GLOBAL EQUITY PERSPECTIVES 15 MARCH 2021

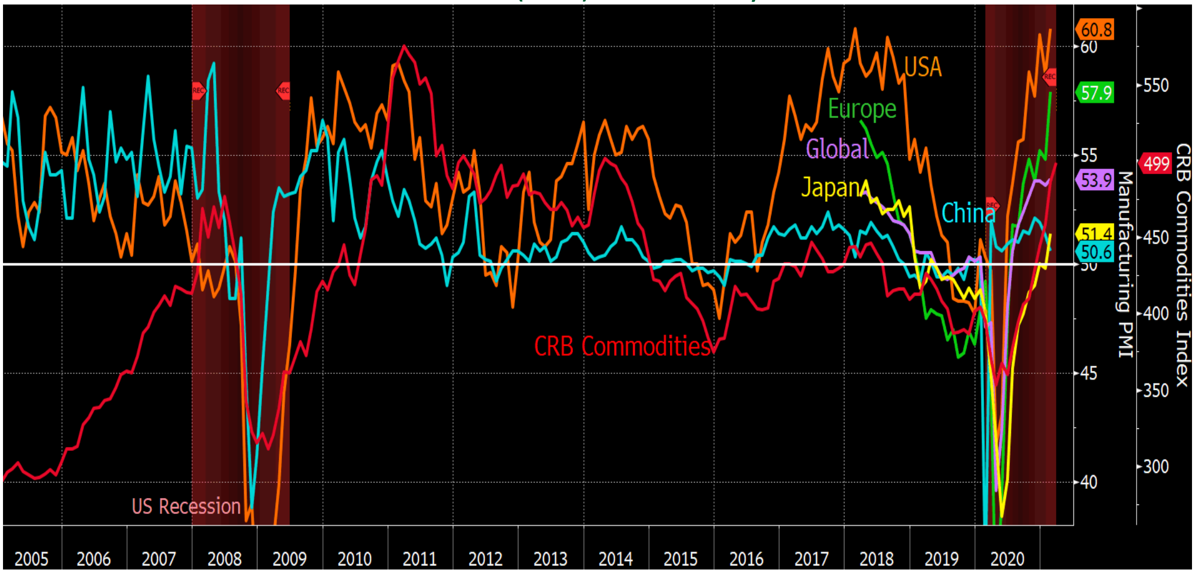
"Out of difficulties grow miracles."

Jean de la Bruyère

1. ECONOMIC RECOVERY

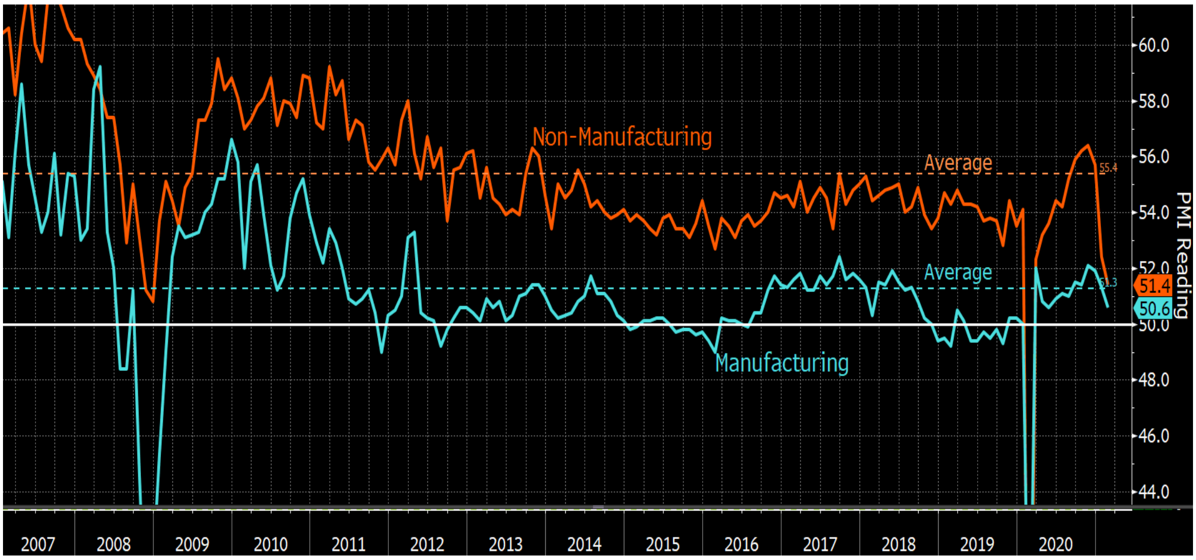
The global economic outlook seems to continue to improve as reflected in the following chart:

Regional Purchasing Manufacturer's Indices (Manufacturing PMI's) vs Commodity Research Bureau (CRB) Commodity Price Index



The US's PMI index in the above chart is back at record levels. This is closely followed by the European PMI, with a notable spike recently. The overall Global PMI is also well above its pre-pandemic levels. Whilst Japan has recovered well, it still lags the other regions (apart from China). Very relevant, the Commodity Research Bureau (CRB) Commodity index reflects this positive outlook, currently at its highest since 2014.

China Federation PMI Indices



Contrary to the overall positive picture above, it is striking how both China's Manufacturing and Non-Manufacturing equivalent PMI indices recently dropped to less positive levels, well below average. This is a negative surprise, but the readings remain in constructive territory.

Source: Bloomberg & Stonehage Fleming Investment Management Limited. March 2021. ***Past performance is not a guide to future performance.***

2. EARNINGS AND VALUATIONS

We have updated our S&P 500 earnings chart, and it deserves a mention:

S&P 500 – Index vs 12-Month Forward Consensus Earnings Expectations

The 12-month forward consensus earnings expectations index keeps rising and currently exceeds its peak level prior to the pandemic. This is despite the fact that the inclusion of Tesla in December last year has hurt the earnings index. On this basis, the damage to earnings from the pandemic has now been overcome – a year from when the pandemic struck.

MSCI World Index vs 12-Month Consensus Target Valuation

The above chart reflects the consolidated 12-month target consensus valuations of the MSCI World index constituents (the orange line, presented twelve months forward in the chart). The dip in the chart at the current timing clearly reflects the cuts in valuations when the pandemic struck a year ago. It is clear from the chart how the price index follows the valuation index over time.

It is striking at what a steep angle valuations are being revised upwards. The target valuation is currently 11% above the current price. This is on the ten-year average upside level. On this basis, it seems the market reflects fair value.

Source: Bloomberg & Stonehage Fleming Investment Management Limited. March 2021. ***Past performance is not a guide to future performance.***

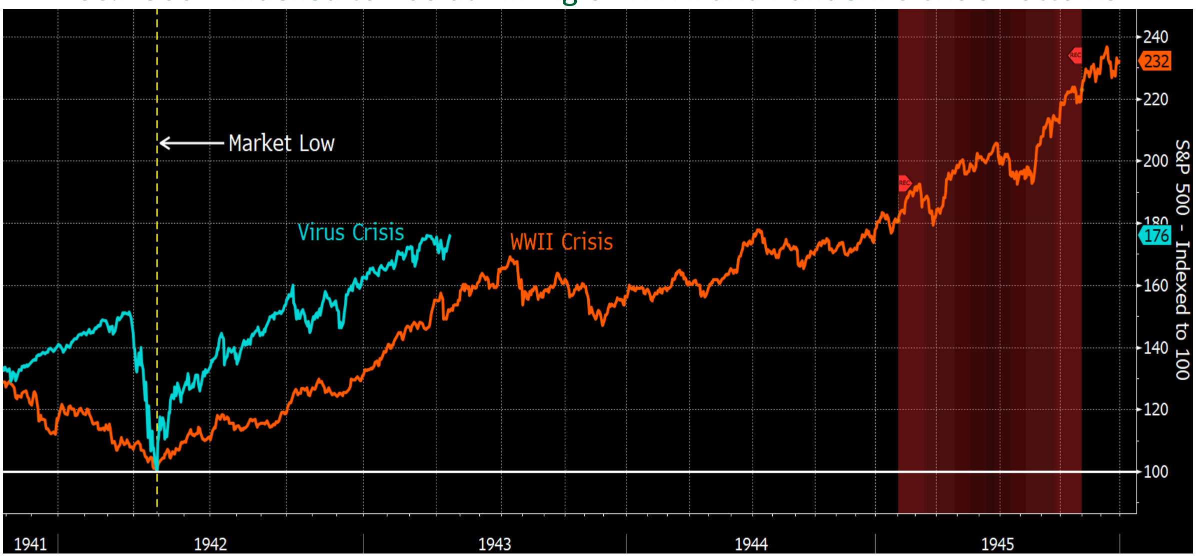
3. PRICE RECOVERIES

It is interesting to compare the current stock market recovery to those of previous economic crises. Clearly all crises have very different causes and effects, and caution in interpretation is important. The following chart indexes the S&P to 100 at the bottom of the particular crisis.

S&P 500 – Indexed to 100 at Timing of Economic Crisis Bottoms

The above chart compares the current S&P 500 recovery track with those during the Financial Crisis and the Inflation Crisis that Federal Reserve Chair Volcker had to address. The stock market patterns since the respective bottoms have been quite similar up to the current timing. Volcker had a huge task, and whilst his strategy was initially taken well by the market, he had to dampen credit availability and constrain the economy. This dampened the market from this point going forward. The market continued performing for a while during the Financial Crisis at this time, had a small correction, and continued its recovery track. Amongst these three crises, our perception is that the current crisis has undergone the least structural damage.

S&P 500 – Indexed to 100 at Timing of WWII and Pandemic Crisis Bottoms



A comparison with the World War II experience is quite interesting. Whilst the market then performed badly initially, it had a strong recovery from 1942 during the war. This followed from the economic stimulatory effects the war had, following the economic damage from the depression years. The stock market did very well for almost four years – until inflation rocketed to double digits.

The market is currently following a similar recovery track to the WWII one, clearly supported by the Biden administration's strong stimulatory package.

Source: Bloomberg & Stonehage Fleming Investment Management Limited. March 2021. ***Past performance is not a guide to future performance.***

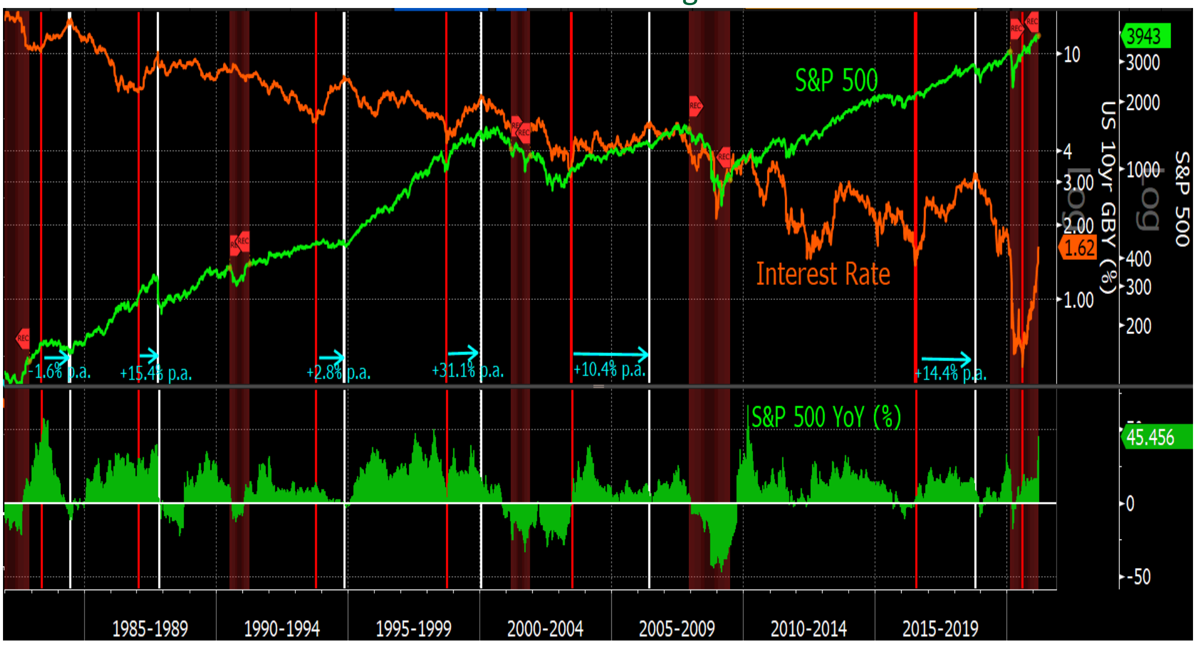
4. INTEREST RATE RISKS

Many investors fear the new phase of rising interest rates. Whilst it is a big subject with various important considerations, the following information may be helpful in this context:

US – S&P 500 vs Real 10-Year Government Bond Yield (%)

In terms of economic activity and business operational issues, the interest rate backdrop has been very supportive since 2011 with very low (and negative) real rates. Despite the recent rate rises, this remains the case with an almost zero real rate level. The current picture rather reflects a 'saved from Armageddon' level with real rates having dropped to the lowest in 40 years.

US – S&P 500 Performance in Rising Interest Rate Periods



The above chart reflects the S&P 500 performance during rising rate periods. The red vertical lines indicate the start of the rising rate era, and the white vertical lines the end of that era. We show in blue numbers the annualized S&P 500 performance during that period, and in the green bars at the bottom the 12-month growth in the index.

Barring the 1983/84 period (>6% real rates then), all others delivered positive annualized returns. The average of the annualized price appreciations over the five rising rate eras is +14.8% p.a., with a median return of +14.4% p.a. On this historic basis, rising rates have favoured equity investors.

Source: Bloomberg & Stonehage Fleming Investment Management Limited. March 2021. ***Past performance is not a guide to future performance.***

5. TECHNOLOGY SHORTS

The futures market is an indication of investor sentiment. The Technology sector is out of favour currently.

Nasdaq Index vs Net Number of Non-Commercial Futures Contracts

The above chart reflects a negative net position in Nasdaq futures currently. The index itself has recently picked up after a small correction. The earnings outlook is strong. With the net futures position already at quite low historic levels, this may indicate more index stability ahead.

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