Stanhope Capital Fortnightly Bulletin

Period ending 15th October 2019

Tactical Positioning

We wrote at the end of September that we believed that the US-China trade issues might be 'gently de-fused' and that this should provide some upside to Asian stock markets. Following a meeting of trade delegates, a 'partial deal' seems to have been achieved, improving investor sentiment across the board. The whole issue of disruption in trade has led Central Banks to hit the easing 'button' this year with interest rates falling in the US and elsewhere. This, in turn, has triggered interest in gold which tends to have an inverse correlation with falling rates. Whilst gold has recovered this year to $1500, it is still 18% below the high of $1770 achieved in 2012. Interest rates look set to fall further as Central Banks aim to prevent a possible recession and this could push gold back to its highs. With this in mind, we have increased our existing gold exposure across portfolios.

Market Moves

	Equities (incl. Dividends)						
15-Oct-19	World ($)	US ($)	Europe[1] (€)	UK (£)	Japan (¥)	EM ($)	Asia ($)
Month to Date	0.6%	0.7%	0.6%	-2.4%	2.0%	1.4%	1.4%
Year to Date	17.9%	20.8%	20.8%	11.5%	11.6%	9.3%	11.3%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	Gold ($)	WTI Oil ($)	EUR	GBP	JPY	UST 10Y[3]
Month to Date	0.9%	0.6%	-2.3%	1.2%	4.1%	-0.7%	11bps
Year to Date	4.0%	15.5%	16.3%	-3.8%	0.3%	0.7%	-91bps

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

At the beginning of October, equity markets declined after the release of poor manufacturing data in the US, before generally moving back into positive territory with the announcement of a partial trade deal between China and the US, as well as growing hopes of a possible Brexit deal between the UK and the European Union ("EU"). An impressive start to the US earnings season also helped lift markets higher. The UK was the worst performing developed equity market, largely hurt by a strengthening sterling, whilst emerging markets and Asia Pacific performed strongly, supported by a softening US dollar.

The likelihood of China and the US reaching an agreement prior to the planned increase in tariffs on 15 October initially appeared slim, especially considering the White House's decision to sanction another eight Chinese technology companies involved in China's surveillance of the Uighur minority group and rumours that US pension funds might be forced to limit their exposure to China. Relations between the two superpowers looked to take another turn for the worse when a tweet from the general manager of the Houston Rockets basketball team openly supporting protestors in Hong Kong led to the Chinese state broadcaster refusing to air any National Basketball Association ("NBA") games. Despite these obstacles, President Trump's meeting with Chinese Vice Premier Liu He in Washington delivered a 'phase one' deal, whereby the US agreed to suspend its planned increase in tariffs and China agreed to implement reforms covering intellectual property laws, financial market openness and foreign exchange transparency. Although the deal drove global equity markets higher, there was an overwhelming feeling that some of the critical issues had simply been kicked down the road.

A summit between UK Prime Minister, Boris Johnson, and the Republic of Ireland Prime Minister, Leo Varadkar, ended with a surprisingly optimistic joint statement that opened the door to a possible Brexit deal by 31s October.

Sterling rallied sharply and UK gilt yields jumped on the back of the news. Markets were caught off-guard, as the probability of either side softening their position on the question of the Irish 'backstop' had looked increasingly remote, particularly following an abrasive phone call between Johnson and the Chancellor of Germany, Angela Merkel. Not all details have been shared, but the plan includes Northern Ireland remaining legally part of the UK's customs union but part of the EU's customs union in practice, with rebates from the UK government available to Northern Irish businesses when duties are misaligned. At the time of writing, there remain several hurdles left to overcome before a draft Brexit deal can be reached, including Johnson convincing Northern Ireland's Democratic Unionist Party to agree on a deal designed around some form of border between Northern Ireland and the rest of the UK, traditionally not something they would ever countenance.

Elsewhere, the World Trade Organisation ruled that the EU handed over excessive subsidies to Airbus and the Trump administration swiftly introduced tariffs covering goods worth $7.5 billion on EU goods, including duties of 10% on aircraft and 25% on products such as cheese, wine and whisky. At home, facing the prospect of the fourth presidential impeachment inquiry in US history, President Trump made it clear in a letter to Speaker Nancy Pelosi that he had no intention of providing documents to the House of Representatives or allowing his staff to testify at any future hearing. His foreign policy proved to be equally contentious, with the President suddenly announcing the withdrawal of US troops from Syria, providing President Erdogan the pretext to send the Turkish army into Syria and overrun Kurdish positions. In response, the US sanctioned the Turkish ministers of defence, interior and energy, raised steel tariffs back to 50% and stopped negotiations on a potential $100 billion trade agreement.

Oil prices declined amidst growing fears about slowing global economic growth as well as a surprise build-up of US crude inventories.

Economic Update

On balance, economic data released in the US was disappointing. A dreadful Institute of Supply Managers (''ISM'') Manufacturing Index set the tone, coming in at 47.8 against 50.0 expected, the lowest figure since the Global Financial Crisis in 2009. This reading fell below even the most bearish economist's estimate on Bloomberg and, in the fine print, only three out of the eighteen featured industries reported growth. Most concerningly, it suggests a synchronised slowdown in global manufacturing following a continued period of negative readings in Europe and China. The picture was not improved by a weaker than expected ISM Non-Manufacturing Index, which came in at 52.6 against 55.0 expected. Notwithstanding, despite payroll figures falling short of expectations, by some 9,000, we note that the previous two months were revised upwards by a combined total of 45,000 and the overall unemployment rate fell to a 50-year low of 3.5%. The Federal Reserve ("Fed") reacted to last month's heightened volatility in the rate charged for intrabank loans (the repo rate), by initiating a new $60 billion monthly programme of Treasury Bill purchases. Jerome Powell, Chair of the Fed, stressed that this move was a technical adjustment and not a disguised round of quantitative easing as some observers have cautioned.

This side of the Atlantic, most final European Purchasing Manufacturers Indices ("PMI") were revised down. The focus was on Germany, where its Services PMI fell from 52.5 to 51.4, taking the composite PMI to 48.5, the first time Germany has had the lowest print out of the largest four European economies since the turn of the century. The UK was not immune to disappointment with industrial production decreasing by 1.8% year-on-year, the largest contraction since August 2013. Turning to Southern Europe, Greece issued €487.5 million of three-month debt at a yield of negative 0.02% - the country seems to have made great strides since it almost defaulted on its sovereign debt at the start of this decade.

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Important Information