September Market Reflection

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Equity markets spent much of September on the back foot, with little offsetting assistance from government bonds. Hard asset safe havens such as gold also fell back. For once, it was US equities that led global indices lower, owing to a sharp reversal in the fortunes of Technology leaders. In many respects this was a welcome unwinding of speculative buying that had been accelerating during August. High valuations were also undermined by a relatively small increase in real interest rates, itself a function of weakening expectations for future inflation. This in turn was the result of a re-evaluation of economic recovery prospects in the face of surging coronavirus cases and the introduction of more stringent social distancing measures. A lack of progress in the signing of a new US stimulus package also hampered risk assets, as did the wrangling over the appointment of Ruth Bader Ginsburg's replacement on the US Supreme Court. Covid and Brexit continue to vie for top billing in the UK, with the latter gaining more column inches as we edge closer to the final departure date with no sign of a deal in sight. The "level playing field" of state aid remains a key sticking point. The pound, as in the past, has been the main victim of the uncertainty, which at least helped to shield sterling portfolios from greater falls owing to holdings in overseas assets as well as the predominantly non-sterling base of FTSE 100 company profits. Investors still appear willing to "buy the dips", steadfast in their belief that both governments and central banks have no alternative but to continue with their supportive policies.

For the present, large fiscal deficits are sustainable in an environment of low interest rates and depressed bond yields, a situation that central banks appear willing to perpetuate.

- The IMF's latest forecast sees the global economy shrinking by 4.9% in 2020, followed by a recovery of 5.4% in 2021.

- Markets are increasingly driven in the short term by the ebb and flow of news on the development of a Covid vaccine. Expectations for one being widely available continue to centre on the first half of 2021. Any slippage in the timetable would be of concern.

- Aggregate company earnings estimates have held steady during the summer, providing some respite. However, a resumption of halted dividend payments is slow to materialise.

- The US Presidential race moves into the final furlong in October, promising to raise volatility. It is not guaranteed that the result will be declared immediately, owing to the late counting of postal votes of which there are forecast to be a record number this year – assuming that Donald Trump accepts their validity.

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- The majority of investors expect, and profess to prefer, a Biden victory because he will return to a more diplomatic style of leadership. However, there are also risks associated with potential Democratic policies that will lead to a redistribution of wealth through taxation.

- Both candidates will continue to espouse an aggressive stance towards China, if only because a strong majority of voters say they have an unfavourable opinion of China.

- In the longer term, portfolio construction will depend greatly upon any change in inflation trends following four decades of persistent disinflation.