JOHN RAISIN FINANCIAL SERVICES LIMITED

Independent Advisors Report

Market Background October to December 2019

The period October to December 2019 was clearly positive for world equity market as a whole. Not only did the MSCI World Index gain over 8% (in $ terms) but both the major developed and other markets experienced a clearly positive quarter. A crucial factor was renewed optimism regarding US-China trade relations progressively developing over the Quarter. The US S&P 500 index gained 9%, while the MSCI EMU Index (which tracks the largest companies in the Eurozone) was up 5% (in Euro terms), the FTSE All Share gained 4% (in £ terms) and the Japanese Nikkei 225 gained approaching 9%. In contrast to the July to September Quarter this Quarter saw significant gains for the MSCI AC Asia (exc Japan) Index and the MSCI Emerging Markets Index which both saw gains (in $ terms) of over 11%. In contrast, the major Government Bond yields rose (and prices consequently fell).

The S&P 500 advanced from 2,977 at the end of September to close at 3,231 on 31 December 2019. At the end of its 29-30 October 2019 meeting the Federal Open Markets Committee (FOMC) again lowered the federal funds rate (its main interest rate) by 0.25% to 1.5 to 1.75%. At the press conference following the October meeting Chair Jay Powell stated *"Today we decided to lower the interest rate for the third time this year…..weakness in global growth and trade developments have weighed on the economy and pose ongoing risks. These factors, in conjunction with muted inflation pressures, have led us to lower our assessment of the appropriate level of the federal funds rate….In both July and September, we reduced the target rate [range] for the federal funds rate by ¼ percentage point, and we did so again today…"* Chair Powell however then went on to indicate that this would likely be the last rate change in this cycle although he did state (as he had at the September press conference) that *"Policy is not on a preset course."* At the meeting of the FOMC which concluded on 11 December 2019 the committee unanimously voted to retain the federal funds rate at its existing level.

Trade tensions between the US and China clearly eased during the Quarter. On 11 October President Trump announced a preliminary Phase 1 deal including suspension of threatened tariffs. On 12-13 December both sides announced significant progress on Phase 1 including that new tariffs set to start on 15 December would be indefinitely postponed. The S&P reached a (then) new closing high of 3,169 on 13 December.

The US consumer appeared confident but business less so. Chair Jay Powell at his December Press Conference summarised the US economy as follows – *"Household spending has been strong, supported by a healthy job market, rising incomes, and solid consumer confidence. In contrast, business investment and exports remain weak, and manufacturing output has declined over the past year. As has been the case for some time, sluggish growth abroad and trade developments have been weighing on those sectors. Even so, the overall economy has been growing moderately."*

Inflation continued its long trend of running clearly below the Federal Reserve's 2% target. US inflation as measured by the Personal Consumption Expenditures (PCE) Index (the US Federal Reserve's preferred inflation measure) was 1.4% in both October and November, and 1.6% in December. Core PCE which excludes food and energy was 1.6% in October, 1.5% in November and 1.6% in December. US unemployment which had reached another fifty year low in September 2019 of 3.5% remained at the same level at December 2019. The University of Michigan Surveys of Consumers indicated very positive consumer confidence with a clear increase since September and levels above those at the end of June 2019.

Eurozone equities had a positive Quarter with the MSCI EMU index advancing 5%. This was doubtlessly aided by the positive developments in US-China trade relations as well as greater clarity over the exit of the UK from the EU, together with the implementation of further monetary policy loosening (quantitative easing) and better than expected economic growth reported for the third Quarter of 2019 (July to September).

The meeting of the Governing Council of the European Central Bank (ECB) on 12 September had, in view of continuing low inflation and to support expansion of the Euro area economy, taken a number of decisions to loosen monetary policy including reducing the deposit interest rate by 0.1% to minus 0.5% and the reintroduction of quantitative easing with effect from 1 November 2019. The two Governing Council meetings held during this Quarter (24 October and 12 December) reaffirmed the policy decisions of 12 September and quantitative easing was restarted on 1 November at the rate of asset purchases of 20 billion Euros per month.

Eurozone unemployment which had fallen to 7.5% in June 2019 (its lowest level since July 2008) fell further to 7.4% in December. Other economic indicators appear less positive however. While the headline inflation rate increased from 0.8% in September to 1.3% in December it remains well below the ECB policy objective of below, but close to, 2% over the medium term. Additionally, based on the five year, five year inflation swap market investors anticipate inflation of little more than 1.2% by the mid 2020s. While the eurozone grew by 0.3% in the July to September Quarter which was above expectations the initial data released, on 14 February 2020, by Eurostat (the EU statistics Directorate) indicated that the Eurozone grew by only 0.1% in the final Quarter of 2019. As in the previous Quarter the German economy, the largest in the Eurozone and a major centre of manufacturing demonstrated clear signs of faltering.

The FTSE All Share advanced by 4% over the Quarter. While the internationally focussed FTSE 100 was up by approximately 3% the more domestically focussed FTSE 250 advanced by over 10%. Share prices – particularly the FTSE 250 – progressively advanced at the same time that events in British politics resulted in reduced uncertainty about the future relationship between Britain and the EU with the passing of the EU Withdrawal Bill in October and the victory of the Conservative party at the December 2019 General Election. The FTSE 250 advanced by 6% in two (working) days following the General Election. The actual future relationship between the UK and EU is, however, far from settled and 2020 may well see “cliff edge” negotiations and deadlines.

Unemployment, according to the Office for National Statistics (ONS), fell to 3.8% for the period October to December 2019 its lowest level since 1974. The ONS also reported that *"For the first time since March 2008, real regular average weekly earnings exceeded the highest level reached before the economic downturn (2008 to 2009)."* Other economic news was not so positive. The ONS reported that Gross Domestic Product was flat during the October to December Quarter with increases in services and construction offset by poor performance from manufacturing. Consumer Price Inflation (CPI) fell from its September level of 1.7% to 1.5% in October and November, and 1.3% in December compared with the Bank of England (BoE) target of 2%.

The November and December Monetary Policy Committee (MPC) meetings of the Bank of England voted to maintain Bank Rate at 0.75%. At both meetings, however, two external members voted for a reduction to 0.5% citing concerns over the economy and (low) inflation.

It was a clearly positive Quarter for Japanese equities with the Nikkei 225 advancing by 9%. As not only a major world trading economy, but an economy with close trading links with both the US and China, Japan benefitted from the thaw in US-China relations with a clear upward trend in the Nikkei 225 apparent after the announcement of the preliminary Phase 1 arrangement between the US and China in October 2019.

At both its 31 October and 19 December 2019 meetings the Bank of Japan again continued its policy of huge monetary policy stimulus. This included maintaining interest rates at minus 0.1%, together with a target of *"around zero percent"* for 10 year bond yields and major ongoing asset purchase operations. Despite huge monetary stimulus since 2013 Japanese Core CPI inflation has remained well below the 2% target. It did however reach 0.7% in December 2019 up from a 2019 low of 0.3% in September. December 2019 also saw the Japanese Government announce a fiscal stimulus to repair typhoon damage, improve infrastructure and invest in new technology.

Asia (excluding Japan) and emerging market equity markets enjoyed a positive Quarter. The MSCI AC Asia (exc Japan) Index and the MSCI Emerging Markets Index both saw gains (in $ terms) of over 11%. The positive progress in US-China trade talks was clearly a major positive and a weaker US$ another.

Chinese growth (as reported by the China National Bureau of Statistics) was an annualised 6% in the October to December Quarter the same rate as for the July to September 2019 Quarter. Chinese growth in 2019 was the lowest since 1990. In November China's central bank slightly reduced benchmark lending rates. This was seen as a reaction to slowing economic growth.

The easing of trade tensions which was a major feature of the Quarter resulted in a greater appetite for risk as demonstrated by the clear advances in equity valuations. In contrast major Government bonds suffered as equities and high yield bonds were favoured by investors. The US 10 year Treasury Bond fell in value as its yield increased from 1.66 at the end of September to 1.92 at the end of December. The 10 year Gilt yield – also influenced by less uncertainty around Brexit and the Conservative Election victory – rose from 0.49 to 0.82. The German 10 year Bund yield rose from -0.57 to -0.19.

In Conclusion the October to December 2019 Quarter was heavily influenced by the clearly positive turn in US-China relations. Again, continued loose monetary policy provided both economic support and support to markets. Equity valuations are however high and the additional tools available to the major central banks to support the economy and markets in a downturn are somewhat limited. Fiscal policy which could provide further economic support has not, however, yet been widely applied.