Weekly Digest
11 September 2017

Investec
Wealth & Investment

The weekly insight into world stock markets

# Bullets Dodged… For Now

There was an apocalyptic feel to the news as last week progressed, with hurricane activity combining with the earthquake in Mexico to produce harrowing news footage. Markets, though, remained relatively unmoved. Although there will be economic disruption, it will be fairly short-lived and "one off" in nature. Indeed, evidence was already appearing in last week's US Jobless Claims data, which jumped to 298,000 from a recent average in the 230s. It was also the highest reading since early 2015. Unemployment is a key factor in the Federal Reserve's monetary policy decision-making, and all the data for these series is going to be affected for a while, which will hinder the committee's deliberations. On balance, the members are likely to err on the side of caution - that is they will resist the temptation to tighten policy more aggressively until the picture becomes clearer. That is supportive for financial markets.

I highlighted in the last Digest a number of obstacles that investors would have to navigate before the end of the year, with US monetary policy being just one. Two others were successfully dodged last week. First, Donald Trump and Congress agreed to suspend the debt ceiling before the government effectively ran out of funds. Even the most cynical bunch of politicians was not going to block a deal that ensured the approval of $15.3bn of hurricane relief, although 90 legislators in the House and 17 senators, including some from Texas and Florida who refused to compromise their principles, did vote against the bill. However, this is yet another case of the proverbial can being kicked down the road, as the agreement runs for just three months, so 8th December is the new date to mark in calendars.

The European Central Bank also failed to cause a stir last week as it left policy unchanged and gave no further clues as to the quantum of its potential reduction in monthly asset purchases. However, this is no more than a deferral of the inevitable, so now it's all eyes on the next meeting on 26th October.

The latest element of relief this morning is that North Korea failed to launch another test missile over the weekend, something that the regime might have done to celebrate the anniversary of the country's foundation in 1948. Some wags are speculating that they have run out of missiles, but I doubt we have seen the last of this threat. More worrisome, perhaps, is that the US only has a total of thirty-six ground-based interceptors in the event that it needs to fend off an attack. I have provided some short comments on North Korea in recent weeks, but the situation deserves further analysis.

There has been much surprise expressed that financial markets have been relatively unmoved by the news of missile tests and the detonation of a huge nuclear device. However, markets do seem to be acting rationally. (Admittedly, one cannot be sure that the two lead protagonists, Donald Trump and Kim Jong-un, are themselves rational). A key question one has to ask is what exactly is Mr Kim trying achieve? He seems to have no appetite for territorial gain; he is not reacting to an actual physical threat; and he is not trying to impose an ideology on the rest of the world. He seems, more than anything else, to be looking for a little respect and the ability to get on with managing his country as he sees fit – an unconventional style, to say the least, that has included obliterating people who threaten or displease him by means of anti-aircraft missiles, mortar rounds and a flamethrower! His nuclear capabilities, even if not yet fully developed, are his leverage, and are seen as defensive rather than offensive. It has been pointed out that Colonel Gaddafi and Saddam Hussein both ceded their nuclear weapons and ended up in the mortuary, so you can see why Kim is not going to relent.

That means that the situation is going to rumble on for a while yet, and the trouble is that for a resolution to be reached the tension levels will probably have to be ratcheted up further. That does raise the possibility of an accident of some type. This could be a missile malfunction, meaning that one that was intended to fall harmlessly into the sea could land on solid ground, possibly Japan. Or it could be an error of communication from either side, possibly an errant tweet from the US President. In either event it will require the injured party to turn the other cheek, something that might prove difficult.

Playing out in the background is a tense political game involving the US and China. It is generally accepted that if China cut off all oil supplies to North Korea the country would quickly grind to a halt. But China itself has a vested interest in not destabilising its neighbour. First of all there is the huge historic investment in military casualties that China made during the Korean War which it is apparently unwilling to write off. Then there is the possibility of as many as an estimated fifteen million refugees heading over the border into China.

The best and, in fact, most probable outcome is a return to the status quo, a long rei(g)n for Mr Kim (he is only thirty-three years old), no more missile tests and regular inspections. Thus we continue to make no changes to our asset allocation to reflect the risks. For those of a more nervous disposition, we would expect the US dollar, the Swiss franc, Gold and government bonds to be the beneficiaries of escalation or outright conflict.

Finally, Henry Campbell-Bannerman was the only Prime Minister to die at 10 Downing Street. This week, what was the French Blue, which went missing on this day in 1792?

**John Wyn-Evans**
Head of Investment Strategy

## FTSE 100 Weekly Winners

| | |
|---|---|
| Micro Focus International | 7.1% |
| Next | 5.3% |
| Johnson Matthey | 4.4% |
| AstraZeneca | 4.3% |
| Paddy Power Betfair | 4.1% |
| DCC | 3.2% |
| Shire | 2.9% |

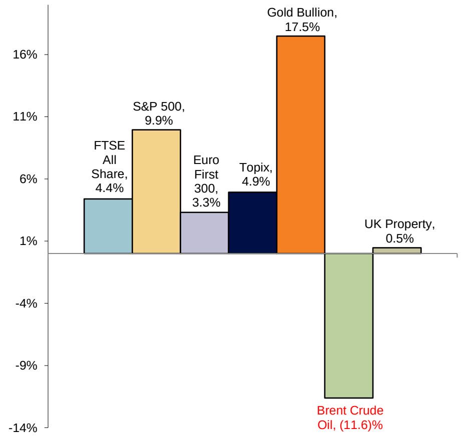
Source: FactSet

## FTSE 100 Weekly Losers

| | |
|---|---|
| Provident Financial | -8.8% |
| Carnival | -6.1% |
| BHP Billiton | -5.5% |
| Admiral Group | -4.8% |
| Standard Life Aberdeen | -4.8% |
| Mondi | -4.8% |
| Antofagasta | -4.7% |

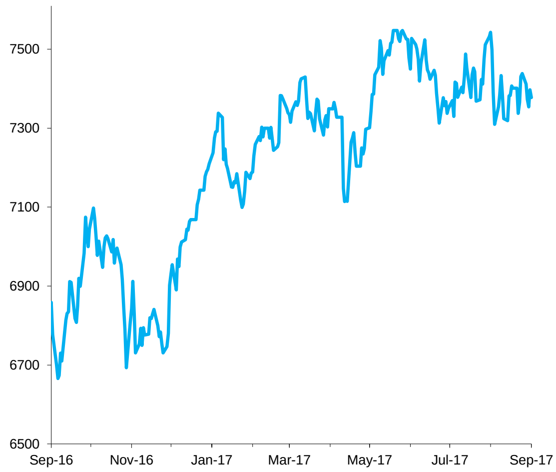
Source: FactSet

## Year to Date Market Performance




Source: FactSet

## FTSE 100 Index, Past 12 Months




Source: FactSet



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