

G20 has reduced the risk of protectionism, says RCM

Lucy MacDonald, CIO Global Equities at RCM, the specialist global equity company within Allianz Global Investors, comments on the impact of the G20 Summit on the global economy, and the consequences for global investors:

“The impact of an additional \$1 trillion for institutions such as the International Monetary Fund (IMF) and the World Bank, although less significant than the \$5 trillion fiscal stimulus already announced by the G20 nations, is on balance a minor positive for confidence in financial markets. Also beneficial is the vision of a concerted global effort to alleviate the financial crisis and its aftermath, and a reduced risk of greater protectionism.

Why is the threat of protectionism important for global investors?

“The growth in trade has been one of the main drivers of globalisation, and therefore a support for the increased growth in global investing. Other drivers have been the increasing proportion of profits derived from non-domestic operations (around 30% of US companies’ profits are from overseas) and the increased internationalisation of financial markets, with rising foreign ownership of domestic equity markets. If these trends were to reverse, the case for global investing could be undermined.

“Fears of protectionism have been rising since the economic downturn begun, with some grounding in fact. According to the World Bank, since the last G20 summit in November 2008, 17 of the G20 have implemented 47 measures aimed at ‘restricting trade at the expense of other countries’. Yet, these actions are not supported by the wider global economic infrastructure. With the World Trade Organisation fully established and a common understanding, reinforced by the rhetoric from the G20 Summit, that all economies rely on trade to continue to grow their domestic economies, a return to full protectionist policies and a collapse of globalisation is an improbable scenario, despite the cyclical pull back in trade.

“So to the second driver, the increased proportion of corporate profits from abroad. In the short-term stricter regulation in financials could lead to increased domestic bias if exposure through overseas subsidiaries was a source of capital destruction. In the UK, the experience of the domestic banks versus the global banks would not support this view. So far, the worst losses seem to have been generated quite close to home geographically, although often far from home intellectually, but this is an area to watch going forward. Outside of the Financial sector, it is unlikely that the likes of Vodafone or Nestle would start to retreat from overseas markets. In fact it is the overseas operations that are driving their growth through the downturn.

So what of the investment community?

“Are institutional investors, who are the largest proportion of market ownership, likely to shift back into their domestic markets on anything other than a tactical risk averse move? Is the move in foreign ownership of US equities from 2% in 1957 to 12% in 2007 going to be reversed? Not in our experience to date. Having some US equities in a portfolio during the crisis reduced the downside for non-US investors, partly due to the broad diversified market, and also due to the risk aversion supporting the dollar. Investing in global equities continues to prove a sensible method of diversifying your investments while providing the opportunity to capture alpha through exploiting inefficiencies in the global markets.

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