FOR PROFESSIONAL ADVISERS ONLY

Market Update

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SQUARE MILE
INVESTMENT SERVICES

Investors have benefited from a further quarter of strong returns with the FTSE All Share index climbing by 3% and the MSCI World index surging 6.5% higher. This leaves most equity indices up well into double figures over the year so far. Bond markets also contributed to the quarter's returns with the average UK government and investment grade corporate bond delivering a useful percentage point or two of return. Doubts are mounting about the sustainability of the pace of global growth and markets continue to be buoyed by expectations that central banks will act to stimulate economies by cutting interest rates. The pound weakened noticeably in the foreign exchange markets, suffering from the ongoing Brexit uncertainty.

Although the UK economy continues to grow, there are increasing signs that the Brexit conundrum is beginning to weigh. While a no-deal Brexit situation is widely considered to be bad for business, in many ways the lingering uncertainty with the overhang of a no-deal Brexit is even worse. Understandably, businesses are loath to commit to large scale investment plans and the longer this situation continues, the more damage will be done to the economy's health. Theresa May's resignation may allow a path to a solution, but the fundamental issue remains that Parliament and the Nation are both spilt on the issue. There is a risk that the current Brexit deadline of October 31st will have to be extended.

Strong market gains

President Trump's ongoing trade spat with China has been a further negative. Tariff rates on Chinese imports have been increased as Trump tries to force the Chinese to renegotiate their terms of trade. The issue is also complicated by America's strategic desire to protect its technological lead. Over recent years there have been a series of cyber attacks which have been rumoured to have originated in China. The US is becoming increasingly uncomfortable sharing technology as a price of accessing the vast and rapidly growing Chinese market. We have always been a little sceptical about Chinese willingness to bend far on these trade issues. The ratcheting up of US tariffs is beginning to impact the profits growth of a number of US firms. At the moment, this is unhelpful rather than a serious concern and we are pleased that the flagging trade talks have been kept alive by Trump. This is something that we will have to keep an eye on.

Tensions in the Gulf are also escalating as President Trump extended sanctions on Iran. Unsurprisingly, Iran has reacted by restarting its nuclear programme. Sanctions are already having a severe effect on the Iranian economy and tightening them will increase the risk that the Iranian leaders will lash out in desperation. Already there have been attacks on oil tankers in the region's busy shipping lanes. Thankfully, the strategic importance of the Gulf has diminished a little, thanks to the recent surge in US oil production. New techniques have been developed to unlock oil trapped in rocks deep underground and remarkably, America now produces more crude oil than Saudi Arabia.

The lingering effects of the global credit crisis 10 years ago makes the economic outlook very uncertain and the gathering pace of technological advances are having a profound impact on many businesses. This perhaps is most evident in the nation's high streets, but technology has changed the face of many other businesses operating in areas such as the media, travel and postal services. This brings great challenges for investors but also it brings opportunities.

Markets have advanced a long way this year, principally because expectations of higher interest rates have flipped to expectations of cuts. This reflects the weakening growth outlook in the main developed economies. In the short term, we do not see much further stockmarket upside from here. After all, interest rates can only be expected to fall so far. We are mindful, however, that markets often benefit from the emergence of 'good news' as we enter the run up to the US Presidential elections which take place next year. Hence, while we remain cautious after such a strong run, a positive surprise may arise which could push markets higher.

Important Information