DART CAPITAL

Market Commentary

July 2019

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Despite a global economy which continues to show signs of slowing, the prospect of rate cuts from the world's major Central Banks – led by the US Federal Reserve and the European Central Bank - helped fuel gains across equity and bond markets over the month. Domestic political uncertainty continued to put pressure on the Pound, as the market priced in the growing likelihood of a no-deal Brexit under the new Prime Minister, Boris Johnson.

UK

Despite official data from the Office of National Statistics (ONS) which showed that the economy grew 0.3% over May, aided by a recovery in car production, the broad trend in domestic data has been one of weakness with main bedrock of the economy - consumer spending – under pressure amidst weak household confidence. Widespread US Dollar strength and the growing likelihood of a hard Brexit outcome under the new Prime Minister, Boris Johnson, put further pressure on the Pound, with the GBP/US Dollar exchange rate falling 4.2% over the month, to end the period at $1.22, its lowest level since early 2017.

The growing risk of a Hard Brexit is particularly impactful on the Pound because, in such an event, it is expected that the Bank of England would apply further monetary stimulus, most likely through cutting the base rate from the current level of 0.75% and potentially even embarking on more Quantitative Easing. We note that whilst holding overseas currencies remains an important element of our managed portfolios, we believe there are risks to shifting too heavily into currencies such as the US Dollar or the Euro at this time, not least because both currencies suffer from political and economic risks of their own whilst the Pound looks increasingly cheap against both. Within the domestic equity market there remained a sharp contrast between globally exposed stocks, which benefitted from the weakness of sterling, and those companies which are more exposed to the domestic economy which continued to lag amidst the weak sentiment towards the domestic economy. MSCI UK All-Cap gained 1.8% in sterling terms.

By the end of the month, the yields on Gilts of all maturities had fallen to levels last seen in the immediate aftermath of the EU Referendum in 2016, with the yield on the 10 and 15 year Gilts falling to 0.5% and 0.9%, having started the year at 1.2% and 1.6% respectively. Although this move that has conferred significant gains to existing holders of longer-dated government bonds, it is worth highlighting that whilst Gilts are often referred to as a "risk-free" asset, this is only true from the perspective of default risk as after all the Bank of England can always print more money to pay bond investors at redemption. Importantly, investors holding long-dated nominal Gilts are still exposed to elevated risks of a different kind. For instance, investors in the aforementioned 15 year Gilt are exposed to high levels of inflation risk (the inflation-adjusted proceeds investors get back in a decade and a half's time will be far lower than the value invested), and interest rate risk (the not inconsiderable risk that market interest rates on UK debt move higher at some point between now and redemption in 2034). With yields as low as they are currently, we would question whether Gilt investors are being sufficiently compensated for these risks, particularly given the growing likelihood that the UK government will pursue more aggressive spending policies over coming years.

US

US economic growth slowed to an annualised pace of 2.1% over the second quarter, with this slowing blamed largely on the impact of tariffs and weaker overseas demand. However, household spending remained a source of strength within the figures, with personal consumption growing at annualised pace of 4.3%, whilst government spending also helped bolster growth. With inflation still below the US Federal Reserve's target, and a domestic and global economy that has slowed, at least one interest rate cut by the Federal Reserve had become an increasing certainty over recent months, with the prospect of looser monetary policy helping spur equity indices higher across the globe.

On the last day of the month the US Federal Reserve's monetary policy committee (known as the FOMC) followed and met these expectations, agreeing to cut the Federal Funds Rate (base rate) by 25 basis points, from 2.5% to 2.25%, the first time the Federal Reserve (the Fed) have cut rates since 2008. Given the move was widely anticipated, markets were most interested in the comments from Chairman of the Fed, Jerome Powell, in his press conference following the meeting, where he indicated that the cut was likely to be a "mid-cycle adjustment". This moderate stance disappointed some investors who had expected the Fed to signal the start of an aggressive rate cutting cycle, and the S&P 500 declined slightly on the back of the comments whilst bond yields rose slightly. Despite facing pressure from the White House to take a more aggressive approach to cutting rates, we expect the Federal Reserve to remain data-dependent in their approach to setting policy and it could be argued that the more encouraging economic data emanating from the US economy over the last month doesn't justify slashing rates even more aggressively at this time. Over the month as a whole, the S&P 500 gained 1.3% in US Dollar terms.

Eurozone

Christine Lagarde is now set to replace Mario Draghi as President of the European Central Bank (ECB) on 1st November following the EU's Finance Ministers signing off on her nomination. Lagarde, a lawyer and former politician, recently resigned from head of the International Monetary Fund (IMF) in anticipation of her new role and whilst Lagarde's approach to monetary policy has not been overly publicised, her public comments over recent years suggest she supports the unconventional stimulus measures taken by Draghi over recent years.

Draghi's eight-year term has been characterised by extremely loose monetary policy including the introduction of negative interest rates, bond purchases and bank loans. Having spent much of 2018 speaking about his desire to raise interest rates before leaving his post, Draghi has reversed course and has set the stage for the ECB to deliver another round of stimulus to combat the current economic slowdown the Eurozone is currently experiencing. Alongside this, Draghi highlighted that should the current slowdown continue, an increase in government spending from the Eurozone's governments, led by the ever-austere German government, would be vital in reinvigorating the currency bloc's economy. MSCI Europe ex-UK gained 0.1% in local currency terms.

Asia

Faced with the prospect of lower exports to the US, the Chinese authorities have employed ample fiscal and monetary stimulus to help support domestic demand although this wasn't sufficient to stop the economy's growth rate slowing to its lowest rate in 30 years over the second quarter. Further compounding the challenges faced by the world's largest economy has been the slowing housing market which has suffered as result of tighter government controls. The Japanese government cut its growth forecast for this fiscal year, citing weak exports, combined with the strengthening of the Yen over recent months further curbing overseas demand for Japanese products. MSCI Japan gained 0.9% in Yen terms.

Commodities

The gold price was broadly unchanged in Dollar terms over the month following a very strong second quarter, with investor interest in the precious metal having been bolstered significantly by the prospect of lower US interest rates. The gold price gained 0.3% over the month in US Dollar terms. The oil price spiked following Iran's seizure of a British oil tanker in the Strait of Hormuz mid-month, although concerns over future demand growth did quell price gains later in the period. The oil price, as measured by Brent Crude, ended the month $1 lower at $65 per barrel.

Asset Class Performance – End July 2019 (in Sterling terms)

Asset Class	Dart Capital Position	1 Month	3 Months	12 Months	Index
Cash	↘	+0.07%	+0.19%	+0.75%	Bank Of England Base Rate in GBP
Fixed Interest	↘	+1.26%	+3.71%	+5.24%	L&G All Stocks Gilt Index Trust I Inc in GBP
Equities – UK	→	+1.77%	+1.41%	-3.49%	MSCI UK All Cap in GBP
Equities – International	↗	+4.23%	+6.59%	+8.68%	MSCI All Country World Index ex UK in GBP
Property	↘	+0.13%	+0.19%	+1.07%	FE UK Property Proxy in GBP
Alternatives	↗	+0.07%	+0.19%	+0.75%	Bank of England Base Rate in GBP

Benchmarks are capital return which excludes income
Month to 31 July 2019
All performance data supplied by Financial Express Analytics
Dart Capital positions based on Dart Capital mid risk strategy

↗ Overweight
→ Neutral
↘ Underweight