WeekWatch

28 January 2019

Stock Take

The late comic Victoria Wood once said, “Life's not fair, is it? Some of us drink champagne in the fast lane, and some of us eat our sandwiches by the loose chippings on the A597.” Last week, many of the former could be found glad-handing their way through the World Economic Forum in Davos. Two notable absences, however, were Donald Trump and Theresa May, whose domestic troubles kept them away from the slopes and the champagne.

However, the bubbles may have stuck in the throats of those who were able to attend, as they reflected on some gloomy figures released by the IMF. It has cut global growth forecasts in 2019 to 3.5% – down from the 3.7% it had predicted at the end of October.

One of the biggest drags on the global picture is China, where growth of 6.6% in 2018 was the lowest rate since 1990. Although this was in line with forecasts, slowing growth could mean China struggles to reduce its huge domestic debt. There was a bright spot though, as retail sales are predicted to reach more than $5.6 trillion in 2019; about $100 billion more than the US.

“On a longer-term basis, we believe that China’s growth story remains intact,” said Alistair Thompson of First State Stewart Asia, manager of the St. James’s Place Asia Pacific fund. “Chinese companies have been focusing more on research and development, and product innovation, in order to compete with global peers.”

The World Bank has expressed fears over the impact China could have on other Asian markets, due to what it called “deep regional and global integration”. To this end, the ongoing trade war with the US is jangling nerves, particularly in Taiwan, Singapore and Korea, which are net exporters to China. China and the US are keen to agree a deal before 1 March when tariffs on $200 billion of Chinese goods will rise from 10% to 25%.

A high-level delegation will travel from Beijing to Washington this week to hold talks aimed at resolving the dispute, amid signs that the weakening economy is putting pressure on the Communist Party of China to ensure it delivers the ‘Chinese dream’ to its people. Rising unemployment is seen as a near-term risk, compounded by a growing trend of foreign companies diversifying their sourcing and production away from China.

However, in an interview last week, US Secretary of Commerce Wilbur Ross dampened optimism, stating that “we’re miles and miles from getting a resolution”.

On the other side of the trade war, Donald Trump has had to contend with an equally draining domestic battle, which kept him away from Davos, as the longest-ever government shutdown eventually ended after 35 days – longer than the entire presidency of William Henry Harrison, who died after just 31 days in office in 1841. Trump was forced to postpone his State of the Union Address before he eventually backed down on Friday and agreed a short-term funding solution to reopen the government. It has been estimated that the shutdown reduced economic growth by 0.13% for every week it lasted. The Dow Jones, Nasdaq and S&P 500 indices all regained ground following the end of the shutdown and on the back of strong earnings figures, having suffered losses earlier in the week. The Dow crossed 24,800 for the first time this year, hitting a level last struck in early December.

Domestic stalemate also explained Theresa May's absence from Davos, as the Brexit debate rumbled on. There was indication that some Brexiteers and the DUP would consider backing her deal if she can time-limit the Northern Ireland backstop; these hopes helped the pound climb over 1% against the dollar to a three-month high. The words of business leaders may be playing on the minds of politicians, as Airbus, Goldman Sachs and Sony all announced strong opposition to a 'no deal Brexit; although Fujitsu said it had no intention of moving its European headquarters away from London.

The week saw yet more confusion and division. Chancellor Philip Hammond claimed that the EU might be prepared to drop some of its red lines, while Commons leader Andrea Leadsom said the EU would agree to a short extension of Article 50. Downing Street stated that it was not considering an extension while, at the weekend, Ireland's deputy prime minister said the backstop plan was "not going to change".

The prime minister would have been heartened that employment reached a new record, while average earnings increased by 3.3% (annualised) to the end of November – the biggest gain in 10 years; moreover, wage rises outpaced inflation. Andrew Wishart of Capital Economics said the figures were "reassuring, showing no sign of any hit to firms' hiring ambitions due to Brexit".

First State Stewart Asia is a fund manager for St. James's Place.