WeekWatch

11 February 2019

Stock Take

The Chinese Year of the Pig, which began last Tuesday, is traditionally linked to luck and wealth – just not for the pigs. Wholesale pork prices in the last week of January were down 15% (annualised) after an outbreak of African swine flu spurred Chinese farmers to rush to market. More than half the pigs consumed worldwide this year will be eaten in China, while close to half of the world's feed crops will end up in the troughs of China's 433 million swine.

If only China's headline growth numbers were so easy to herd; instead, most analysts believe the official figures are inflated. Having pledged to double GDP between 2010 and 2020, Beijing certainly has the incentive to tell a few porkies. Last week's Chinese factory production figures pointed to declining demand for Western imports. All the same, global reliance on China continues to rise; Japan now exports more to China than to the US.

Indeed, Nissan's announcement that it would not build the new X-Trail at its Sunderland plant – despite £80 million of government funding – probably said more about the company's long-term geographical priorities than it did about Brexit. (Caveat lector: a Yougov poll last week found that 47% of Leave voters blamed business reasons for the pull-out while 74% of Remain voters blamed Brexit.)

Toyota, meanwhile, announced a fourth quarter profits slide of 81%, annualised – and spoke out against a no-deal Brexit. But the eyebrow-raising results were less to do with sales than with Toyota getting burned by dabbling in stock markets. In its core business, Japan's biggest carmaker saw a 15% rise in Asia sales, even as US sales slipped.

"Toyota's recent strong business results in the Chinese market were partly attributed to the sales increase in its hybrid vehicles, of which the company has expanded the product line," said Yoshihiko Ito of Nippon Value Investors, manager of the St. James's Place Japan fund. "The company forecasts an 8% increase in sales in the Chinese market to 1.6 million units in 2019, reflecting strong sales of hybrid vehicles. Toyota is expected to maintain its strong sales in the Chinese market by increasing local production."

The TOPIX index fell through the week, however, reflecting persistent fears over the outlook for US–China trade. Donald Trump's comment that he would not be meeting with the Chinese President ahead of the next sanctions deadline had traders fretting, after a State of the Union Address that offered little red meat to markets and a World Bank president nomination that looked decidedly anti-globalist.

The S&P 500 ended the week essentially flat, as a corporate earnings-driven run finally petered out. Yet short-term market zigzags should not be confused with economic fundamentals: if the current US expansion continues past 120 months later this year, it will be the longest on record.

In the UK, the Brexit saga offered a few more staging posts for the wearied onlooker: Donald Tusk warned there was “a special place in hell” for those who'd argued for Brexit “without any hint of a plan”; Jeremy Corbyn offered up Labour’s Brexit deal conditions – and Theresa May rejected them; the UK and EU agreed to reopen negotiations; the Department for International Trade admitted to a paucity of trade deals in the can; details emerged of ‘Project After’, a government initiative to plan for a no-deal Brexit; and there was news of a fresh amendment that could see Theresa May’s deal through parliament, if she then holds a referendum on the deal.

The Bank of England cut its 2019 UK growth forecasts from 1.7% to 1.2%, the worst since 2009; official growth figures for December showed last year was the UK's slowest year for growth since 2012. The FTSE 100, meanwhile, enjoyed a strong week, aided in great part by BP announcing a doubling of annual profits on buoyant oil and gas output; new figures showed that the US had become the UK’s top oil supplier for the first time since the Suez Crisis.

"If you look at the operating expenditure per barrel of oil produced, it’s gone down by 50%," said Nick Purves of RWC Partners, manager of the St. James’s Place Equity Income fund. “The market is still cynical about these kinds of turnarounds. You can still buy BP and Shell at dividend yields over 6% at a time when the free cashflow to pay those dividends is close to 10%, so they are well-covered dividends.”

Across Continental Europe, trends looked far from robust, with weak services data for Italy and France, and poor manufacturing data in Germany, raising fears of a eurozone-wide slowdown; Italian government bond yields jumped sharply after the European Commission cut Italy's growth forecast from 1.2% to just 0.2%. The threat of African swine fever was also making itself felt in Europe; Denmark is currently building a wall on its German border to keep out wild boar, which might otherwise pass the disease to its 28 million pigs.

Nippon Value Investors and RWC Partners are fund managers for St. James's Place.

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