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Global CIO Outlook
Davos as Contra-Indicator

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Two years ago, when I last attended the World Economic Forum in Davos, a growing consensus saw the global economy at the brink of recession. The spread between credit securities like bank loans and high yield bonds had dramatically increased relative to lower risk assets like U.S. Treasury securities. Stocks had sold off, and many pundits predicted that we were at the brink of a new bear market. Oil was collapsing toward our earlier established target price of $25 per barrel for West Texas Intermediate. Declining asset prices were offered up as full evidence that the U.S. and probably the entire global economy was at the precipice of recession.

At the time, we argued that correlation was not causality and that oil, stocks, and high yield bonds were approaching a bottom. In our clients' accounts we were increasing exposures to high beta asset classes like mezzanine collateralized loan obligations (CLOs), bank loans and high yield bonds. While we stayed the course with our client portfolios, the consensus at Davos lead me to conform by allowing for further price erosion when I should have pounded the table that it was time to buy. Fortunately, my words didn't exactly match our actions. I remember explaining on a CNBC appearance that no one can time the bottom and despite any comments to the contrary, it was time to start buying on weakness. The good news is our investments performed well as we continued to load up on energy exposures and leveraged credit risk in the form of mezzanine CLO securities.

As things kick off here in Davos, the sentiment couldn't be more radically different from January 2016. Global growth is accelerating and risk assets are soaring. Sentiment is so positive, it feels like the discussion will focus on "How high is up?" This is occurring in the face of U.S. tariffs on solar panels and washing machines, while CNN and the BBC run documentaries on a rising tide of nationalism, and against a backdrop of discussions on restricting immigration just when healthy Western economies are starting to experience labor shortages in certain key industries.

While I am still a Davos neophyte—it is only my fifth visit to Davos—I am starting to consider that Davos may be a valuable contra-indicator. A few years back the big story here was about the emergence of Africa onto the global scene as an important component of future global growth. While I think that view is ultimately correct, the immediate experience proved very disappointing for investors. Rather than a buying opportunity, investors would have done better to go short for the near term.

While I am hesitant to jump to a conclusion, I'm troubled by the euphoria undergirding the gathering here. I will be listening closely and speaking occasionally, most likely asking more questions than providing opinion. I have seen bull market tsunamis before. They can be both rewarding and destructive. The key is to know when to get out.