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Global Market Strategy – August 2019

Goldilocks continues for the moment - despite Trump taunts to China

President Trump decided this week to taunt China. “We hold the cards”, he said.

Trump thinks the tariffs he has put in place on Chinese goods coming into the US has brought billions of dollars into the US economy, and that China is “dying to do a deal with me” because of the hurt being inflicted on the Chinese economy by the tariffs. Chinese exports to the US have fallen 8.5% in the first half of this year, as reported by the New York Times, however infrastructure spending in China has mitigated the reduction in exports.

Trump went onto boast that the US economy was doing brilliantly under his administration. True enough, when measured by the performance in the US stock market, the US is roaring ahead of other countries. The Dow Jones index has risen 4000 points this year, to 27,000, and the US president reckons the advance would have been even greater if the Federal Reserve had not caused a bear market during the fourth quarter last year.

True also that the US consumer is in a good place - at least the US consumer who is able to take advantage of US Stockmarket gains. It’s unlikely under current circumstances that the US will fall into recession, and yet there are plenty of sectors of the economy which are slowing, and for that reason the Federal Reserve cut interest rates yesterday.

There is an assumption that the dollar will weaken and so aid emerging markets (as a large percentage of their borrowing is in dollars). However, the dovishness of the Federal Reserve is prompting other central banks to return to or increase monetary easing, ie a reduction in interest rates or bond buying, or a combination of the two. “Don’t fear dollar strength”, Mohammed El Erian, chief economic advisor at Allianz, said this week. Despite the interest rate cut yesterday, US interest rates are still the highest of any country in the developed world, so the dollar will remain well supported.

Most stocks in the US are expensive but one that isn’t is Apple. The company reported its half year results on Tuesday and such is the market cap of the company, it alone pushed the Dow higher on Wednesday, rising more than 5%. For exposure to a currency that is holding its value, Apple is a place to start. The share price is up 828% over the last 10 years, 127% up over the last 5 and 37% higher year to date. The rising share price has shrunk the dividend yield which is now 1.4%. The share trades on a value of 19 times earnings which, compared to Microsoft at 27 times, Facebook at 33 times and Amazon at 79 times, is cheap. IPhone revenue may have been down 12% in the last quarter (at $31 billion) but Services were up 13% (at £11 billion). Total revenue for the quarter was just shy of $54 billion, and the company has over $200 billion in cash, part of which will be used to buy some of its own available shares in the market. Apple’s continual buy-back of its outstanding shares reduces the supply, the result of which camouflages the true success of the business. There is a concern among analysts as to exactly how Apple will replace revenue from declining phone sales. The likely success of the Apple Credit Card, going live to the public today, will address some those fears.

The UK’s Conservative party appointment of Boris Johnson as Prime Minister to replace Theresa May has given a mood of optimism to the UK which has not been present for many years. Theresa May never really got off the ground as PM, as it appeared she was too conciliatory to European leaders in the wake of the Brexit vote. There’s no question the UK has obstacles to overcome if the country does manage to finally exit the EU on October 31st, but the state of limbo in which the country has been for three years has done nothing for UK business or the UK economy. The fear of a no-deal exit however saw the pound down to its lowest level for two years. It is now at 1.22 to the dollar and less than 1.10 to the euro, indeed most forex rates for currency exchange are below parity for the pound/euro. There’s not much to recommend the euro either however, with growth moribund across much of Europe.

To be fair, Europe saw healthy economic expansion during the first quarter 2019, however the second quarter has been weak, especially the services sectors. Manufacturing also fared poorly, recording its worst quarter since Q1 2013, and there was a sharp fall in industry confidence. Nevertheless, unemployment has fallen to a decade low. Nominations of Christine Lagarde to President of the ECB, and Ursula Von Leyen to head of the European Commission, point to continuing French and German domination of influence in the region.

The ECB has said it will delay any interest rate hike until at least the second half of 2020 because inflation remains subdued (at 1.2%) and there is growing concern at the rate of growth across the Continent.

Investment prognosis still favours exposure to equities in favour of any other asset. Of course stock values are more expensive than they were 10 years ago but bonds are expensive (anyone for the Austria Century Bond at 1.2%, or a 10 year UK Gilt at 0.61%, or a 10 year German Bund at - (minus) 0.438%?), cash yields nothing and property is taxed out and illiquid. Above all, there is no euphoria. John Templeton, one of the most successful fund managers ever who died aged 95 in 2008, said "Bull **markets** are born on **pessimism**, **grown** on scepticism, mature on optimism, and die on euphoria". With China, the US Europe and the UK slowing, and US forced to make its first interest rate cut for 11 years, there is certainly no euphoria in stocks, and yet there is continual corporate stock buy-backs. Why would corporates buy back their stock at today's levels if they expected a significant downturn in equity prices? The US's Dow Jones index trades on 17 times earnings which is not excessive even though it is above the long term average of 15. China's Shanghai Composite trades on 14 and is the real long term growth story and major influencer of wider Asian success.

UK Technical

Confusion exists on the consequences of parents gifting or selling property to their children. A gift of property to a son or daughter is treated as a sale by the parents at full market value for capital gains tax purposes. Parents may be able to avoid CGT if the property was their main residence ('principal private residence relief'). If it is a straight gift and no money is paid by the offspring for the property, stamp duty land tax (SDLT) will be payable only if there is a mortgage attached to the property and the new owner assumes responsibility for it. SDLT is paid by the person who assumes responsibility for the mortgage, ie the transferee.

Favoured investment plays:

Nil risk:	**Cash**
Cautious risk:	AAA Corporate bonds
Balanced risk:	Managed / Multi-asset funds
Market risk:	UK equity
Adventurous risk:	**Asia, US equity,** European equity
Speculative risk:	**Technology, Healthcare, China, India, Other EM**

Disclosure:
Nicholas Chappell has the following personal investment exposure: Technology (including new energy, all US) 20%, China 7%, Asia 7%, Pharmaceuticals 3%, Global Equity 40%, UK equities 7%, US equities 9%, Emerging Market equity 7%,

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