

Go your own way

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Countries are falling out of love with each other just as Stevie Nicks and Lindsey Buckingham did before writing the track from which this week's blog takes its title. President Trump's wall at the southern border with Mexico, disagreement over which has left the US government in shutdown since 21 December, may become the enduring symbol of the trend towards national self-interest and protectionist policies at the expense of the international order. We should not get too downbeat however; integration between countries has fluctuated over time and, for us as investors, uncertainty over trade policy has contributed to some attractive valuation opportunities at the start of 2019.

This is not the first time we've seen a pullback from integration. Even today the level of foreign investment is not as high as it was at times during the 19th and 20th centuries: for example, only a third of the capital raised in the UK between 1865 and 1914 was invested in the UK itself, and a quarter of the world's stock of foreign capital in 1913 was invested in countries with relatively low per capita GDP compared to just 5% in 1997¹.

Now I may have my own view that pulling away from integration is imprudent: larger markets benefit us all economically and there are some problems which can only be tackled by cooperation between nation states. But this breakdown of international relations is no reason to get too downbeat. There is a natural ebb and flow of integration and separation and this is just the latest wave. Such an analogy may seem inappropriate given that the end of the last great 'wave' of integration coincided with – and some would argue helped cause – the events of 1914. While it is our job to think about these tail risks, a dire outcome like this is an extremely remote possibility, thankfully.

Trump and Xi are locked in negotiations after agreeing not to raise any further trade barriers against each other for a period of 90 days at the start of December. Talks between mid-level US and Chinese officials in Beijing concluded on Wednesday last week and so far both sides are making positive noises about the prospects for a deal. This is very important for markets, with the IMF warning of the impact of trade wars on global growth. Barring a very negative outcome – and by now the market should be used to President Trump's hyperbole – we should see some rejigging of the terms of trade and then life goes on.

Arm-wrestles over trade introduces frictions out of which emerge winners and losers. Our underlying managers are specialists in discerning genuine opportunities from things that only appear attractive at first glance, and hence together with them we continue to pay close attention to the investments in our portfolios. I received a note on Thursday last week from one of our European equity managers, discussing a logistics firm in their universe that could see headline revenue decline by approximately 2-3% as a result of reduced trade between China and the US, but has been penalised a multiple of this by the market and hence is now attractively priced.

While painful in the short term, volatility caused by geopolitical events creates opportunities for disciplined long term investors, just as the disintegration of the relationships within the band coincided with Fleetwood Mac writing one of the best-selling albums of all time. At today's level, equities are not expensive and hence we have been adding selectively in our portfolios.

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¹Ferguson, N., (2008). The Ascent of Money. A Financial History of the World. London: The Penguin Group.

Market Focus

- » Global equity markets moved higher on the week.
- » Economic indicators flashing red in some regions.
- » Brent Crude breached \$60 again, ending the week up 6% at \$60.6.
- » Gold rose 0.5% to \$1290.3 per ounce.

US

- » The federal government shutdown over the Mexican wall entered its third week and an estimated 800,000 federal workers have missed their first salaries of the year. President Trump's primetime address to the public failed to mobilise much support.
- » US stocks rose for the third week in a row with the major gauge rising 2.6%. Industrials performed well, and energy stocks were buoyed by a rally in oil prices. Healthcare and financials lagged behind.
- » Apple's chief executive Tim Cook announced a cut to revenue forecasts due to weak iPhone sales, particularly in the critical Chinese market. Apple's shares ended Thursday down nearly 10%.
- » US Core CPI, excluding volatile items such as food and energy, increased 2.2% year-on-year in December 2018, this was in line with forecasts.
- » US 10-year treasury yields ended the week higher at 2.7%, and credit spreads on corporates tightened.

UK

- » Jaguar confirmed it is cutting 4500 jobs, citing a lack of demand for diesel cars. The slowdown in China and ongoing concerns around Brexit have put pressure on auto stocks.
- » Large-Cap UK stocks increased 1.2% on the week.
- » PM Theresa May's authority was further undermined this week following two parliamentary defeats. These provided parliament with greater control over the timetable in the event of her Brexit deal being voted down and the ability to curb the government's power in the event of a no deal. The pound rallied 1%, as the likelihood increased that the UK's departure from the EU would be delayed past its March 29th deadline.
- » UK house prices rose by 1.3% in Q4 of 2018 compared with the same period last year.

Europe

- » In Germany, industrial production fell 1.9% in November following a drop of 0.8% in the previous month, putting it at risk of slipping into recession. The decline was led by the energy sector (-3.1%), consumer goods (-4.1%) and a fall in exports.
- » France also saw a fall in industrial production, declining 2.1%.
- » European equities rose 1.6% on the week buoyed by optimism over a breakthrough in the US-China trade war.

Rest of the World/Asia

- » Car sales in China fell for the first time in 20 years, declining by 6.0% in 2018.
- » Three days of trade talks between China and the US have made headway around energy and agriculture. The fact that talks have been extended for a day is seen as a positive step.
- » Japanese equities increased by 4.0%.
- » China's equity benchmark rose 1.9% with the yuan rising to a five-month high against the US dollar.

Past performance is not indicative of future returns.

Source: Bloomberg, returns in local currency unless otherwise stated.

Currency returns					
Asset class/region	Currency	Week ending 11 January	Month to date	YTD 2019	12 months
Developed markets equities					
United States	USD	2.6%	3.6%	3.6%	-4.9%
United Kingdom	GBP	1.2%	2.9%	2.9%	-7.1%
Continental Europe	EUR	1.6%	3.4%	3.4%	-10.2%
Japan	JPY	4.0%	2.4%	2.4%	-17.2%
Asia Pacific (ex Japan)	USD	4.1%	3.0%	3.0%	-13.8%
Australia	AUD	2.8%	2.3%	2.3%	-0.7%
Global	USD	2.8%	3.9%	3.9%	-8.1%
Emerging markets equities					
Emerging Europe	USD	2.7%	5.4%	5.4%	-11.9%
Emerging Asia	USD	4.0%	2.3%	2.3%	-16.4%
Emerging Latin America	USD	2.9%	9.9%	9.9%	-2.0%
BRICs	USD	3.5%	4.4%	4.4%	-14.4%
MENA countries	USD	3.4%	3.6%	3.6%	7.0%
South Africa	USD	4.0%	6.5%	6.5%	-18.2%
India	USD	-0.5%	-1.6%	-1.6%	-6.9%
Global emerging markets	USD	3.8%	3.7%	3.7%	-14.3%
Bonds					
US Treasuries	USD	-0.3%	0.0%	0.0%	1.4%
US Treasuries (inflation protected)	USD	0.2%	0.7%	0.7%	-0.1%
US Corporate (investment grade)	USD	0.3%	0.5%	0.5%	-1.6%
US High Yield	USD	1.9%	3.1%	3.1%	0.3%
UK Gilts	GBP	-0.2%	-0.1%	-0.1%	1.5%
UK Corporate (investment grade)	GBP	0.0%	-0.1%	-0.1%	-1.9%
Euro Government Bonds	EUR	0.2%	0.0%	0.0%	1.3%
Euro Corporate (investment grade)	EUR	0.1%	-0.1%	-0.1%	-1.2%
Euro High Yield	EUR	1.4%	0.9%	0.9%	-3.3%
Japanese Government	JPY	-0.3%	0.2%	0.2%	1.5%
Australian Government	AUD	-0.4%	0.1%	0.1%	5.7%
Global Government Bonds	USD	0.1%	0.5%	0.5%	0.0%
Global Bonds	USD	0.2%	0.4%	0.4%	-0.7%
Global Convertible Bonds	USD	2.0%	2.4%	2.4%	-4.8%
Emerging Market Bonds	USD	0.7%	2.3%	2.3%	-2.9%

Source: Bloomberg. **Past performance is not indicative of future returns.**

Currency returns					
Asset class/region	Currency	Week ending 11 January	Month to date	YTD 2019	12 months
Property					
US Property Securities	USD	4.9%	4.4%	4.4%	2.8%
Australian Property Securities	AUD	3.7%	3.8%	3.8%	3.7%
Asia Property Securities	USD	3.7%	4.4%	4.4%	-7.2%
Global Property Securities	USD	4.2%	4.4%	4.4%	-2.6%
Currencies					
Euro	USD	0.7%	0.3%	0.3%	-4.6%
UK Pound Sterling	USD	1.1%	0.9%	0.9%	-5.1%
Japanese Yen	USD	0.1%	1.2%	1.2%	2.7%
Australian Dollar	USD	1.4%	2.3%	2.3%	-8.6%
South African Rand	USD	0.9%	4.0%	4.0%	-10.2%
Swiss Franc	USD	0.3%	0.0%	0.0%	-0.8%
Chinese Yuan	USD	1.6%	1.7%	1.7%	-3.9%
Commodities & Alternatives					
Commodities	USD	2.7%	5.0%	5.0%	-5.8%
Agricultural Commodities	USD	0.5%	1.6%	1.6%	-4.7%
Oil	USD	6.0%	12.4%	12.4%	-12.7%
Gold	USD	0.5%	0.7%	0.7%	-2.4%
Hedge funds	USD	0.7%	1.7%	1.7%	-7.0%

Source: Bloomberg.

Past performance is not indicative of future returns.

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