Stanhope Capital Fortnightly Bulletin

Period ending 15th July 2021

Tactical Positioning

With many markets hitting new highs during the period, we continue to maintain our neutral to slightly overweight exposure to equity markets. However, we have turned cautious, short term, on committing new cash to equities as the corporate results season for Q2 2021, which is now upon us, may cause pause for thought as investors look beyond 2021 into 2022. Next year could bring more earnings growth but also some tax rises as the bills for Covid roll in. Overall, we remain positive on the outlook for markets, but the Summer could see some moderation in positive sentiment as trading volumes fall and central banks fall silent over the holiday period.

Market Moves

	Equities *(incl. Dividends)*						
15-Jul-21	World ($)	US ($)	Europe[1] (€)	UK (£)	Japan (¥)	EM ($)	Asia ($)
Month to Date	0.6%	1.5%	0.8%	-0.3%	-1.8%	-1.7%	-1.5%
Year to Date	12.9%	17.0%	16.1%	10.6%	3.9%	5.6%	5.2%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	Gold ($)	WTI Oil ($)	EUR	GBP	JPY	UST 10Y[3]
Month to Date	-0.4%	3.4%	-2.5%	-0.4%	0.0%	1.1%	-17bps
Year to Date	20.6%	-3.6%	47.7%	-3.3%	1.2%	-6.0%	39bps

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 obvious place to start isn't with markets, but football, because over the last few weeks it seemed to provide a break from Covid-related news, lifting spirits and enthusiasm across Europe. With an estimated 13 million pints of beer being sold in the UK on final day and a potential €4bn GDP boost in Italy following their victory, the hospitality sectors in both economies were standout winners. Meanwhile, Richard Branson was truly on top of the world with the world's first commercial trip to space with Virgin Galactic.

As we enter July, the second half of the year is unlikely to match the first half's achievements that included the strong 17% increase in the S&P 500, which rose for a fifth straight month in June. Equities have set new all-time highs in the US and Europe but have recently been subdued owing to growth fears and the spread of Covid's Delta variant. The equities of Covid-impacted companies have been struggling again, with the STOXX 600 travel and leisure index remaining on track for a 3rd consecutive monthly decline. Oil remains one of the top performing markets this year despite falling in July after discussions between the OPEC and the UAE resulted in the approval of increased supply.

Bond market movements have been interesting recently. In theory bond yields should rise as inflation increases, but this week, as US inflation rose to 5.4% year-on-year (up 0.9% in June), US 10-year yields fell to 1.30%, from 1.47% at the close of June. The marvel of this bond market behaviour reflects investors' beliefs that the current inflation is transitory.

Higher inflation may mean that loose monetary policies are gradually tightened, but this will only happen very slowly, as members of the Federal Open Market Committee (FOMC) have conflicting views on inflation risks. Fed Chair Powell emphasises that labour markets are nowhere near recovered and supply chain bottlenecks will soon unwind. The expected average inflation for the US over the next 10 years, based on market pricing, is 2.34%, up from 1.55% a year ago.

Equity market prices had a mixed reaction to the decline in bond yields: lower yields should improve the relative attraction of equities. However, the implied slowdown could damage earnings growth. Most major markets ended the fortnight up slightly but dipped materially on the 7th and 8th, around the time the increase in inflation was announced. The STOXX 600 fell 1.70%, with the CAC 40 down 2.00%, the US fall was smaller with the S&P 500 down 0.86%. Banks performed worst, as yield curves flattened. This growing anxiety around growth prospects hit most cyclical and Covid-sensitive assets the hardest.

Turning to central banks, the European Central Bank ("ECB") strategy meeting resulted in a new "symmetric 2% inflation target" over the medium term instead of "below, but close to, 2%". This is not the same as the Fed's flexible average inflation targeting policy, but it does give the ECB the flexibility to keep monetary policy looser as inflation increases.

Most major economies are beginning to benefit from vaccination programmes though there is still plenty of inconsistency across rollouts. The UK is easing nearly all Covid-related restrictions from Monday 19th July despite an increase in cases whilst in Japan, where infections are at lower levels, it has been decided that there will be no spectators at the Olympics. Eyes worldwide will be on the UK's hospitalisation rates as we test the waters of normality.

Economic Updates

In China, GDP growth has been slower than the 8.1% expected, at 7.9% for the year to the end of Q2 2021 probably owing to higher raw material costs and virus outbreaks. There was also evidence of the housing market cooling off which is a big driver in the economy. The People's Bank of China reduced the required reserve ratio for banks and spoke about other easings to support growth; something that might seem bizarre to European investors dreaming of these levels of growth. June consumer prices (inflation) in China underperformed expectations, at 1.1% year-on-year.

In Germany, numbers were mainly dreary. Although, the German Manufacturing Purchasing Managers Index ("PMI") was higher than forecast, factory orders were down 3.7% in May and industrial production fell, against an expected increase, whilst retail sales and the Services PMI underperformed forecasts. In the wider Eurozone however, data was more positive. Retail sales, along with all major PMIs outperformed expectations, as well as seeing unemployment falling to 7.9%, versus 8% expected. In the UK, all PMIs for June were above 60 (>50 is expansionary) and only manufacturing underperformed expectations. Inflation, as measured by consumer prices showed a 2.5% year-on-year increase.

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15th July 2021

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