Weekly Digest
28 October 2019
The weekly insight into world stock markets

Investec Wealth & Investment

Ditch or No Ditch?

If the Prime Minister is a man of his word, this time next week we could be attending a state funeral. The EU27 have agreed to a further “flextension” of Article 50, with January 31st being the latest deadline. All of which means that the list of potential outcomes remains pretty much as I outlined last week. At the margin, the probability of a general election before Christmas has risen, and while that could bring the current phase of Brexit to a head, it also threatens to uncover a whole new range of uncertainties for investors, not least certain Labour policies that threaten companies and investors. Even so, although psephology is not our primary stock in trade, we still struggle to see any single party commanding a parliamentary majority.

My trip to Northern Ireland last week sadly failed to offer any further elucidation on the subject of the border. Having presciently identified the problem to me 18 months ago, none of the attendees of our conference that I spoke to were able to offer a definitive solution. That seems to be a theme that runs through much of politics the world over at the moment, and I’m sure will also feature in debates over the next few days as I head north of the border into Scotland. A number of articles I read over the weekend highlighted varying levels of social unrest and civil disturbance in countries as far apart as Hong Kong, Lebanon, Algeria and Chile. Argentina has just kicked out a(n admittedly not very successful) reformist president after a four year experiment with a non-radical regime, returning the Peronist leadership that bears much of the responsibility for getting the country into its current financial situation. The promise of an end to austerity (sound familiar?) was too great to resist.

The main problem that underlies all of this is insufficient growth. I noted last week that the International Monetary Fund had downgraded its global growth forecast for this year to just 3%. Prior to the financial crisis global growth was humming along at 4 or 5%. That’s all in real terms, and so allowing for inflation. In nominal terms, the contrast is even greater, especially in mature developed economies, owing to the combination of lower real growth and lower inflation. Workers are not even offered the illusion of greater wealth. In the past I have cited the work of the economist James C Davis, who in 1962 came up with his “J-Curve” to illustrate how the mismatch between a population’s expectations of future living standards and the reality could create social unrest. After years of growth, supported by combinations of new technologies, productivity enhancements, financial deregulation, credit creation and globalisation, we have finally hit a soft patch – one from which it is proving very hard to exit. To exacerbate the situation, some of the remedies – mainly in the realms of monetary policy – have only served to increase the wealth divide. Baby Boomers stand accused of having stolen the future from Generation X and the Millennials, with the latter group characterised as having no prospect of ever “getting on the housing ladder” or cobbling together sufficient savings to be able to retire.

If you are hoping or expecting that I have the answers to all of this, I’m afraid you are going to be disappointed - hey, I’m not running for Prime Minister or for the presidency of a Latin American country! Logic dictates (to me, at least), that initially the “haves”, both companies and individuals, are going to have to pony up a bit more tax, and that the “have nots” will have to set their sights a little lower, but I can see how difficult that will be to sell to an electorate. The more probable short-term solution is a shift towards greater fiscal stimulus enabled by exceptionally low bond yields. How durable that solution is will depend greatly on the how productive the spending is. Straight “bungs” to consumers probably won’t have any lasting benefit – quite the opposite, in fact.

There was another electoral shift in Germany over the weekend, and even though it was in just one state, Thuringia, the trend in favour of more radical, disruptive parties continued. Both the Christian Democrats (Chancellor Merkel’s party) and the Social Democrats (her coalition partners in the federal government) lost out to the populist, right wing AfD Party. Federal elections are not scheduled until 2022, and so Germany remains on the back burner for now. The next major election in western democracies (if I discount the UK) will be just over a year away in the United States. I will return to that event specifically more and more as it approaches, as it has huge implications for policy, especially if Elizabeth Warren gains the Democrat nomination and wins the presidency.

In the meantime, though, a lot will hang on the strength of the US economy over the next twelve months, and this week could give us some key pointers. The Federal Reserve’s Open Market Committee convenes this week to decide its latest monetary policy move, with the market expecting a third quarter-point interest rate cut this year. However, there is greater uncertainty as to what happens next, although Chairman Powell is unlikely to box himself in. The tone and fine detail of his statement will be under extreme scrutiny. There will be two sets of economic data out this week to help guide the way. Third quarter US gross domestic product is expected to be lacklustre, decelerating further to just 1.6%, but that will look positively stellar combined to the euro zone’s expected +0.1%. On Friday we have the monthly US Payroll data. Employment growth has been a cornerstone of US consumer confidence, and so any severe deterioration there would be taken badly. Forecast headline jobs growth of 90,000 in October will look disappointing against 136,000 in September, but 46,000 lay-offs at General Motors will have to be taken into account.

John Wyn-Evans
Head of Investment Strategy

FTSE 100 Weekly Winners

JUST EAT	21.2%
Fresnillo	10.6%
AstraZeneca	9.0%
Prudential	8.2%
Burberry Group	7.8%
WPP	6.4%
Rightmove	6.3%

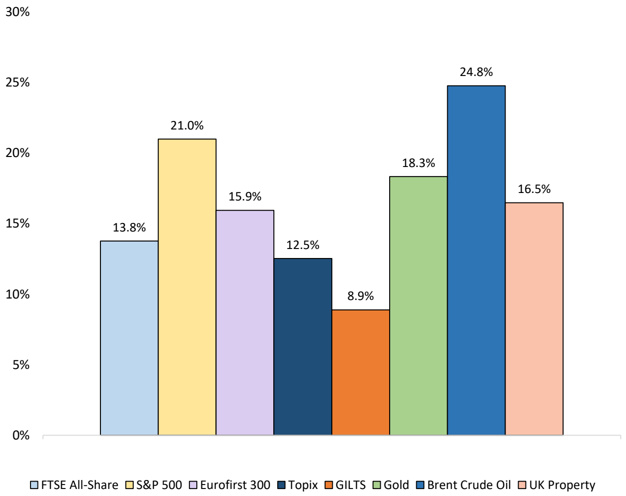
Source:FactSet

FTSE 100 Weekly Losers

Marks and Spencer	-8.6%
Smith & Nephew	-7.5%
NMC Health	-6.8%
Royal Bank of Scotland	-5.2%
Barratt Developments	-4.2%
London Stock Exchange	-4.0%
TUI AG	-4.0%

Source: FactSet

Year to Date Market Performance



Source: FactSet

FTSE 100 Index, Past 12 Months

Source: FactSet