TPO Investment Market Update

Brexit in the balance; Biden in the chair; Vaccinations at last

10th December 2020

From a UK perspective, all eyes are on the Brexit deal, or rather the lack of it! After some 4 1/2 years of negotiating, we seem to be no nearer than we were at the outset to achieving the deal. At the time of writing there are 22 days left and outside of the negotiating room it is virtually impossible to call the outcome (probably in it as well!). As commented before, a no deal will spell bad news for sterling and much of the domestic market in the short term. A deal will probably see an increase in sterling and a boost for (UK) markets. The point here, from an investing perspective, is that we are not in the gambling game and portfolio construction is not based on a heads we win, tails we lose basis. Diversification is the key and whatever the outcome, our focus is on creating well balanced portfolios with exposure to both UK and Global assets of all classes, essential for solid, long term growth.

Globally, of course, Brexit is a relatively minor local skirmish and the real news is the arrival of Covid-19 vaccines. The 8th December will go down in history as the first fully tested and authorised Covid-19 vaccine on the planet was administered in the UK. Not even Brexit can spoil this party as we all look forward to a return to relative normality in 2021.

In the US, markets have reacted well to the President elect. Even a split government (in the event of Biden failing to gain control of the Senate) may not be a bad thing and history would suggest that markets actually prefer compromised governments. Perhaps, in these environments, business can get on with business without too much political hindrance.

But now is a time to celebrate and put 2020 behind us as we see light at the end of the tunnel.

US

Joe Biden officially secured enough electoral votes to become President following California's certification. Meanwhile Georgia's secretary of state, Brad Raffensperger recertified the state's results and confirmed that Biden has won the state.

Further fiscal stimulus may be on the horizon with a new package expected to be signed off as early as next week. The proposal includes relief of $288bn to small businesses, $180bn in local state funding and $17bn to the airline industry which continues to struggle with the fallout of the pandemic.

President Biden has also made the astonishing promise of 100 Million Vaccinations in his first 100 days in office.

On the economic data front, we saw the unemployment rate fall to 6.7%, however October nonfarm payroll data missed consensus expectations with the slowest pace of growth recorded following the lifting of lockdown restrictions.

EU

Infection rates in Europe continue to fall with the weekly average rate trending downward after countries imposed lockdown restrictions. France has seen daily cases fall from 50,000 to 10,000 while Belgium, who a few months ago was one of the worst impacted countries, now has the fifth lowest infection in Europe.

The ECB are looking to implement a more targeted stimulus approach which is set to include a continuation of the PEPP (Pandemic Emergency Purchase Programme) which is an asset purchase programme structured around buying both private and public sector securities.

We urge you to stay safe and remember that your TPO advisers are here to guide you through this storm. If you have any questions or concerns, please do get in touch.

The value of investments can fall as well as rise. You may not get back what you invest.

UK

A vaccine from Pfizer has been approved by the regulators for use in the UK. The vaccines were rolled out earlier in the week and based on current estimates there will be enough to vaccinate 20 million people with each individual expected to receive two shots.

We've seen a 30% fall in infection rates on the back of lockdown measures imposed, however; it will be key to monitor this figure as lockdown measures have been (somewhat) lifted and the Christmas holidays are fast approaching.

The OECD predicts the UK economy will shrink in 2020 by 11.2%, followed by growth of 4.2% and 4.1% in the next two years which, among major economies, only Argentina is expected to do worse. This is following the largest GDP drawdown the UK economy has experienced since the 1970's (see Figure 1.)

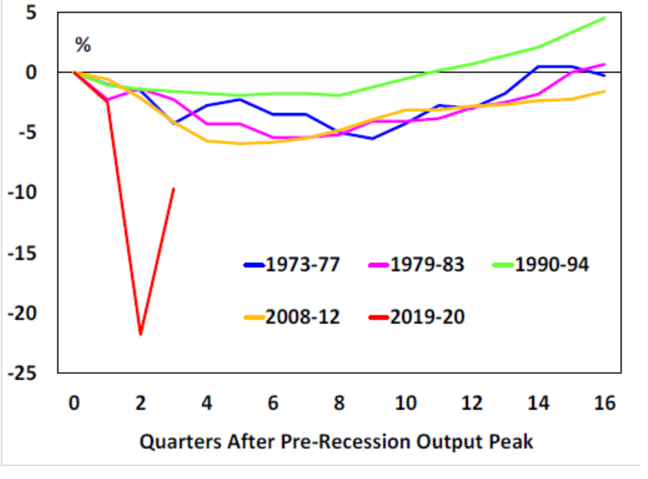

Figure 1. Change in level of real UK GDP in recessions and recoveries, 1970-2020 (source: The Bank of England)

Hopes that the UK and the EU would strike a post-Brexit trade deal have faded as disagreements persist on fishing rights, state aid and free movement policy. It is hard to discern what is media posturing and what is reality but Clément Beaune, the French minster for Europe warned that France would veto a deal that did not align with French interests.

CHINA

Manufacturing PMI data rose to 52.1 in November which is its ninth straight month of staying in expansionary territory and further evidence of China's recovery. Meanwhile foreign ownership of the countries Government bonds continues to attract demand with foreign investors now owning 9.6% of Chinese debt.

The US labelled four more Chinese listed companies as state sponsored entities and having links to China's military, which means US investors are now unable to trade these securities. This included the China National Offshore Oil Corporation; whose shares fell 14.0% on the news.

More broadly US regulators look to continue their scrutiny on Chinese listed stocks with the House of Representatives approving legislation that could force US-listed Chinese companies to delist if an accounting regulator is not allowed to review their audited accounts.

Light at the end of the tunnel

Following the positive news of the vaccine development we have seen three-week capital inflows to global equities reach a high not seen since 2005 on the back of positive sentiment (see Figure 2.). This was also supported by improvements in the forecast of company earnings over the next two years.

Figure 2. Three-week global equity capital flows

Corporate earnings are expected to rebound with most countries returning to 2019 levels by 2021. That said we have seen the growth expectations tempered in Europe and the UK as the uncertainty of Brexit continues to dampen investor optimism. Conversely, if a deal is done, expectations will rise.

At the other end of the scale, we do see Asia ex-Japan and Emerging Market companies expecting the greatest earning growth rate with a 18% and 14% increase respectively. There are a few factors which are driving this forecast most notably a falling dollar value, China's continued expansion (which will benefit those trade dependent economies) and that most countries in region seem to have the pandemic under control.

Let us hope the light in the tunnel is not an approaching freight train!

Earnings rebased	2019	2020	2021	2022	Share price performance year-to-date
US	100	84.5	103.3	120.5	9.7%
Asia ex-Japan	100	98.7	118.3	137.3	9.9%
Euro area	100	58.4	85.7	102.1	-6.8%
UK	100	55.0	75.9	89.9	-16.5%
Switzerland	100	91.0	101.9	112.5	-2.4%
EM	100	93.4	114.5	132.7	5.9%
Developed markets	100	83.2	103.8	119.8	6.3%
Global	100	84.4	105.2	121.9	6.3%

Note: Consensus estimates for 2022
Source: Refinitiv Datastream, UBS, as of 11 November, 2020

Figure 3. Forecasted earnings (2019-22) Please note: Such forecasts are not a reliable indicator of future performance.

TPO Portfolios

As predicted in last month's bulletin, November proved to be a spectacular month for all of our Portfolios. All of our main styles (Passive, Managed and ESG) achieved impressive returns with each of the 12 models performing better than their benchmarks with Passive IV almost producing a double digit return of 9.72% in the month!

In relative terms, Managed II was the star performer achieving 7.12% compared with the benchmark of 4.8% (ARC Sterling Balanced Asset PCI TR).

Against some pretty tough markets, all of our ESG portfolios enter December positive for the year to date.

Season of goodwill

As we cast our thoughts back over what has been a tumultuous year for everyone, and assuming no ill headwinds in December (whilst always a dangerous assumption!) we move into 2021 with positive hopes of a clear pathway out of the pandemic and the higher level of certainty that will produce making for a calmer, more compassionate and, hopefully, more sustainable future.

Let us never forget the hard work of all of those who have strived to improve global health this year and we look forwards to communicating again with you in 2021.

Our Investment commentary is not designed as specific individual advice, and should you have any questions or concerns please do contact your TPO adviser or contact us via the website, email or telephone. More information can be found at www.theprivateoffice.com.

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