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An investment in knowledge pays the best interest

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"I like the serendipitous surprises of reality" Lawrence Wright

A little over a month into 2017 and it is increasingly clear that there are only two investing themes to worry about over the balance of the year. If I had to write a couple of paragraphs summary of January it would look something like this:

"If you ignore politics then it really has been a very attractive start to the year. Certainly, the UK stock market has not made heroic progress, but the Pound has started to firm up on the global foreign exchanges, and both global economic data as well as the corporate earnings results season indicate some general progress is being made.

And so it should be. Last week's utterances by the Bank of England, where they coyly raised their economic growth and inflation expectations for the UK economy in 2017, reflect a world where Central Bankers – except in China - are still pressing the 'Go' button, which typically is good for equity markets"

Did you spot the two pre-eminent investing themes?

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Let's start with the one in the second paragraph: inflation. We all know that changeable price levels can hugely influence asset allocation decisions and, unsurprisingly, this has manifested itself in a general upward movement of bond yields. Meanwhile, equities – especially more cyclical or financial sector equities – have remained relatively nonplussed. This is hardly a great surprise. One of the better attributes of equities is the ability of the better or stronger underlying company management teams to respond to a change in the economic backdrop, and a little bit of inflation is the perfect backdrop to put through that long overdue price increase, to help keep operating margins heading in the preferred direction.

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However, surely all of this should be giving the world's Central Banks panic attacks and leaving them primed to spring into action with overtly higher interest rates?

Well, to understand this it is important to acknowledge the second clear investment theme of 2017: the political backdrop. Be it the evolution of power in the United States, the constitutional technicalities of the Brexit debate, or the General Election winner prediction game going on in a variety of Eurozone countries, 'politics' is being used as a short hand for potential risk.

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> The best investment opportunities occur when there is a large difference between perception and reality

Now the purists will argue that the proudly independent Bank of England, Federal Reserve or European Central Bank should be focusing exclusively on the control of inflation and the generation of a suitably attractive, and predictable, economic backdrop, to give businesses the comfort to invest and help generate economic growth and wealth. All very laudable… and theoretical. As the Bank of England's interactions with the Brexit debate has shown over recent months, the influence on policy and economic forecasts from big political issues unsurprisingly matter.

And so, given all of this, the major Central Banks of the world will – to use a good 16th Century phrase – play a little bit fast and loose, reckoning that the risk of a little bit of inflation, from a continuation of generally very loose monetary policy, is a worthwhile price paying just in case some of the scarily disruptive political issues come true.

After too many years of looking at all of this it seems to me that the best investment opportunities occur when there is a large difference between perception and reality, and hence for every month that these current political risks remain more a future concern than an impactful reality, global equity exposure is more likely than not to continue to appreciate in value.

In market parlance, such an occurrence is often referred to as 'climbing the wall of worry'. We all know that investment matters are rarely straightforward, particularly over shorter time periods, but if we look at that phrase a little more closely it is not hard to discern that it implies an action. So, whilst at first glance the world of quantitative easing and extraordinarily loose Central Bank policy – apparent since 2009 – appears to be effortlessly continuing, the reality is that a little bit of inflation (which has been suppressed until now by oil market oversupply, a firm US dollar and the recent ever-cheaper production miracle of modern China) can make a real difference, as not every company management team will be able to raise their prices.

Call it 'mix' or 'dispersion' – the biggest investment thematic of 2017 is not inflation or political event risk, it is that the choice of specific investments is going to matter more than at any point in the last decade.

As Benjamin Franklin once said: *"An investment in knowledge pays the best interest."* Too true.

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