Blessed Are The Cheesemakers

Or, indeed, as quoted from Monty Python's Life of Brian, "any manufacturers of dairy products". This is especially the case in Canada, where I am writing this week's Weekly Digest. It became apparent to me when I was here last Christmas seeking burrata and parmesan cheese in the supermarket that the price of imported European cheese is, to say the least, extortionate. A brief perusal of the Customs Tariff Schedule explained why. Beyond certain very low quotas, imported cheese is taxed at rates between 201.5% and 292.5% (effectively between two and three times the underlying price of the product) depending on the fat content. This is down to a decades-old initiative to protect Canada's dairy farmers (under the guise of guaranteeing supply to consumers), with the result that much of the cheese sold here is of the consistency of rubber and doesn't taste much better. Great for farmers, dreadful for consumers.

The not unsurprising outcome is that cheese smuggling is rife, and my own baggage allowance may or may not have consisted of a few kilos of cheese, depending on who is reading this. (On the return journey I am laden with maple syrup!) This practice might yet be unnecessary in future thanks to the fact that cheese was one of the major components of the trade deal that was recently agreed between the EU and Canada (although I guess that if Brexit happens there will still be demand for bootlegged Stilton or Wensleydale). Canada has agreed to lift its annual tariff-free import quota to 16.5 million kilos by 2022, which might sound like a lot but only accounts for 3 % of consumption. However, a bit of digging reveals allegations that Canada has been backsliding on its commitments, fudging the quotas, and effectively making the system as inefficient as possible. Why? Because the provinces of Ontario and Quebec, which between them account for 80% of Canada's milk production, are crucial to Justin Trudeau's re-election chances this autumn. Well, that's the cynics' view hereabouts.

Cheese was also a major sticking point in negotiations between the US and Canada for the US, Canada and Mexico trade agreement (NAFTA as was), with President Trump apparently incensed by the level of protectionism. That is in spite of the fact that the US, according to one article I read, subsidises its own dairy industry to the tune of $22 billion per annum.

You might be wondering where I am going with all of this. I am not going to draw any deep conclusions about the direction of global trade, but what I can observe is that it is clear that trade deals are subject to all sorts of historical entrenched positions and vested interests, which suggests to me that any hope of fast-track Free Trade Agreements between the UK and potential trade partners are pie in the sky. And it is often going to be what are in effect small industries but which have very high emotional value, such as the UK's fishing industry, for example, that could end up putting a spanner in the works.

The whole trade issue has come into sharp focus again during the final stages of the Conservative Party leadership campaign, with both remaining candidates pledging to take the UK out of the EU by October 31st come hell or high water. The probability of a No-Deal Brexit has risen thanks to this brinkmanship, reflected in another uncomfortable period for the pound, which hit two-year lows against the dollar last week. I still have some belief that both Boris Johnson and Jeremy Hunt are playing to the gallery of the party membership, because they know that taking a soft line on Europe would end their chances of entering Number 10. In Boris's case, his aim is to fulfil an ambition he has had since the age of five to become the "leader of the world" (well, the UK isn't quite there, but the presidencies of the US and China are off the table); Mr Hunt is just doing what he has to do to remain in the race. It is quite possible that the winner's stance will become more accommodative.

Since before the referendum, we have generally recommended that managers take a defensive posture vis-à-vis Brexit by underweighting sterling and having more exposure towards UK companies with greater overseas earnings. The risk/reward balance suggests we should continue to adopt such a position. Even if there isn't a No-Deal Brexit, any deal is going to require a long period of horse-trading before implementation, and there is always the risk of a general election, which itself brings the prospect of a very left wing (and therefore very market-unfriendly) Labour government. At our most recent Asset Allocation Committee meeting there was a proposal to increase the sterling underweight (i.e to buy more non-sterling assets), which in the end boiled down to a single question: how many committee members believed that there will be a No-Deal Brexit on 31st October. The outcome was 7-4 in favour of No-Deal being avoided. Not necessarily a great deal, and certainly not a revocation of Article 50; most probably another can-kicking exercise. But not an event that will immediately send the pound down another 10% or more. We'll find out a bit more in the next few days once we know the identity of our new Prime Minister.

Finally, as I'm now in holiday mode, I recall the story of a friend's Canadian uncle (long-since passed away, and so not liable to prosecution) with a penchant for hard liquor, which is another of life's pleasures that is heavily taxed in Canada. Every winter he would drive his Winnebago (giant camper van) to Florida, and return in the spring with nine months' supply of whisky in the water tank – but with just enough water in the tap to ensure that he could get through any border checks safely. Tariffs are a pain, but they do inspire ingenuity.

John Wyn-Evans
Head of Investment Strategy

FTSE 100 Weekly Winners

Burberry	16.1%
EasyJet	11.0%
Antofagasta	8.2%
British American Tobacco	6.5%
Imperial Brands	5.5%
GVC Holdings	5.1%
TUI	4.9%

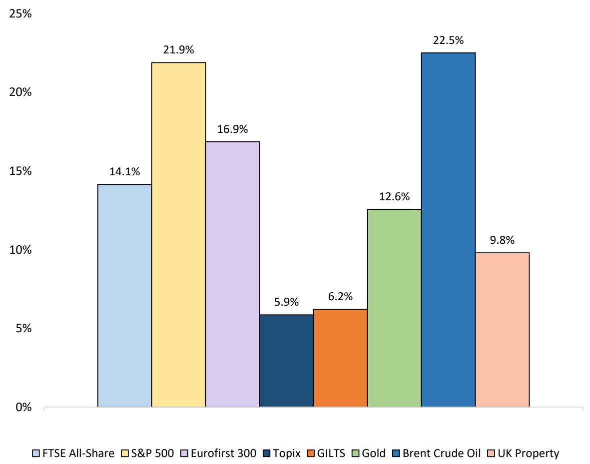
Source:FactSet

FTSE 100 Weekly Losers

Fresnillo	-9.6%
Micro Focus International	-6.0%
BP	-5.2%
Johnson Matthey	-5.0%
WPP	-4.6%
Rightmove	-2.9%
DS Smith	-2.7%

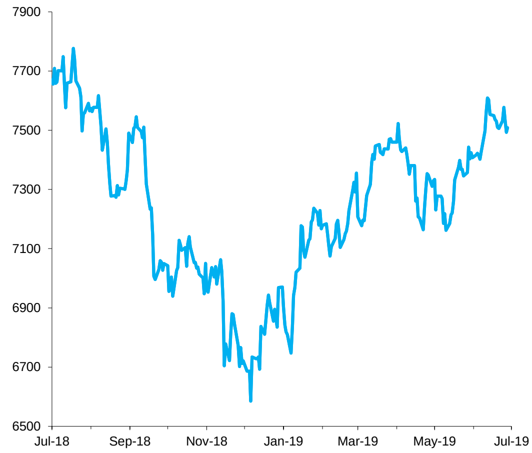
Source:FactSet

Year to Date Market Performance



Source: FactSet

FTSE 100 Index, Past 12 Months



Source: FactSet