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# Global Market Strategy – August 2017

## *No need to change bullish equity strategy…*

US stocks continue to trend higher, despite worries over high valuations.

If you didn't have exposure to the US, or were wisely diversified away from it, you experienced as lacklustre a July performance as June's.

"Ignore US equities at your peril" was the headline in one financial periodical last week, and judging by the way US futures indicate the trajectory for US stocks at the start of August, you have to agree the author has a point.

Bond yields are rising, financials' stock prices are rising, the oil price is rising, earnings are growing, interest rates are low, the dollar is weakening, China is growing, employment is (for the most part) strong. This is a good background for the markets to continue moving forward, and especially for emerging and international markets outside the US to gather some momentum.

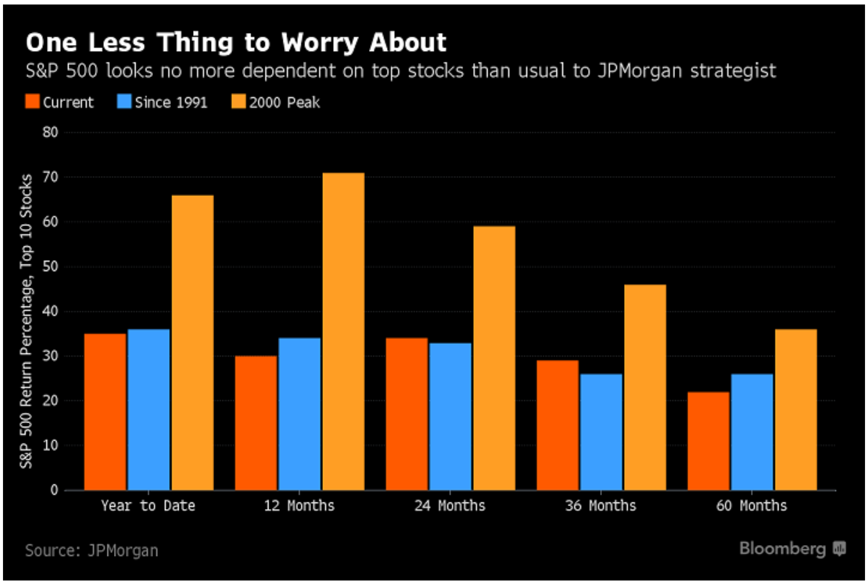
US earnings for the last two quarters have been particularly strong. Earnings grew 16% for the first quarter and currently, with about 70% of companies having reported, earnings growth for the second quarter are on track for 12% growth, which is about 4% higher than expected. Much of the growth can be attributed to the weaker dollar (falling because of weakening expectation of imminent interest rate rises by the Fed) but a weaker dollar should now boost those international economies where there is greater value in stock prices.

The stronger euro has diminished for the time being the attraction of European equities but there is much to be positive about on Europe. Unemployment fell in the Eurozone during June to its lowest level in eight years. Inflation picked up to a four year high of 1.3% in July, although wage growth is noticeable by its absence. It is reckoned that inflation will move to a maximum over the next two years of 1.5%, far short of the ECB's target rate of 2%, and therefore although the ECB seems set to taper its asset purchases, interest rate rises by the Bank are a long way off.

Another player for the equity bulls is China. Far from experiencing a hard or soft economic landing either of which would have an impact on overseas earnings to those exporting there, China's construction industry reported solid numbers for the last two months, suggesting greater resiliency to the supposed sluggish world economy, and the figures were supported by a healthy purchasing manager's index at 51.4 and an even healthier construction sub-index at 62.5, the highest since December 2015. Nicole Elliott, independent technical analyst who writes for the Financial Times, sees bullish indications for Chinese shares from the Chinese Securities index, the CSI300, below, and helpfully for a market which has been a rollercoaster since the build-up to the global financial crisis, the Shanghai A Shares index is, at 7%, at its lowest ever level.


***Shanghai A Share Index, 10 years (Source [BigChart.MarketWatch.com](BigChart.MarketWatch.com))***

One of the real dilemnas is that there are too few quality stocks to take the cash awaiting investment. It sounds scary that only a few stocks are responsible for most of the gains but the key question is: "Are we in an aberrational period relative to the past, or is this merely business as usual?" The answer to that question comes from JPMorgan's Dubravko Lakos-Bujas. He found it to be be overstated. The data showed the **10 stocks adding the most to the index this year accounted for a combined 35 percent of its advance**. This was in line with the 36 percent average for five-month time periods since 1991 and far below the 66 percent when stocks peaked in 2000 (see below chart courtesy of JP Morgan and [www.ritholtz.com](www.ritholtz.com)).




The last week or so must have been a big deal for those who recently bought a new diesel car, possibly encouraged to do so by a UK government which just a few years ago endorsed diesel as the cleaner driving option. Now the UK government is to ban petrol and diesel cars from 2040.

Clearly, the future is Electric. VW and BMW may have more experience in building cars, but Tesla has more experience of building electric cars and last week delivered the first production run of its new more affordable Model 3 electric car to its own employees. The $35,000 entry level car contains a battery with a range of 218 miles, while the more expensive $44,000 version has a range of 310 miles. Breaking the 300 mile barrier is a game-changer, even though it takes the best part of an hour to fully charge. The big deal for the UK is now ensuring there are more charging points, and ensuring the charging points are not broken. A new recharging infrastructure is being rapidly developed across the UK, and it is worth noting that the government provides financial support for consumers to install a charge point at their home premises via the Electric Vehicle Homecharge Scheme which will cover up to 75% of the total costs.

**Favoured investment plays:**

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|---|---|
| Nil risk: | USD cash (in preference to Euro cash) |
| Cautious risk: | AAA Corporate |
| Balanced risk: | Managed / Multi-asset funds / Long-Short Absolute Return funds |
| Market risk: | UK, **European equity** |
| Adventurous risk: | **Japan, Asia, Germany,** US equity, UK/European/US smaller company sector |
| Speculative risk: | Water, Technology, **China, India, Other EM** |

**Disclosure:**

Nicholas Chappell has the following personal investment exposure: Technology (US) 15%, Global Equity 18%, US smaller cos 2%, (Other) US equity 8%, UK equity 5%, Germany 5%, (Other) European equity 9%, India 5%, (Other) Asia 18%, Pharmaceuticals 9%, Energy 1%, Precious metals 5%



McLaren Asset Management, S.L. Regus Business Centre, Ricardo Soriano 72, 29601 Marbella, (Malaga), Spain
McLaren Wealth Management UK Limited. Abbotsmere, Tilford, Farnham, Surrey GU10 2DD