Securities | USD | 1.5% | 1.3% | -2.3% | 7.1% |
| **Currencies** | | | | | |
| Euro | USD | -1.5% | -1.8% | 0.7% | 11.4% |
| UK Pound Sterling | USD | -1.9% | -1.8% | 1.9% | 6.8% |
| Japanese Yen | USD | -1.4% | -2.6% | 3.2% | 2.0% |
| Australian Dollar | USD | -1.4% | -1.5% | -3.1% | 1.4% |
| South African Rand | USD | -2.3% | -4.4% | 0.1% | 7.9% |
| Swiss Franc | USD | -1.4% | -3.5% | -1.5% | 0.6% |
| Chinese Yuan | USD | -0.6% | -0.8% | 2.8% | 8.8% |
| **Commodities & Alternatives** | | | | | |
| Commodities | USD | -0.6% | 3.0% | 5.2% | 15.4% |
| Agricultural Commodities | USD | 1.1% | 1.6% | 4.5% | 2.1% |
| Oil | USD | 0.8% | 6.2% | 11.6% | 45.1% |
| Gold | USD | -1.2% | -0.4% | 1.2% | 4.5% |
| Hedge funds | USD | -0.5% | 0.3% | -0.8% | 3.0% |

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