Weekly Digest

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And Finally…?

This is theoretically the last Weekly Digest of 2020. However, given that there are a few unresolved issues it is well within the bounds of possibility that I will have to put my metaphorical pen to paper at least once more. Amongst the key outstanding items are Brexit (of course), a few central bank meetings, the last knockings (hopefully) of the US elections, and all-things Covid-related. It has certainly been a year quite like no other so far, but there might well be a final twist in the tale.

Having relegated Brexit to the epilogue last week, I will promote it to top billing today. One of the perks of my job is to receive invitations to conference calls that are not open to the press with well-connected people. Some of them do write the odd newspaper column, but their spoken comments in a more private forum tend to be a bit less guarded. These people are not necessarily “insiders” (in the sense that they are taking part in the negotiations), but they are exceptionally well connected and informed. Last week I was lucky enough to be able to listen to Sir Olly Robbins (Theresa May’s Chief EU Negotiator – now employed at Goldman Sachs), Lord Hague (you know him), and Sir Ivan Rogers (former Permanent Representative of the UK to the EU).

I am not going to attribute specific comments to any of them, but there were certain themes that were consistent to all. First, and perhaps most important, is the fact that both sides are still talking. If there was no will to do a deal, then bags would have been packed already. Neither side wants to be the one to be seen to walk away.

Bearing that in mind, there is still no deadline other than 31st December, so this could go to the wire – and even then formal ratification in various parliaments could be delayed into the New Year. Even so, it must be borne in mind that the differences between “deal” and “no deal” as currently framed are minimal. This will be a “very hard” Brexit whatever happens, and our terms of trade with the EU will be far less generous.

It is universally acknowledged that the key sticking point is now the concept of the “level playing field” as it pertains to regulatory alignment and the policing thereof. Although fisheries have been a totemic point of disagreement, there is a pragmatic solution to be reached that both sides can call a victory. It appears that Mr Johnson, even at this late stage in proceedings, spectacularly misread the resolve of the EU as he entered last week’s dinner meeting. First of all, in trying to by-pass the appointed negotiating team of Ursula von der Leyen and Michel Barnier he failed to recognise the concept of European unity and the fact that the negotiators represent all 27 countries. Second, he seemed to be genuinely shocked by the fact that the EU stuck to its position. This stance was underlined by Angela Merkel in a speech to the

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Bundestag earlier in the week, when she underlined the concepts of non-regression and evolution. It’s possible that there was some misinterpretation of what she said, but the good thing is that everyone now knows what they are trying to resolve.

Briefly, “non-regression” is about agreeing what regulations are locked in on the day of departure. “Evolution” is about what happens when regulations (in Europe) evolve in the future, and whether we must follow those changes. Allied to this is the all-important aspect of governance – what recourse is there if either side is deemed not to have complied? And, crucially, who will be the arbiter in case of dispute. This is where is the issue of “sovereignty” kicks in, and, for all the talk of trade, it is sovereignty that has, in many respects, always been the primary motivation within the Conservative Party behind the push for Brexit.

Interestingly, all of the speakers were rather less certain of a deal being reached than they had been a couple of weeks earlier, but still put the probability of success at around 60%. None thought that any of last week’s histrionics were “posturing”, and that the breakdown in talks was genuine. By the same token, the resumption of talks is genuine too. However, the warning was made that if everything falls apart in the end and no deal can be reached, the fall-out will be spectacular, with both sides blaming the other and little hope of any sort of smooth transition to the new environment.

Financial markets are handling things just as one might expect given past experience. The pound is the key barometer, and it has bounced again this morning as hopes for resolution rise. The FTSE 100 Index, dominated by overseas earners, remains inversely correlated to sterling, while more domestically exposed stocks rise and fall with the probability of a deal. Many strategists are pointing to the value inherent in the UK equity market, anticipating an unleashing of global investor demand once we have some certainty – either way. While we would welcome that, we still see better long-term benefits from owning a more broadly internationally diversified portfolio.

The big political set piece on the other side of the Atlantic should be resolved this week as the US Electoral College meets to tally its votes. Barring any major shock, this will pave the way for Joe Biden’s inauguration on 20th January. Meanwhile, though, there are still those important run-offs for the final two Senate seats in Georgia to get past on January 5th. They will define how far to the left government policy will be able to shift during the next Presidency.

Neither the US Federal Reserve nor the Bank of England are expected to announce earth-shattering policy changes this week. Our central bank raised its asset purchase ceiling by £150bn at the last meeting, and was only expected to do anything at all this week if a “no deal” Brexit was confirmed. One of the remaining policy options is a negative base rate, a prospect generally not welcomed by the financial industry or savers, and a phenomenon whose benefits have not been adequately demonstrated.

Still, such a move has not been ruled out, and it will be interesting to see if the Bank has reached a conclusion on the subject. The Fed could update its asset purchase policy, mainly in terms of where on the yield curve it will concentrate its firepower. A shift to longer-duration purchases would signal a desire to forestall a major rise in bonds yields, effectively (but probably not in name) introducing ‘”yield curve control” and more concrete evidence of “financial repression”.

As for Covid, the tug-of-war between case growth today and the benefits of vaccines tomorrow has become more competitive again. Even so, we continue to believe that markets will “look through” the current situation. That is not to say that the news will get any better soon. You might recall that my go-to man on Covid, Michael Osterholme, has been forecasting for months that the Northern Hemisphere winter would be the perfect environment for a massive spike in cases as we all headed indoors, with the situation exacerbated by holiday celebrations (US Thanksgiving, followed by Christmas and New Year). Unfortunately, the virus does not take its own public holidays.
It certainly looks as though tougher measures are on their way in many parts of Europe, the UK and North America, and, online retail gluttony notwithstanding, a “double-dip” contraction is on the cards during

the fourth quarter. However, the effects of further restrictions combined with seasonality and the slow-but-sure distribution of vaccines should ensure that this is the worst of it. It is possible that risk assets have a wobble in the next couple of weeks, especially given that various measures of market sentiment are looking a toppy and liquidity will be reduced, but that should be no major cause for alarm. Indeed, one could embrace longer-term buying opportunities.

Finally, I am looking forward to a bit of non-Brexit-related extra-curricular reading over the holiday. The top two books on my pile (yes, still a pile) are Factfulness by the late Hans Rosling, and The Future is Faster Than You Think by Peter Diamandis and Steven Kotler. The former promises to allow me to see all the positive things happening in the world by focusing on facts (rather than all the noisy opinions).

The latter I have already started, and it's a fascinating insight into how all sorts of new technologies can and will converge to extraordinary effect. First impressions are that it is almost impossible for someone not well versed in this sort of thinking to imagine quite what might lie ahead. I can myself only rue a few gift-horses that I have looked in the mouth over the course of my career in the City owing to my inability to have sufficient imagination (or, perhaps, risk tolerance) to make the required leap of faith. Still, no mention of a global pandemic so far or in the index, and so even the brightest futurologists are not blessed with perfect foresight! (It was published in January.) I also note that the very first story they introduce is the aerial ridesharing concept, Uber Elevate. The business was sold last week so that Uber can concentrate on its core activities.

Lighter reading comes in the form of what I guess will now have been John le Carré's last novel, Agent Running in the Field, and Matthew Syed's The Greatest, which is a compendium of his columns from The Times, and from which I hope to wring out a few tips to elongate the twilight of my sporting career!

In the event that this is the last missive of the year, thank-you, as always, for taking the time to read these letters, especially as our publishing technology now allows me to ramble on for longer than when I had a hard ceiling of 900 words. I wish you all a thoroughly relaxing Christmas and New Year, and goodness knows we all need one this year.

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Last week's Economic Highlights

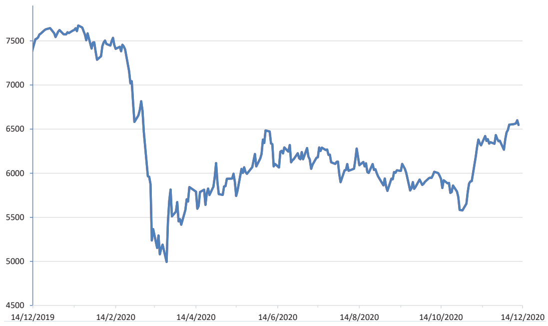
FTSE 100 Weekly Winners

Imperial Brands PLC	7.5%
British American Tobacco PLC	7.2%
DS Smith PLC	5.8%
Bunzl PLC	5.4%
Spirax-Sarco Engineering PLC	5.3%
Evraz PLC	5.2%
Prudential PLC	4.3%

FTSE 100 Weekly Losers

Persimmon PLC	-14.1%
Lloyds Banking Group PLC	-12.7%
NatWest Group PLC	-11.9%
Berkeley Group Holdings PLC	-11.8%
Barratt Developments PLC	-10.7%
Rolls-Royce Holdings PLC	-10.2%
Barclays PLC	-8.5%

FTSE 100 Index, Past 12 Months



Source:FactSet

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