Stanhope Capital

Stanhope Capital Fortnightly Bulletin

Period ending 31st August 2021

Tactical Positioning

Exposure to global equities continues to pay off with prices in August boosted by reaffirmation by the US Federal Reserve that they do not intend to raise interest rates in the foreseeable future. After a solid stock market rise, it would be easy to move into a 'profit taking' mindset, but 2021 is turning out to be a year of significant earnings growth which helps to justify the market increase. Although the pandemic saw a rapid move by companies to cut costs, they have been very cautious about adding costs back as the world unlocks and demand recovers. This has led to turbo-charged corporate earnings with forecast growth of 42% in the US in 2021 and 63% in Europe. Margins have also improved significantly. History shows that in periods when growth forecasts for corporate earnings are being continually upgraded, as they are now, equity markets tend to perform well.

Market Moves

	Equities *(incl. Dividends)*						
31-Aug-21	**World ($)**	**US ($)**	**Europe[1] (€)**	**UK (£)**	**Japan (¥)**	**EM ($)**	**Asia ($)**
Last 2 Weeks	0.8%	1.3%	-1.0%	-1.1%	0.4%	2.3%	1.5%
August	2.5%	3.0%	2.2%	2.1%	3.0%	2.6%	2.2%
Year to Date	15.9%	21.6%	20.1%	13.3%	3.2%	2.8%	2.0%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	**Gold ($)**	**WTI Oil ($)**	**EUR**	**GBP**	**JPY**	**UST 10Y[3]**
Last 2 Weeks	0.9%	1.9%	0.1%	0.1%	-0.8%	-0.4%	3bps
August	-0.3%	0.0%	-7.4%	-0.5%	-1.1%	-0.3%	9bps
Year to Date	23.0%	-4.5%	41.2%	-3.3%	0.6%	-6.1%	40bps

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 situation in Afghanistan and the resulting geopolitical tensions contrast with positive sentiments surrounding the Tokyo Paralympic Games. As far as markets are concerned, the key developments for investors have been the spread of Covid's Delta variant, which plateaued at the end of August, and Federal Reserve Chairman Jerome Powell's speech at the Jackson Hole Economic Symposium conference.

The week commencing August 16th had investors stuck in 'risk-off' mode, whereby riskier assets (equities and commodities) moved down, and safer assets (Treasuries and the US dollar) moved up. The reason was predominantly data releases implying the slowdown of China's economy and the spread of the Delta variant (which saw New Zealand go into lockdown over one case). It was also owing to concerns relating to the US Federal Reserve's stance on tapering. Investors had reason to be concerned because, on the 18th, the Federal Open Market Committee meeting minutes revealed that most officials supported the tapering (or reducing) of bond purchases (i.e. a reduction in economic support) by the end of this year. Investors were naturally concerned that this might be followed by an increase in the bank deposit rate.

By Friday 20th the S&P 500 was down -0.6%, Nikkei -3.4%, Euro Stoxx -1.5%, MSCI World -1.4%, and MSCI Emerging Markets -4.7%. The dollar rose significantly versus most major currencies and oil fell nearly 9%. US 10-year inflation expectations went down from 2.38% to 2.26%.

In Powell's subsequent Jackson Hole speech he made it clear that although such tapering of asset purchases may begin this year, he emphasised that tapering does not mean interest rate hikes are around the corner and that policy makers will not react to what he sees as only transitory inflation pressures.

As September approached, headlines switched to Afghanistan. The August 31 deadline for the supported evacuation held firm, and over 100,000 people were evacuated despite explosions outside Kabul's airport killing at least 100, claimed by ISIS. The crisis dampened investor sentiment but the impact on market prices was minimal.

Equity markets moved up in the last week of the month supported by a variety of factors: The Peoples Bank of China stated that they aimed to improve credit support for the real economy; COVID cases plateaued; there was positive vaccine news from Pfizer/Biontech which has received full FDA approval and positive indications from the US House of Representatives on the Democrats' plans for more fiscal spending. This backdrop of continued support through loose monetary policies continues to please markets. August closed with most equity markets up after a seven-month advance. The S&P 500 and the Euro STOXX 600 are both up by over 20% this year, although European equites were slightly lower over the fortnight. Gold was flat for the month and oil slumped, posting the biggest monthly decline this year.

The US corporate earnings season came to an end with over 86% of companies reporting earnings ahead of expectations with the highest earnings per share figures since late 2019. Cyclical stocks outperformed the market as they benefited from a stimulus fuelled economic recovery and there was no sign of margin erosion from increased input costs, although this is likely to filter through at some point.

Economic Updates

From the Euro area, inflation for August significantly exceeded expectations at 3.0% (the highest since November 2011). The unemployment level in Germany fell 0.1% to 5.5% and the Purchasing Managers' Surveys ("PMI") were strong at over 60, albeit slightly lower than forecast. Eurozone PMIs slightly underperformed too but also hovered around 60. The pace of growth in both the manufacturing and services sectors fell slightly from the preceding month but remained strong relative to historical levels. In the UK retail sales underperformed, but employment showed resilience with unemployment falling 0.1% to 4.7%.

In the US, the labour market is strengthening but is at risk of stalling on the Delta variant spreading. Jobless claims were slightly better than expectations at 358k but were a little higher than the previous two weeks' 353k and 349k readings.

In China, sentiment was knocked by weaker-than-expected August PMIs (indicating a slowdown in growth). Non-manufacturing PMI was below 50 (contraction) at 47.5. The manufacturing reading was 50.1 and the composite PMI was at 48.9. This is China's first sub-50 aggregate PMI print since February 2020.

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31 August 2021

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