Stanhope Capital Fortnightly Bulletin

Period ending 31 January 2019

Tactical Positioning

We have not made any further tactical moves in the last two weeks as the equity market recovery has continued. Markets are now close to their technical resistance levels (for those who use charts) but we believe there is a fair chance that they could rise through these. The more relaxed stance from the Federal Reserve regarding US interest rates, as mentioned below, is certainly a useful prop to risk assets. On a broader spectrum, the US earnings season, together with progress in the US/China trade negotiations, could also prove to be positive catalysts.

Market Moves

	Equities *(Local Currency, incl. Dividends)*						
31-Jan-19	**World**	**US**	**Europe[1]**	**UK**	**Japan**	**GEM**	**Asia**
Last 2 Weeks	3.2%	3.6%	2.9%	1.2%	1.6%	3.7%	3.2%
Year to Date	7.2%	8.0%	6.3%	4.2%	5.2%	7.2%	6.5%

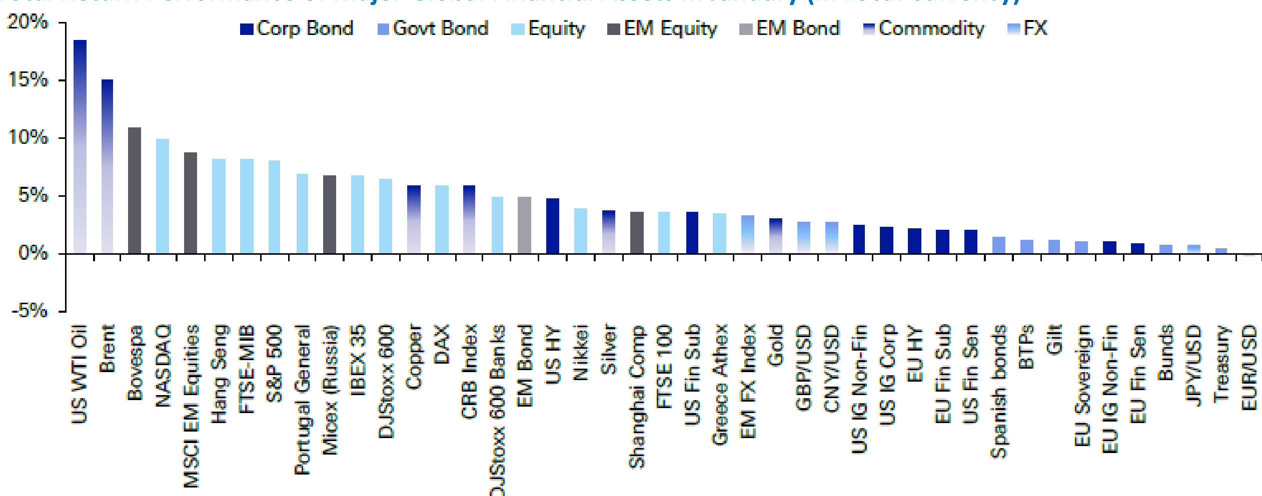
	Commodities			Currencies *(vs. USD)*			Gov't
	BCOM	**Gold**	**WTI Oil**	**EUR**	**GBP**	**JPY**	**UST 10Y[2]**
Last 2 Weeks	0.9%	2.5%	3.2%	0.3%	1.9%	-0.2%	-8 bps
Year to Date	5.4%	3.0%	18.5%	-0.2%	2.8%	0.7%	-5 bps

[1]*Europe excluding UK* [2]*US Treasury 10 Year Yield shows absolute, not percentage, change in yield*

Source: Bloomberg

Assets continued to rebound strongly in the second half of January in a broad-based rally for equities, bonds and commodities. Indeed, this is the first time since Deutsche Bank started producing the chart below in 2007 that all assets in their sample have finished the month with a positive total return in local currency terms.

Total Return Performance of Major Global Financial Assets in January (in Local Currency)



As mentioned in our last bulletin, investors were encouraged by the prospect of a more dovish Federal Reserve ("Fed") earlier in the month with Fed Chair Jerome Powell voicing concerns about the direction of travel for interest rates, having only just raised rates a few weeks previously. At the meeting last week, the Fed executed one of its sharpest U-turns in recent memory by delivering a surprisingly dovish policy statement - rates were held

steady and the promise of "further gradual increases" in rates was dropped. On quantitative tightening, it said both that it planned to permanently retain a large stock of securities for monetary policy purposes and that it was prepared to adjust its current policy of selling down its stock of securities. In December, Mr. Powell described the balance sheet normalisation policy as "on autopilot" and earlier this month he promised "substantially smaller" asset holdings so this change in policy is really quite a dramatic pivot.

Changes to its guidance were needed, Mr Powell argued, because of "cross-currents" that had emerged recently. Among them were slower global growth, trade tensions, the risk of a hard Brexit and the federal government shutdown. What is perplexing is that many of those concerns were already apparent at the time of the central bank's December meeting, when it lifted rates and kept in place language pointing to further increases. Commentators were therefore quick to criticise Powell for capitulating to the market. By contrast, market participants clearly think that one should change one's mind when wrong, welcoming the unambiguously supportive policy statement. It was the first time since Chair Powell's tenure began that the S&P 500 rallied on a Fed meeting day.

Another positive catalyst for equity markets came from companies' earnings reports with more than 40% of S&P 500 companies having now reported. Although the percentage of companies beating estimates is running below trend, the market has taken a 'better-than-feared' attitude and rewarded companies that painted a rosier outlook picture. Although Apple's revenue and profits were slightly down for the quarter, the shares jumped on the news that the company has a strong pipeline of products and services to be launched later in the year. Facebook saw their shares rally 11% as they beat expectations on profits, revenue, and active users. Meanwhile Amazon shares slid 5%, despite beating expectations on revenue and profits, as guidance was a touch lower than anticipated and international momentum softened. The shares are still up 27% since Christmas Eve though and the NYSE Fang Index is up 13% this month.

Outside the US, Emerging Markets and Asia performed strongly, up 3.7% and 3.2% respectively for the fortnight. The Fed's decision to pause its interest-rate hiking has helped lift pressure off Emerging Market currencies. Optimistic sound-bites on trade from the US/China talks have also been beneficial. While there has been no decisive news, on balance the tweets from President Trump have been encouraging: "Meetings are going well with good intent and spirit on both sides". They are working towards an agreement by March 1st which is when tariffs on Chinese goods are due to go up to 25%, so we will see over the course of this month. Furthermore, Brazilian equities have climbed to all-time highs with the Bovespa index up 17.8% since the beginning of the year (and the inauguration of President Jair Bolsonaro), fuelled by hopes of market liberalisation and privatisations.

As mentioned above, government bonds and corporate credit have also enjoyed a good start to the year. Credit has benefitted from the risk-on rally and the prospect of an earlier end to the Fed's monetary tightening saw yields tighten. The yield on the 10-year Treasury fell 8 basis points over the fortnight. In commodities, oil (WTI) ended the month 18.5% higher, although this does follow three straight months of declines. Nevertheless, signs of an improving supply-demand picture and accompanying rhetoric from OPEC and non-OPEC members have helped prices move higher.

Finally, Brexit continued to dominate the headlines in the UK. Theresa May won a confidence vote with 325 votes to 306 immediately after her deal was rejected in the House of Commons. Graham Brady's amendment, which asks the government to renegotiate the withdrawal agreement to accommodate an alternative arrangement to the Irish backstop, passed a vote in the House. This does not appear to clarify much given that Brussels has said they won't reopen negotiations on this, but recent sterling strength illustrates the growing expectation that Britain can avoid a no-deal exit.

Economic Updates

In the US, the government shutdown (December 22nd through January 25th), although largely ignored by markets, delayed key releases of economic data on consumer spending, trade, and manufacturing activity. Despite the economic blind spots this creates, the limited hard data indicators appear to have held up well as compared with the soft data (surveys) which have eased markedly. Initial jobless claims fell to 199,000 the lowest level since 1969,

as the US labour market continues to strengthen. On the flip side, the January consumer confidence reading slumped to 120.2 (vs. 124.0 expected) from a downwardly revised 126.6 in December.

Outside the US, the data continues to support the idea that global economic activity is moderating. The eurozone macro surprise index (a measure of whether economic data is doing better or worse than anticipated) has fallen to -88 with the 200-day moving average -54, the lowest outside a financial crisis on record. The composite Purchasing Managers Index (PMI) fell to 50.7, the lowest level since July 2013. At this level, the reading suggests growth of just 0.1% quarter-on-quarter. In China, too, a slowdown seems to be continuing, with purchasing manager indices showing a contraction in manufacturing and official GDP figures indicating that economic growth has fallen to 6.6%, the lowest annual rate since 1990.

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31 January 2019

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