Stanhope Capital Fortnightly Bulletin

Period ending 30th November 2019

Tactical Positioning

Equity markets currently remain underpinned by high levels of liquidity being provided by central banks. As we look into 2020 there are also hopes of an upturn in the global economy based on some form of stand-off in the current trade situation. Despite sentiment swinging from optimism to pessimism and back, the general direction of travel seems to be towards a partial trade deal.

Turning to the UK, the general election might bring clarity to the direction of government and Brexit. A victory for the Conservative party, as currently predicted by the polls, may lead to a Brexit deal and a relief rally on the back of reduced uncertainty. Brexit will certainly bring disruptions and the negotiation of a trade deal is likely to lead to another bout of uncertainty but it is likely to be less confusing than the current range of alternatives! Some of our clients, particularly from overseas, have highlighted that there seem to be significant pockets of value in the UK. With this in mind, we are adding some UK equity exposure to a number of portfolios. Our interest is drawn to the FTSE 250, the 250 companies that sit just below the FTSE 100 Index in terms of market capitalisation. These companies tend to be relatively dependent on the UK domestic economy and currently stand on a 23% dividend yield premium to their 10-year average.

Market Moves

	Equities (incl. Dividends)						
30-Nov-19	World ($)	US ($)	Europe[1] (€)	UK (£)	Japan (¥)	EM ($)	Asia ($)
Last 2 Weeks	0.5%	0.7%	0.1%	0.8%	0.2%	-0.5%	0.0%
November	2.8%	3.6%	2.5%	1.8%	1.9%	0.6%	1.0%
Year to Date	22.9%	26.9%	24.8%	14.1%	17.0%	11.6%	14.1%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	Gold ($)	WTI Oil ($)	EUR	GBP	JPY	UST 10Y[3]
Last 2 Weeks	-2.4%	-0.3%	-4.4%	-0.3%	0.2%	-0.6%	-6bps
November	-2.6%	-3.2%	1.8%	-1.2%	-0.1%	-1.3%	8bps
Year to Date	2.5%	14.2%	21.5%	-3.9%	1.3%	0.1%	-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

The second half of November saw a continuation of the rally across most risk assets, albeit at a slower pace as investors awaited concrete developments in the US-China trade negotiations. There were no central bank policy meetings over the fortnight and limited major catalysts to rattle markets. The stabilisation of macroeconomic data, particularly Purchasing Managers Indices ("PMI's"), has helped calm markets. Indeed, investors appear sanguine going into December, with the VIX Index (a measure of volatility implied in S&P 500 options) close to multi-year lows. Given the disorderly bear market seen last December, a continuation would be welcome to many investors.

Trade negotiations between the US and China were the main focus over the fortnight although news flow centred around political chatter, briefings and speculation rather than concrete developments. On balance, there were market-friendly, tentative signs of progress. The Chinese regime announced that they would increase penalties for infringement of intellectual property rights (a key US demand) and China's Global Times newspaper stated broad agreement had been reached over the contents of a Phase One trade deal. Meanwhile, US tariffs of 15% on $156 billion of Chinese imports (expected to be cancelled as part of a deal) are due to come into force on 15th December.

The Hong Kong Human Rights and Democracy Act requires the US State Department to conduct annual reviews of whether Hong Kong is "sufficiently autonomous" to justify its special status with the US. It mandates the President to impose sanctions on those denying human rights in Hong Kong and stops applicants being blocked from receiving US visas on the grounds of involvement in pro-democracy protests. However, the lack of response from the Chinese regime suggests that the Act is unlikely to have any significant immediate or even medium-term effect. Given US interests in Hong Kong (including 1,300 US firms operating there according to the State Department), it is unlikely that their special status would be withdrawn. Hong Kong local elections showed rock-solid support for pro-democracy candidates who won 90% of the seats.

Closer to home, European politics remain at the centre of future uncertainty. In Germany, the left-wing SPD's leadership election produced a surprise result as two candidates from the left-wing of the party were elected leaders. They have announced they will be looking to "improve" policies and "perhaps loosen the black zero" - the rule that the federal government must run a balanced budget. Allowing deficit spending in Germany would likely be positive for risk markets. UK politics remains a battleground between opposing visions of the country, although all the main parties are agreed on the need for higher public spending, paid for through higher taxes and borrowing. It is impossible to know the outcome at this stage, as the electoral system makes it difficult to use national polls to get a seat by seat forecast of which of the marginal seats each party will win. That said, a hung parliament or a Conservative majority seem to be the most likely outcomes. Polls at the end of the fortnight had the Conservatives on a 6-15 point lead over Labour.

Monetary policy developments were limited over the fortnight. Christine Lagarde said in her inaugural speech as European Central Bank President that weak macroeconomic conditions in the Eurozone should be met with higher public spending by members' national governments. US Federal Reserve Chairman, Jerome Powell, stated that the Fed is "strongly committed" to maintaining 2% inflation, meaning we are unlikely to see a rate rise soon. For reference, US Core PCE (Personal Consumption Expenditure, the Fed's preferred measure of price inflation) is running at 1.6%.

Economic Updates

The stabilisation of macroeconomic data across the major economies was a source of reassurance for investors in risk assets over the period. In the US, manufacturing and services PMIs beat expectations and are now comfortably above 50 (indicating expansion). Also above market expectations, were retail sales and headline consumer inflation (CPI). Below market forecasts were core retail sales, core CPI, industrial production, housing starts, jobless claims, house prices and existing home sales.

In the Eurozone, we saw an improving trend with the German and Eurozone manufacturing PMIs above market expectations, although their services PMIs disappointed. Also coming in better than anticipated were Eurozone and German GDP growth, Eurozone industrial production, Eurozone consumer confidence and ZEW Economic Sentiment for the Eurozone/Germany. Below market consensus predictions we had Eurozone CPI and Eurozone/German composite PMIs.

UK data was generally disappointing, with GDP growth, core retail sales, services/manufacturing PMIs (both in contraction territory), industrial/manufacturing production, inflation, wage growth, house prices, the trade balance and public sector borrowing all coming in below market expectations. The limited bright spots included business investment, construction output and employment statistics which beat expectations (although these were less bad than expected rather than any real cause for optimism).

The only major Chinese data release during the fortnight was the manufacturing PMI, which came in slightly above forecasts, although only just in expansion territory.

JONATHAN BELL
IVO COULSON
LEO SUCH
3rd December 2019

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