TalkingPoint Schroders

MARKETS

# Are there any safe haven investments left?

**After nearly a decade of low interest rates and central banks pumping money into financial markets traditional safe haven investments have become expensive, so where could investors look to keep their investments safe?**

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**30 Minutes**
Unstructured
Learning Time

Gold, the US dollar, “defensive” stocks such as utilities and pharmaceuticals, government bonds, cash, what do they have in common? In times of economic stress and market turmoil, they are seen as safe havens for investors.

## The fear driving investors

Investors were already cautious and snapping up safe haven assets before Brexit, but the result has greatly increased concerns. They fear:

- A recession in the UK
- A slowdown in Europe and the global economy
- A break-up of the EU
- Increased global political risk

There is no doubt that these scenarios are all possible, but by flocking to traditional safe havens in such huge numbers investors are paying a high price for protection:

- In the UK, if you want to put your money into a government bond for 10 years, the government will pay you just 79 pence a year for every £100 you lend it.
- In Germany, investors have to pay the German government to own its bonds. A German 10-year bond yields -0.2%.

We are currently in the second longest stockmarket bull run in history and gains have been driven primarily by defensive stocks, which has arguably made them expensive.

The shares of household goods firm Unilever, for example, are valued at a multiple of 22 times the company’s earnings. The shares of Reckitt Benckiser, a similar company behind brands such as Cillit Bang and Calgon, have a price to earnings ratio[1] (P/E) of 29, according to Bloomberg data.

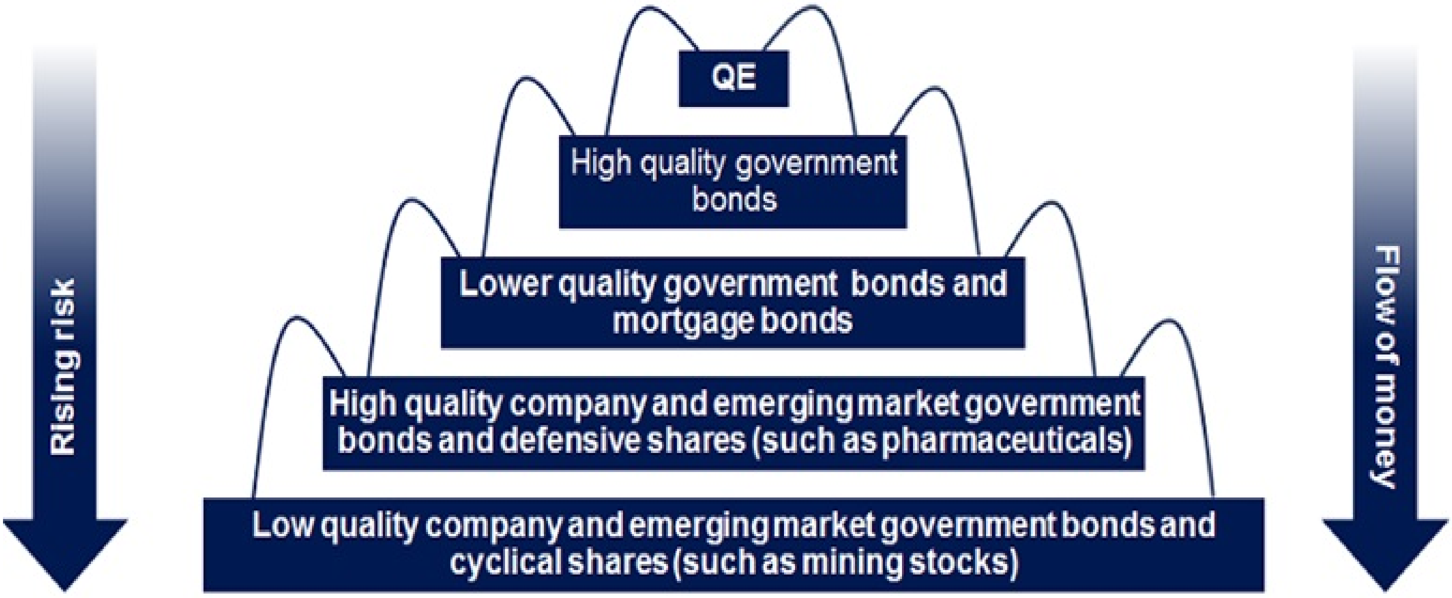
Both stocks have surged in recent weeks and their valuations compare to a forward 12-month P/E of 15.5 times for the FTSE All-Share, according to data from Peel Hunt.

## Paying the price of safety

It is a high price to pay for the feeling of security. It has happened because, in a world of economic uncertainty, the money pumped into financial markets by central banks via quantitative easing (QE) has been invested in the highest quality assets first.

From there, the slew of central bank money has trickled down the investment pyramid into lower quality assets as investors have gone in search of higher returns.

*Chart: QE: the fountain of money*




*Source: Schroders. For illustrative purposes only*

But paying such a high price for protection in traditional safe havens is a risk in itself.

Like buying a house at the top of the market there is the risk that the price can't go much higher. Even worse, if the scenarios described above fail to come to fruition prices could fall sharply.

While traditional safe haven assets may provide some protection for your investments in times of economic and financial strife, they all currently carry risk because of their high prices.

Is it worth paying such a high price for an asset that yields less than the interest you can get in your bank account and could fall dramatically if investors' worst case scenarios don't unfold?

## Where are the safe havens now?

Options for safe haven seekers are very limited.

Gold remains the ultimate safe haven as it is seen as a store of value. The price tends to rise at times of uncertainty and when there is a threat of inflation.

The price of bullion has soared 9% to $1,366.33 an ounce since the EU referendum. But it offers no income.

## What else to consider?

The rush to safe havens may have created other opportunities in areas previously considered risky: cyclical shares (shares where the prices are particularly affected by ups and downs in the overall economy).

If the economy recovers or the fears of investors don't materialise then there is a strong argument that cyclical share prices will rise sharply.

If investors' fears do come true then those cyclical shares don't have too far to fall. They also pay healthy dividends, so they could provide an income greater than is available in more traditional safe havens.

For instance, financials are currently the cheapest sector in the MSCI World Value Index according to their price-to-earnings valuation and also offer a dividend yield of more than 4%, four times the yield on a UK government bond. Share prices in this sector have been very volatile.

*Graphic: Which MSCI World sectors pay the most divdends and are cheapest on P/E valuations?*

| Sector | Dividend yield (%) | Price-to-earnings (x) |
|---|---|---|
| Financials | 4.07 | 16.57 |
| Industrials | 2.78 | 17.22 |
| Telecommunication Services | 4.31 | 17.39 |
| Utilities | 3.73 | 18.23 |
| Health Care | 2.47 | 18.74 |
| Information Technology | 2.45 | 21.19 |
| Materials | 2.59 | 21.29 |
| Consumer Staples | 2.68 | 21.87 |
| Consumer Discretionary | 2.81 | 24.26 |
| Energy | 3.81 | 29.52 |

*Source: Schroders, Bloomberg as at 6 July 2016. MSCI World Value Index.*

Past performance is not a guide to future performance and may not be repeated. The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.

1. Price-to-earnings: the price investors are willing to pay for the asset compared with the value of company's assets. The lower the number, the cheaper the shares.↩