Stanhope Capital Fortnightly Bulletin

Period ending 15th September 2019

Tactical Positioning

Investor sentiment changed rapidly over the first two weeks of the month with the negative malaise of August being replaced by broader optimism. We have not made any major tactical changes, having maintained our faith in equity markets despite the increase in volatility, given that falling interest rates and additional monetary stimulus are likely to support prices.

Market Moves

	Equities *(incl. Dividends)*						
15 -Sep -19	World ($)	US ($)	Europe[1] (€)	UK (£)	Japan (¥)	EM ($)	Asia ($)
Last 2 Weeks	6.0%	5.7%	7.5%	4.5%	8.7%	5.8%	5.9%
Year to Date	18.2%	21.2%	20.0%	13.6%	10.3%	9.6%	12.0%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	Gold ($)	WTI Oil ($)	EUR	GBP	JPY	UST 10Y[3]
Last 2 Weeks	2.8%	-2.3%	0.7%	-0.3%	3.4%	-1.8%	+37 bps
Year to Date	4.3%	16.1%	20.8%	-3.4%	-2.0%	1.4%	-79 bps

Note: [1]Europe excluding UK; [2]Bloomberg Commodity Index; [3]US Treasury 10 Year Yield shows absolute, not percentage, change in yield; Source: Bloomberg

Equities across all regions rose in the first half of September with reduced trade war tensions and the announcement of further monetary easing in Europe providing a boost to sentiment. Japan led the rise, supported by a fall in the yen (which itself is associated with a rising risk appetite). US Treasury yields rose by 40 basis points as confidence recovered from low levels. US equities came close to a record high after President Trump announced he would push back the start date for higher tariffs on $250 billion of Chinese goods from October 1st to October 15th as a 'gesture of goodwill'. This prevents the new tariffs coming into effect on the 70th anniversary of the formation of the People's Republic of China and pushes back the date until after the next round of talks.

In response to falling inflation in the Eurozone, Germany being close to recession, trade war related risks and disorderly Brexit discussions, the European Central Bank (''ECB'') announced a fresh stimulus package of rate cuts and renewed quantitative easing (''QE''). The stimulus package announced by the ECB included reducing the deposit rate by a further 10 basis points from -0.4% to -0.5% and the restarting of QE in the form of bond purchases of €20 billion a month from November for an unlimited period until inflation expectations come 'sufficiently close to but below 2%'. The ECB also eased the terms of its long-term loans to banks and introduced a tiered deposit rate. The Central Bank also reduced its growth forecasts for the Eurozone by 0.1% to 1.0% for this year and by 0.2% to 1.2% for 2020. ECB President, Mario Draghi, warned governments that they needed to act quickly to revive slowing economic growth and placed pressure on them to take fiscal measures in the form of tax cuts and public spending. This implies that we may be reaching the limit of the extent to which monetary policy alone can boost economic growth in the region, particularly given the side effect of negative rates impairing banks' ability to raise profitability.

UK equities and sterling rose on news of Parliament passing a bill designed to prevent a 'no deal' Brexit. Despite the subsequent suspension of Parliament until October 14th, it is clear that the majority of parliamentarians are against Britain leaving the EU without some form of agreement. According to government officials, Boris Johnson's team has drawn up a detailed plan under which he would secure a deal with the EU at the forthcoming Brussels summit on October 17th, marking a decisive shift away from his 'no deal' hard Brexit stance and more in-line with Theresa May's withdrawal agreement.

Elsewhere in markets, gold fell slightly, in tandem with the positive sentiment in markets, and oil fell during the fortnight, but rose sharply following the end of the period under review, in response to the attacks on Saudi oil facilities over the weekend which knocked out half of the kingdom's production capacity.

Economic Update

In Europe, data continued to point to weakening growth. Eurozone industrial production for July was considerably below expectations at -0.4% (month-on-month) versus forecasts of a 0.1% decline. August Consumer Price Index readings for France and Germany remained at +0.5% and -0.1% respectively. In the UK, the Manufacturing Purchasing Manager Index fell to 47.4 in August from 48.0 in July. IHS Markit, which compiles the survey, attributed the fall in production to the political uncertainty and global trade tensions.

In the US, economic indicators released over the fortnight were mixed. The Institute of Supply Management Manufacturing Index fell to 49.1 in August from 51.2 in July, marking the lowest reading since 2016 as the New Orders component fell 3.6 points to 47.2 and the Production Index fell 1.3 points to 49.5. By contrast, the revised reading of the Purchasing Manager's Index improved moderately, rising to 50.3 from its initial reading of 49.9. In addition, the August reading of the Core Consumer Price Index came in higher than expected at +0.3% for the month of August versus expectations of 0.2%, which was enough to push the annualised rate to 2.4%, a post crisis high. The Conference Board Consumer Confidence Survey and the University of Michigan Consumer Sentiment Survey diverged to their widest point since 1969. Whilst differences in the survey components mean that this is not atypical, a wide divergence has traditionally signalled a recession, with the current spread pointing to a 30-40% risk of a recession over the next 12 months. (This, of course could be described more positively as a 60-70% chance of no recession in the next 12 months!).

In China, data continued to reveal signs that the economy is slowing in the face of US tariffs. China's GDP grew by 6.2% for the second quarter, its slowest growth rate for 27 years and the trade balance for August was $34.8 billion (versus $44.3 billion expected). This was largely due to an unexpected decline in exports which fell 1.0% year-on-year versus forecasts of a 2.2% rise. In addition, industrial output disappointed in August, rising by 4.4% year-on-year versus 4.8% in July and expectations of 5.2%, the lowest rate of growth since 2002, and manufacturing as measured by the Purchasing Manager's Index fell to 49.5 in August from 49.7 in July. In response, the People's Bank of China cut the reserve requirement ratio for some small and medium sized banks, which effectively should enable them to increase lending. Further stimulus is likely with China's premier Li Keqiang stating that an overall economic growth rate of 6% or more would be 'very difficult' in the current economic climate.

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IVO COULSON
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17th September 2019

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