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Global Market Strategy – October 2018

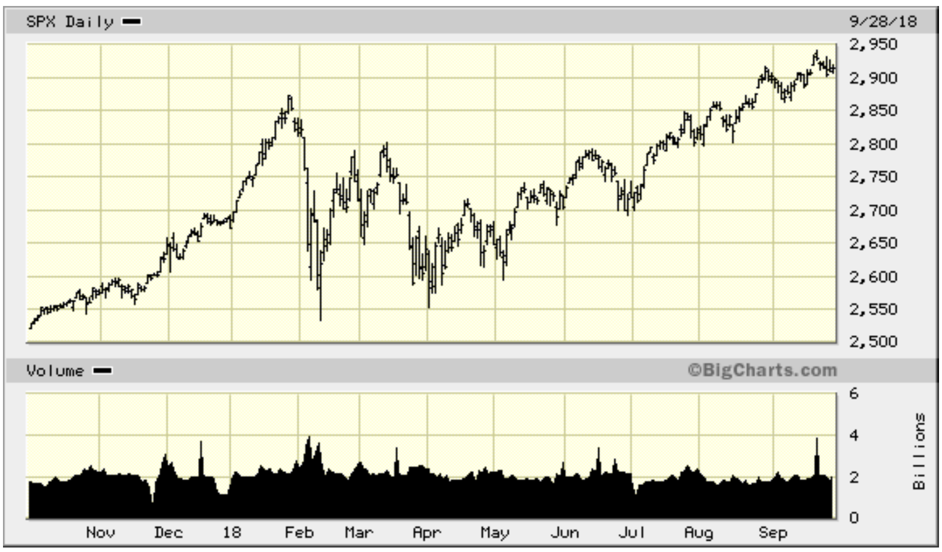
- ***US Fed removes "accommodative" from September statement***
- ***2 year Treasuries get strong bid at 2.86%***

Federal Reserve chairman Jerome Powell told the markets last week in his September statement that effectively interest rates are now, at 2.25%, in a sweet spot of where they should be, given the current state of the US economy.

"We see no great risk of inflation to the upside", Powell stated. "We see very good signs in the economy but it's not perfect", which is why the Fed removed from its statement the word "accommodative". There is no need anymore for the Central Bank to give a helping hand to the economy by doing a little extra to help it.

Powell also indicated that although the dollar is a matter for the Treasury, the Federal Reserve is keeping an eye on it. Economic (and technical) data is supporting the case for further stockmarket rises on the back of further corporate investment and strong earnings and outlook, and strong growth will equal higher rates, but the Fed is attempting to suppress enthusiasm for stocks by saying that too strong a dollar will hurt trade. The economy may be comfortable on the high wire now but keep looking straight ahead. This explains the muted reaction of the market following the chairman's statement and is not surprising given US indices reached new all time highs during the last week of September.

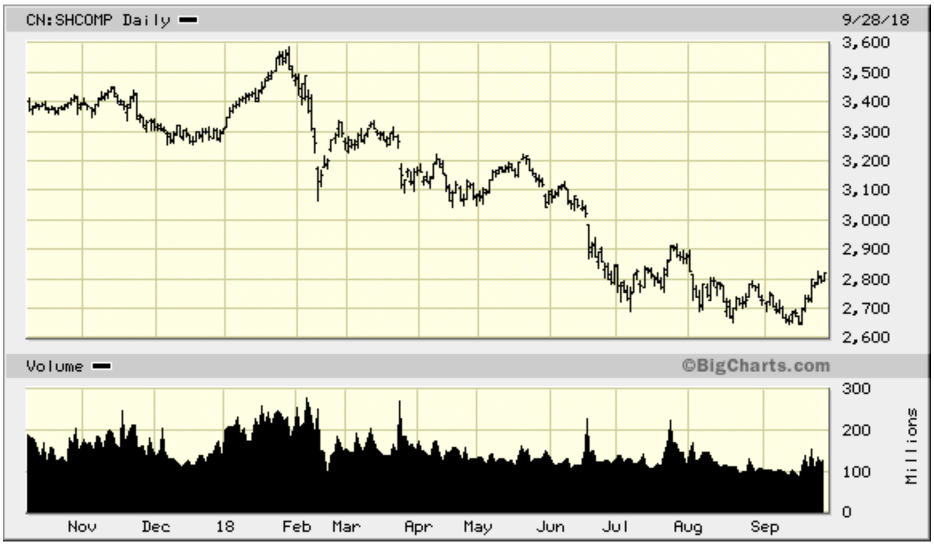
Suddenly, US Treasuries are getting bid again. You couldn't be seen buying bonds over the last 12 months if you wanted to maintain self-respect but with the 2 year treasury at 2.86% - where it was when Lehman fell in 2008 - and at a level at or slightly above the rate of inflation, this particular bond is proving attractive, although the more attractive it looks, the more costly it becomes.



S&P500 Index, September 30th 2018 (Source: BigCharts.com)

Emerging Markets have seen an uptick during the second half of September. It's a small rally over a short period of time but it may carry weight now the dollar index has moved below 100 on the back of weakened expectations of continual US rate rises. The fact the market now can see a halt to rate increases is likely the reason for the dollar index backing off, even though, as alluded to earlier, there will be a need for the occasional rate rise next year as US unemployment touches 3% and threatens wage inflation. It is fancifully possible that markets could experience nirvana, where the dollar weakens during continued US market strength, where US corporate tax cuts are used predominantly for investment overseas, which stimulates European and emerging market growth.

MSCI US$ Emerging Markets Index, September 30th 2018 (Source: BigCharts.com)



Shanghai Composite Index, September 30th 2018 (Source: BigCharts.com)

The UK market has little to recommend it in the current Brexit environment. Even the FTSE250 mid-cap index which looked undervalued and overlooked a few months ago has fallen into the same trough as the headline index. There are undoubtedly good companies in which to invest, with good yield and cashflow, but the ETF route is a no-no.

FTSE250 Index, September 30th 2018 (Source: BigCharts.com)

Technical

The UK's annual personal pension contribution allowance of £40,000, which is reduced by £1 for every £2 over the Adjusted Income figure of £150,000 subject to a maximum reduction of £30,000, has caught out many working individuals, according to latest reports from Her Majesty's Revenue & Customs (HMRC). Those falling foul of the allowance limit in the last tax year doubled from the previous tax year to nearly 19,000, and those who breached the then Lifetime Allowance for a pension fund of £1.25m for 2016/17 allowed HMRC to collect more than £100m in tax via the Lifetime Allowance Charge (25% on the excess if taken as income, 55% if taken as a lump sum).

Few people realise that the UK tax regime is very lenient if allowances are used in the right way. Only tax-preferential jurisdictions such as the UAE, Singapore, Hong Kong, Bermuda, the Channel Islands have more tax-light laws than the UK, and even when the UK's numerous allowances are fully used, there still exists the opportunity to defer paying tax for 20 years through skilful use of onshore and offshore Single Premium Bonds. These 'Bonds' are not traditional debt instruments, they are tax 'wrappers' which don't give rise to capital gains tax on movements within them, fall under income tax rules when chargeable, do not give rise to a tax charge on dividend income, can be segmented to provide encashment flexibility, can be assigned to mitigate tax and perhaps help adult children, are simple to administer and thus are widely used for estate planning. For those UK residents who have used their pensions allowance, their Individual Savings Account allowance, their capital gains allowance, perhaps even their tolerance for higher risk EIS and VCT investment, Single Premium Bonds are worth consideration.

Favoured investment plays:

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

Disclosure:

Nicholas Chappell has the following personal investment exposure: Technology (including new energy, all US) 38%, UK Equity 7%, US smaller cos 3%, (Other) US equity 18%, India 4%, China 4%, (Other) Asia 13%, Pharmaceuticals 13%

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