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FINANCIAL PLANNING

Market Update

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INVESTMENT SERVICES

The portfolio made further progress over the final quarter to complete a very profitable year for investors. The prospect of interest rates remaining at very low levels has lifted valuations of all financial assets, despite the disappointing progress of the global economy. The growth in the global economy is still weak but has at least shown signs of stabilisation following several quarters of deterioration. Given that we previously warned about the possibility of some key global economies slipping into recession, this is encouraging. However, we don't think we are out of the woods yet and it will take a further quarter or two before we can start to become more confident in the outlook. We are pleased with the returns generated by the portfolio, which have been achieved without resorting to taking an aggressive stance.

There have been many issues which could have derailed markets over the last year. One of them being President Trump's trade policies which have caused a trade war between the US and China. Thankfully, Presidents Trump and Xi agreed the first part of a deal in December, which has at least stopped an escalation in the dispute though we can't help but feel that this is little more than a temporary truce to cover the period leading up to the US Presidential elections.

The US Presidential election takes place in November and the early polls are suggesting that the outcome could go either way. We suspect that if Trump secures a second term, the trade dispute will reignite. Alternatively, a Democratic President may look to reverse some, or all, of the recent corporate tax cuts. Such a move would knock US share prices. Given this risk, we have decided to reduce exposure to the US and reallocate proceeds to the UK stock market, which has lagged the performance of the US market by a considerable margin over the last 5 years.

> Low interest rates
> support high valuations

The big news for the UK market has been the convincing win by the Conservative Party in the General Election. For the first time in over 10 years the UK has a strong Government with room to increase spending or cut taxes. Prime Minister Johnson now has a clear mandate to proceed with the UK's exit from the EU, although the precise terms of the withdrawal agreement have yet to be finalised. This has lifted some of the political fog which has plagued the economy since the referendum. The UK stock market celebrated the news by rallying but the main impact has been on the price of sterling, which has begun to climb in the foreign exchange markets.

A stronger pound has impacted the value of the portfolio's overseas holdings, which has held back returns over the quarter. That said, the price of sterling remains a long way below where it stood just before the referendum. If Johnson can secure a sensible settlement with the EU, we suspect that there is further room for sterling to rally from here. However, this is by no means a certainty and a 'hard Brexit' is still possible. We believe that the odds of a damaging hard Brexit occurring have fallen, so we have modestly increased exposure to the UK market.

The performance of the UK economy has been very disappointing over the last few years. For example, productivity growth has been dire and the trade deficit has remained stubbornly wide, despite the more favourable exchange rate for exporters. Hopefully this has largely been caused by Brexit uncertainties and the economy will improve as these are clarified. If so, we may look to lift further our exposure to the UK economy.

Stock market returns over 2019 have been extraordinarily good given that profits across the main markets have failed to grow as expected and that the performance of the main economies has been disappointing, manufacturers in particular have struggled. Long term interest rate expectations have been ratcheted down once again causing the existing income streams generated by both bonds and shares to become increasingly valuable. Hence share and bond prices have risen. The prospects for economic growth at best seem lacklustre and low interest rates will mean that future portfolio returns are likely to be modest especially in comparison to the recent gains. Nevertheless, returns from equities should average well ahead of those generated by cash though they are unlikely to come as steadily as they have done over the last 12 months.

> Finally the UK has a strong
> Government valuations

Important Information