GLOBAL EQUITY PERSPECTIVES 8 JUNE 2020

"The whole is more than the sum of its parts."

Aristotle

1. SKY GETTING BLUER

The market got a welcome surprise last week about the new US employment numbers of 2.5 million in May.

US – Citi Economic Surprise Index vs S&P 500

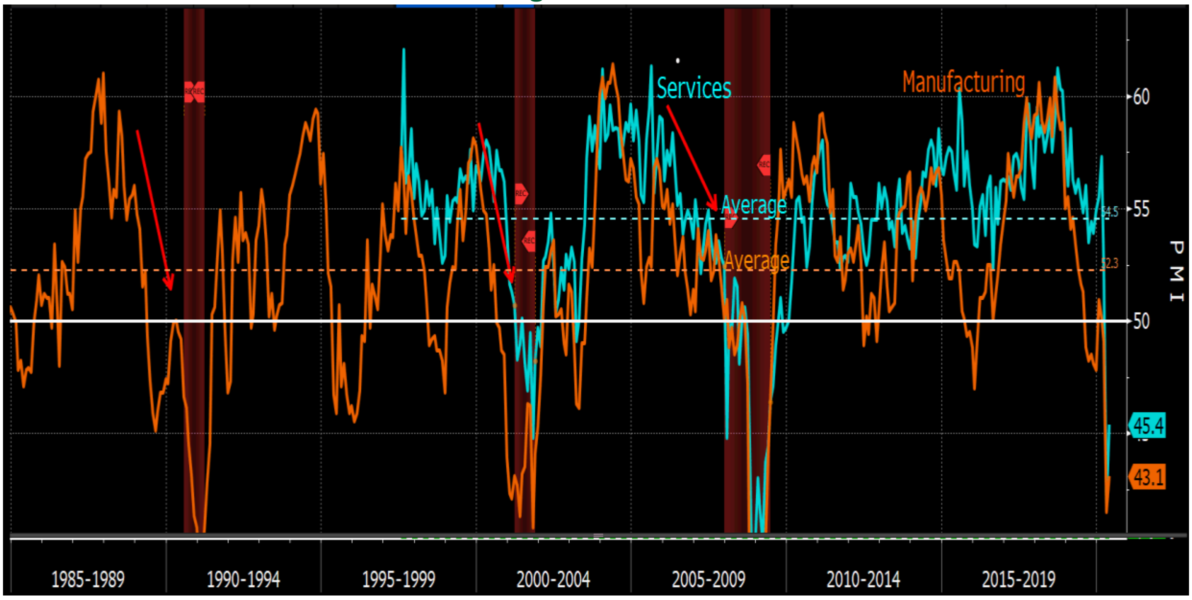
The above economic surprise index reflects new economic data compared to market expectations. It is currently experiencing a strong recovery from its very low base with COVID-19. This clearly supports the stock market well.

COVID-19 Fear Index vs S&P 500

We created a stock market index reflecting investor fears around the virus by simply reflecting the S&P Retail index's performance relative to the S&P Travel index. It shows a clear negative correlation with the S&P 500 in the above chart, currently receding sharply. This supports investor confidence.

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

US – Manufacturing & Services ISM PMI Indices

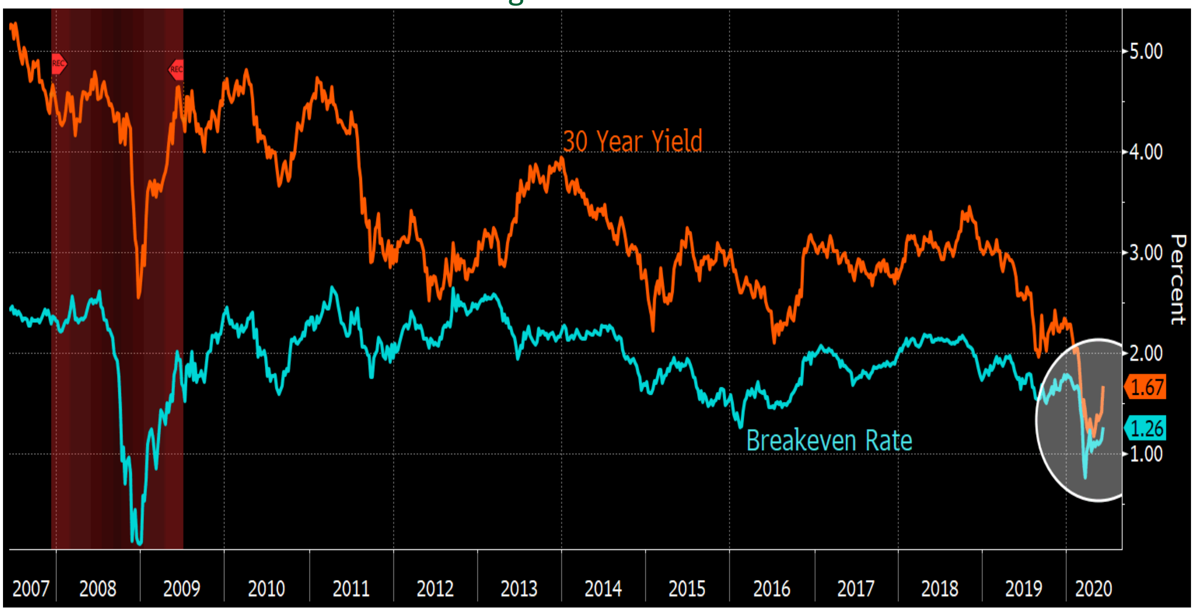


Interestingly, both the Manufacturing and Services PMI indices dropped sharply, but no more than with previous recessions, and have already turned upwards in May. Whilst we can expect them to remain in the contraction area for a while (<50 levels), the trend rather than the absolute values is expected to be more determinant of investor sentiment at this stage.

2. BOND MARKET INDICATIONS

We follow developments in the bond market closely to understand its perceptions around the economic outlook.

US – Long Term Interest Rates

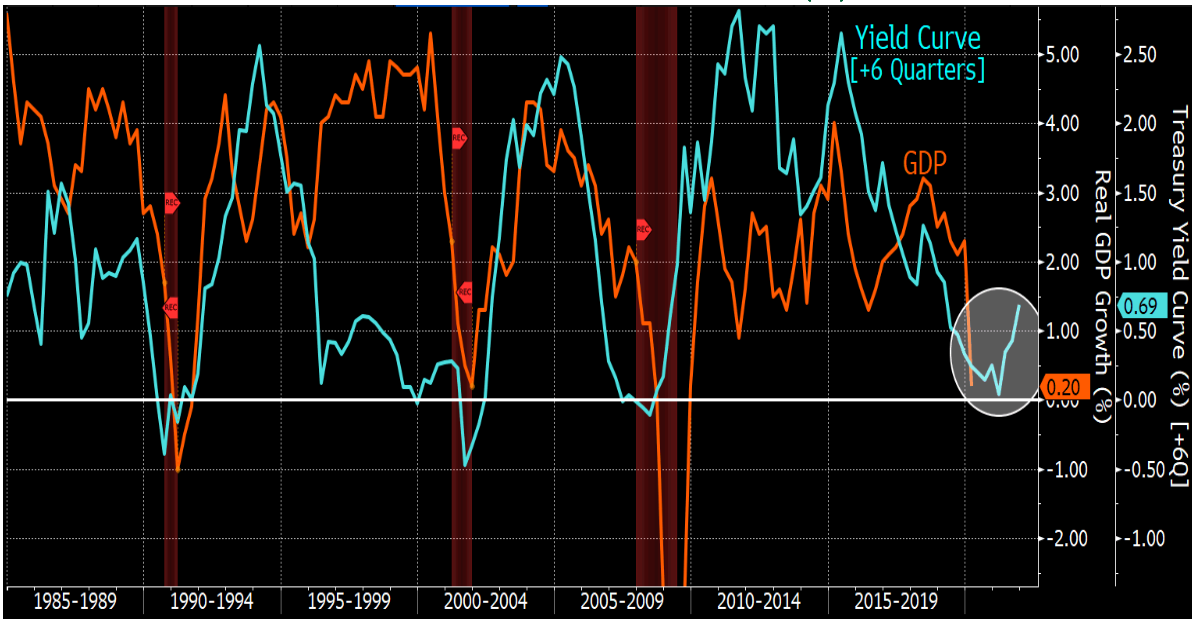


The three-year Treasury yield dropped sharply with the COVID-19 crisis, as it usually does with economic crises. It bottomed at 1.17% in late April, and has already recovered 50 basis points to the current 1.67%. The ten-year Breakeven yield reflecting the outlook for inflation also dropped sharply to a low of 0.76% in late March, and has also recovered 50 basis points to 1.26% currently. These rising trends reflect positive economic changes of perceptions in the bond market.

We show our chart of the US yield curve along with changes in economic growth on the next page. The chart of the yield curve is extended by six quarters as it serves as a leading indicator.

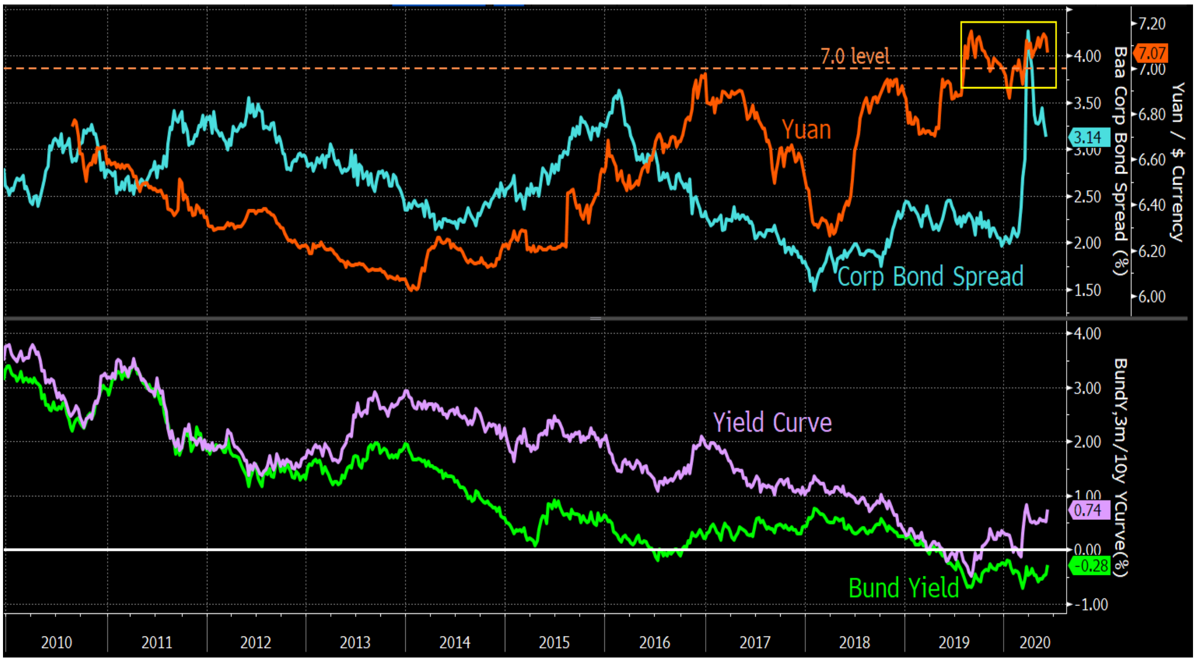
Source: Bloomberg & Stonehage Fleming Investment Management Limited. June 2020. ***Past performance should not be used as a guide to future performance.***

US – Yield Curve vs GDP Growth (%)



Obviously, GDP levels are going to drop sharply over the second quarter, and most possibly over the third quarter. Strikingly, though, the yield curve is currently steepening quite sharply. Bearing in mind the historic leading relationship with economic growth, this bodes well for economic recovery off a depressed base hopefully next year.

Four That Matter



We combine four key metrics reflecting the state of investor sentiment in the above chart. The Corporate Bond spread is currently quite high, but with a constructive trend. The short yield curve is steepening, while the German Bund yield seems stable. The Yuan currency is still above the key 7.0 level to the dollar, probably reflecting geopolitical strains.

All in all, the broader bond market is currently looking more positive. It is not out of the woods yet, but general trends seem constructive.

3. COPPER INDICATIONS

The copper price is a handy investor tool to assess overall economic circumstances:

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

Copper/Gold Price Ratio vs S&P 500 Growth (%)

The Copper/Gold price ratio dropped to an historic low in the midst of the GVC (Great Virus Crisis). The ratio has recently turned upwards with Copper rising and Gold remaining stable. This is a positive economic indicator should this trend persist.

This ratio has a clear correlation with the growth in the S&P 500 index.

Copper/Gold Price Ratio vs AUD/JPY Currency Ratio

A similar positive correlation is reflected between the Copper/Gold ratio and the AUD/JPY currency in the above chart. The AUD is currently strengthening in this context, reflecting a more risk-on cyclical outlook. The obvious question is how sustainable the latter can be under current world health circumstances.

4. FINANCIALS

The Financial sector has underperformed materially this year, due largely to the collapse in interest rates because of GVC. Interest rates have now stabilised and turned for the better. As reflected in the chart on the next page, the financial sector is now following suit.

The big question is clearly how sustainable the recent rising trend in interest rates are.

US – Treasury Yield (%) vs Financials Relative Performance

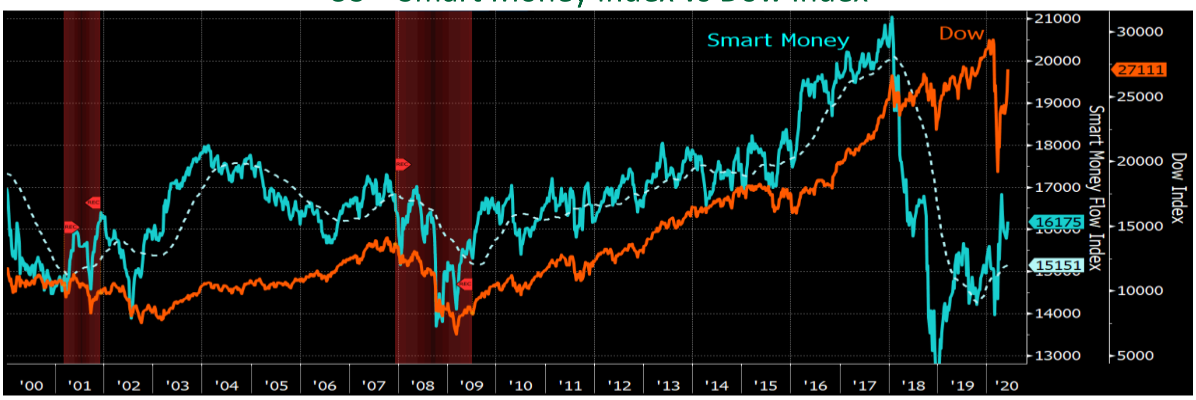
5. TECHNICAL PICTURE

The S&P 500 index is currently at an interesting juncture:

S&P 500 – Technical Readings

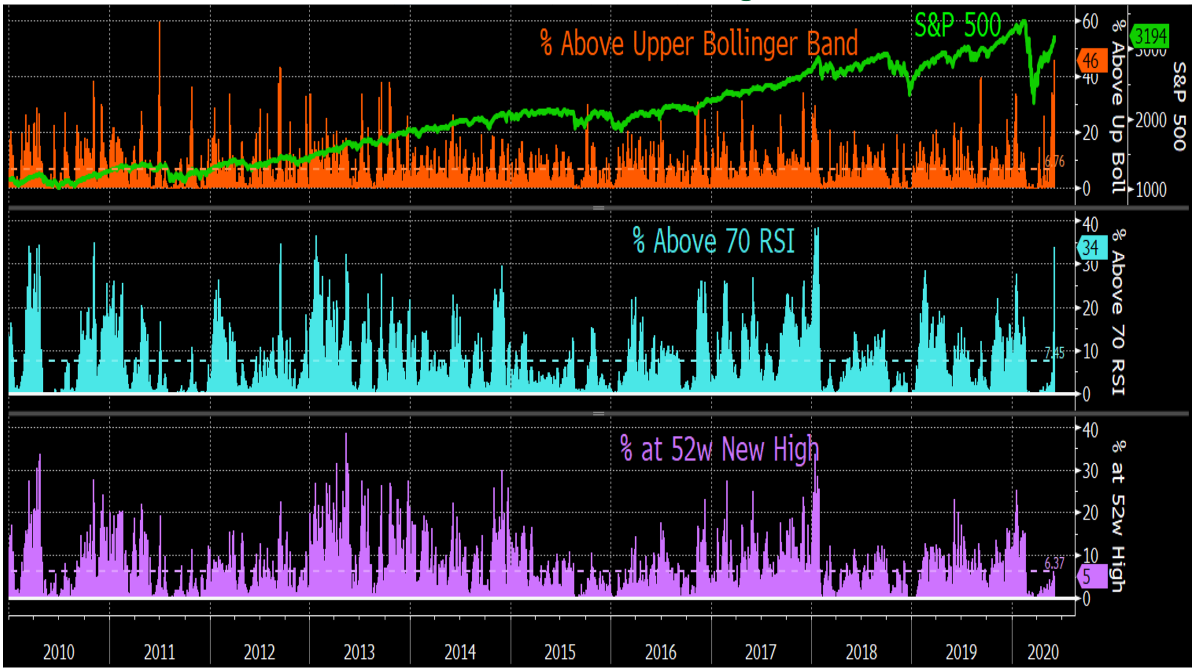
The index has successfully crossed its 50-day moving average, its Fibonacci golden ratio and its 200-day moving averages. Along with this, its 50-day moving average is in a rising trend. The only outstanding trigger is for its 50-day moving average to cross its 200-day moving average thereby forming a golden cross which confirms a structural rising trend. This may take some time to complete, if it is going to happen.

US – Smart Money Index vs Dow Index



As reflected in the previous chart, the smart money is currently buying, seemingly trusting the technical picture.

S&P 500 – Level of Overboughtness



The recent market strength is starting to indicate some technical overbought levels. 46% of the S&P 500 constituents are trading above their upper Bollinger bands and 34% are trading above their 70 RSI Overbought levels. Against this, only 5% of the members are trading at new 52-week highs.

Historically, such high levels predominantly held for a while before the market adjusted.

Our thoughts are with everyone affected by COVID-19, be it directly or indirectly.

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