Standard Life

October 2017 market review

For financial advisers only

Has this October bucked the seasonal stock market trend? Andrew Milligan, Head of Global Strategy at Standard Life Investments, discusses this and where he sees future opportunities.

Some bad stock market crashes have happened in autumn but this October seems to have bucked the trend

It's true that the infamous 1929, 1987 and 2008 stock market crashes happened in the autumn. However, at Standard Life Investments, we prefer to focus on economic and company fundamentals, our analysis of politics and investor flows, an understanding of government policy and market valuations. We've remained heavily invested in global equities in October, partly because the markets are starting to look forward to possible tax cuts in the US, which could boost profits.

The difficulty with the phenomena of seasonality in investing is that it isn't apparent every year, and after the cost of buying and selling stocks is taken into account, there's little evidence that it's a consistently profitable exercise.

Why we still like US equities

Tax cuts are top of the political agenda in the USA at present. There are many hurdles to cross for the US and for the Republican party in general. The Trump Presidency in particular needs some form of legislative success before the mid-term elections in autumn 2019. After all, healthcare, the wall, trade and migration matters have become much more complicated issues or embroiled in difficult discussions in recent months. So, Washington is trying very hard to pass some form of tax cuts by next spring – not tax reforms, as the money is just not there to finance anything too aggressive.

There's also been considerable speculation in financial markets about the next Fed Chair. President Trump has considerable opportunity to alter the balance of the Fed between doves and hawks. Markets were reassured that Jerome Powell is scheduled to replace Janet Yellen in this role, as he's seen as the continuity candidate.

With so many competing factions within Congress, an early resolution to any of the hurdles facing the US and the Republican party would be surprising. The stock markets have not yet priced in any major changes, especially in reference to tax cuts, so it's one of the reasons why we like US equities in our holdings.

UK markets and interest rates: now and in 2018

It's no surprise that the Bank of England raised rates at the Monetary Policy Committee's (MPC) meeting on 1 November. But it's a change that markets had priced in based on recent economic data and speeches from many of the MPC members.

The key issue for the markets will be how far and how often the Bank of England moves interest rates in 2018. Here the debate is really rather wide. There are different views about a number of factors, including:

- inflation
- sterling
- the impact of Brexit on confidence
- the boost from global trade
- fiscal changes in the Budget

All in all, we expect another move by the Bank in 2018 but it's very data dependent.

For example, the Bank's worried about levels of consumer debt and has encouraged the banking system to lend more cautiously. However, Brexit uncertainty does appear to be affecting business confidence and so capital spending. The UK looks to be a slow-growing economy for some time to come.

Prospects remaining good for a solid economic expansion in 2018

While media headlines highlight political uncertainty that's affecting individual countries, our fund managers take this into account through their stock selection. For example, we temper our house view and the risk levels in our portfolio to seek out opportunities in a range of global equities, such as Europe, despite what's happening around the world, whether that's in Europe, the tensions in the Middle East or if the US agrees a revision to the North American Free Trade Agreement (NAFTA) with Canada and Mexico.

In our view, there are still prospects in emerging market equities and selected emerging market debt too. Obviously though, there have been apparent risks for some time: markets would be concerned by any combination of an aggressive Federal Reserve, a sharp appreciation of the US dollar or a much weaker situation in China.

However, the backdrop of an expansion in global economic activity in general and regional trade in particular is very beneficial for emerging market assets. Our analysis has indicated that financial imbalances in many, not all, emerging markets have improved.

Putting aside a situation such as military conflict in North Korea, we see the prospects remaining good for a solid economic expansion around the world into 2018.

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