SIGNIA TALKING POINTS

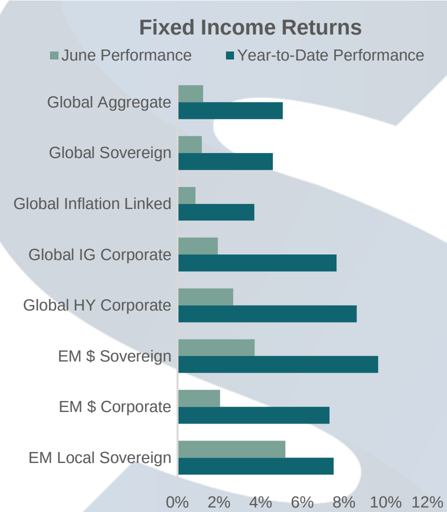
June 2019

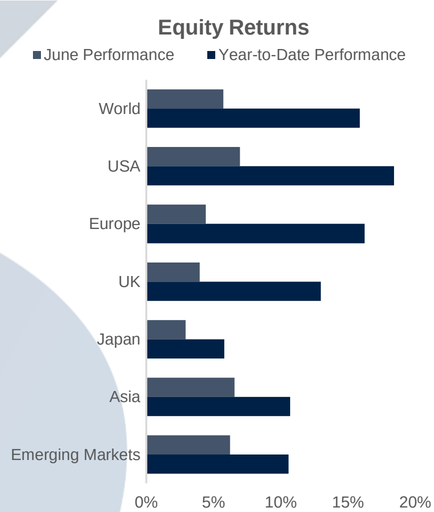
Three Years of Brexit

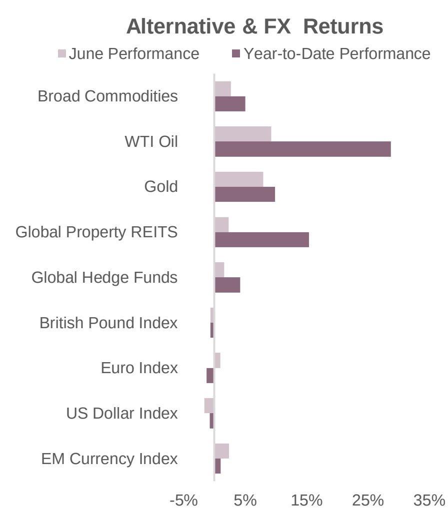
As far as soap operas go even the most imaginative and patient writers couldn't conjure up a Brexit saga to compete with the reality that has transpired over the last three years. June marked the third anniversary of the 2016 Brexit referendum, but instead of Brexiteers embracing their first British summer from outside the European Union, it was an anniversary that the UK and its cast of 66 million people (Brexiteers and Remainers alike) did not anticipate. Two deadline extensions on and the UK remains in the EU, albeit on shaky ground, but well past its original 29 March 2019 deadline and now committed to finding a parliamentary solution to the Brexit deadlock by Halloween on 31 October. Scary as this sounds, both candidates in the running to replace Theresa May as Prime Minister this month have expressed their willingness to take the UK out of the European Union with or without a trade deal, potentially forcing a hard Brexit on the country and its trading partners.

The consequences of this on the future of the British economy and union of the Kingdom are highly uncertain and unlikely to be good. The alternative scenario – parliament blocking a hard Brexit for a second time – would have equally uncertain implications as the likelihood of a general election leading to a far left Labour or far right Brexit populist government could quickly become a reality. Unsurprisingly, the British Pound has depreciated 14% since the Brexit referendum and 6% from its highs this year to price in these rising event risks. At first glance, UK equity returns seem to have done well over the last three years, rising 34% in Sterling terms and keeping apace with World equity returns, but a closer look reveals that FTSE 100 returns have in fact significantly lagged the broader equity markets when measured in US Dollars or even Euros.

UK FTSE 100 Equity Returns have Underperformed when Adjusted for Sterling Depreciation







Source: Bloomberg, Signia Wealth. Data as at 30/06/2019.

Global Agg: Bloomberg Global Aggregate TR Hedged GBP; Global Sovereign: Bloomberg Global Treasury TR Hedged GBP; Global IL: Bloomberg World Govt Inflation Linked Bonds 1-10Y TR Hedged GBP; Global IG: Bloomberg Global Corporate TR Hedged GBP; Global HY: Bloomberg Global High Yield TR Hedged GBP; EM$ Sov: Bloomberg Emerging Markets Sovereigns TR Hedged GBP; EM$ Corp: Bloomberg EM USD Corporate 10% Cap Hedged GBP; EM Local Sov: Bloomberg EM Local Currency Govt TR Unhedged USD; Equities: Equity indices reflect net total returns in local currency, except Asia and EM in USD; Commodities: Bloomberg Commodity TR Index; Global Property REITS: FTSE EPRA/NAREIT Global Index; Global Hedge Fund: HFRX Global Hedge Fund Index; British Pound: Bloomberg British Pound Index; Euro: Bloomberg Euro Index; US Dollar: Bloomberg US Dollar Index; EM Currency: JP Morgan Emerging Market Currency Index.

Fixed Income

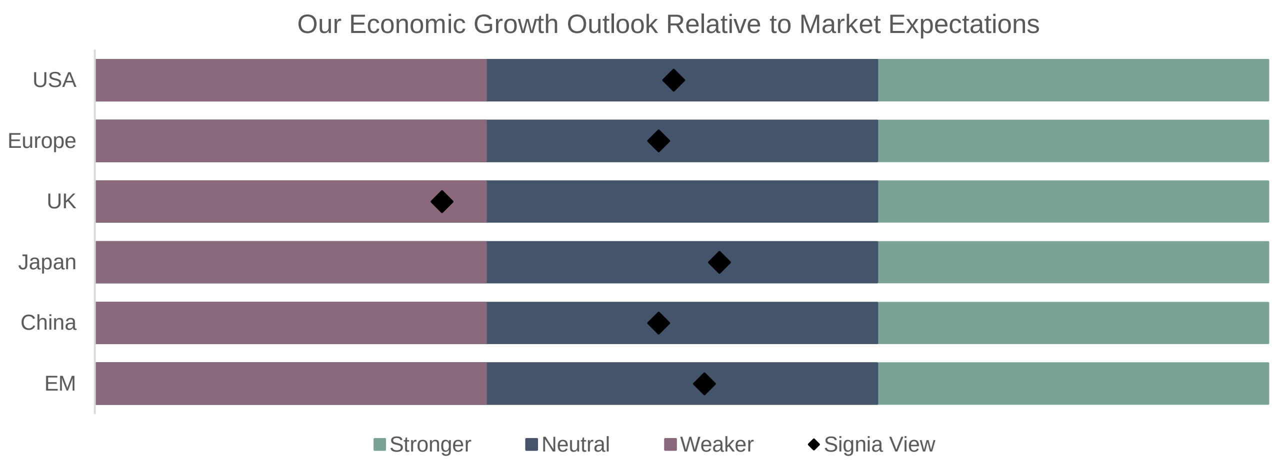
- Safe haven assets benefitted from the increasingly dovish rhetoric from central banks with all global fixed income assets generating positive returns.
- Emerging Market local debt was the strongest performing sub-asset class, benefitting from the weakening dollar
- The weak dollar and dovish tone of central banks was also positive for global investment grade and high yield credit, the latter further benefitting from the strong upward price movement in oil

Equities

- US equities performed strongest in June, following an increasingly dovish tone from the Federal Reserve on US monetary policy
- Asian and emerging market equities were the next best performers, with monetary easing and positive trade news helping to buoy sentiment
- European bourses also performed well, fuelled by the European Central Bank showing willingness to ease monetary policy further
- UK and Japanese equity markets were positive but lagged their developed market peers, with the former affected by continued Brexit uncertainty

Alternatives & FX

- Oil (+9%) and Industrial Metals (+2%) performed well, especially Iron Ore (+14%), which has also been helped this year but declining output from key players
- Gold also performed strongly, benefiting from expectations of lower real interest rates
- Given a weak US Dollar, most major currencies performed well, with the South Korea Won and Canadian Dollar both rising 3%



Source: Signia, Bloomberg. Market Expectations are represented by the Bloomberg Contributor Composite. Data as at 30.06.19.

- USA: Leading growth indicators have declined sharply but from a high base and the Fed has pivoted towards being ready to cut interest rates. Rising wages and productivity growth is keeping domestic consumers in good health and household balance sheets strong. However, profit margins have peaked and leverage is rising in the corporate sector. Despite a partially inverted yield curve a recession in 2019 remains unlikely. Trump has re-started trade talks with China.
- Europe: Forward looking economic growth and inflation indicators have weakened, whilst heightened economic uncertainty has caused a decline in real investment and business expectations. However, the ECB stands ready to increase stimulus and wage growth remains resilient and in healthy shape. Liberal and Green parties gained ground in the European parliamentary elections, whilst Centrist and Leftist parties struggled.
- UK: The economy remains in a very delicate state despite a strong jobs market, with monetary policy tied to a Brexit outcome. Profit growth is declining as Brexit uncertainty weighs heavily on business confidence and the British Pound, with the weak currency helping the manufacturing sector by boosting export demand. Conservative MPs have picked Boris Johnson and Jeremy Hunt as Prime Minister contenders to find a solution to the Brexit deadline impasse before 31 October.
- Japan: Despite a still accommodative Bank of Japan, economic growth remains anaemic since peaking at an annualised rate of 2.4% at the end of 2017. With wage growth and consumer sentiment indicators now also deteriorating, and a consumption tax hike on the way in October, the outlook for businesses and the Japanese economy remains depressed for 2019 in the absence of additional BoJ or government stimulus.
- China: As the trade war with the USA weighs on economic growth, authorities have reaffirmed their support to stimulate the economy and contain any slowdown in order to achieve its GDP growth target of 6%-6.5% for 2019. After an initial surge in the first quarter, total social financing (broad money supply) has stagnated with potentially negative implications for economic momentum. An African swine flu epidemic is putting upward pressure on both Chinese food and broad inflation.
- Emerging Markets: Easier financial conditions and a weaker US Dollar from a recent dovish pivot by the US Fed in its rate cycle has been a significant boost for emerging market asset prices, liquidity and investor inflows. A re-escalation of US-China trade tensions remains a primary and existential threat.

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Important Information