Wealth Management
Weekly Market Update

Published 1 September 2020

Market Update

US equities climbed +1.4% last week with, major indices setting new record highs, as US Federal Reserve Chairman Jerome Powell announced a shift in how the Fed views inflation, saying it won't increase interest rates to respond to low unemployment levels and also won't worry as much about low rates triggering a rise in prices. The dovish speech boosted risk assets at the expense of safe haven assets, with the US 10Y Treasury yield closing the week at 0.721%, up 9.3bps. European equities were up +0.2%, while Global and Emerging Market equities both returned +0.8%. Japanese stocks fell -1.3% as news of Prime Minister Shinzo Abe's resignation emerged. Abe, who has served longer than any other prime minister in Japanese history, is resigning due to health conditions. UK equities fell -0.6%, as the export heavy FTSE 100 was pressured by Sterling, which touched an eight-month high against the US Dollar. The Dollar had fallen in the aftermath of Jerome Powell's speech. UK 10Y Gilts yields ended the week at 0.311%, up 10.5bps. Gold fell -0.6%, now trading at $1,989 per troy ounce. Oil prices also fell -0.1%.

UK Stocks	US Stocks	EU Stocks	Global Stocks	EM Stocks	Japan Stocks	Gilts	GBP/USD
▼ -0.6%	▲ +1.4%	▲ +0.2%	▲ +0.8%	▲ +0.8%	▼ -1.3%	▼ -1.2%	▲ +2.0%

all returns in GBP to Friday close

Macro News

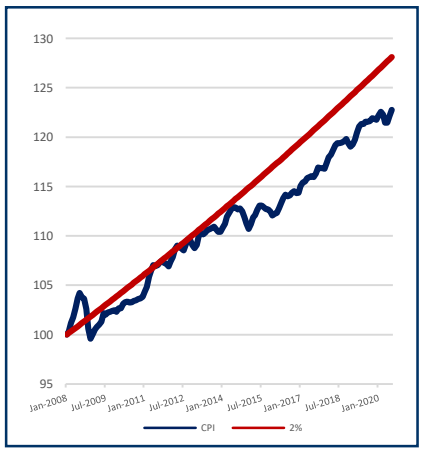
- At the Jackson Hole symposium, the Federal Reserve adopted a flexible average inflation target that could see inflation 'moderately' above its original 2% target. The Federal Reserve hopes to shift inflation expectations higher. There is some evidence it has worked as 5-year, 5-year forward inflation expectations rose to the highest level since 2019 on Friday.
- Firms now have to share the cost of furloughed workers' wages with the government. Employers contribute 10% of salary from today, with the government providing 70%. In October firms will be required to pay 20%. As firms are required to contribute increasing amounts between now and the end of the scheme, a rise in the rate of redundancies is likely.

The Week Ahead

- May and June delivered an all-time high growth in two-month payrolls. July, whilst slowing, beat expectations. US nonfarm payrolls data for August is released this Friday. Consensus expectations are that 1.40 million jobs were created last month, down from 1.76 million in July.

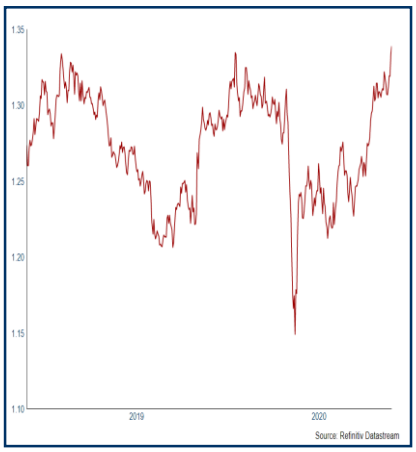
Week in Charts

Fig1: US Inflation Against 2% Growth



US CPI has consistently been lower than the Federal Reserve's 2% target since the beginning of 2008. With the shift towards an average inflation target, lower-for-longer interest rates and rising inflation expectations could see this trend reverse. This would mean inflation being allowed to 'run hot' moderately above its 2% target for some, as yet unclear, time.

Fig 2: Cable Exchange Rate



The Pound has surged close to its December high against the US Dollar, close to $1.35. The US Dollar weakened materially on Thursday after the Federal Reserve's comments implies rates will remain lower-for-longer in the United States. As interest rates fall this tends to lower foreign demand for a currency and thus lower the value.

View From the Desk

In a decision for the history books, the US Federal Reserve, the world's de facto central bank, abandoned a hard 2% inflation target in favour of a more flexible regime, attempting to prevent deflation resulting from secular stagnation exacerbated by the persistent COVID-recession.

Over the short and medium term, this is good news for investors and risk assets, as markets, still disconnected from the real economy, were eager to see more monetary stimulus. The Fed is widely expected to follow with more expansive policies in September, most of which, however, might already be priced in.

Over the long term, however, "slow money" investors are troubled, as high debt, sluggish growth, low capital expenditure, a depreciating currency, yield curve tampering and inflation-feeding measures strongly echo the painful story of Japan. On the road to Japanification, attempts to stoke inflation are an inescapable stop. Is failure as inevitable?

While the mechanics between Japan, a surprisingly "closed" economic ecosystem, and the US, the world's most open consumer economy and owner of the global reserve currency, are as prodigiously different as are their chances of success, investors can't help but wonder if these moves are band-aids, signs that the global economic order is in grave need of an overhaul. Until such time as this question is answered, we expect investors to be careful, suspicious of recoveries and overall growth lethargic and uneven. In other words a repetition of the last decade when fiscal initiatives gave way to constant monetary stimulus as means to keep the world chugging along. And the question is not simply whether stocks and bonds can keep growing while ignoring real economy pains, but rather can quantitative easing, which worked under an ailing economic system, continue to boost risk assets under a possibly failing one.

David Baker, CIO

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