STONEHAGE FLEMING

5 October 2020

Dear Equity Client

GLOBAL EQUITIES – 3rd Quarter 2020

World equity markets continued their recovery in the third quarter from their Virus Crisis nightmare. The MSCI World Index (including Emerging Markets and dividends) appreciated by a further +8.1% (US$ terms, +3.7% UK£ terms) over the quarter. This brought the index over the nine months to +1.4% (US$ terms, +4.1% UK£ terms).

Investors' nerves were somewhat calmed by the second quarter earnings season. Results were generally dismal in absolute terms, with sales for the S&P 500 constituents dropping by double digits and bottom line earnings evaporating. However, about two thirds of the constituents declared better sales than the feared consensus numbers, with 85% declaring better than expected earnings. Analysts continued revising their projections for next year further upwards (almost +10% over the quarter alone), supporting investor sentiment.

The third quarter traditionally delivers the weakest stock market performance in the year. US election years usually experience even more uncertainties and stock market volatility in the months immediately preceding the election. This year has been no exception. Furthermore, many northern hemisphere economies are currently at a critical juncture in their battle with Coronavirus. Investors understandably are concerned about the outlook as we head into the winter season, but we would guard against too much pessimism. Our constructive stance is not based on particular optimism, but rather on a view of a continuing slow economic recovery, supporting stronger than expected earnings growth for many important businesses.

Many (if not most) businesses have cut costs to the bone during the Virus Crisis. We believe they will continue to be very cautious in accepting back all of those manageable costs as the economy recovers. Along with this, commodity and especially energy prices are low, saving many businesses large amounts in material and logistics costs. Further to this, finance costs are at historic lows currently, and are expected to remain as such for some time to come.

We will not be surprised to see more of the same investor surprise factor when the third quarter earnings season starts in the second half of this month. Then, going further forward, it may turn out that the operational gearing and margin recovery themes mentioned above start playing a larger role in earnings recovering than the economy does. The market usually reacts favourably to margin expansion and positive surprises.

We are grateful for all your support.

With best wishes.

Gerrit Smit, Partner – Head of Equity Management

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