

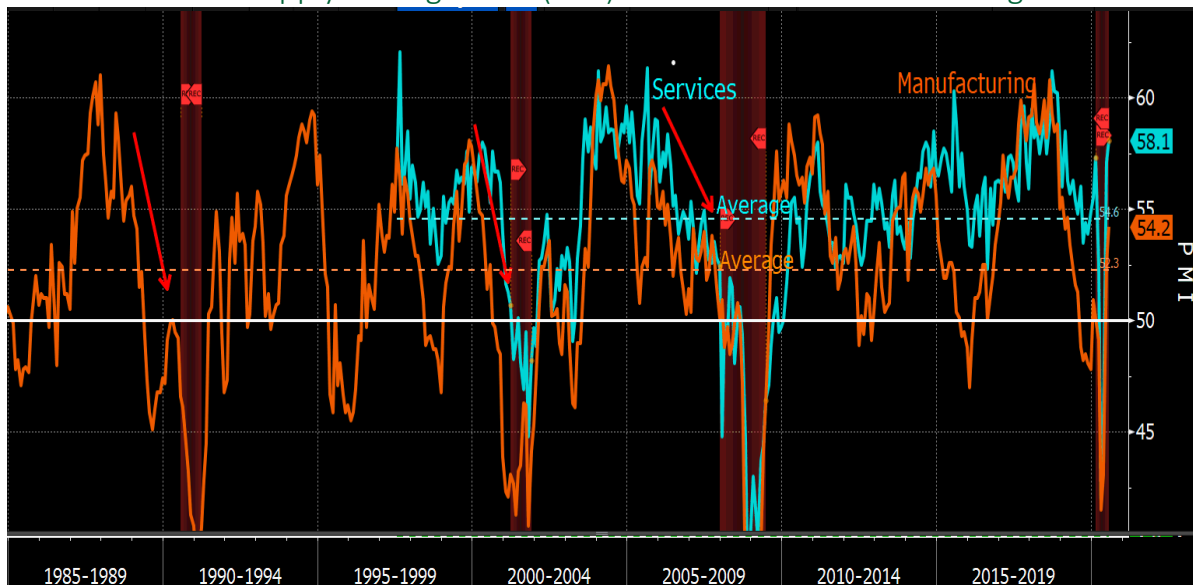
"The difference between ordinary and extraordinary is that little extra."

Jimmy Johnson

1. ECONOMIC OUTLOOK

Investors value the Purchasing Managers' Indices (PMI's) as an indication of where the economy is heading.

US Institute for Supply Management (ISM) PMI Indices – Manufacturing & Services



Both the Manufacturing and Services PMI indices have recovered to levels well above their respective long-term averages. Whilst these readings reflect the managers' month-on-month experiences, and are off the ultra-low Virus Crisis levels, the charts are consistent with trends during earlier recessions. It seems that, if historic trends in this PMI context can be maintained, this recession may stand a chance of being one of the shortest recessions on record.

ISM Manufacturing PMI Index vs S&P 500 Earnings growth (%)

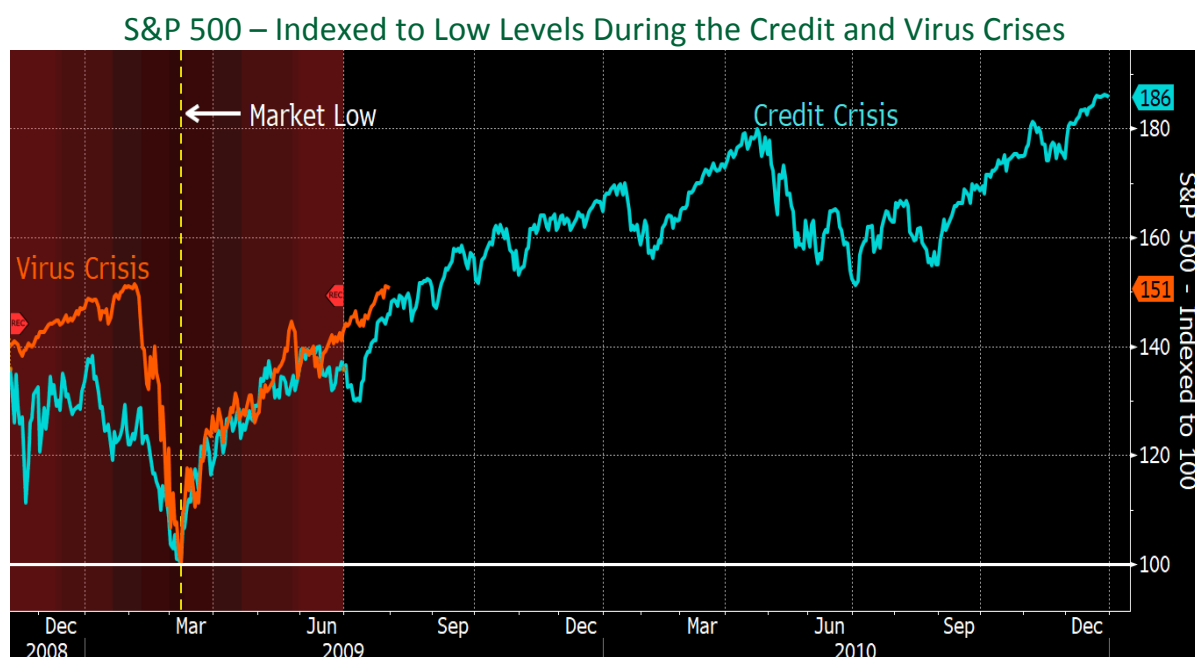


The Manufacturing PMI index has a strong historic correlation with the growth in S&P 500 index earnings, as reflected in the above chart. On this basis, the current PMI trend therefore bodes well for an earnings recovery in the not too distant future.

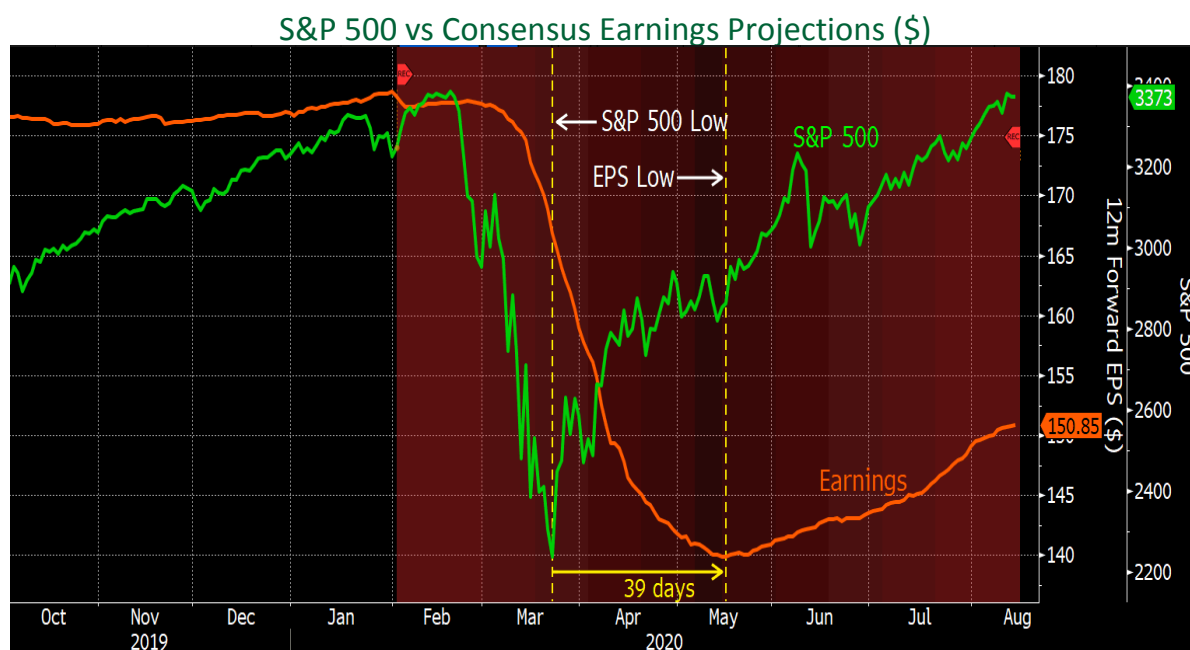
Source: Bloomberg & Stonehage Fleming Investment Management Limited. August 2020. **Past performance should not be used as a guide to future performance.**

2. RECOVERY PROCESS

We plot in the following chart the S&P 500 index evolution relative to its absolute low levels during the Credit and the Virus crises:



It is striking how similar the current recovery cycle compares to the Credit Crisis. If this recession does turn out to be as short as it currently indicates it may be, many investors may continue to draw the above comparison.



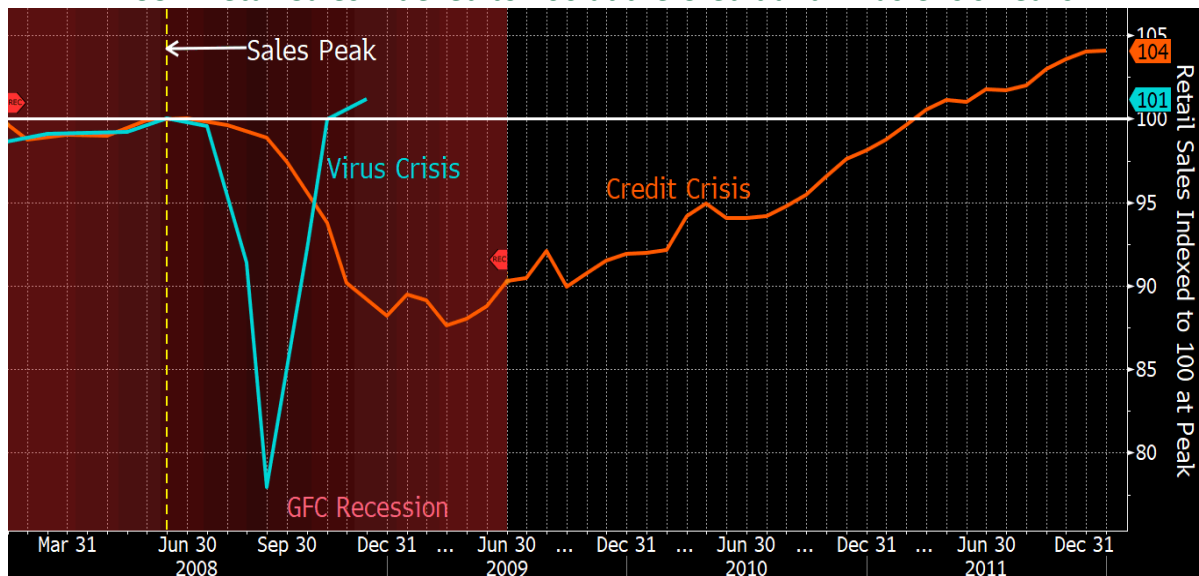
We have updated our chart of consensus earnings expectations. The revisions continue to be upwards, following the better than expected current reporting season. The latest number is +8% from the low in May, which is double the +4% we showed in a recent note. This positive trend clearly supports investor sentiment.

The following chart reflects an interesting experience in the US consumer market:

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



US – Retail Sales Indexed to 100 at the Credit and Virus Crisis Peaks

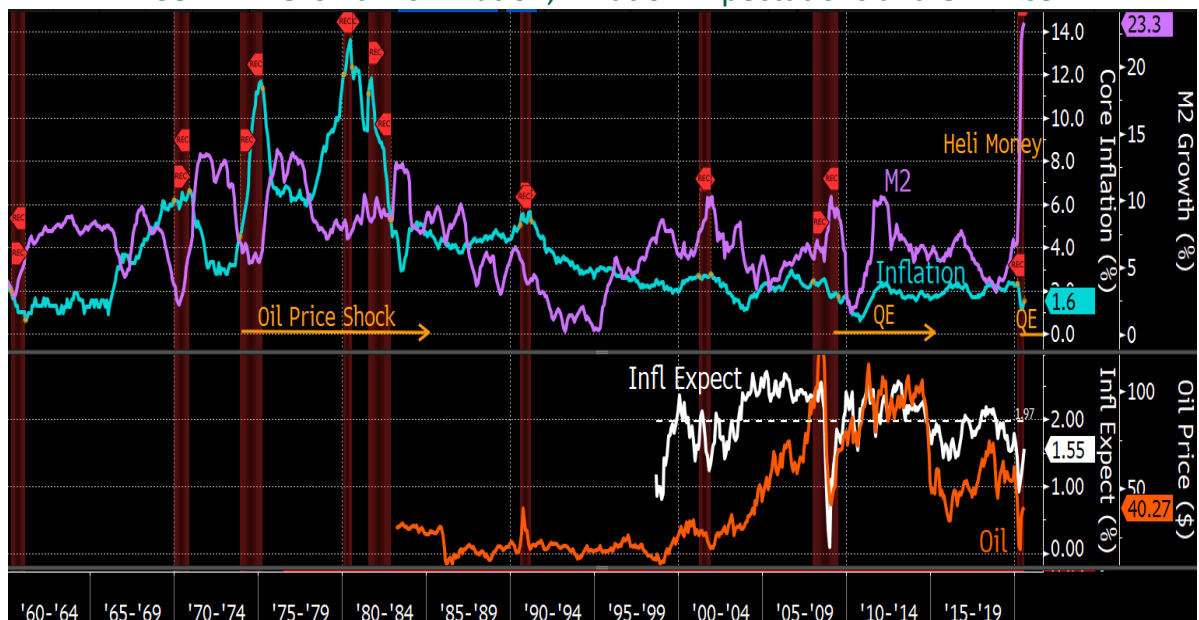


Retail sales took over nine quarters to recover to their 2008 peak level with the Credit Crisis. They have now with the Virus Crisis taken just two quarters to recover to their recent peak level. This is another indication that the US economic recovery process is well on course.

3. INFLATION

Many investors fear high inflation following the large quantitative easing programs throughout the world. We have the following information to share in this context:

US – M2 Growth vs Inflation, Inflation Expectations and Oil Price



Inflation is currently at a low level (the blue line). Although the current M2 growth level is at an extraordinary level, inflation seems to have historically reacted more on the oil price than on M2 growth.

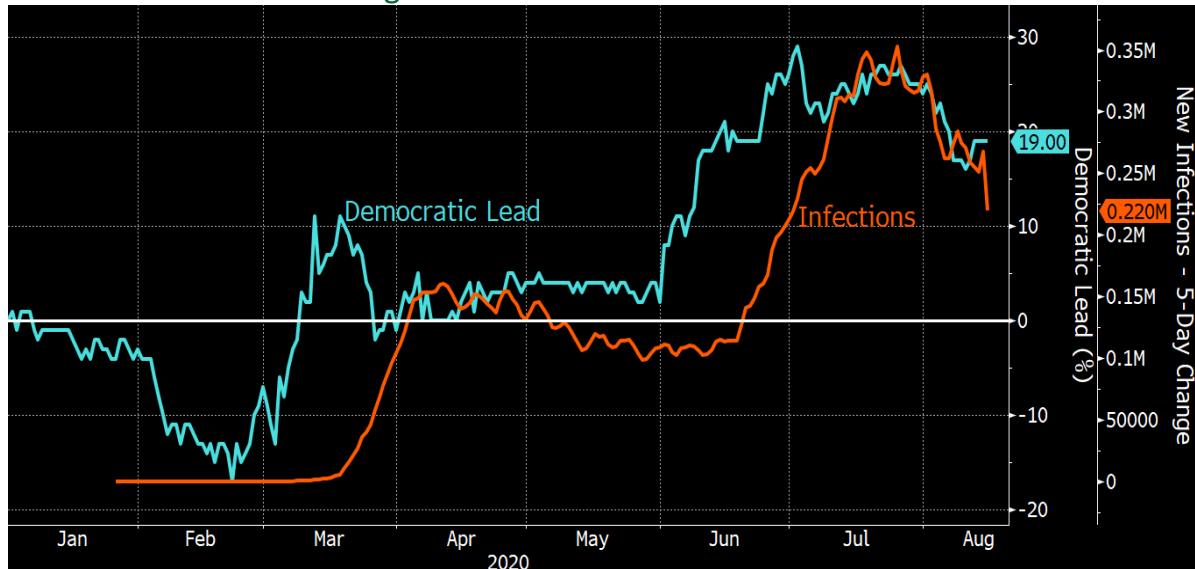
Ten-year inflation expectations (the white line) collapsed with the Virus Crisis and recovered to a level of 1.6%. This level is well below its average, and the Fed's target of 2% (the dotted line, interestingly the same level as the average). We believe the low energy price, low commodity prices and an abundance of labour on offer can keep inflation at bay for a while.



4. US ELECTION

Most surveys currently expect the next US president to be the Democratic candidate. There are fears amongst investors about more regulation and higher corporate taxes should this turn out to be the case. The following chart sheds further light on this topic:

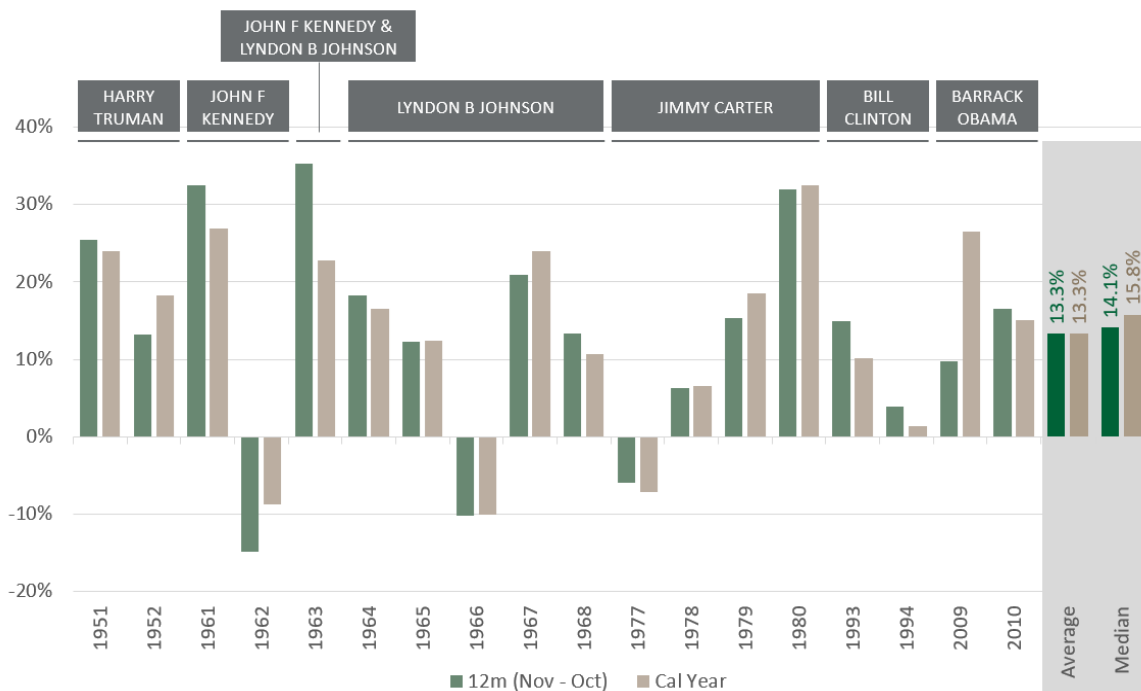
Spread of Implied Probability of a Democratic vs a Republic Presidential Win vs Change in New COVID-19 Virus infections



It is interesting how the change in virus infections seem to correlate with the candidates' odds to win. We can therefore expect a lot of COVID-19 rhetoric over the coming two months.

There are also general perceptions that a clean sweep of both houses by the Democrats may be taken particularly badly by capital markets. We did a study in this context:

S&P 500 Total Return when Democrats Control Both Senate and Congress (%)



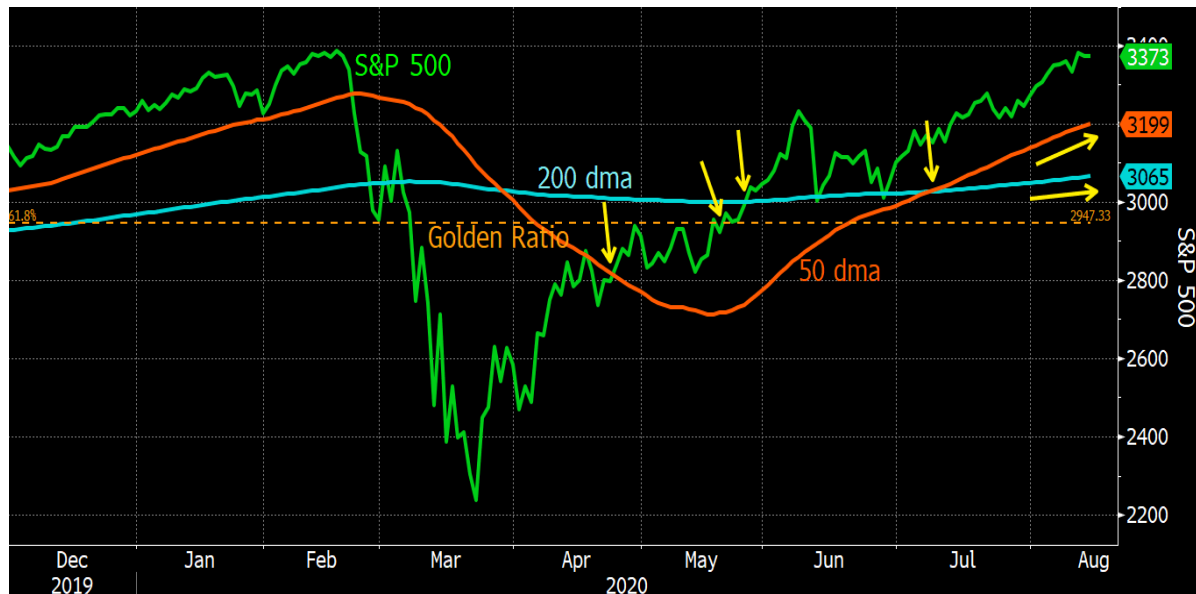
We calculated the returns over both the twelve months following the elections and the subsequent calendar years. There were only three occasions with negative returns, with both average and median returns well into double digits (compared to the return of +11.1% including all the other periods up to now). On this basis a Democrat sweep does not seem such a threat to Equity investors.

Source: US Department of Commerce & Stonehage Fleming Investment Management Limited. August 2020.

Past performance should not be used as a guide to future performance.

5. TECHNICAL PICTURE

S&P 500 – Price Index with 50- & 200-Day Moving Average



The S&P 500 index currently complies with all the positive technical tests, in sequence:

- It has crossed its 50-day moving average
- It has crossed its Fibonacci golden ratio
- It has crossed its 200-day moving average
- Its 50-day moving average is in a rising trend
- Its 50-day moving average has crossed its 200-day moving average
- Its 200-day moving average is in a rising trend

We are more fundamentally orientated investors. Purely from a technical perspective, this is a confirmed buy signal.

Gerrit Smit

**Partner - Head of Equity Management
Stonehage Fleming Investment Management Limited**

15 Suffolk Street
London
SW1Y 4HG

T +44 20 7087 0000
Email gerrit.smit@stonehagefleming.com
www.stonehagefleming.com/gbi

Source: US Department of Commerce & Stonehage Fleming Investment Management Limited .August 2020.
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Stonehage Fleming Investment Management Limited
15 Suffolk Street
London
SW1Y 4HG

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