Autumn

Market outlook.

Brought to you by the Investment Management team at my wealth
WEALTH at work

Written by Peter Quayle & Jonathan Wiseman, Fund Managers, **my wealth**

The UK Economy

For the first time in over 10 years, the Bank of England's monetary policy committee (MPC) voted to raise interest rates on Thursday 2nd November to 0.50%, from 0.25%. This was widely anticipated as inflation reached 3% in September, the highest reading in over 5 years and 1% above the MPC's 2% target.

Inflation has been steadily rising following the Brexit vote last year which has put pressure on the value of the pound and increased the cost of imported goods. Whilst the MPC expects imported inflation to peak in the coming months, they anticipate domestic inflationary pressures to gradually pick up as spare capacity in the economy is absorbed, additionally, with unemployment is at a 42 year low, they anticipate a recovery in wage growth.

The MPC factors two more interest rate rises into their projections, although at present, the market is not expecting another until September 2018 and the implications of this rise are yet to be measured. As a result, the next step is anything but certain and in time, this rise could prove to be a policy error, if for example the consumer does not have the capacity to absorb the extra interest burden on their debt and with business investment hindered by Brexit, the outlook for employment is uncertain.

Following their decision to abolish the spring budget, the UK government will set out fiscal policy in its first autumn Budget on Wednesday 22nd November. The Budget focuses on domestic policy, however, internationally, Brexit negotions have continued to make headlines with both sides apparently unwilling to soften stance on policy and demands, and so it is still uncertain how the UK will ultimately separate from the European Union, some terming the choice of outcomes hard or soft Brexit, regardless of the term, the way we depart will have different consequences for the economy.

The Japanese Economy

Japan has had a tough year in terms of core data, with GDP missing expectations, inflation present but lagging expectations, and real wages floundering. That being said, October has seen a rally in Japanese markets ahead of (and immediately following) the snap election called by Prime Minister Abe. With Abe's popularity dropping and the rise of Tokyo Governor Koike's 'Party of Hope', Abe used the short term buoy in his ratings (off the back of his reaction to the North Korean frictions) to bring forward the election by a year to September 2017. The results saw Abe win a two thirds majority (a Super Majority), meaning that he now has the power to push through policy changes and make

constitutional changes. This is key both in terms of Japan's national security and for domestic level policy. The question that now remains is whether the Japanese market has run too hard off the back of the election result, as in reality nothing has changed. With the likelihood of Abe now focussing on pushing ahead with a further sales tax hike, military spending likely to increase considerably, fiscal spending stagnant and the Bank of Japan still 'sitting on its hands' in terms of policy development, a decline in real wages and continually faltering inflation are likely to hinder the economy in the foreseeable future. It is more than feasible that these factors will weigh on markets into 2018 once the election euphoria dies away.

The Emerging Markets & Asia Economy

The Asian and Emerging Markets have been the strongest performing equity markets year to date, in sterling terms, and have proved remarkably resilient. There are still pockets of turmoil in certain countries, such as Brazil's corruption scandals, and Mexican Peso and leadership uncertainties. That being said, both of these countries have elections in mid to late 2018 at which stage there will be more clarity on political and economic progress/potential. For the most part, there are still many positives in these asset classes. October saw China's Communist Party Congress, held every 5 years, at which top party leaders are appointed. The biggest move by the party saw them elevate the status of President Xi Jinping, allowing him an extended and unchallenged stay in power, writing his name into the constitution; making him the most powerful Chinese leader in decades. This can be seen as a strong long term positive for the markets, as the announcement of a Chinese 40 year growth plan and integration with global trade, broader economics and politics will likely see it continue to develop strongly. Hand in hand with this, India's transformation under its Prime Minster Narendra Modi continues to go from strength to strength, as we have seen not only major steps to cleanse India of its 'black-market economy' via demonetisation and the introduction of an efficient sales tax system (Goods and Services Tax), but the strong relationship with Japan has seen the first pieces of infrastructure laid for a Bullet Train. The train is a big move on infrastructure spend and is designed to increase trade and employment mobility between Mumbai and Ahmedabad. It is yet another statement of intent by Modi's government. With all of this in mind, and looking at valuations in the Emerging Markets and Asian regions compared to the rest of the world, there continues to be immense opportunity relative to other key equity asset classes running into 2018 and over the longer term.

The US Economy

By its own standards, the past quarter has been relatively muted both politically and economically in the US, seeing the market slowly begin to gain an element of stability. With this in mind there are still political shadows overhanging the US both in terms of North Korea, which appears to have partially calmed for the time being, and indeed the probe into Russia's involvement in the 2016 presidential elections. In the immediate future it appears to be the latter that is holding up policy drives on taxation, a stumbling block to allow a strong drive into 2018 for the domestically focussed businesses, employment, consumption, and ultimately inflation! Whilst US valuations look high compared to historical averages, the current climate can be seen to be agnostic of this due to the distorted nature of the fundamentals, with inflation still low, wage growth in need of a stronger pick up, and of course unemployment data needing to settle at a more sustainable level. With all this in mind, and with Donald Trump's policies likely to develop going into 2018, it is the Federal Reserve Bank (Fed) that is coming to the fore with Trump to announce the new Fed Chair at the beginning of November. Given the stock markets propensity to price in events early, this appointment is key for markets. As, a Fed chair that is 'hawkish' could cause global markets to pull back over expectation of a sharper interest rate rise cycle. With expectation of Jerome Powell to be Trump's appointment, his known 'Dovish' stance could give the market the breathing space needed to allow for tightening labour market data and increasing inflation, thus allowing new policy traction and growth in domestically focussed corporates.

The European Economy

The summer has seen an abundance of events in Europe, so deciphering what is just 'noise' has been critical. Catalonian independence has been one of the larger concerns amongst European markets, comparing Catalonia to the Scottish referendum. However to put things into perspective, the two events, whilst similar, are not the same. Catalonia is not a country but rather a region within Spain that has historically been granted autonomy. The referendum that was held in October was against constitutional law enabling the Prime Minister Mariano Rajoy to block the result, giving the separatist movement opportunity to only declare independence illegally. At the end of October Catalan Leader Carles Puigdemont was ousted by Rajoy shortly following Puidgemont declaring Catalonian independence. Whilst Catalonia separating from Spain would be a big hit to the European project, this friction has been going on for decades, and with the government taking a hard line, loosely backed by the European courts and European Central Bank, a separation seems unlikely, leaving this friction as merely 'noise' in the market. Spain aside, we have also seen another setback for the anti-establishment parties in Europe, seeing the German elections reseat Angela Merkel as Chancellor, and whilst we await the formal outcome of the coalition, 'more of the same' is expected from German politics going forward. It has become apparent that this has all been noise, presenting buying opportunities. So, that leaves only expectation of what the European Central Bank (ECB) is set to do going forward. With the head of the ECB, Mario Draghi, stating on October 26th that they will be maintaining the 'open ended' nature of their current policies (no winding down of Quantitative Easing) and remain accommodative, when coupled with attractive valuations in many parts of the asset class on a relative basis, European markets appear to have a strong perch going into 2018.

Fixed Interest

Following some 'hawkish' comments from the Bank of England in recent months, there is still uncertainty surrounding their longer term plans for an interest rate rise cycle. Whilst there has been a recent 0.25% rate increase, this is likely to be isolated rather than the signalling of a sharp rate rise cycle, with any more rate adjustments being data dependent. With this in mind, rates are likely to be lower for longer. This is compounded by uncertainty around the Fed's leadership and interest rate cycle, and the ECB's recently unchanged tact on monetary stimulus. With this uncertainty and money still awash in the system, coupled with valuations and opportunity remaining strong in many equity markets, equities continue to appear better value. This is compounded when you look at the strong year credit has had in 2017, and with spreads continuing to tighten, opportunity in the asset class is difficult to find. Correlations between bond markets and equity markets remain stronger than historical averages, suggesting corporate debt still offers a better opportunity set than government issuance.

Contact us

0800 028 3200

www.wealthatwork.co.uk/mywealth

@_mywealth

mywealth@wealthatwork.co.uk

The opinions expressed are those held by WEALTH at work at the time of going to print and are subject to change. This material is not, and should not be considered by the reader as a recommendation to the acquisition or disposal of investments and is not investment advice. WEALTH at work and my wealth are trading names of Wealth at Work Limited which is authorised and regulated by the Financial Conduct Authority and is a member of the Wealth at Work group of companies. Registered in England and Wales No.05225819. Registered Office 5 Temple Square, Temple St, Liverpool, L2 5RH. Telephone calls may be recorded for operational and training purposes.

my wealth
WEALTH at work