Weekly Digest
16 July 2018

Investec Wealth & Investment

The weekly insight into world stock markets

It's Donald – Duck (Again)!

Last week I congratulated myself on being up with the latest developments on the political front, but this turned out to be somewhat premature, because no sooner had we pressed "Send" to distribute the Weekly Digest than Boris Johnson resigned as Foreign Secretary! Cue another knee-jerk sell-off for the pound. However, as I write again this morning, it's notable that sterling is almost exactly where it was against the dollar and the euro early on Friday 6th July before the Chequers summit. Since then we have had various cabinet resignations and much internecine strife within the Tory Party, not to mention Mr Trump's intervention into the Brexit debate, during which he managed to contradict himself completely on several aspects within the space of twenty-four hours. All of this serves to emphasise that being over-reactive to news headlines is not conducive to effective portfolio management, and we continue to take a longer view of events.

I like to emphasise that there is a big difference between inertia and making conscious decisions not to meddle with our investments – a discipline once beautifully described by the late Ian Rushbrook of the Personal Assets Trust as "masterly inactivity". One reason not to be making bold asset allocation decisions at the moment is the lack of clarity over the outcome of the trade disputes, especially as any resolution will depend to a great degree on the whim (and I use that word quite deliberately) of the US President. The range of outcomes is captured in a note published by one of the major investment banks over the weekend, in which they dramatically reduce – by almost 20% - their performance target for the MSCI Asia ex-Japan equity index to just below current levels. One might argue that they were too positive to begin with, but what is notable is the very wide range of potential outcomes. The best case scenario, which would see no further tariffs imposed than currently, promises 20% upside again. If the latest proposals are followed through and enacted in September, there could be another 17% downside in their opinion. An all-out trade war, which would see tariffs imposed on 100% of China's exports to the US, threatens a potential 40% fall from current levels. Now I must make clear that these are just one bank's range of possible outcomes as opposed to firm forecasts, but they do underline the uncertainty that Trump's actions are creating.

We remain optimistic on the outlook for Emerging Market investments on a long-term basis, although we currently recommend the lowest exposure that we have done for several years. Consistently higher headline growth rates are on offer than in much of the Developed World, and these should deliver higher rewards. The majority of research projecting long-term (7-10 years) returns for a range of asset classes concludes that EM equities are the place to be. Our own work, which we update annually, arrives at the same conclusion. But that doesn't mean that politics and cyclical influences won't intervene along the way. Despite what the last few years have encouraged some people to believe, markets tend not to move from A to B in a straight line.

And speaking of linearity (or the lack of it) in investing, it helps to apply this thinking to current threats. Supply chains, which one might think of as a smooth set of links between a raw product and the consumer, are much more complicated than they first appear. A bit like the "butterfly effect", small disruptions early in the chain can be magnified hugely at the end. You might well have read about the recent disruption to both the beer and poultry industries caused by a shortage of carbon dioxide. Now think what might happen when thousands of products become less freely available owing to the imposition of trade restrictions. And I'm not just talking about trade wars. I fear that a "no-deal" Brexit could cause any number of such unforeseen consequences. A few politicians need to have this risk made abundantly clear to them.

Meanwhile companies are going about their business as best they can, and we have moved into the reporting season for second quarter earnings. These are forecast to be positive, especially in the US, where the effects of corporate tax cuts are kicking in with a vengeance. Analysts are looking for around 23% growth in earnings from US companies compared with the second quarter of 2017. Unfortunately, this could well be as good as it gets, but for now earnings momentum remains a positive counterbalance to geopolitical uncertainty and the progressive tightening of monetary policy.

Finally, a bit of consumer advice. I mentioned "inertia" earlier, and I finally overcame this force last week to renew my car insurance. Having had the same car for fifteen years (!), a terminal MOT test failure forced me to acquire another one, so I actually had to engage with my insurance company. Despite twenty-two years of no-claims, I was quoted an eye-watering premium (£1,750). When I baulked, they responded with their "best price" of £1,450, which just enraged me further as they could at least have started with this. Is there no regulation of such sharp practice?? Anyway, a spot of on-line investigation plus the use of a leading price-comparison site led me to another (household name) provider, and I ended up taking out an equivalent policy for the princely sum of £466! I note a report today that the average UK car insurance premium fell 11% in the year to June. It could be a lot more than that once I have exhorted anyone who will listen to me to shop around!

John Wyn-Evans
Head of Investment Strategy

FTSE 100 Weekly Winners

Barratt Developments	7.1%
Coca-Cola	7.1%
NMC Health	6.5%
AstraZeneca	5.8%
Kingfisher	5.6%
Melrose Industries	5.5%
Sky	5.4%

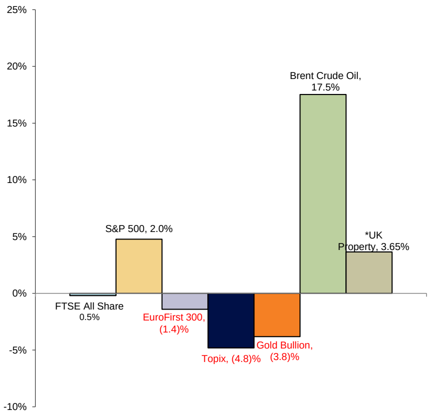
Source: FactSet

FTSE 100 Weekly Losers

United Utilities Group	-6.3%
Severn Trent	-6.1%
Vodafone Group	-5.0%
Glencore	-4.8%
Randgold Resources Limited	-4.1%
BT Group	-4.0%
Standard Chartered	-3.4%

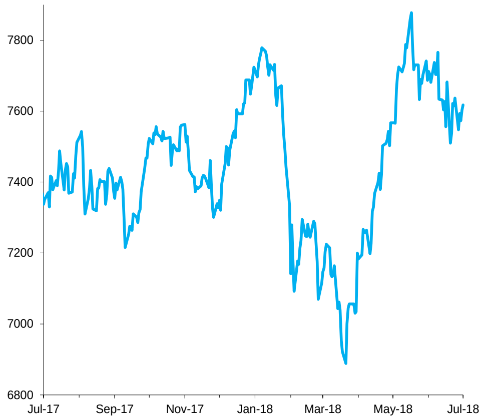
Source: FactSet

Year to Date Market Performance



Source: FactSet

FTSE 100 Index, Past 12 Months



Source: FactSet

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