DART CAPITAL

Market Commentary

August 2019

Investment Managers

Richard Whitehead
richard.whitehead@dartcapital.com

Chris Bellchambers
chris.bellchambers@dartcapital.com

Andrew Savage
andrew.savage@dartcapital.com

Research Team

Alexander George
alexander.george@dartcapital.com

Michael High
michael.high@dartcapital.com

Dart Capital
61 Queen Street, London EC4R 1EB
Tel: 020 7283 1117
Fax: 020 7283 0891

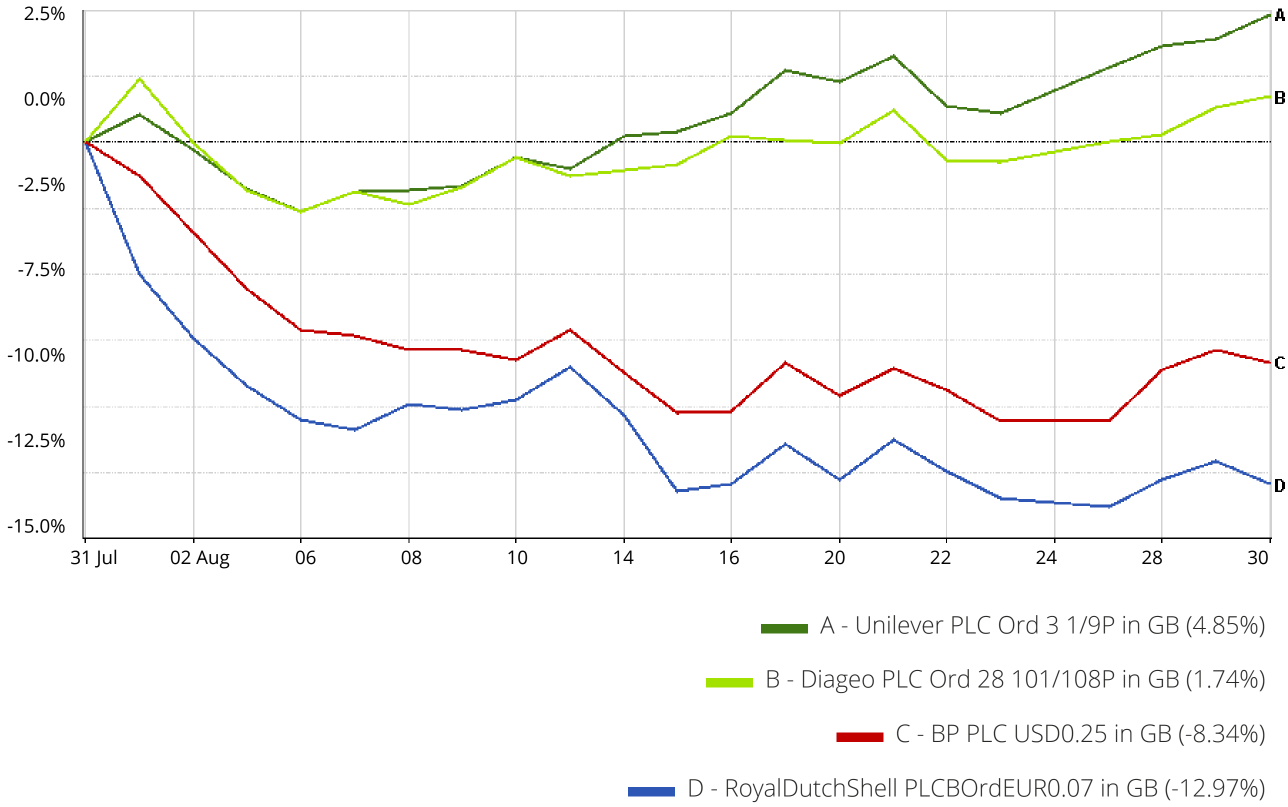
August saw dramatic moves across US and European bond markets, with yields declining back close to all-time lows in many markets on the back of expectations of further interest rate cuts by the world's major Central Banks as they fight slowing growth and the uncertainty caused by the trade tensions between the US and China. In the UK, the political situation remains at the forefront of everyone's mind with the UK inching closer to its planned exit from the EU on the 31st October. In light of the continued uncertainties around the Brexit process, it is important to note that our portfolios retain significant exposure to overseas assets and currencies.

Market dynamics

Expectations of further interest rate cuts by the US Federal Reserve drove down the yield on long-dated Treasuries, with the yield on the 10 year US Treasury eventually falling below the yield on the 2 year Treasury. This so-called "inversion" of the yield curve has historically been a concerning sign for the global economy as each US recession since World War II has been preceded by an inverted yield curve. However, whilst the inversion of the yield curve is certainly not a positive sign, it is my no means the harbinger of imminent doom that some headlines in the media seem to imply, with it providing no guarantee that a recession and a significant equity market decline is imminent. This is well demonstrated by the experience of the late 1990s, when the S&P 500 gained roughly 40% from the time the yield curve first inverted in mid-1998 to the market's eventual peak in August 2000. The 1998 comparison is perhaps particularly apt because at that time domestic US data was reasonable and concerns were mainly coming from overseas, most notably the lingering after effects of the Asian Crisis and spill-over effects of the Russian default.

The risk-off environment led most global equity indices to end the month down whilst the dramatic move in bond yields – the 10 year US Treasury yield declined 50 basis points over the month to end at only 1.5% - caused a sharp divergence in share price performance within the stock market. Most notably, companies which are viewed as less cyclical continued their strong run, whilst more economically sensitive stocks performed poorly. In the UK market, this dynamic was reflected by the strong performance of companies which sell staple items, with shares in Unilever and Diageo seeing their share prices rise whilst stocks in more cyclical industries, particularly commodity producers, struggled as shown below. We note that whilst these "defensive" stocks have continued their strong run so far this year, their valuations have moved well above their historical range whilst cyclical stocks are trading on far more modest valuations.

Unilever and Diageo outperformed BP and Shell over the month



31/07/2019 - 30/08/2019 Data from FE 2019

UK

The UK economy contracted over the second quarter according to preliminary data from the Office of National Statistics (ONS), with GDP declining 0.2% over April-June. The manufacturing sector has remained the primary source of weakness, as factories have suffered from weaker global demand and the unwind in stockpiling activity, which had previously helped bolster growth over the first quarter. Further cause for concern has come from sluggish business investment, which has – somewhat understandably – taken a hit amidst the continued Brexit uncertainty. However, it is certainly not all negative for the UK economy, with ONS data released over the month indicating that wages grew at their fastest pace for 11 years over the second quarter and the services sector remains in expansion territory.

Prime Minister Boris Johnson's plan to suspend Parliament for the six weeks in the run-up to the UK's planned departure from the EU at the end of October, along with his refusal to rule out a no-deal Brexit, put further pressure on sentiment towards UK assets at the end of the month. Despite this, the Pound held up far better than it did over July with sterling ending the month largely unmoved against the Dollar. The UK equity market was one of the worst performers over the month, with the aforementioned poor performance of commodity producing companies (which are heavily represented in the UK index) providing a notable drag on returns. MSCI UK All-Cap ended the month down 4.7% in capital return terms.

US

Having seen the US Federal Reserve (The Fed) cut the Federal Funds rate by 25 bps on the last day of July, President Trump upset markets on the first day of the month, with his threats to impose 10% tariffs on a further $300bn worth of Chinese imports causing a risk-off move in global markets. The threat of more tariffs comes at a time that inflation has shown signs of perking up, with the Consumer Price Index (CPI) gaining 0.3% in July, which pushed the index up to 1.8% for the 12 months to July. Despite concerns over the manufacturing sector which contracted slightly in August according to survey data, the labour market across the wider economy has remained reasonably buoyant with the economy adding 164,000 jobs in the most recent data release. Amidst political pressure to cut rates more aggressively, the Fed are expected to agree a further 25 bps cut in interest rates at their meeting in mid-September. The S&P 500 ended the month down 1.8% in US Dollar terms.

Eurozone

Eurozone economic growth slowed through the second quarter of 2019, with the preliminary reading for the period showing the economy grew at a mere 0.2% as economies across the region lost steam with the currency bloc's largest economy, Germany, actually contracting. Most notably, Germany's manufacturing sector has struggled over recent months with output undoubtedly hit by the ongoing US-China trade war, along with weakness within the very large automotive sector. The European Central Bank (ECB) are widely expected to cut interest rates further into negative territory in their September meeting and have warned that monetary policy may not be enough to boost the Eurozone economy, calling for an increase in fiscal stimulus from the German government. Although Chancellor Angela Merkel said mid-month she did not see any need for a fiscal stimulus package to combat the slowdown, as concerns over an impending recession have increased, Finance Minister Olaf Scholz suggested Germany are prepared to spend an extra 50 billion euros if it were required. Furthermore, towards the end of the month Peter Altmaier, Germany's Economy Minister, proposed cutting its corporate tax burden to 25%, supporting Germany's so-called 'Mittelstand', (small and medium-sized businesses). MSCI Europe ex-UK returned -0.9% over the month in local currency terms.

Asia

Asian stocks were shaken over the month by the Chinese government's move to weaken the Renminbi below the level of 7 Renminbi per US Dollar which the Chinese authorities have historically not wanted to breach, in an attempt to lessen the impact of higher tariffs on exports to the US and the strength of the US Dollar. Alongside their loosening of monetary conditions, the Chinese authorities have pulled a number of policy levers in an attempt to support the economy, most notably tax cuts and increased infrastructure spending. MSCI China H ended the month 6.0% lower in local currency terms.

Commodities

Investor demand for gold surged on the back of declining government bonds yields across the globe, with the gold price gaining 7.5% in US Dollar terms. In contrast, commodities, which are more sensitive to the state of the global economy, were weaker, highlighted by oil which declined from $65 per barrel to $60 and iron ore which fell from $120 per ton to $91.

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

Asset Class	Dart Capital Position	1 Month	3 Months	12 Months	Index
Cash	↘	+0.06%	+0.19%	+0.75%	Bank Of England Base Rate in GBP
Fixed Interest	↘	+4.43%	+5.83%	+9.81%	L&G All Stocks Gilt Index Trust I Inc in GBP
Equities – UK	↗	-4.72%	+0.06%	-4.66%	MSCI UK All Cap in GBP
Equities – International	↗	-1.88%	+7.82%	+4.69%	MSCI All Country World Index ex UK in GBP
Property	↘	+0.04%	0.00%	+0.83%	FE UK Property Proxy in GBP
Alternatives	↗	+0.06%	+0.19%	+0.75%	Bank of England Base Rate in GBP

Benchmarks are capital return which excludes income
Month to 31 August 2019
All performance data supplied by Financial Express Analytics

Dart Capital positions based on Dart Capital mid risk strategy

↗ Overweight
→ Neutral
↘ Underweight