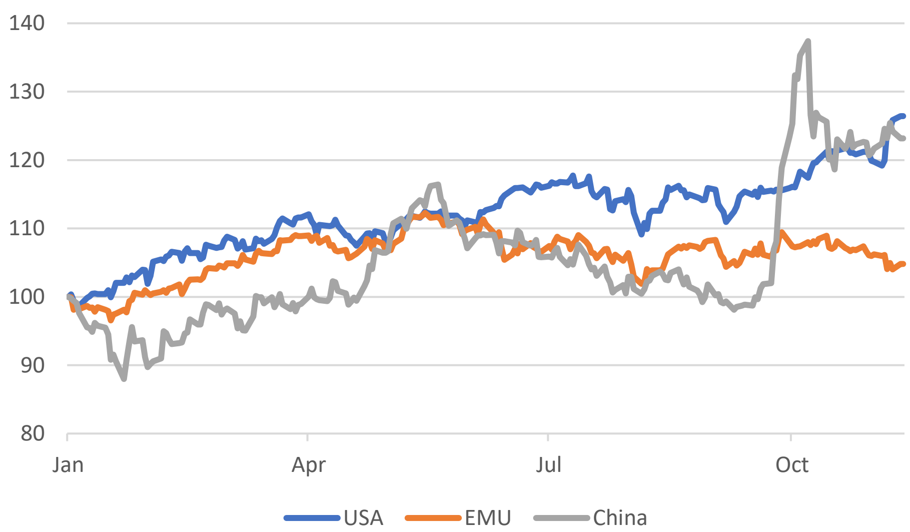
"Not a creature was stirring, not even a mouse": In this article Westminster Asset Management Investment Strategist, Peter Lucas, discusses recent major political and market developments. Peter suggests the investment landscape is broadly positive for equities, although a pause is likely ahead before we enter the traditional strong period for markets.

I last focused on the prospects for equities three months ago, when markets were reeling due to yen volatility, disappointing US economic data and political uncertainty in France. My message was one of cautious optimism ("Keep calm and carry on", August 2024). Although the evidence on inflation was mixed, the US growth indicator was in accelerating mode and sentiment was at the sort of level of despondency that has often resulted in short-term lows. Indeed, I pointed out at the time that it was a rare combination of indicators that had historically produced strong market bounces. Three months on, what do we see? The World Index is up almost 10% in sterling terms and the S&P 500 an even more impressive 12%. So far, so good, but where do we go from here?

Much has happened in the intervening period, including the re-election of President Trump and China finally getting serious about boosting their moribund economy. Indeed, I am happy to say that I released a positive note on China the day that share prices embarked on a rapid 40-50% rally. The timing of the note was more luck than judgement, but at least I was right about the direction of travel.

<u>YTD Equity Returns, GBP Terms</u>



Source: Bloomberg

It is fair to say that the Republican margin of victory was a surprise. However, what it means is that much of the uncertainty about the timing of the result and the policy agenda is now gone. On the plus side, Trump is talking about lower corporation tax, deregulation, cost cutting in the public sector, and a more supportive policy environment for energy producers, which should result in more investment, growth and profitability. The implications for inflation are less clear. Whilst supply-side reforms would be good news, tariffs on imports from the result of the world and most particularly China, will raise the cost of living for many (although that could be mitigated to some extent by a stronger dollar). Furthermore, the large and growing budget deficit remains an ever present inflationary black cloud, particularly in the presence of low unemployment (for more details see: "Baked in the cake", September 2021). Short of a nasty geopolitical surprise, this is an environment that is broadly supportive for US equities and neutral/negative for US Treasuries. The one red flag for equities is sentiment, which is once again approaching levels that normally trigger a short-term setback.

Investors are not wholly convinced by the drip-drip procession of measures that have been announced in China. Yes, fund managers are now long of Chinse stocks (having been massively underweight) but many remain unconvinced, as evidenced by the relatively wide discounts on China investment trusts. My suspicion is that Chinese equities will continue to struggle in the short-term but another decent buying opportunity is at hand. I am encouraged by China's reticence to throw the kitchen sink at the economy as they might have done 10-20 years ago. I would also point out that there is always a cycle, no matter what policy makers do and besides, Chinese equity valuations remain very undemanding by historical standards.

As US and Chinese equities have thrived, Europe has lagged despite falling interest rates, due to sluggish growth and building political risks in France and Germany. Indeed, I find it hard to be optimistic about the 'Old Continent' over anything but the very short-term (see also; "Eurozone in crisis (again)!", June 2024).

Precious metals have been one of the big winners of 2024, and although the environment remains broadly supportive, this looks like a good time for a breather. The optimism and excitement generated by the Trump agenda is pushing bond yields and the dollar higher, both of which are bad news for gold. Eventually, we expect inflation fears to return, but until they do, gold might find the going tougher.

All in all, this looks like a good time for markets to go to sleep for a bit. Until, no doubt, they awake in excitement for the traditional Christmas rally!

Peter Lucas – November 2024