GLOBAL EQUITY PERSPECTIVES 27 JANUARY 2020

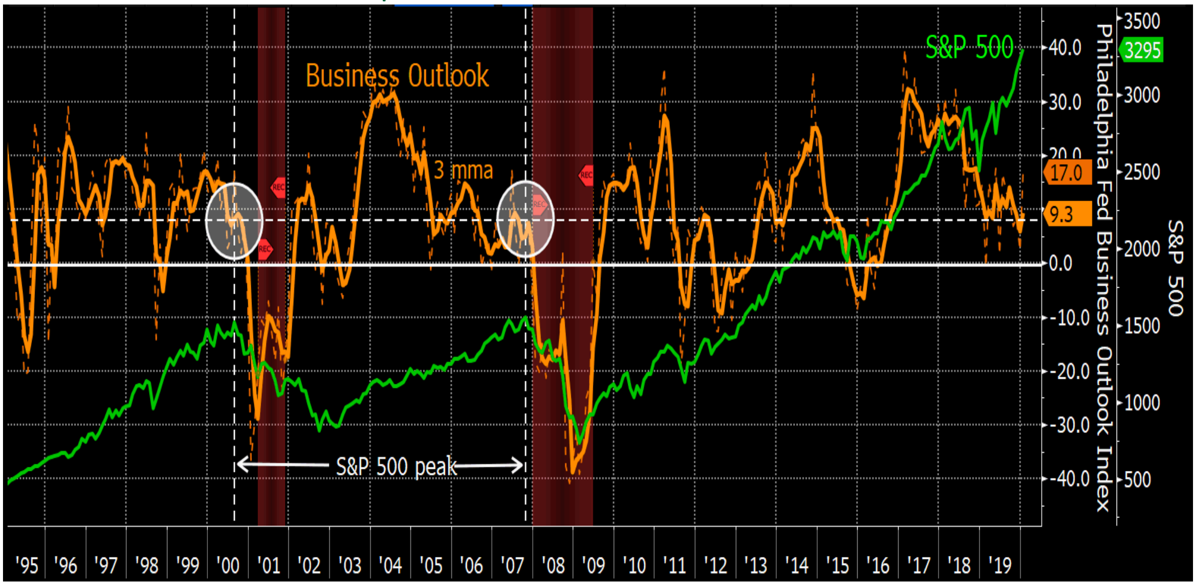
"I cannot teach anybody anything, I can only make them think."

Socrates

1. BUSINESS OUTLOOK

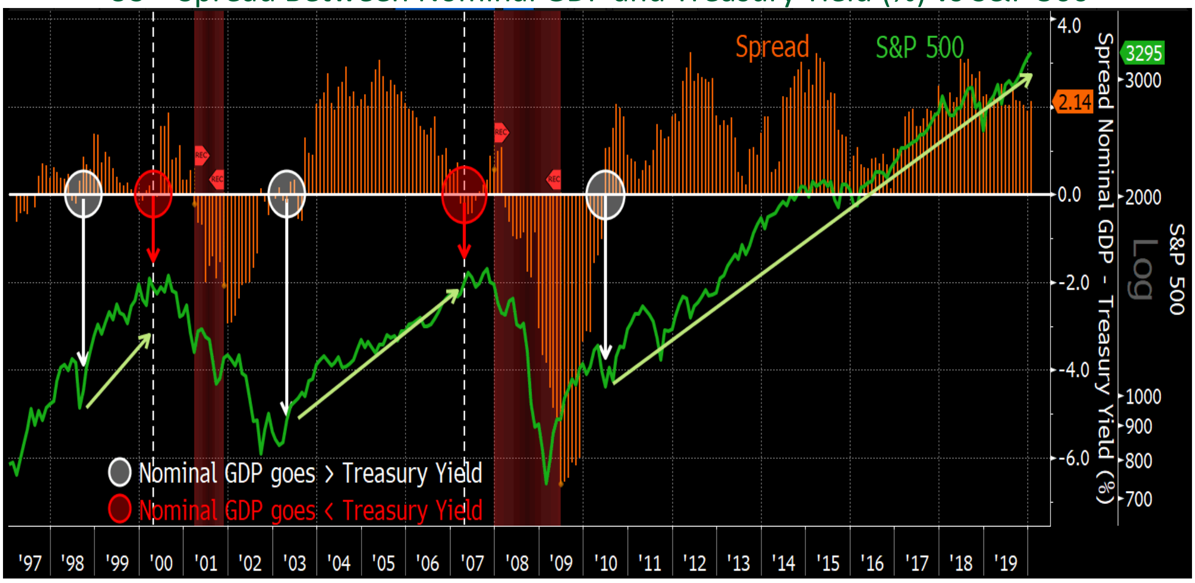
The Philadelphia Federal Reserve produces a valuable business outlook index:

US – Philadelphia Fed Business Outlook Index vs S&P 500



The index warns of a possible US recession when it drops to a zero level. It historically also indicated risk of a stock market peak at an index reading of around nine points. It has recently hovered around that level, but the most recent reading rose to 17.3, well above the risk zone.

US – Spread Between Nominal GDP and Treasury Yield (%) vs S&P 500



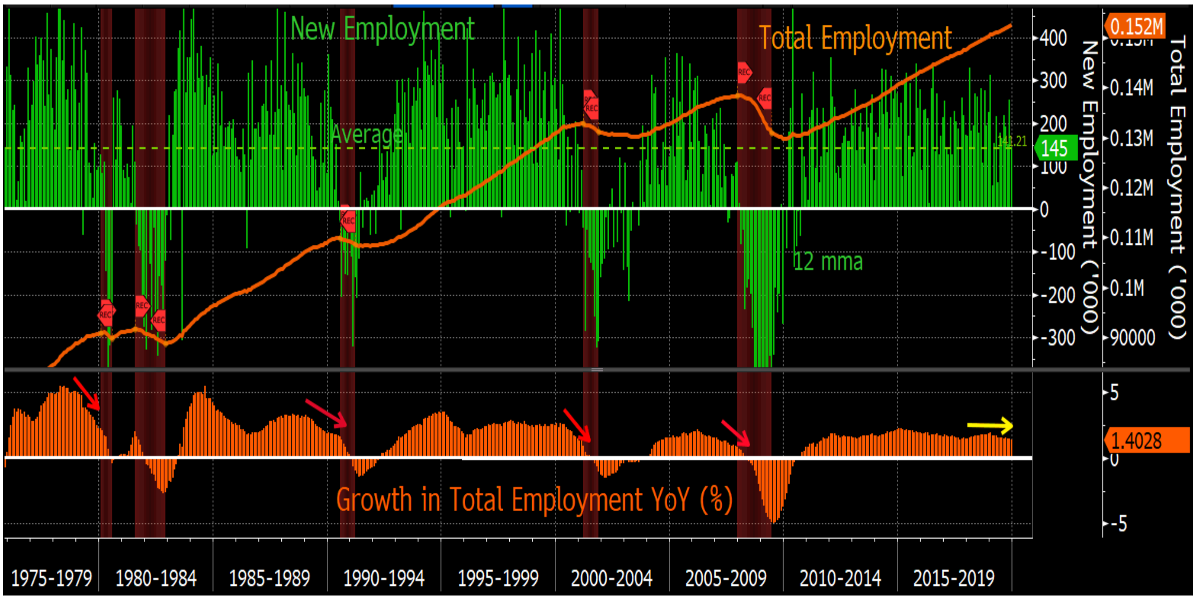
The spread between the nominal US GDP and interest rates (the ten-year yield in the above chart) remains at relatively elevated levels. When this spread dropped to a zero level (the red circles in the chart) it historically warned of stock market peaks. This supports the Philadelphia Fed's constructive business outlook.

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

2. EMPLOYMENT

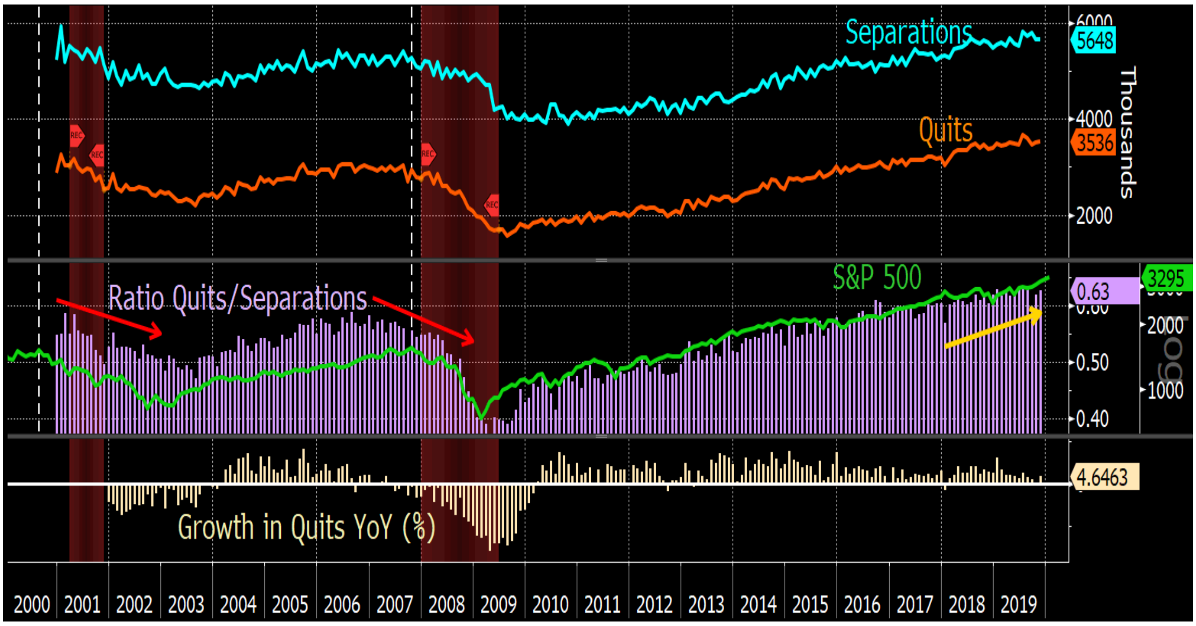
The US employment market message has recently changed to some degree:

US – New and Total Employment ('000)



New employment numbers remain relatively strong. Total employment numbers continue growing at +1.4%. Historically these growth numbers dropped before the inception of the respective recessions (see the red arrows in the above chart). We do not yet detect such warning signals. Notably also, manufacturing employment still grows at +0.8% while it has historically dropped below zero before the respective recessions (not reflected in the chart).

US – Job Separations vs Quits

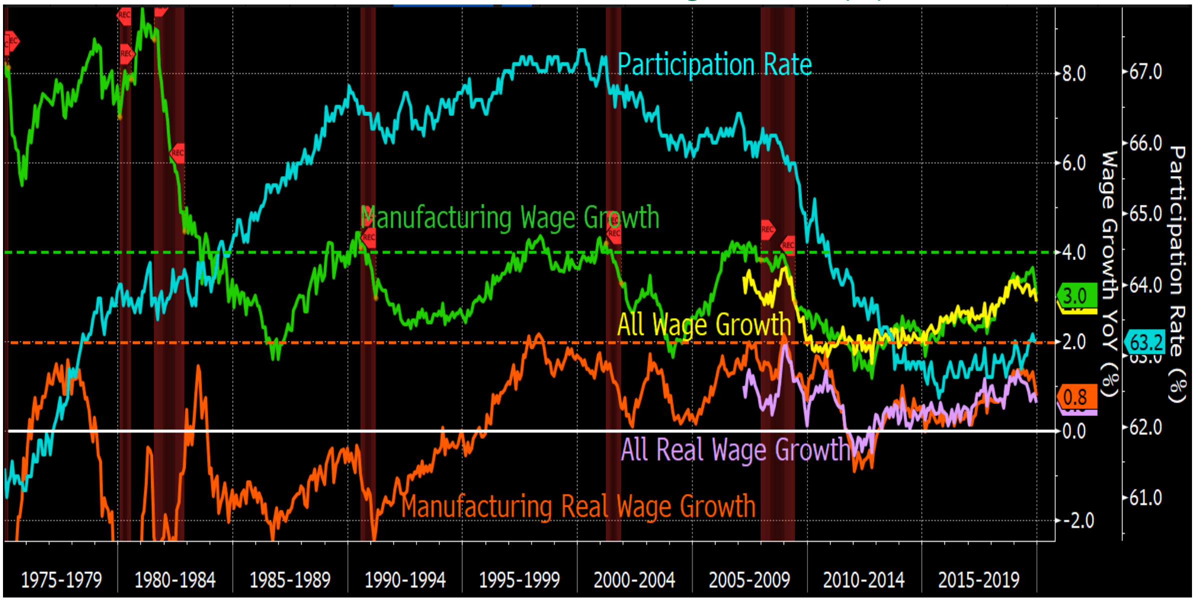


Both job separations and quits remain in rising trends. Importantly, the ratio of quits to separations also remain in a rising trend (the purple bars in the chart above). This historically reflected a continuing growing economy and rising share prices.

Contrary to the above strong messages, it seems that wage growth has peaked in the manufacturing sector and the overall economy, in both nominal and real terms (see the chart on the following page). On the one hand that further dampens inflationary and recession risks further, indicating continuing low interest rates and good profit margins. On the other hand, the question may become whether the consumer market may soften as result.

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

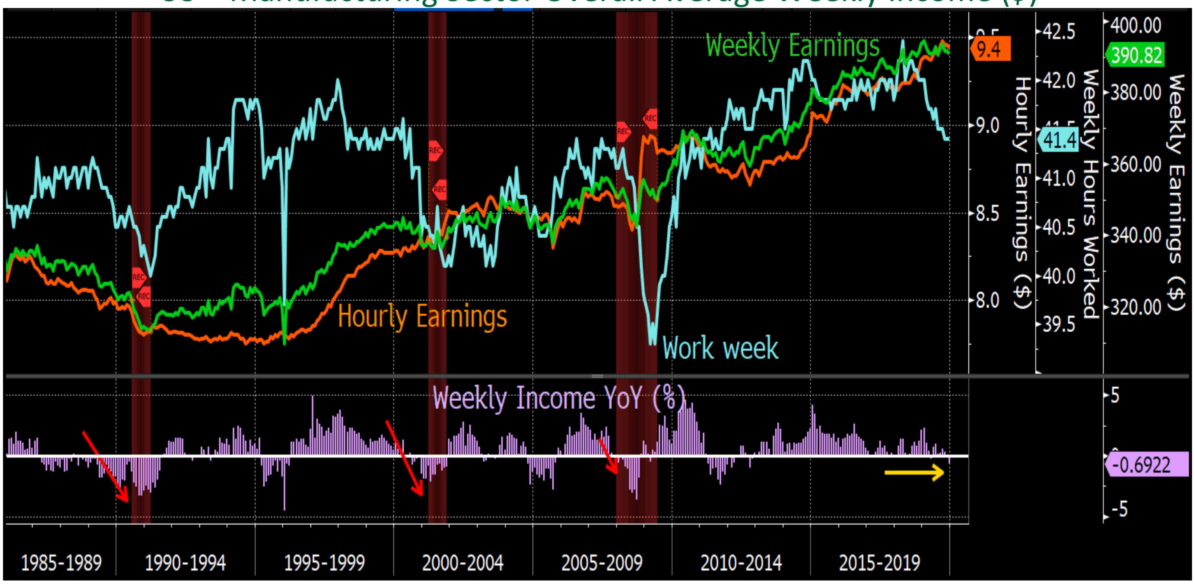
US – Nominal and Real Wage Growth (%)



Notably, wage growth in manufacturing (+3.0%) has most recently dropped the most but very interestingly remains slightly above overall national numbers. This can support a continuing stable consumer market.

The following chart reflects further important data regarding the manufacturing sector.

US – Manufacturing Sector Overall Average Weekly Income ($)



While average hourly manufacturing earnings keep growing (the orange line in the above chart) the average length of the work week has started to decrease (the blue line). The net weekly income result has now for the first time in seven years registered negative growth.

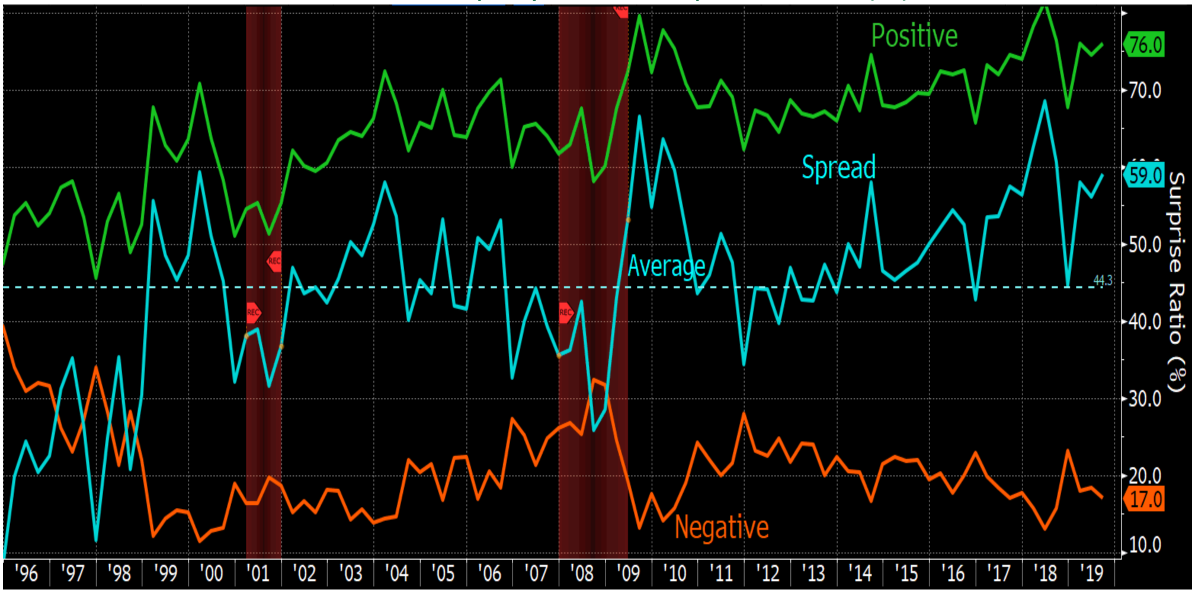
Whilst this picture does not build confidence, it is important to recall that manufacturing makes up only 12% of US GDP, that unemployment remains at record low levels and that consumers' balance sheets are healthy with a high savings rate and their confidence levels remain elevated. We however take cognisance of the above.

3. EARNINGS

The fourth quarter reporting season has started. Perceptions are that calendar year earnings for the S&P 500 index companies may be flat. Company results compared to expectations and managements' comments around their outlook often trigger tactical share price moves.

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

S&P 500 Company Result Surprise Ratios (%)



The recent history of earnings surprises has been rather constructive, as reflected in the above chart. More than three quarters of the S&P 500 companies announced better than expected results in the third quarter. The spread between the positive and negative surprises (59%, the blue chart) is at an elevated level, contrary to levels immediately preceding recessions.

S&P 500 Forward Earnings vs South Korea Exports Growth (%)

Strikingly, analysts are starting to marginally increase their twelve month forward earnings growth for the S&P 500 index companies. This correlates well with the uptick in South Korean export growth which often leads the S&P 500 earnings growth. If these trends may persist, we expect it to support the capital markets.

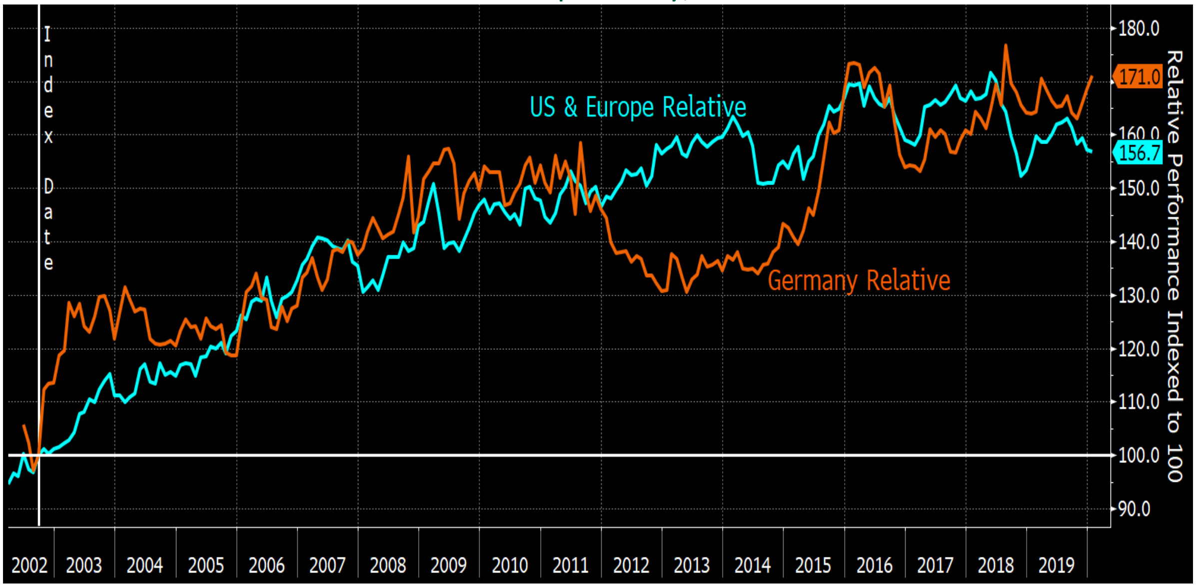
4. FAMILY MATTERS

We focus intensely on the quality of business management and the corporate culture to support and drive sustainable growth. In this context, we often find that businesses under family control have a longer-term orientation and manage their business with a more strategic mindset.

The following chart reflects the relative performances of shares of larger businesses under family control in the US and Europe:

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

US & Europe and Germany Family Control Share Performances Relative to MSCI World and DAX Respectively, Indexed to 100



Both the above family indices outperformed their respective World and Germany indices handsomely over time. The levels of outperformance compare well between the two series in the chart, with an average performance of +64% over and above the benchmark indices. This level of outperformance equates to a compounded level of outperformance of +2.9% p.a. over the period.

This is a pleasing result for many family members and their minority shareholders.

5. GROWTH STILL KICKING

MSCI World Value/Growth Ratio vs US Yield Curve (%)

As reflected in the above chart, the growth theme continues delivering, currently at a record level of outperformance (the orange line in the above chart) trending along with the yield curve. Other ratios (e.g. copper/gold) paint a similar picture suggesting that it is too early to call the demise of growth investing.

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

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