Global Market Strategy - February 2018

- ***US equity tide is turning but no panic yet***
- ***Dollar weakness to propel Emerging Markets***

At last, an equity market bump in the road! Until January 29th, the start of the year had been the best ever for shares. The 1-2% falls each day across all markets during the 29th and 30th were a welcome relief to those concerned markets were verging on the euphoric. There was a small rally for equities on the last day of the month but the hiccup gives good pause for thought.

There is a lot going on now and a lot to take in. US equities have been steadily rising since March 2009 but with 13.7% projected S&P500 earnings growth and 7.4% revenue growth, gentle inflation, gradual interest rate rises, healthy employment, low wage inflation and a much weaker dollar, why shouldn't they continue? There is a warning signal appearing in US Treasuries, with the 10 year at 2.73%, edging closer to 3% in anticipation of higher US interest rates but even there, if corporate earnings are maintained, share values could justifiably carry on appreciating. For sure, 3% Treasury yields will attract many investors following the extended equity bull market but if that takes some heat out of the stockmarket, increases volatility and steadies already subdued inflation, that is a good result all round.

The US dollar is obligingly weakening (the dollar index has fallen steadily and rapidly as investors believe Donald Trump's infrastructure and tax projects are not as inflationary as first feared) and the help a weaker dollar is providing to Emerging Market and Commodity related companies is facilitating broad global growth.

Gold, which has rallied from the high 1100s to the mid 1300s, has staged a predictable rally but its lack of yield and a dearth of geopolitical upset has seen it largely shunned in favour of fund inflows into European and Asian equities in particular, together with a continued sprinkling into the US and UK stock markets 'for fear of missing out' ('FOMO').

Predictably, financials are attracting further investment in the current forward-looking rising interest rate environment (as banking margins can increase if lending at higher rates is possible), hence combined with commodity exposed businesses, the FTSE100 benchmark index has shown some signs of life early this new year but generally, with continuing uncertainty around Brexit and a stronger pound, many UK corporates will struggle to make much share price headway in 2018.

Japan is turning the corner on inflation, just, but weaker dollar good news for emerging markets is not such good news for a resultant stronger yen. Japanese stocks, like those of Europe, are undervalued and have plenty of catch-up in them but they'll find things tough in the current exchange rate environment.

This time of year in the UK sees those eligible scurrying to understand changing pension legislation and how much of a contribution they can make before the end of the tax year to take advantage of generous government tax breaks. For those who had in place already a personal pension in some form three years ago and whose 'net relevant earnings' are of a level to support it, the maximum contribution which could be made before April 6th 2018 is currently £160,000 gross, using 'carry forward' of prior year unused allowances. Although the flexible pension rules brought in by George Osborne in 2015 have been revolutionarily generous in their flexibility, the detail of their complexity has led many to sleepwalk into problems, typically by continuing to fund their pension when they might have ceased and been able to apply for a larger Lifetime Allowance than the current £1.030,000, or more commonly, by thinking they can begin to draw an income from their pension and later still be able to fund it. The latter circumstance triggers the special Money Purchase Allowance Allowance of just £4,000 future annual gross pension contributions in order to prevent 'recycling' back into the pension fund in order to benefit again from tax relief.

The beauty of the new Flexible Access Drawdown pensions in the UK is the ability to pass unused funds on death to Dependents, Nominees or Successors. In this regard it is important to ensure a Nomination Form or Expression of Wish is reviewed regularly, preferably once a year, to ensure pension fund owners either haven't changed their mind or their circumstances haven't changed. Ideally, any grandchildren considered, should be named rather than referred to as a class (such as 'my grandchildren in equal shares') although of course this will not be possible if they are as yet unborn. It is particularly important that pension funds are distributed by a deceased's executors (or more specifically are requested to be distributed by a deceased's executors) within two years of the date of death, otherwise tax free benefits where the deceased died before age 75, or (preferential) taxed benefits where the deceased died after age 75, will be lost. Currently, one in four of those who die with Flexible Access drawdown pensions lose the flexibility associated with their pension because of delays or ignorance in the execution of their affairs by their executors.

US dollar Index, one year (Source: BigCharts.com)

Pound / Dollar exchange rate, one year (Source: BigCharts.com)

NYSE Bitcoin Index (INDEX), one year (Source: BigCharts.com)

Favoured investment plays:

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 (including new energy, all US) 32%, Global Equity 17%, US smaller cos 2%, (Other) US equity 7%, Germany 5%, India 4%, (Other) Asia 12%, Pharmaceuticals 15%, Cash 6%

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