

# OCM Asset Management

## Discretionary Asset Managers | Stockbrokers

### Global Economic Update – 13<sup>th</sup> January 2021

**Globally**, world trade recovered sharply toward the end of 2020 and is expected to continue growing throughout 2021. However, as we have mentioned before with other areas of the global, the rebound is highly uneven across regions, economies and sectors. Transport and travel remain deeply depressed, weighing on services trade. Goods trade is doing better than services, but sectors like food and consumer goods are far outpacing capital goods. If vaccine rollout proves faster than expected, allowing a quicker removal of restrictions, trade growth this year might exceed 12%, according to Oxford economics. A slower-than-expected vaccine rollout and a renewed upsurge in infections, by contrast, could see the recent trade recovery stall and be delayed into 2022.

Across the world, the largest vaccination campaign in history is well under way. Over 30 million doses have been administered so far across 43 countries. The Pfizer-BioNTech vaccine has now been cleared for use across North America, Europe and the Middle East, while the Oxford AstraZeneca vaccine has gained its first major authorisation by the UK. There remain several logistical hurdles in rolling out the vaccine on a larger scale, but swift progress is boosting hopes for economic and social activity to begin to return to normal in H2 2021. However, the accelerated vaccine program continues to battle against increasing cases in many key economies around the world.

**In the UK**, speculation surrounding the implementation of negative interest rates from the Bank of England continued this week. Policymaker Silvana Teneyro said Monday that slashing interest rates below zero could boost the economy by more than expanding bond purchases. She also warned that the recent intensification of the current wave of Covid would imply a worse near-term outlook than anticipated in November. At the same time, Governor Andrew Bailey raised his doubts, warning that that negative interest rates would create complications for the banking sector at an already challenging period.

Record daily case numbers in the first week of the new year prompted the government to place the UK into its third national lockdown, in order to prevent the NHS from becoming overwhelmed. As a result, economists now predict that the UK will enter a double-dip recession, as they are almost certain that the UK economy will shrink in the first quarter of 2021, although the outlook from there brightens, as the impact of vaccinations should begin to feed into the virus data. The vaccination campaign is well under way in the UK, with a target of vaccinating 200,000 people per day in an attempt to return to normality as soon as possible.

**In Europe**, governments are extending and intensifying nationwide lockdowns as the continent battles with surging virus cases and the new, more contagious variant of Covid 19. Escalating the situation is the slow pace of vaccine distribution across the continent, even countries like Germany and Finland that had a relatively good record of managing infections and limiting mortality last year are now way behind global pacesetters such as Israel and the UK in the vaccine rollout. The sluggishness in response has attracted widespread criticism, however urgency does appear to be picking up.

European Central Bank President Christine Lagarde said the central bank's projections for 2021 growth were still very clearly plausible even with much of the 19-member euro area in lockdown. On the data front, PMI's

were revised lower in December, services remained the leading drag on economic output, with activity falling for a fourth consecutive month due to the effects of social distancing and travel restrictions, which will likely continue into the new year. On a brighter note, the bloc's industrial production rose 2.5% in November, marking the seventh consecutive month of growth and defying market expectations of a much smaller 0.2% increase.

**In the US**, violent protests in Washington did not disrupt a legitimate transition to a new presidency, with Congress certifying Joe Biden as the 46th President of the US. Meanwhile, Democrats took control of the Senate after winning the two runoff elections in Georgia, paving the way for more stimulus to revive the US economy. Joe Biden's full control of the US government is expected to allow him to implement major pieces of his agenda, raising fears over tax hikes and increased regulation further down the road, though it could signal more stimulus to come in the short term.

The dollar index lost ground for the 2nd straight session to trade around 90 on Wednesday, as the recent rally fuelled by soaring Treasury yields seems to be running out of steam as Fed officials eased speculation that asset purchases could be tapered soon. Meanwhile, the annual inflation rate in the US increased to 1.4% in December of 2020, from 1.2% in November and slightly higher than market forecasts of 1.3%. On a monthly basis, consumer prices increased 0.4%, higher than 0.2% in November and in line with expectations, mainly driven by an 8.4% increase in the gasoline index, which accounted for more than 60% of the overall rise.

**In Emerging Markets**, the outlook continues to vary with the prevalence of Covid-19, but unlike much of the developed economies, EM countries don't appear to be experiencing a severe second wave of the pandemic. China's GDP grew less than expected in Q3, however the recovery in its domestic demand cycle should continue, boding well for other emerging markets. Other Asian economies are also recovering, but as in Europe and the US, the sharp rebound in activity thus far is unsustainable, particularly as stimulus measures are scaled back. Meanwhile, EM economies are set to benefit from 2020's currency movements, namely the impact of the dollar weakening against other major currencies since June.

## Barometers

***The Barometers below look at some of the data we review on a day by day basis and by having these detailed, it gives you some insight into what is happening.***

*US Earnings are important because if the US starts to slow down, then so does the rest of the world.*

For Q4 2020, the estimated earnings decline for the S&P 500 is -8.8%. If -8.8% is the actual decline for the quarter, it will mark the third-largest (year-over-year) decline in earnings reported by the index since Q3 2009. On September 30, the estimated earnings decline for Q4 2020 was -12.7%. Seven sectors have smaller earnings declines or higher earnings growth rates today (compared to September 30) due to upward revisions to EPS estimates. For Q4 2020, 29 S&P 500 companies have issued negative EPS guidance and 56 S&P 500 companies have issued positive EPS guidance. The forward 12-month P/E ratio for the S&P 500 is 22.6. This P/E ratio is above the 5-year average (17.5) and above the 10-year average (15.7).

## Money Flows;

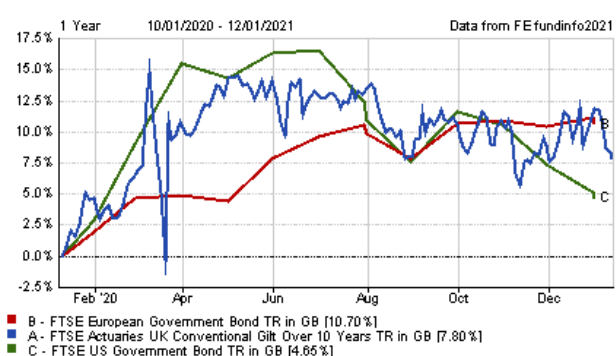
*By calculating money flows, we can analyse investors' perceptions on the markets and quantify whether they were positive or negative. A positive money flow is when a stock is purchased at a higher price, or an uptick and vice versa. This indication will give us a sign as to where we are on the economic cycle. To be able to quantify this, we have looked at the Money Flow Index (MFI) which is a momentum indicator that measures the strength of money entering or leaving a market. The MFI adds volume to the Relative Strength Index (RSI) and is also commonly referred to as the volume-weighted RSI. An MFI of over 80 suggests that the security in question is overbought and under 20 indicates that it is oversold (over the past week).*

In comparison to last week's MFI data, net money inflows into global equities increased as accelerating vaccination programmes and hopes for further stimulus from the US continue to boost market sentiment. Overall, we are starting to see flows returning after a challenging period, with institutional investors returning to markets.

MFI.FTSE	FTSE 100	= 75.710	Previously 63.856 (Increase)
MFI.INX	S&P 500	= 71.949	Previously 65.778 (Increase)
MFI.STOXX	Euro STOXX 600	= 75.700	Previously 59.629 (Increase)

## UK & Non-UK Government Bonds;

UK and Non-UK Government Debt are a good measure, as they indicate whether we expect the economy to improve or worsen, with rising yields reflecting positive environment and reflecting positive interest rate movements as we look out. The opposite with lowering yields as the expectation is worsening economic conditions.



Over the week, global government bond prices fell as speculation of a tapering of rates in the US and expectations for higher inflation helped push yields higher. Overall, we expect to see an increasing trend in government bond yields as the global economy recovers given current historically low yields.

## US 10-2 Year Treasury Spread

The 10-year/2-year spread refers to the divergence between the 10-year US Treasury bond and the 2-year Treasury note. In normal economic circumstances, the yield on the 10-year should be greater than the 2-year, creating a positive spread. This signals some combination of positive future growth expectations, positive future inflation expectations, and basic recognition that more adverse economic events are likelier to transpire over a longer timeframe than a shorter timeframe. Therefore, investors are compensated for taking on the higher risk of longer-duration bonds in the form of higher yields.

0.961 -0.03 (-3.0272%)



The spread between the 10-2 Year US Treasury yield widened this week as rate tapering speculation and inflation expectations caused a significant increase in yields at the longer end of the yield curve. Overall, the yield curve has steepened in recent months as the market is more optimistic about the future of the US economy and is signalling that the worst may soon be behind us. This trend is expected to continue as the economy recovers from the coronavirus.

#### GBP to USD/Euro/JPY;

*We monitor the GBP rate to see how much of the returns are coming from underlying equity valuation increases and movements in the currency, to see if we should be locking in the gains and hedging the risks. The 12-month expected range we have set below for sterling across the US Dollar, Euro and Japanese Yen is given the current economic climate and it is to reflect a more positive stance on Sterling in the near short term. Despite Brexit, the UK economy is quite resilient in showing optimism. It is inevitable that over the long term, as Brexit matures, Sterling will be more volatile and unpredictable, therefore it could potentially weaken further as the negotiations mature.*

Sterling reached a seven week high against the euro this week, building on gains from Bank of England Governor Andrew Bailey's comments about the negative implications of cutting interest rates below zero. Meanwhile the US dollar bounced off of its multi-year lows this week as a rise in US yields triggered some unwinding of bearish bets on the currency, however the outlook for the greenback remains negative as more stimulus is expected.

GBP / USD	–	Range 1.40 – 1.22	–	Today at 1.3648
GBP / EUR	–	Range 1.20 – 1.06	–	Today at 1.1214
GBP / JPY	–	Range 150 – 125	–	Today at 141.774
DX (Spot USD)	–		–	Today at 90.041

#### Oil Price;

*We monitor the oil price as it is a strong indicator of global consumption when balancing the output and inventory data. Strong supply and usage denote a strong global economy. Opposite reflects underlying weaknesses.*

Oil prices gained over the week, rising to their highest since late February, on continued optimism on the outlook for the commodity after Saudi Arabia announced a large voluntary production cut last week. Overall, geopolitical tensions and recessionary concerns continue to weigh on prices, and the oil outlook remains weak. Brent crude is

currently trading at \$56.22, up 3.80% in comparison to the previous week's price and WTI crude is trading at \$53.00, up 5.45% from last week.

#### **Gold Price;**

*Gold is a safe haven and a spike in price can be an indicator of increasing underlying economic concerns and as always, the opposite.*

The price of gold fell 3.0% over the week and is currently trading at \$1858 per troy ounce due to dollar strength. Overall, gold continues to be relatively well supported around current levels in the short term by cautious investors as geopolitical tensions weigh on sentiment amid an uncertain global economic outlook.

***Should you have any questions on any of the information contained in this document, please don't hesitate to get in touch.***

**Joe Kennedy | Associate Portfolio Analyst**

*Past performance cannot be used as a guide to future performance and the value of your investment will fall as well as rise in value. You may not get back all of your investment and the final value of your investment will depend on the performance of your portfolio. The actual performance of an individual client's portfolio may differ due to different funds being used and being restricted in relation to certain asset allocations. Performance figures quoted include fund manager charges but exclude adviser, discretionary, custodian and switch charges. Unless stated, income is reinvested into the portfolio. The information contained in in this document is for information purposes only. It does not constitute advice or a recommendation or an offer or solicitation for investment.*

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