BREWIN DOLPHIN

Markets in a Minute

8 December 2020

Equity rally continues despite rising infections

The rally in global equities continued over the past week, with most markets in Asia, the UK and US making steady gains. Europe was mixed, as the strengthening euro weighed on some eurozone markets. Bond yields rose, consistent with an increased appetite for risk, while the US dollar continued to weaken.

US indices hit new record highs on several days despite Covid-19 deaths and hospitalisations rising to their worst ever levels, while UK shares rose despite little clear progress in the Brexit talks.

Last week's markets performance*

- FTSE100: +2.86%
- S&P500: +1.67%
- Dow: +1.02%
- Nasdaq: +2.11%
- Dax: -0.27%
- Hang Seng: -0.21%
- Shanghai Composite: +1.06%
- Nikkei: +0.39%

**Data for week to close of business on Friday 4 December.*

Stocks fall as investors take some profits

Global markets mostly fell on Monday after many hit fresh records last week. Disappointing news on US jobs, uncertainty around Brexit and the much-needed US stimulus package, together with yet more tensions between the US and China are all adding to the twitchy mood in markets. The pan-European Stoxx 600 index closed down 0.30% as a no-deal Brexit appeared to become a real possibility, with talks stalling. The FTSE100 closed down just 0.08% to 6,555.39 as the pound fell sharply, helping companies that earn in dollars. But the more domestically focused FTSE250 fell by 1.25% on Brexit stress.

In the US, indices were mixed, with the Dow losing 0.49% and the S&P 500 falling by 0.19%. But the Nasdaq rose by 0.45% to 12,519.95 as the threat of lockdowns increased amid rising Covid-19 cases.

Brexit

Frantic diplomacy on Monday was insufficient to break through to a deal, so Boris Johnson will arrive in Brussels today to try to broker some kind of deal in person.

The pound fell 1.6% against the dollar at one point before recovering to 0.6% lower in late trading. Against the euro, the pound was down 0.8%. Sources put the chance of any deal at around 50% as there seems to be diminishing patience with Boris Johnson's stance in Europe, especially in France. However, it is hoped Angela Merkel could help broker some kind of compromise.

Outlook for Christmas and beyond

November was the best month of the current millennium for many markets – including the FTSE100, which rose by 12.4%.

But even after such a strong month December has started pretty well. December has historically been a strong month for equities, but it is worth remembering that January's losses have tended to be even more pronounced.

With markets at record levels but with so much uncertainty around, there are clearly risks to equity valuations in the very short term. But looking further ahead, we are more confident.

What to expect in 2021

There are plenty of reasons we think there is scope for a durable economic and market recovery over the medium term. For example:

- Consumer confidence usually peaks with the market, but is currently depressed.
- The yield curve is generally inverted ahead of recessions (ie yields are expected to be lower), but it has been steepening lately, suggesting the market thinks the outlook is improving.
- High unemployment suggests plenty of slack in the economy which, again, tends to show we are early in a durable economic expansion.

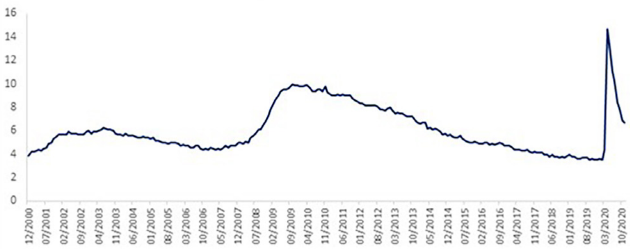
The outlying financial indicator is credit, which this week broadly erased the last of the spread widening that has occurred since Covid-19 struck. Those thin spreads come on top of tiny sovereign yields offering very little cushion against either deteriorating credit conditions or rising interest rate expectations. Bonds are very expensive.

Climbing the wall of worry

One of the reasons that the wall of worry remains there for climbing is the immediately challenging state of the US economy. US fiscal support began falling in August and is set to fall off a fiscal cliff of sorts. On 26 December, a program that extended traditional unemployment benefits from the standard 26 weeks by another 13 weeks will expire, as will the program that made self-employed workers eligible.

That has caused the hitherto resilient retail sales to see momentum ebbing along with economic jobs sentiment. High Covid-19 cases and instances of diminishing hospital capacity are prompting intensifying lockdown measures creating more economic uncertainty.

US unemployment rate



Source: Bureau of Labor Statistics, U.S. Department of Labor

Last week's US non-farm payrolls saw just 245,000 new jobs created, down from 610,000 in October, echoing the weakness shown in the ADP employment survey earlier last week. Our guess would be that the jobs position has continued to deteriorate since the survey dates. November's data showed the unemployment rate falling due to people returning from temporary layoffs but those on permanent layoff continue to rise (albeit at a slower pace than October).

All told, this paints a worrying picture that places more pressure on US legislators to pass a stimulus bill before the end of the year. And reports suggest that the $908bn package proposed by the Democrats last week could get some traction, and even be signed this week. It would certainly give markets more impetus.

Capital and income are at risk.

Neither simulated nor actual past performance are reliable indicators of future performance.

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No investment is suitable in all cases and if you have any doubts as to an investment's suitability then you should contact us.

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