STONEHAGE FLEMING

# GLOBAL EQUITY PERSPECTIVES 14 DECEMBER 2020

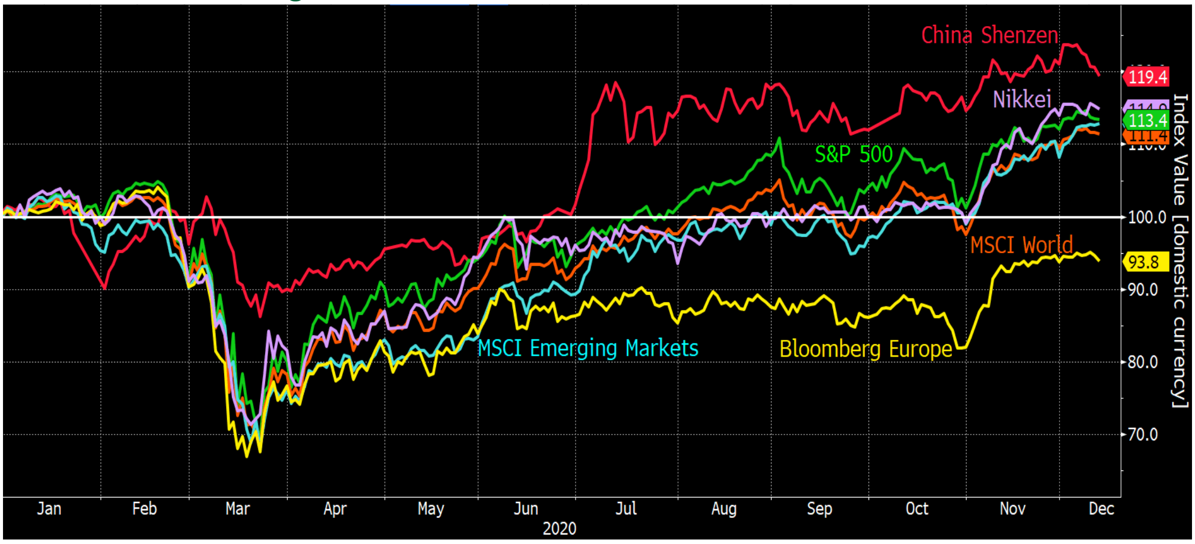
*"Nothing is more noble, nothing more venerable, than loyalty."*

*Marcus Tullius Cicero*

## 1. WHAT A YEAR

2020 was probably the most extraordinary year for most investors. Despite the experiences of 1987, 2000 and 2008 few, if any, were prepared for 2020. The global virus crisis (GVC) caught everyone by surprise, with no idea how its effects could pan out. Many commentators presented stock market scenarios of W, U and even L-shape economic outlooks. Those with a V-shape view were by far in the minority.

Regional Stock Market Indices – 1 Jan 2020 = 100




The minority view seems to be winning the bet currently. After only six months since the start of the GVC all the major stock market indices, apart from Europe, were in the black for the year. China is today up almost one fifth, with all of the S&P 500, Emerging Markets and Nikkei indices up in double digits.

S&P 500 Sector Indices – Indexed to 100 at S&P 500 Peak in Feb 2020

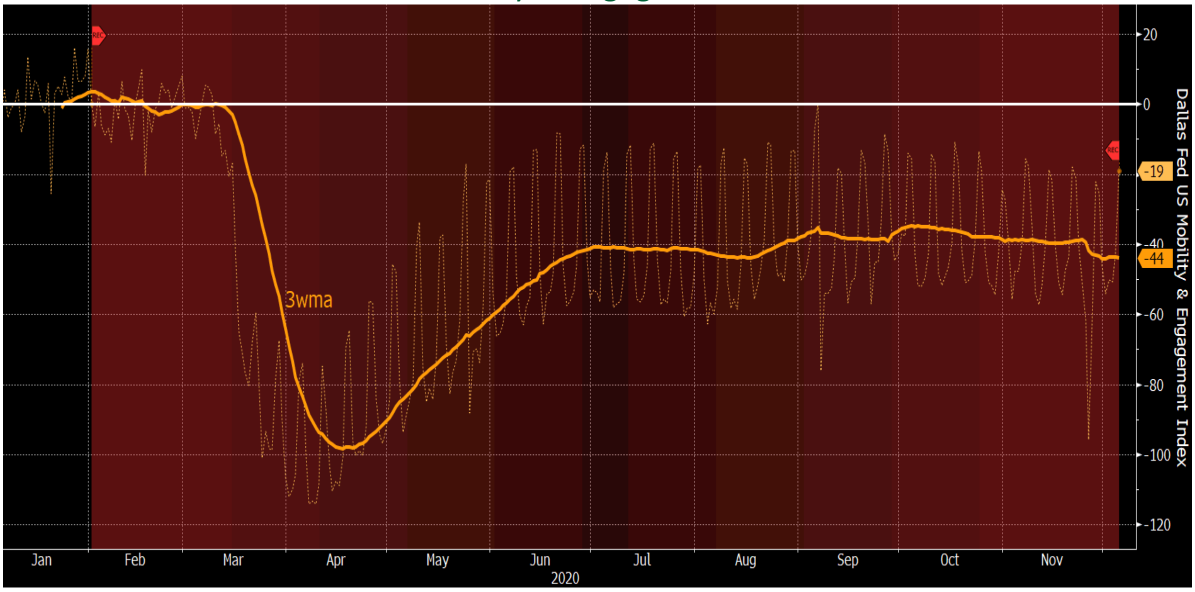

Compared to the February stock market peak, the Technology and Discretionary sectors have increased over a fifth, with Health Care and Industrials also in positive territory. Whilst Financials and Energy lag quite materially, they have picked up well since November. Seeing the low index levels in March, this year has truly shown the scale of the investment opportunity an unexpected crisis can offer.

*Source: Bloomberg & Stonehage Fleming Investment Management Limited. December 2020.* ***Past performance should not be used as a guide to future performance.***

## 2. IMMEDIATE OUTLOOK

Investors have enjoyed a cocktail of good news over the past few weeks – the US reporting season delivered better than expected results, the US presidential election result indicates a more moderate than feared US economic policy and all the good news on multiple successful vaccines boost confidence on the economic outlook for next year.

US Mobility & Engagement Index




The current economic environment is, though, still saddled with high virus infections and the UK/Europe Brexit negotiations making no progress with increasing risk of economic constraints following a potential no-deal result. As the above Mobility & Engagement chart indicates, economic activity in the US already seems to be slowing.

Whilst investor optimism has a strong foundation for the medium term, we are conscious that a normal economic environment is still some months away and that we may face a relatively short period of continuing economic constrains and volatility.

Global Money Supply ($tn) vs S&P 500

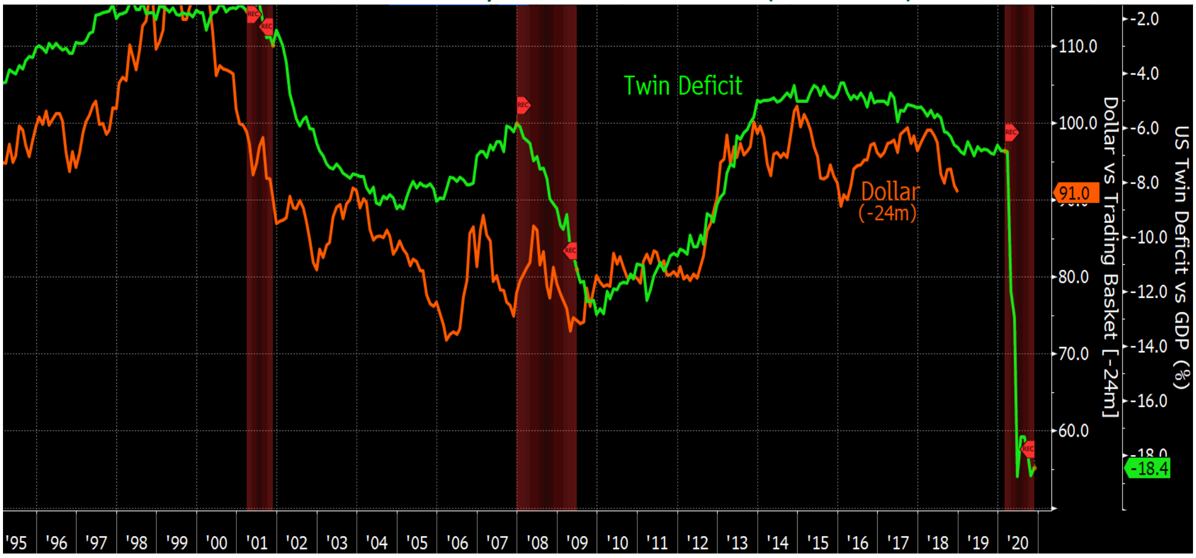

In our view the world economy and capital markets will for this period continue to be dependent on both fiscal and monetary support. We have little reason to fear that support not materializing. As the above chart illustrates, it almost seems that share prices follow and correct to the global money supply line. Should we experience a setback in the stock market we will therefore see that as a buying opportunity.

*Source: Bloomberg & Stonehage Fleming Investment Management Limited. December 2020.* ***Past performance should not be used as a guide to future performance.***

## 3. DOLLAR CURRENCY

The consensus view for the Dollar outlook is strongly bearish currently. This follows mainly from the following chart:

Dollar Currency vs US Twin Deficit (% of GDP)




The US twin deficit has mushroomed with the GVC to unprecedented levels. The above chart illustrates a clear historic relationship with the Dollar. On this basis the Dollar outlook is anything but rosy.

We also follow data in the currency non-commercial futures market, which essentially reflects the capital markets' views of the currency's outlook. The net book has been slightly negative since the middle of this year, but not remotely to the extent of the twin deficit. The fact remains that it is in negative territory and that there does not seem to be material reason for optimism – apart from the Renminbi probably getting a bit strong for their authorities' sake.

We perceive a relatively weak Dollar as good news for world trade and the global economy. Obviously, the latter two go hand-in-hand and we have a constructive global economic outlook, but it is also striking how world trade is currently picking up along with the weaker Dollar.

S&P 500 12-month Forward Earnings Growth vs Dollar Value Growth (%)

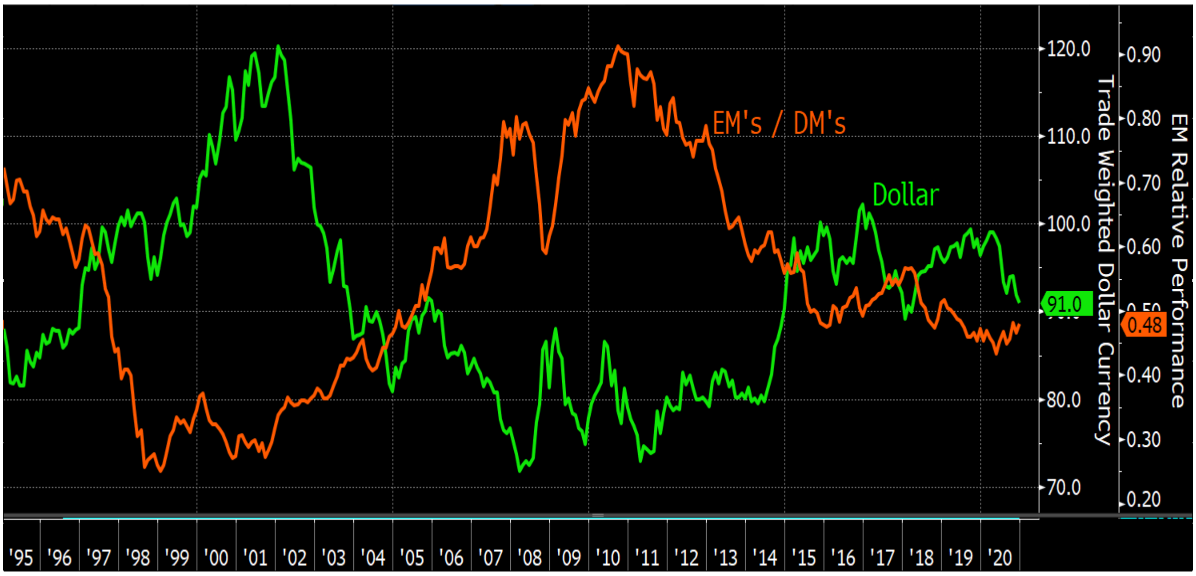

There is a clear correlation between S&P 500 earnings growth and the Dollar value, as reflected in the above chart. Many us companies have large international operations and export to the rest of the world, both benefitting from a weaker currency. Whilst extreme currency volatility will not be welcome, these shareholders are clearly looking forward to improving earnings results.

*Source: Bloomberg & Stonehage Fleming Investment Management Limited. December 2020.* ***Past performance should not be used as a guide to future performance.***

## 4. EMERGING MARKETS

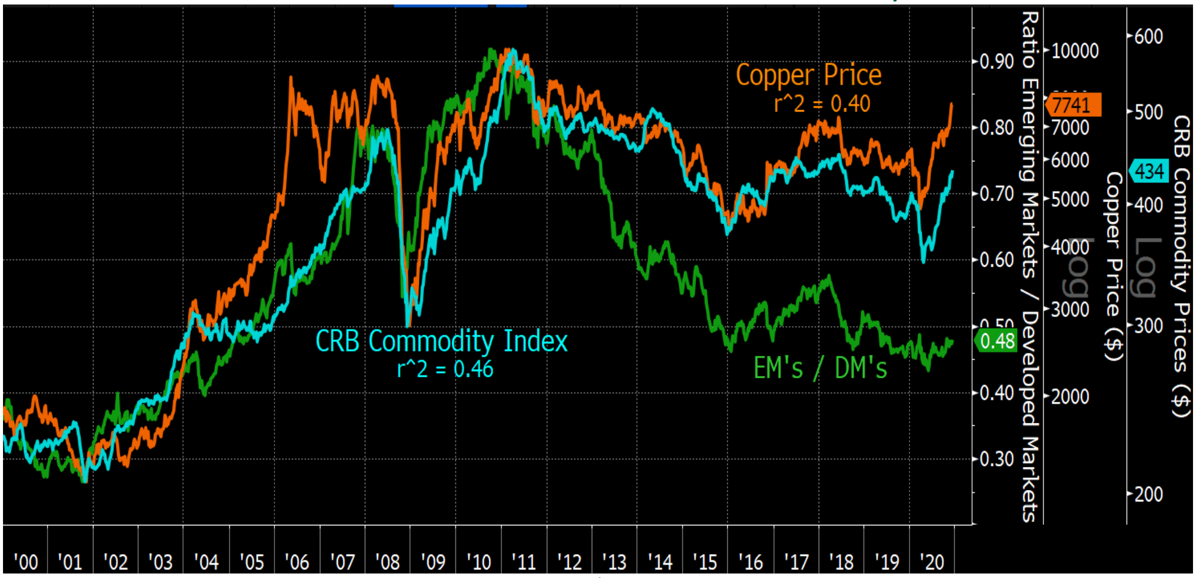
The weaker Dollar and an improving global economic outlook favour the Emerging Market theme:

Dollar Currency vs Emerging (EM) /Developed Market (DM) Relative Stock Market Performance




As reflected in the above chart, the relative EM/DM stock market performance mirrors the Dollar's performance and has recently bottomed out, seemingly starting to appreciate.

EM/DM Stock Market Performance vs Commodity Prices




The above chart reflects the same relative EM/DM stock market performance against the CRB Commodity Index and the Copper Price. We can draw a similar constructive conclusion on Emerging Markets seeing the current positive trend in commodity prices.

## 5. EQUITY VALUATIONS

Many commentators believe the stock market has run ahead of economic realities and is overvalued. We believe the stock market rather discounts the future than current economic conditions, and that company results in many cases may grow into seemingly high current valuations.

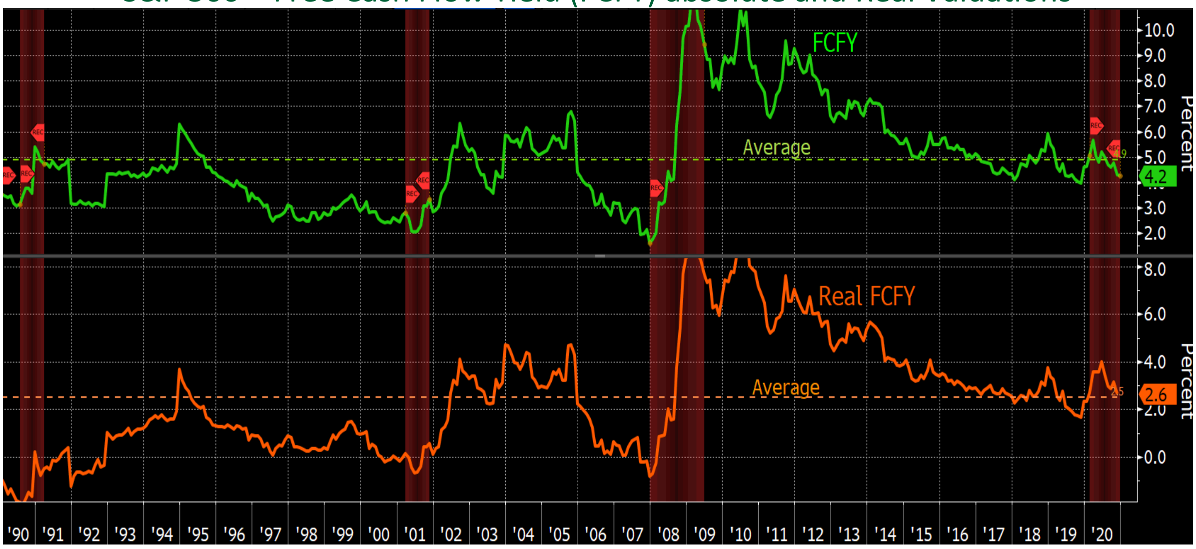
The first chart on the next page reflects the consolidated analyst valuations of all the individual S&P 500 constituents for the coming twelve months, compared to the S&P 500 index. Our conclusion from the chart is that we can expect a reasonable return for next year on this basis.

*Source: Bloomberg & Stonehage Fleming Investment Management Limited. December 2020.* ***Past performance should not be used as a guide to future performance.***

## S&P 500 – Index vs Forward Valuation


We believe Free Cash Flow Yield is the most important valuation tool. The S&P's current yield of 4.2% is close to the long-term average (the top section of the chart below), while the Real FCFY of 2.6% is marginally above average, and ahead of the US's long-term economic growth level.

## S&P 500 – Free Cash Flow Yield (FCFY) absolute and Real Valuations




We expect strong company results to continue for a while and do not believe we should fear 2021 from a valuation perspective.

*Our sincere gratitude to our clients for another year of support and friendship, and for sharing fascinating investing thoughts through a truly exceptional year. We wish you and yours all the very best for the Festive Season and the New Year.*

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