GLOBAL EQUITY PERSPECTIVES 12 JULY 2020

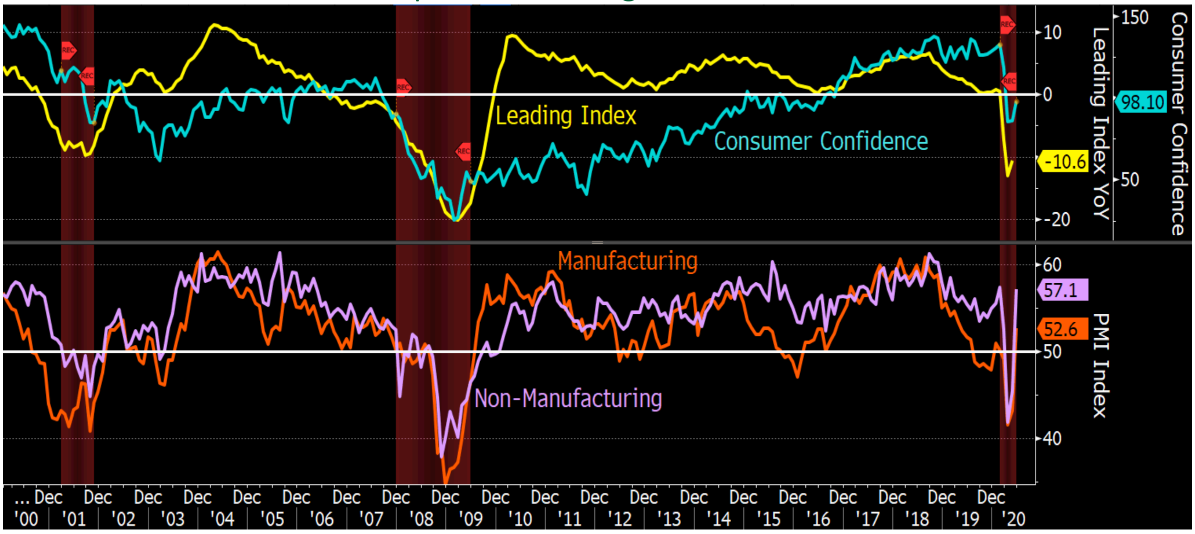
"The best qualification of a prophet is to have a good memory."

George Savile

1. ECONOMIC FUNDAMENTALS

Important leading economic data was released last week:

US – Important Leading Economic Indices



The Conference Board Leading Economic Index has dropped notably less than during the Credit Crisis, and seems to have stabilised. The same comment is true for Consumer Confidence – it has actually stabilised with the previous reading and turned upwards with the most recent reading. Both the Manufacturing and the Non-Manufacturing PMI indices have already recovered into constructive territory (readings above the 50-neutral level).

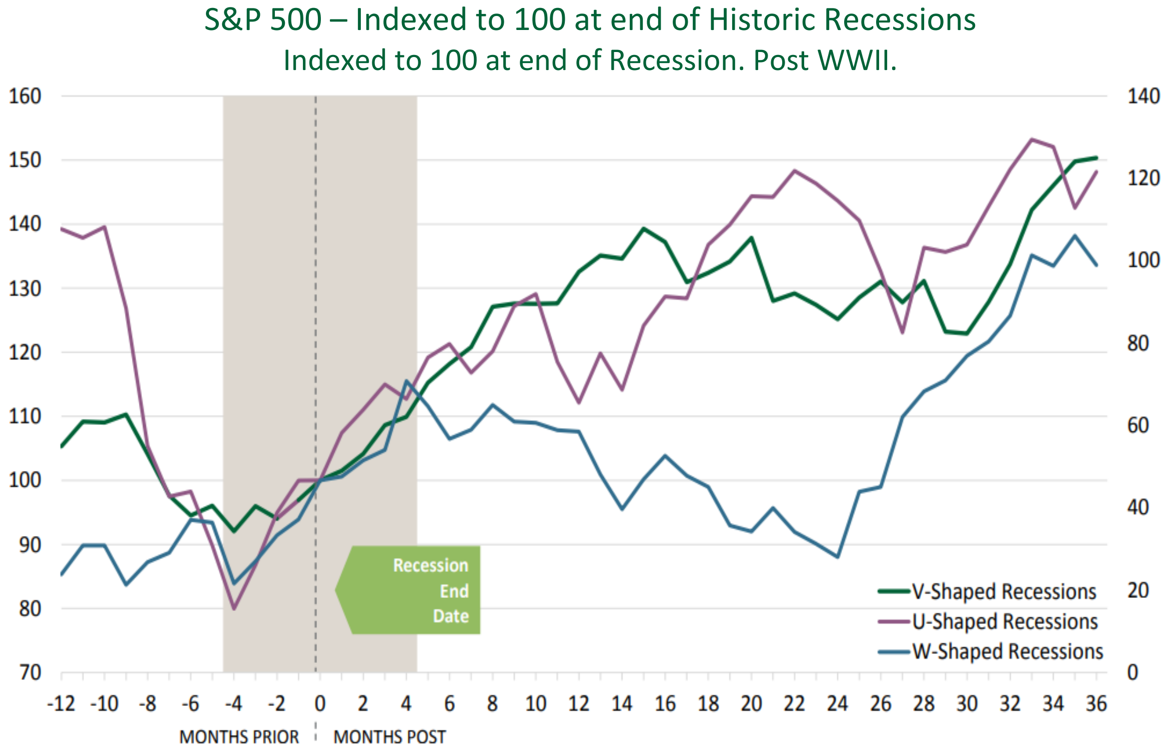
JP Morgan Global Manufacturing PMI Index vs Copper Price ($)

The global Manufacturing PMI index has also recovered well, though not yet to economic expansionary levels yet. The copper price acts as a fair global economic indicator and reflects a similar constructive picture.

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

2. ECONOMIC SHAPE OF RECOVERY

Economists and investors debate the potential shape of the new economic recovery cycle, be it a V, U or a W-shape (a low probability is generally assigned to an L-shape). We have studied the historic shape of the stock market recovery under each of those scenarios:



A few clear trends are identified form the analysis:

- Share prices behaved quite similarly under conditions of all of a V, a U and a W-shape economic recovery environment for about eight months (the shaded area in the chart. Investors had good time to form an impression what shape of economic recovery was heading their way.
- Share prices continued their recovery trend for longer under a V-shape economic recovery environment.
- A U-shape recovery delivered similar returns to the V-shape share price returns for nine months after the end of the recession.
- The U-shape recovery delivered more volatile share price deliveries than the V-shape, but at times outperformed and ended the three-year period with quite a similar overall delivery.
- Whilst the W-shape recovery delivered share price performances as good as the others for four months after the end of the recession, it subsequently underperformed for nine months. Share prices then resumed a strong recovery, ending the three-year period not that far from the V or U-shape economic recoveries.

On the basis of this analysis, investors need not, for a while, be overly concerned about the shape of the economic recovery process coming their way.

3. MARKET RECOVERY

The market has completed an exceptional 3-month performance, of course off a very low base. After dropping close to 35% from its peak in February reacting on the GVC (Great Virus Crisis), the S&P 500 and MSCI AC indices have already recovered by +42%. They are within 6% of their peak levels.

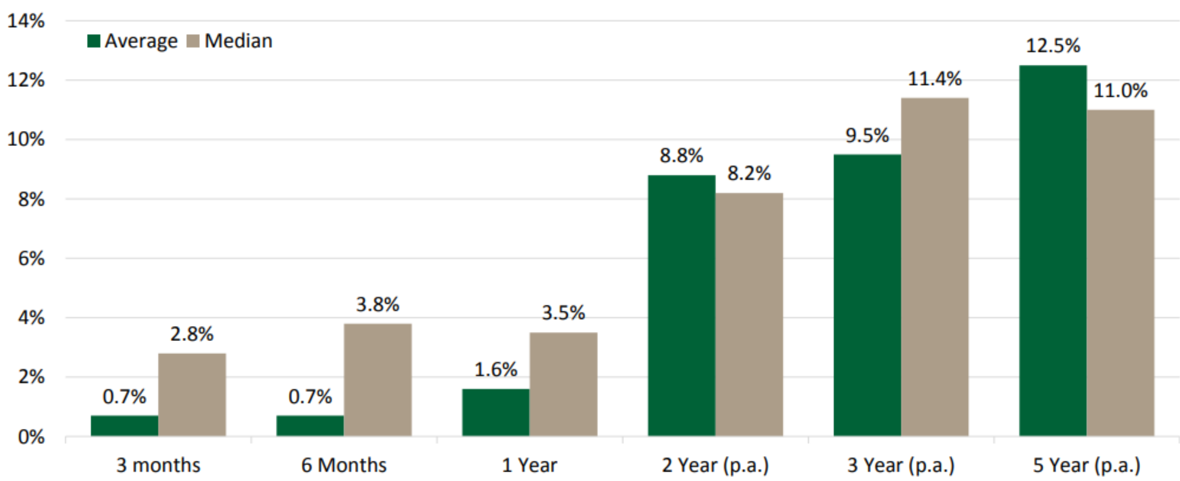
Source: Bloomberg & Stonehage Fleming Investment Management Limited. July 2020. ***Past performance should not be used as a guide to future performance.***

MSCI AC & S&P 500 Indices Indexed to 100 on 19 February 2020

On a rolling 3-month performance basis the S&P 500 index has completed the third best performance since 1950. Investors therefore rightfully wonder whether such a high base is a warning sign for low potential returns going forward.

We have studied the historic returns following the ten occasions with the best 3-month performances of the S&P 500 index since 1950. The results are reflected in the following chart:

S&P 500 Total Returns Following Its 10 Best 3-Month Performances
Data from January 1950 to June 2020



	3 months	6 Months	1 Year	2 Year (p.a.)	3 Year (p.a.)	5 Year (p.a.)
% Positive Readings	78%	67%	89%	89%	90%	70%

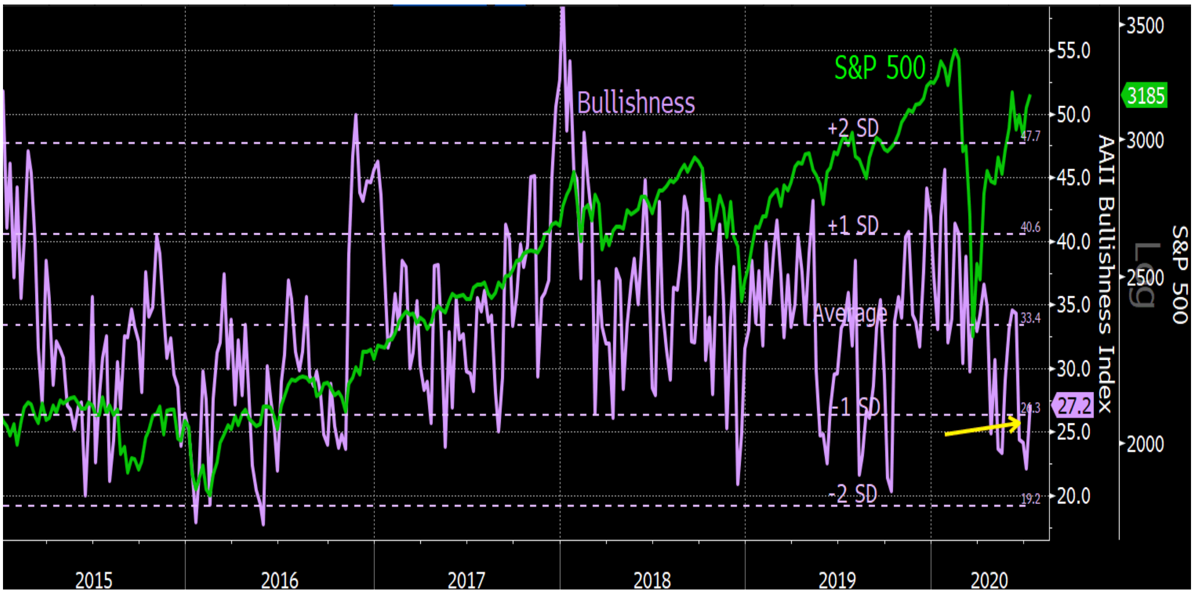
The chart reflects both the average and the median performances following the best performance occasions. The results are pleasing after three months, in some instances well into double digits. The ratios of positive readings are also high in most cases. Based on this chart alone, it therefore seems that investors should not fear the good stock market recovery we're currently experiencing.

4. FEAR OF COMPLACENCY

Many perceive the market to be complacent currently. The following charts provide some context:

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

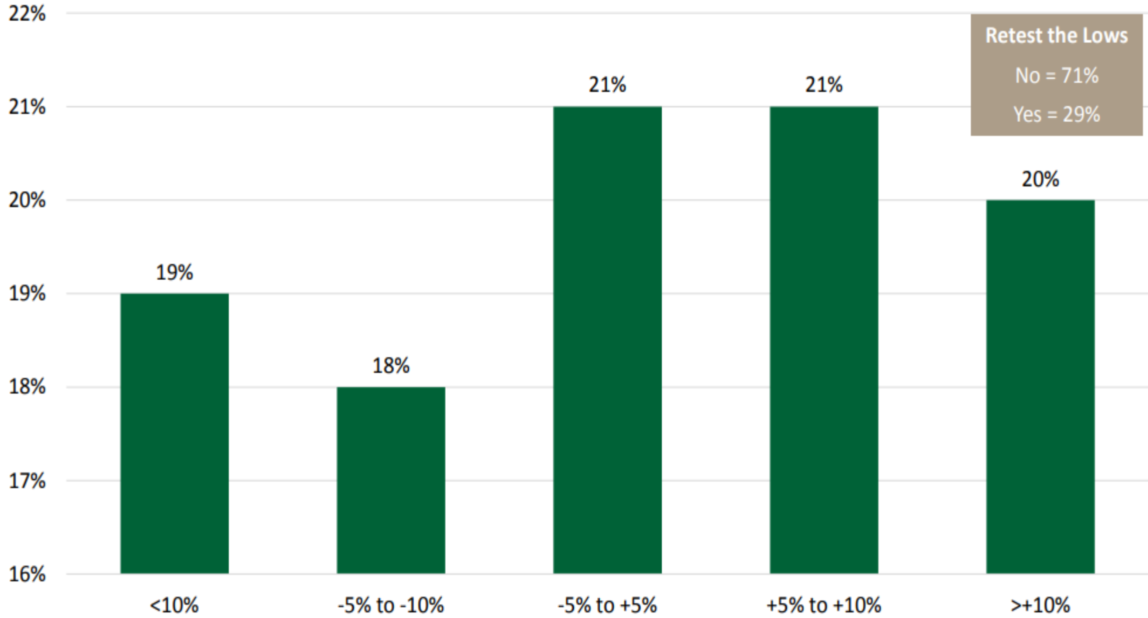
AAII Bullishness Index vs S&P 500



The above chart reflects the level of bullishness in the US retail market, based on the surveys done by the American Institute of Individual Investors. Strikingly, their views have thus far served as good contra-indicators – they are often most bullish at market peaks (the reverse is also true). The Index is currently at -1 SD (Standard Deviation) levels, reflecting severe pessimism. We do not detect any complacency in this chart.

The following chart is helpful in the context of the US institutional market:

Survey Question : Where Will the S&P 500 Index be at Year End
Compared to Current Value



Source : Datatrek survey of investors with 341 respondents (29 June 2020)

Participants in the above recent survey indicated the return bracket they expect by year end. We take the middle bracket (-5% to +5%) as a neutral level. Those readings to the left (the pessimists) add up to 37% of the participants, while those to the right (the optimists) add up to 41%, leaving only a small edge on the pessimists. Further to this, the extreme optimists (>+10%) exceed the extreme pessimists (<-10%) by only 1%. It therefore seems that that institutional market is quite balanced in their views and we do not detect complacency here either.

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

5. EARNINGS CYCLE

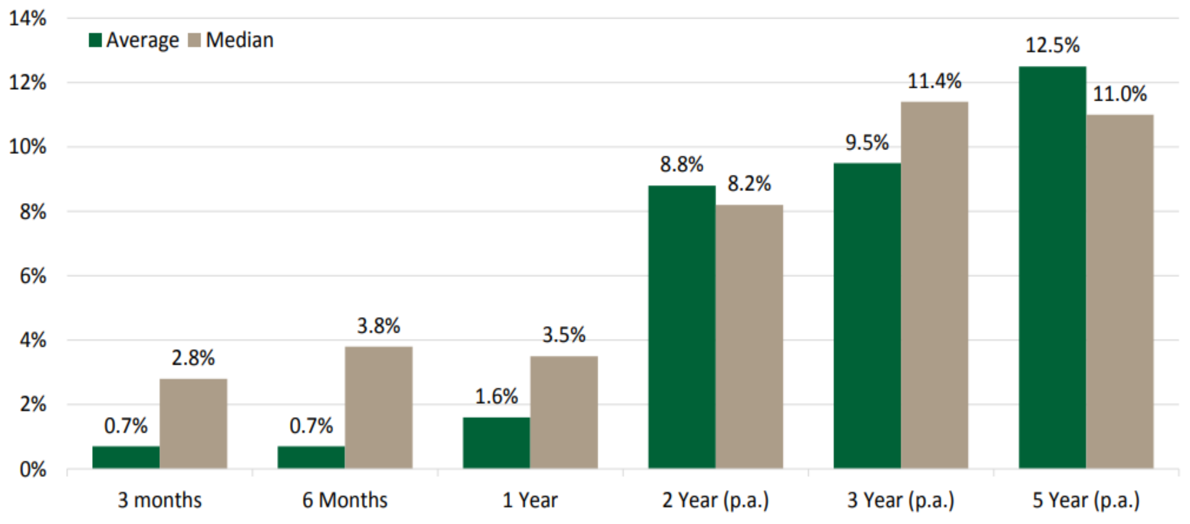
Share prices follow earnings expectations most of the time. As with the GFC (Great Financial Crisis), it seems that the earnings outlook with the GVC has bottomed less than two months after the S&P 500 index bottomed, as reflected in the following chart:

S&P 500 vs Consensus Expectations for 12-month Forward Earnings ($)

It is striking that the earnings expectations keep rising, and are already 10% higher than at their bottom. The earnings trend therefore appears to be structurally supporting share prices.

We have done a study in this context on earnings cycles after US recessions. The results are reflected in the following chart:

S&P 500 – Total Return Following Bottoms in Earnings Cycles
Data from January 1950 to June 2020



% Positive Readings	78%	67%	89%	89%	90%	70%

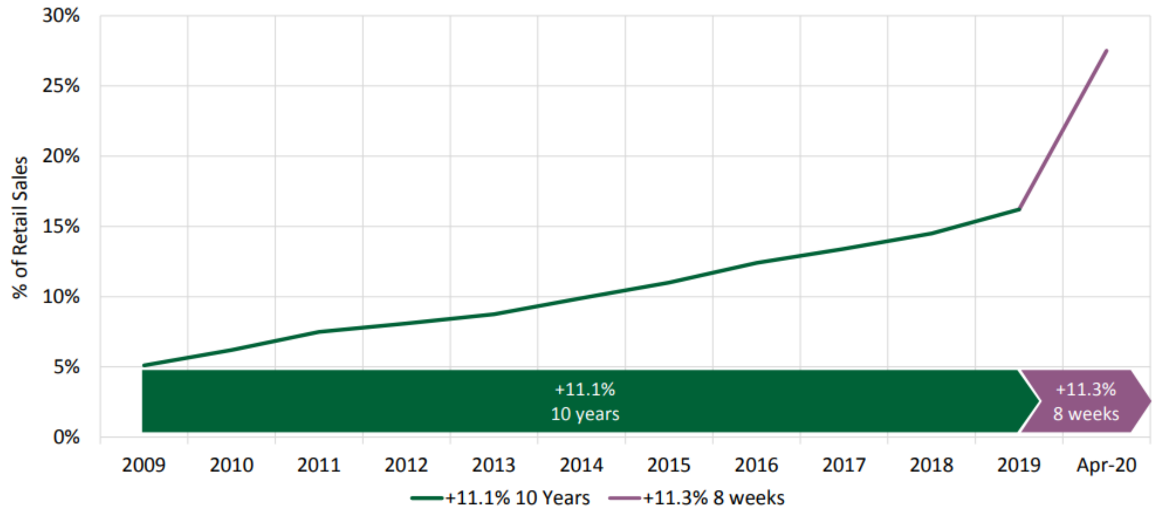
Returns have been predominantly positive after bottoms in earnings cycles, in double digits compounded returns over longer periods. On this basis, it would be good for investors if the current earnings cycle proves to have already bottomed. We believe investors should therefore rather look for entry than exit points to reap the benefits of being in the market.

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

6. E-COMMERCE

The e-Commerce industry has very soon been a major beneficiary of GVC. Whilst this is general knowledge, we wonder whether everyone realises the extent of the structural change:

US – e-Commerce Penetration (% of Sales)
Acceleration of Strong Trend



Before the GVC, the e-Commerce penetration was 16%. It took ten years to increase the penetration by 11%. Within two months of the GVC, the penetration increased by a similar percentage. Effectively, this industry has been propelled into the future, at little cost. The leaders now have an immense competitive edge being ready with their infrastructure, and can be much more profitable immediately.

We cannot recall such a positive seismic shift in any business environment before.

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