Weekly Digest

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The weekly insight into world stock markets

Investec
Wealth & Investment

Letter From Italy

This week's Digest comes to you from Italy, so it seems appropriate to pass some comment on the political situation here. A year or so ago, last week's general election was viewed as a potentially dangerous hurdle for markets to negotiate, as Europe appeared to be on the brink of being overwhelmed by populist parties. As it turned out, the voters of the Netherlands, France and Germany baulked at handing power to the more extreme parties, although any sense of complacency must be tempered by the strong showing of right wing candidates. If the current governments in those countries are unable to reverse some of the hot button trends, including inequality, negligible real wage growth and unwelcome immigration during this electoral cycle, voters might yet force more radical change next time around.

In the end, Italy was the one country that did hand the greatest share of the vote to an anti-establishment group, with the Five Star Movement (5*) capturing just shy of a third (I know that Emmanuel Macron's En Marche! party was even newer, but it – and the president in particular – are cut from much more traditional cloth). A year ago such a result would have appeared catastrophic, but it's fair to say that 5* had toned down much of its anti-Euro(pean Union) invective, probably as a reaction to the lack of ultimate success for the insurgents elsewhere in Europe. Still, the result is a major wake-up call for those who might have thought that the anti-establishment movement was on the wane. That view is reinforced by the gains made by the more right wing Northern League (strongly against immigration, seeking greater fiscal autonomy for the richer part of the country), who polled 17.4% of the votes against just 4.1% in 2013. In fact, perhaps the biggest surprise of the result was that the League (as they now style themselves, presumably to appeal to more southerly voters!) outscored Silvio Berlusconi's Forza Italia (FI) party (14%), and were only 1.5% behind the Democratic Party (PD), who were the big losers with their share of the vote falling from 25.4% to 18.7%. This effectively gives the whip hand to the League in coalition talks involving the centre-right grouping (which includes FI and the League, and took 37% of the vote), a power-broking position they have never before been in a position to exploit.

Market reaction was remarkably relaxed in the end, possibly because no party or grouping has been given a proper mandate, and it could be weeks or months before a government is formed. 5* is the biggest single party, so might be given first shot, although it has previously ruled out forming coalitions. The centre-right parties, as the largest group, are next in the queue. PD seems also to have ruled out any coalition. There is also the fact that the League and 5* are not natural bedfellows. Yes, they are both challenging the status quo, but the whole point of the League is that they don't want to be giving handouts to what they see as the feckless southern half of the country, which is where 5* gained the bulk of its votes. This is all rather comforting "business as usual" for Italy in many respects. There have been sixty-five different governments in the seventy-two years since the founding of the Republic in 1946, and twenty-eight premiers (vs UK 26/15, Germany 24/9 and France 12/10). Unfortunately it also means less chance of progress with much-needed fiscal and labour reforms. I have written before that I believe that Italy's private wealth does much to counterbalance its public debt, but that does not mean that Italy will not once again become a potentially weak link in the financial chain should we enter more stressful times. There are probably still a few more surprises to come from Italy's politicians this year, which will only add to the general sense of global political uncertainty.

Italy is a very young country compared to what it might deem to be its global peer group, and only became much as know it today in 1861. I was reminded of the ephemeral nature of seemingly solid institutions last week when presenting to clients at a City venue called The Ned. This imposing building was designed in the 1920s by Sir Edwin Lutyens to be the Head Office of the Midland Bank, and it was indeed my own branch for several years. The palatial interiors made the process of cashing a cheque (ha!) feel much less mundane than it might otherwise have done. Anyway, now it is a palace of hedonism, boasting no fewer than 250 bedrooms, ten restaurants, six private event spaces, rooftop swimming pool, spa, gym and a private members club (featuring a cocktail bar in the vault that starred in the James Bond film Goldfinger). I guess this is what is called "progress", but I have to say that it all felt very "top-of-the-cycle". Still, that won't stop me taking my mother-in-law there in May for what is, by repute, a legendary Sunday lunch (which one has to book weeks in advance). All this by way of introduction to the fact that the presentation centred on politics (again), and I must say something about Donald Trump's impressive and enduring ability to take us all by surprise. Last week I wrote about the bad Donald and his trade tariffs; this week it's the good Donald and his announced plan to meet North Korean leader Kim Jong-un, potentially defusing decades of tension. Sadly, it's this very inconsistency that investors find so trying, and so, along with the changing inflation and interest rate picture, it adds to the potential for more volatile markets. Finally, the cartoon characters name derived from the traditional anglicised form of Livorno in Italy was Foghorn Leghorn. This week, on which street was the first Warner Brothers Studio?

John Wyn-Evans
Head of Investment Strategy

FTSE 100 Weekly Winners

Smurfit Kappa Group	32.5%
Rolls-Royce Holdings	13.3%
DS Smith	11.0%
Mediclinic International	7.5%
Johnson Matthey	7.3%
Coca-Cola HBC	6.5%
Antofagasta	6.1%

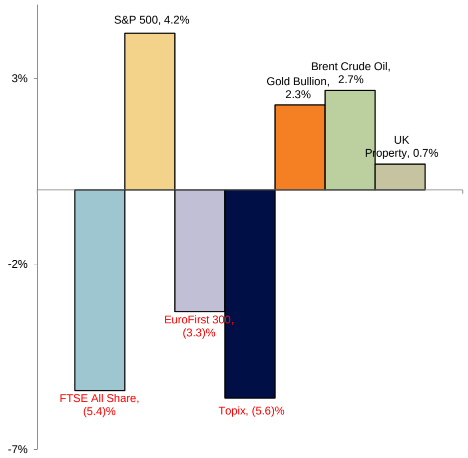
Source: FactSet

FTSE 100 Weekly Losers

JUST EAT	-7.1%
Paddy Power Betfair	-4.9%
WPP	-4.9%
J Sainsbury	-4.0%
Marks and Spencer Group	-3.1%
Sky	-2.6%
Evraz	-1.6%

Source: FactSet

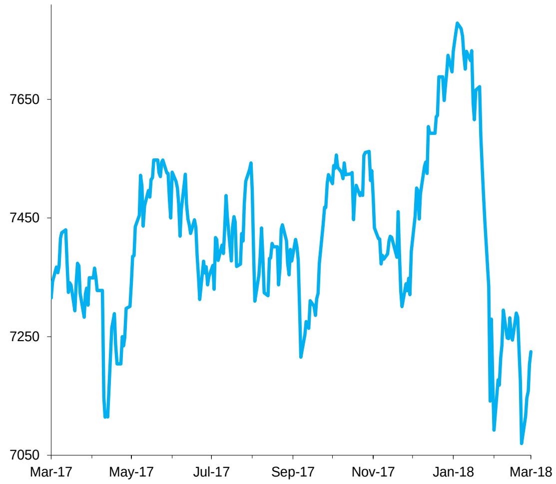
Year to Date Market Performance



*Lagged to latest UK IPD Total Return All Property Index (Jan 2018)

Source: FactSet

FTSE 100 Index, Past 12 Months



Source: FactSet

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