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Lacomp plc

Lacomp plc is an independent investment management company providing portfolio management services to private investors worldwide.

It is now four months since the British electorate voted to leave the EU, and it is worth looking back and seeing what has actually happened in the meantime.

You will recall that in the run-up to the Referendum, the 'Remainers' had assembled a formidable lobby – leading business figures, economists and analysts at the UK Treasury, the Institute of Fiscal Studies, all sorts of financial institutions, spokesmen representing the OECD, IMF and a raft of foreign leaders, including President Obama – to make their case and warn us that leaving the EU would seriously harm the UK economy, both in the short and longer term.

Our then Chancellor George Osborne told us a Brexit vote would force him to prepare an emergency budget, forecasting significant tax hikes and further reductions in public spending. In the event, we did not get an emergency budget, but George Osborne was swiftly shown to the emergency exit by our new PM Theresa May.

The predicted economic Armageddon has not happened. True, the value of the pound has fallen by considerably more than we expected. The pound had remained at around $1.47 for most of the year but fell to $1.36 on the night of the vote and, in subsequent moves has fallen further, exacerbated by the 'flash crash' of early October when it temporarily reached $1.18 in Asian trading.

Of course, the falling pound is providing a much needed fillip for our exporters, which is the main reason the FTSE has been climbing even higher. Many FTSE constituents' earnings come from overseas, making them more competitive in international markets and resulting in nice exchange rate gains. On the downside, the impact of a weak currency on the cost of material imports, particularly those based on dollar prices such as food and fuel, has yet to be felt.

There has also been an upturn in overseas interest in UK firms which now appear relatively cheap – witness the purchase of ARM Holdings by Softbank, a Japanese conglomerate, at a 43% price premium. Having seen the UK share of global M&A decline ahead of the Referendum (down 70% from 2015 levels), the subsequent currency weakness may have sparked renewed overseas interest which shareholders of target companies might welcome even if the affected workforce usually are less than enthusiastic.

Clearly, it is too early to draw any conclusions about the real effects of the referendum outcome. A lot will depend on how the negotiations vis-à-vis the EU nations and the rest of the world develop. The question ultimately is whether we will end up in a better place outside the EU.

Regular readers of our Newsletters already know our long-held belief that the eurozone is heading for deep trouble and that the euro itself was always likely to turn out to be a failed project. Indeed, only this week, Professor Otmar Issing, considered by many to be the main architect in the construction of the single currency, stated that the whole euro venture was unworkable in its current form. "One day, the house of cards will collapse", he said.

Very recently, we heard that German banks were facing difficulties, and it speaks volumes that a German Finance Minister has to stand up and state that their flagship bank (Deutsche Bank) won't go bust! If you think the German banks have problem, Italy's banks are in much deeper trouble.

But it is not only the euro and the economic stresses in the eurozone that are worrying. There are all sorts of deeply worrying problems facing the incumbent governments of the member states. In Italy, the forthcoming constitutional referendum on 4 December (breaking up the ‘Senate of the Republic’ and replacing it with a ‘Senate of Regions’ in an effort to improve the long-lasting instability of the Italian government – the Italians have had 62 different governments since the Second World War...) is rapidly turning into a vote of no-confidence in PM Matteo Renzi and his centre-left Democratic Party. Signor Renzi vowed he would resign if the vote didn’t go his way, and that would lead to yet another general election, where his party would face stiff opposition from rising populist movements, led by the eurosceptic 5 Star Movement. In Germany, last month’s regional election saw Frau Merkel’s CDU party come third behind the socialists (SDP) and the right-wing Alternative für Deutschland (AfD). Recent French polls suggest Marine Le Pen’s National Front party is now representing the views of over 25% of the voters and in Holland the picture is very similar with Geert Wilders’ right-wing and anti-islam Freedom Party registering 22% support, making it the biggest single party. In Austria, there will be a rerun of the Presidential Election which had been held in May and was annulled due to “irregularities in the count of the vote”. The rerun will take place on 4 December, the same day of the Italian referendum, and will be a close thing between the Greens and the Freedom Party, the latter being mainly anti-immigration. Finally, we had a further referendum in Hungary on 2 October, asking its people whether they wished to curb the number of asylum-seekers the EU wanted them to accommodate. Nearly 3.5 million Hungarians voted, and over 98% said no to the EU’s plans. However, voter turnout was 43%, 7% short of the required 50%, and the result thus was rendered invalid.

It is rather sad to see Europe in such disharmony, and the situation now is very different to what the signatories of the Treaty of Rome had in mind back in 1957.

Something equally odd, and very much lacking in harmony, is happening across the pond in the Presidential Election. There are 320 million Americans, and Donald Trump and Hilary Clinton are the best candidates they can come up with!

You will by now have read enough about how the two campaigns are being fought, the accusations and the mud-slinging. Let us concentrate on what is in store when either of the candidates gets elected. Both have quite similar plans when it comes to their economic agendas. Both promise infrastructure improvements. Both are looking for enhancements in the energy sector, Trump by reducing regulation and helping oil companies, Clinton by pushing for more ethanol, which goes with her green agenda and would be perceived to be good for agriculture. There is a clear difference there, as you will find elsewhere. Clinton wants to expand the Affordable Health Care for America Act which will be good for health care and hospital companies; Trump wants to repeal ‘Obamacare’. Clinton wants to increase the minimum wage; Trump wants to abolish it altogether. In fact, Trump wants to abolish a lot of things. He also threatened to tear up existing trade agreements, which could easily lead to trade wars, something the world could do without right now!

Both Clinton and Trump are committed to increased public expenditure, but they hope to raise the money to pay for it by different means. Clinton wants to tax everybody more; Trump wants tax cuts to provide more inflow into the state’s coffers.

So, are we going to get more of the same in the form of a President Clinton, or are we stepping into the unknown with a President Trump? If it is Trump who, against the latest polls’ predictions following Wednesday’s final debate, succeeds, it will be a clear demonstration that voters really are disaffected with authority and fed up with the political establishment. Of course, we know that a lot of ‘Brexiters’ were similarly motivated.

If you are worried about what Donald Trump could do if he gets the keys to the White House, it is worth remembering that the American three-branch system of government, i.e. the President, Congress and

Senate, provides checks and balances that avoid any one branch becoming too powerful. At the moment, the US Senate looks evenly split, but Congress is likely to remain under Republican control. Many Republican representatives, however, are no friends of Trump.

As far as the outlook for the US stock market is concerned, history tells us that a Democratic administration usually does somewhat better (since 1946, the average performance over a Presidential term of the S&P 500 was up by 11.4%) than the Republicans (up 4.6%).

Looking back over the year to date, markets have reversed the falls of the first quarter and gone steadily higher. The FTSE has improved by some 12% this year. As we said above, it is too early to gauge the longer-term effects of the Brexit decision, but the fall in sterling already has had an impact on inflation. Inflation will inevitably rise as the higher food and fuel prices feed through but, for the present, the Bank of England will maintain its easy monetary policy in the interests of economic stability – in the absence of any wage pressure, the greater threat is perceived to be an economic downturn and a rise in unemployment. For this reason, Bank of England Governor Carney cut rates to 0.25% in August and is still hinting at a further cut to come. Inflation figures this week have shown that the consumer price index (CPI) has risen from 0.6% in August to 1% in September. Unimaginably low to those of us who remember the seventies, but the direction of travel is clear.

We are still living in an incredibly low interest environment, highlighted by low or negative rates applicable to government debt issuance. 75% of government 10-year bonds worldwide pay less than 1% on their borrowing, and one third pay negative interest. In other words, you are paying some governments for the privilege of lending them money!

Looking at your valuation, you should be pleased with the action we have taken over the Brexit affair, but we have further de-risked portfolios and built up something of a cash war chest. It is probably a poor analogy, but 85% of fatalities to climbers happen on the descent from Mount Everest, not on the ascent!

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