CAERUS
Portfolio Management

CAERUS Market Commentary – December 2015

2015 Market overview

Post the Great Financial Crisis (GFC) of 2008, the Federal Reserve in the United States was the first central bank to raise interest rates (see below). With the Bank of England forecast to be the second central bank to take action, the developed world is divided into two camps: those like the US and the UK where the period of historic low rates is coming to an end, and Japan and Europe which continue to “print” money in order to generate growth.

UK

The UK had a disappointing 2015 performance with a 0.98% rise. Throughout 2015 there were familiar economic trends; employment remains at all-time highs and unemployment has fallen. Services continue to lead the recovery with manufacturing remaining subdued whilst productivity continues to disappoint. Encouragingly, there appears to be some real wage growth, thus real incomes are higher as inflation remains low, helped by lower oil prices. Although the Bank of England is expected to follow the lead of the Federal Reserve in late 2016 or early 2017, 2016 may be dominated by the upcoming BREXIT vote, a historic once-in-a-generation referendum that may determine our relationship with Europe for many years to come.

US

The rise in rates from 0.25% to 0.50% was the first upward move since 2006. The Federal Reserve feels confident enough that the economy is recovering sufficiently that higher (albeit modest) rates would not derail the recovery. In particular, job growth remains over 200,000 per month and the unemployment rate is at 5%. The strength of the dollar over the past year (which makes exports more expensive and raises import prices) remains a potential problem in terms of impacting profits. Looking ahead, there is an expectation that rates will rise gradually throughout 2016, albeit from still historically low levels.

Europe

Despite its continuing travails (Greece and other Mediterranean countries) Europe did manage a positive performance for 2015 with a rise of 2.78% in sterling terms. The ECB has pursued its own version of quantitative easing, ‘printing’ money, in order to encourage growth. It took further measures in December by increasing the negative rates it charges banks to deposit money (banks have to pay to deposit monies; it is hoped they will lend instead) and an extension to the time it will buy bonds. Although there remains some encouragement from an increase in bank lending, euro-zone inflation in November remained at just 0.1%, with some countries actually experiencing deflation. Although the ECB has a target inflation rate of 2%, its achievement is not being helped by the low oil price.

Japan

Japan was the best performing major stock market in 2015 with a rise of 18.16% in sterling terms. It continues with its ambitious program of Abenomics; quantitative easing, government spending and structural reforms. So far the policy has not led to a significant pickup in growth. However, when compared to other markets, on valuation grounds, the Japanese stock market remains attractive.

Emerging markets

Another disappointing year for emerging markets with a fall of 10% in sterling terms. China and its troubles continue to cast a shadow over many other emerging markets. Chinese growth is widely believed to be 4% rather than the official 7%, as overcapacity in manufacturing and property, plus high debt levels continue to weigh on the economy. This has a knock on effect to commodity exporting countries such as Brazil and Russia. Rising US rates could also hit emerging market companies that have borrowed heavily in US dollars as their costs will rise. Emerging markets may well struggle again in 2016, given the ‘headwinds’ mentioned above.

CAERUS Sentiment Indicator