Stanhope Capital Fortnightly Bulletin

Period ending 15th November 2019

Tactical Positioning

We have not made any major tactical changes in the last two weeks, having added exposure to infrastructure stocks at the beginning of the month. As we discuss below, equity market momentum continues to be favourable in the short term and we are maintaining our exposure to equities, resisting the temptation to take profits. Although the US equity market has risen sharply this year, it is worth bearing in mind that it fell 5% in 2018 even though company earnings rose by almost 25%. In many respects, 2019 has seen a re-rating of the market after a de-rating in 2018 and, as a result, the US market is no more expensive today in relation to earnings than it was at the start of 2018. Looking forward, a US-China trade deal, lower interest rates in 2020 and the prospect of a US Presidential campaign from President Trump, offering further tax cuts, may boost risk assets further.

Market Moves

	Equities *(incl. Dividends)*						
15-Nov-19	**World ($)**	**US ($)**	**Europe[1] (€)**	**UK (£)**	**Japan (¥)**	**EM ($)**	**Asia ($)**
Month to Date	2.4%	2.8%	2.4%	1.0%	1.6%	1.1%	1.0%
Year to Date	22.4%	26.0%	24.6%	13.3%	16.7%	12.2%	14.1%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	**Gold ($)**	**WTI Oil ($)**	**EUR**	**GBP**	**JPY**	**UST 10Y[3]**
Month to Date	-0.1%	-3.0%	6.5%	-0.9%	-0.3%	-0.7%	14bps
Year to Date	5.1%	14.5%	27.1%	-3.6%	1.1%	0.8%	-85bps

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

Positive gains across risk assets and fresh all-time highs in US equities concluded the fortnight. The strong results were mainly driven by signs of progress on the US-China trade deal, better-than-expected corporate earnings results and the dovish stance of central banks. Equity markets, especially in the US, seem to be enjoying the ride with the S&P 500 closing on Friday 15th November at a record level of 3,120 (notably, the pre-Global Financial Crisis record level back in October 2007 was roughly half this at 1,567). This concludes a straight six-week rise for US stocks, the longest such streak in two years.

Europe also saw gains across the board as the global manufacturing slowdown appears to be improving. As in the US, corporate earnings have supported markets, with companies in general surpassing consensus estimates for Q3 for both revenue and profits. Germany managed to avoid a technical recession as Q3 GDP growth came in at an unexpected +0.1%. The result led German finance minister, Olaf Scholz, to reaffirm his claims that there will be no fiscal stimulus in the near future, saying “We are cautiously optimistic. We will have bigger growth next year.”

Emerging Markets are particularly exposed to international trade and therefore benefitted from signs of progress on a trade agreement between the US and China.

The big story this fortnight was the sell-off in bonds, with 10-year Treasury yields up 23.1bps over the first week to reach 1.942%, their highest level since 31st July and nearly 50bps above the closing low of 1.457%

reached back in early September. It was a similar story elsewhere around the world; the 10-year German Bund yield rose 11.9bps, while the yield on the 10-year Japanese Government Bond was up 12.6bps. Notably, the rise in yields meant that countries such as France and Germany saw their 10-year and 20-year yields respectively return to positive territory, albeit just briefly. Another theme was the steepening of yield curves, with the difference between the US 2-year and 10-year yields rising to its highest level since July. The catalyst for the moves seemed to be the apparent trade war developments and renewed hope of a turnaround in economic data. The recent improvement in sentiment has seen investors lower expectations for further central bank easing; the implied probability of another US Federal Reserve cut in 2019 is now down to just 2%.

Improving market sentiment and investor appetite for risk-assets helped push gold prices lower, but still leaves the precious metal up 14.5% this year. Oil continued its rise fuelled in part by forecasts for a cold winter.

Economic Updates

Private equity firms are looking to allocate the large amount of money they have available to them in increasingly larger deals. This became evident in the latest transaction announcement by KKR, one of the industry's leading players. The potential buy-out of Walgreens Boots Alliance is shaping up to become the biggest-ever leveraged buyout, although, at a current market value of $56 billion and $16.8 billion of debt, both parties have admitted that the transaction is potentially not feasible given the amount of financing required.

Meanwhile, Saudi Arabia is currently preparing the initial public offering ("IPO") of shares in Saudi Aramco, although only 1.5% of the shares in the company will be available for outside investors, valuing the company at a staggering $1.6 trillion. This move will instantly dethrone Apple as the largest traded company by market capitalisation. Whether the IPO will be a success remains to be seen, as overseas investors have concerns about the security of assets after September's air assaults on Saudi oil installations, as well as corporate governance questions given the Kingdom's control of the company. Aware of the challenge, the Saudis are tweaking tax rates applied to the company as well as the proposed dividend pay-out in order to increase the attractiveness of the stock.

Over in Asia, it is worth taking note of Singles Day in China last Thursday. What started out as a festival celebrating 'singleness' by students in Nanjing, has been transformed by Chinese e-commerce giant Alibaba into the world's largest online-shopping spree. In the first hour alone, the retailer brought in an estimated $13 billion in sales, finishing the day with sales of $38 billion. By way of comparison, Black Friday sales in the US totalled just $6 billion in 2018. Such results demonstrate China's progress in transforming itself from a manufacturing-led economy to a consumer-led economy.

Lastly, an update on the UK. Like Germany, the UK managed to avoid falling into recession (UK GDP growth was +0.3% in Q3), but the global synchronised slowdown, as well as existing Brexit uncertainties, led to the slowest year-on-year GDP growth rate in almost 10 years. The Bank of England said they stand ready to lower rates should the economy slow further. On the bright side though, Chinese conglomerate Jingye decided to buy British Steel which will save some 4,000 jobs in the UK, although this is a subject to a long due diligence process. The announcement was made on Singles Day.

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19 November 2019

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