Elgin asset management

investment commentary monthly

Monthly Commentary 2nd December 2020

November's gains were the opposite of October's losses, and then some. In fact equity markets set many records for monthly gains in November, bringing smiles to investors in what has otherwise been a horrible year for the World. Led by huge gains in Europe, MSCI World was up by 11.3%. This is massive. Bonds also had a good month, especially corporate and high yield, as did oil, which was up by a quarter. On the flip side there were few losers, the most notable being gold (-5.4%) and the US Dollar (-2.3%).

Now what?

After such a huge run, one would expect a pause, and it might very well happen. But what are the medium-term prospects for the market? It could very well be that "the stars have aligned" to create a favourable environment for equities. This was primarily driven by the good news on vaccines, which should unleash stronger economic growth across the world. Below are our thoughts on the big picture (starting with the negative):

Reasons to be cautious:

- Markets are overbought technically, as they have risen a lot in a short period of time.
- Valuations are stretched, especially for growth stocks.
- Yes, there are vaccines on the horizon but Covid is causing a lot of economic damage until then. It might take years to recover from this shock.

Reasons to buy:

- The Fed and other Central Banks are, and have indicated that they will remain very supportive with monetary stimulus for a long time. This is probably the single biggest reason to stay invested. I.e. do not fight the Fed. Other Central Banks are equally accommodative.
- The Biden administration should provide more certainty on world trade, with fewer surprises. This policy stability is a huge catalyst for companies to invest more in R&D, as well as inventories that will satisfy pent-up demand.

- The new Treasury Secretary, Janet Yellen is a well-respected dove and she will have enough support from senators to have a bigger stimulus package than the Democrats would have done without her, while (probably) facing a Republican-majority Senate. This is very positive as a new meaningful package will support employment, and thus consumption.
- There is still a lot of money that was saved during the crisis that is sitting in bank accounts. In the US, a personal savings rate of about 13% (vs. an average of 8%) is the highest in almost 5 decades. This money will eventually be spent to buy goods and services and/or equities.

So it seems there is a perfect storm in favour of continuing strength in equity markets. Our only hesitation is that this optimism is very consensual amongst the financial cognoscenti. Consensus makes us uneasy.

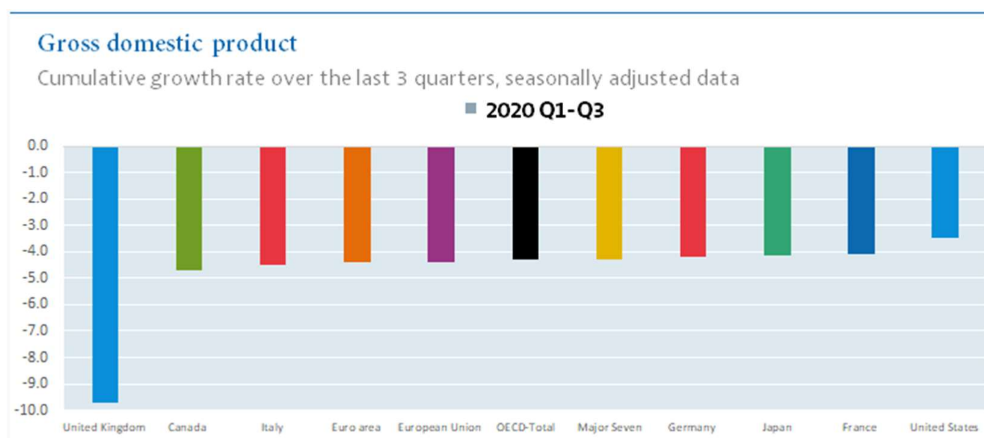
The weakening dollar

Another consensus call is for further weakening of the USD. We are agnostic on this and agree with David Riley, the chief investment strategist at BlueBay Asset Management who said:

"*FX forecasting is a specialist form of financial-market astrology that I remain wary of*".

It is better not to take large currency risk when managing portfolios.

GDP in the first nine months of 2020



The chart above shows the impact on the economic output in major areas of the developed world for the first three quarters of the year. The falls have been

unprecedented, but not as bad as the original forecasts back in March and April. The only standout, in a negative sense, has been the UK, which has had a loss in output that is almost double that of the second worst, Canada. It seems that the UK government has done everything possible to self-destruct. Perhaps it is a lesson to all populist leaders.

US Elections part 2

In November's commentary we dedicated more than a page to the US elections. Based on the results, we are happy to report only one emotion:

The markets also seem to like with the outcome…

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