Weekly Digest
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Investec
Wealth & Investment

The weekly insight into world stock markets

Midsummer Ramble

All the sure signs of summer are here: Wimbledon tennis; the Cricket World Cup coming to the boil with an England vs Australia semi-final; Geraint Thomas crashing on day 1 of his yellow jersey defence in the Tour de France but carrying on as if nothing happened (he once rode pretty much the whole thing with a fractured pelvis); and, of course, rain showers forecast for the one day in the next two weeks when I am scheduled to play golf! Financial markets have also been shown to display some seasonal tendencies, notably the fact that, on average over the long term, equities have tended to produce much better returns over the winter rather than summer months. We have investigated this phenomenon in the past, and concluded that it does make some sense. However, the outcomes are skewed by very large individual single events and there are plenty of rule-proving exceptions.

This lack of certainty is reflected in the divergence of opinions I can read in all the strategy reports that drop into my inbox. For every note that exhorts us to maintain a bullish stance I can find you another one that recommends a more defensive position. Some are extremely bullish; others are outright apocalyptic. It is a continuing source of amazement to me that so many people can observe the same set of data and reach such diverse conclusions. But therein lies the opportunity for outperformance. No doubt some of the opinions are informed by ingrained ideologies – think of the long-running Growth vs Value debate, for example – but some of the difference is also down to methodology. Several strategies rely on the use of the averages of previous cycles to predict the current one, and while this can be a useful guide I tend to find it the most prone to error.

That might especially be the case now owing to the distorting effects of current monetary policy. For example, I have seen various charts recently looking at what has happened to markets and sector rotation within the market historically following the first interest rate cute of a new easing cycle (such as the market is predicting the US Federal Reserve will embark upon later this month). Given that so much money is now managed by funds that rely on examining historical patterns it is quite possible that the initial response could be self-fulfilling, but even a cursory examination of the present situation shows that market action running into this expected rate cut has been very different to the historical averages. This could mean that investors are better at predicting the future these days, but I am skeptical of that assertion. More plausible is that Quantitative Easing and zero/negative interest rates have created a very different market environment. Tim Harford’s piece in this weekend’s Financial Times had some interesting observations on the dangers of averages, which is worth a read.

On monetary policy itself, I have already mentioned the impending US rate cut, but market expectations were thrown into some disarray by stronger-than-expected US employment data on Friday. 224,000 jobs were created in June – a lot more than the predicted 160,000, and a strong bounce from May’s disappointing 72,000. It was that May figure, followed by dovish comments from chairman Powell, which had cemented expectations of a Fed rate cut, possibly as much as 50 basis points. The case for such an aggressive reduction now looks less compelling, which is why equity and bond markets have succumbed to some profit-taking. We live in a counter-intuitive world where bad news (at least to a point) is good news for investors, and good news is bad. That emphasises the importance of liquidity and interest rate levels to financial markets, particularly in the short term, although in the long run sustainable progress cannot be made without growth.

The machinations of a central bank were on view for all to see in the first instalment of the BBC’s two-part documentary about the Bank of England (part two tomorrow). I thought it was very interesting, but also served as a reminder that the Monetary Policy Committee, for all its academic brilliance, is not guaranteed to have perfect foresight into the ebb and flow of the economy and markets. Unfortunately, market participants and commentators seem to have come to expect unerring guidance, and get quite uppity when there is a change of tack, however well justified. This would be appear to be a result of the increasing “financialisation” of the economy. Gone are the days when interest rate announcements would come out of the blue. I thought Governor Carney kept his cool admirably under accusations of being an “unreliable boyfriend”. Perhaps the most remarkable thing on view was the extraordinary bundle of pencils held together by an elastic band employed by external MPC member Ben Broadbent. Refreshingly old school, or willfully old-fashioned?

The other big central bank news last week was the (still-to-be-rubber-stamped) nomination of Christine Lagarde to the role of President of the European Central Bank. If confirmed, she will move from her current role in charge of the International Monetary Fund. News of her nomination was greeted with near-euphoria in financial markets, as she is seen as being a reliable carrier of the torch lit by current incumbent Mario Draghi. Remember that he only recently appeared to set a new loosening path for ECB policy. Moreover, Ms Lagarde has championed higher social spending (investment as well as protection) in her current role, and there is every possibility that she will attempt to build a stronger link between monetary and fiscal stimulus within the euro zone. The important thing is that the EU seems to have avoided having to appoint a hair-shirted German to the job.

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FTSE 100 Weekly Winners

Flutter Entertainment	14.1%
British American Tobacco	8.5%
John Wood Group	7.8%
EasyJet	7.7%
Imperial Brands	6.2%
Hargreaves Lansdown	5.4%
Burberry Group	5.4%

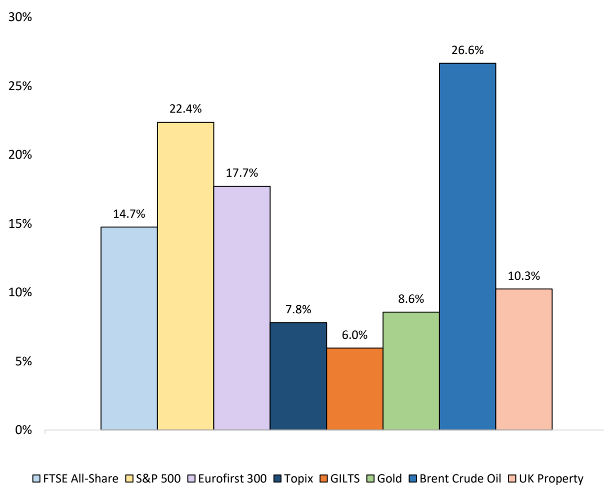
Source: FactSet

FTSE 100 Weekly Losers

Evraz	-5.4%
Antofagasta	-5.0%
Anglo American	-4.8%
Persimmon	-3.7%
Rio Tinto	-3.2%
BHP Group	-2.4%
Next	-2.3%

Source: FactSet

Year to Date Market Performance



Source: FactSet

FTSE 100 Index, Past 12 Months

Source: FactSet

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