

Where to for markets in 2003?

The question everyone is asking is what to expect from investment markets in 2003. There is no easy answer. Markets are probably as hard to pick now as they have been at any time in the last 30 years.

On the optimistic side, the more bullish commentators argue that the markets are oversold and a recovery is overdue. As they see it, all the bad news has already been factored into asset prices and there are good opportunities waiting for canny investors. For example, the benchmark S&P 500 index has fallen more than 50% since peaking in March 2000. Bulls argue that after a fall of that size, recovery is a question of when, not if.

On the face of it, conditions are very favourable for a recovery. In particular, the US Federal Reserve has cut its base rates to an incredibly low 1.25%, while the US Government has increased its spending significantly over the past year. In other words, the world's largest economy is running very favourable economic policies, both monetary and fiscal.

As further evidence, the bulls point out that the relative value of shares to bonds is at its most attractive level for more than 25 years.

While there is the looming threat of war in Iraq, bulls point out that the Kuwaiti war 12 years ago did not have any serious long-term consequences for most major markets – therefore, why expect this one to either.

On the pessimistic side, bears argue the worst is not yet over and the kind of market excesses we saw leading up to March 2000 have not yet been fully corrected. On that basis, they warn the US market could fall further still. The bears also note that bulls are using Wall Street forecasts as evidence of their optimistic forecasts, but they question how much confidence can be inspired on the basis of Wall Street's track record.

Bears also feel the consequences of war in Iraq are being underestimated. They point out that the Middle East is now a vastly different place from 1990-91 when George Bush Sr took on Saddam Hussein. They doubt any war will be over in a few months or be confined just to Iraq.

Finally, bears point to ongoing structural problems with Japan's economy and the now-serious trouble in some emerging markets economies such as Brazil as further reasons to be cautious.

So, if the experts can't agree, where does all this leave investors? The upshot would appear to be that while we must reckon on a weak economy for a little bit longer, there is a glimmer of hope on the horizon. Meantime, a well-diversified portfolio that does not take any significant bets in any one direction should stand you in good stead. For peace of mind, consult a professional adviser in the New Year to make sure your nestegg is well positioned and prudently invested.

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