

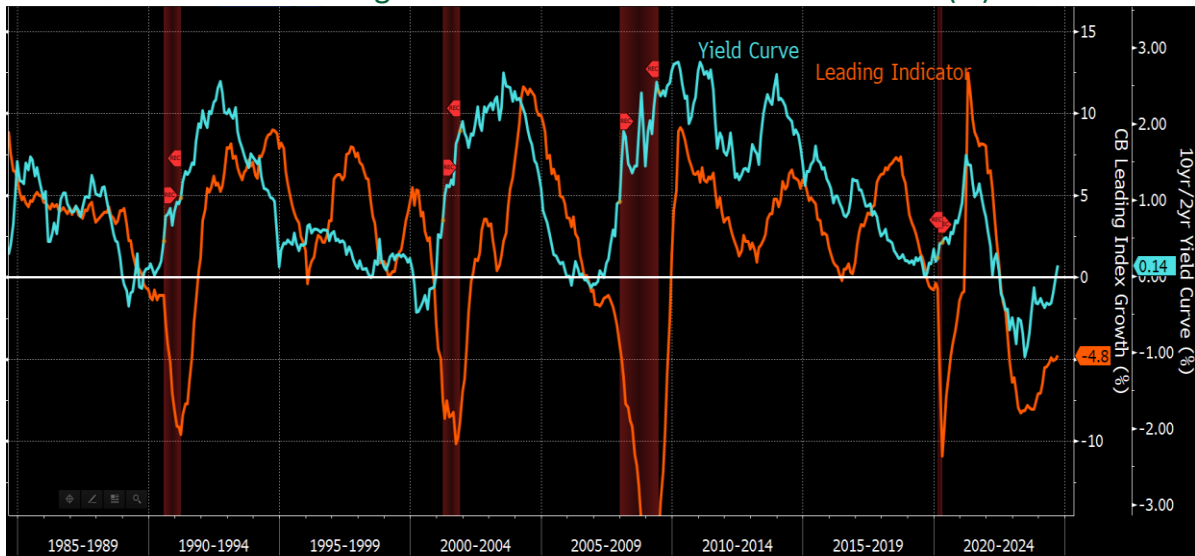
"The whole is more than the sum of its parts."

Aristotle

1. US ECONOMY

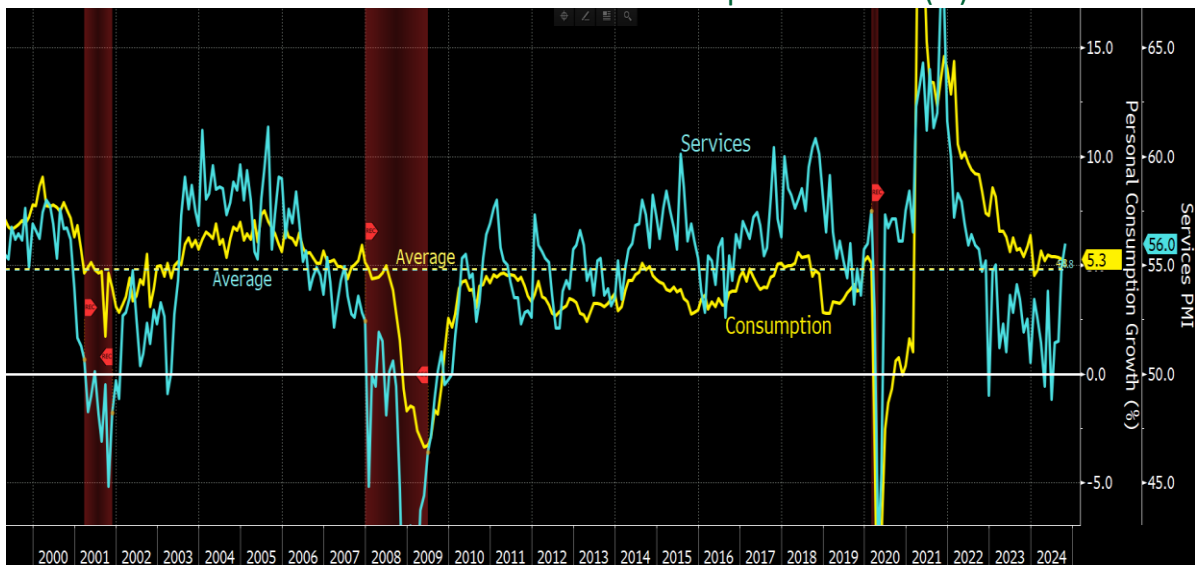
Investors have been facing conflicting signals about the US economic outlook:

US – Leading Economic Index Growth vs Yield Curve (%)



Whilst the critical US Employment data remains generally constructive (not reflected in the chart), the Yield Curve has recently reverted as it has historically done shortly before the start of prior recessions. Against this, the Leading Economic Index continues to recover, as it has historically done towards the end of recessions. With the Federal Reserve's large capacity to further lower its target rate, along with a new US administration, a soft-landing scenario still seems to have merit.

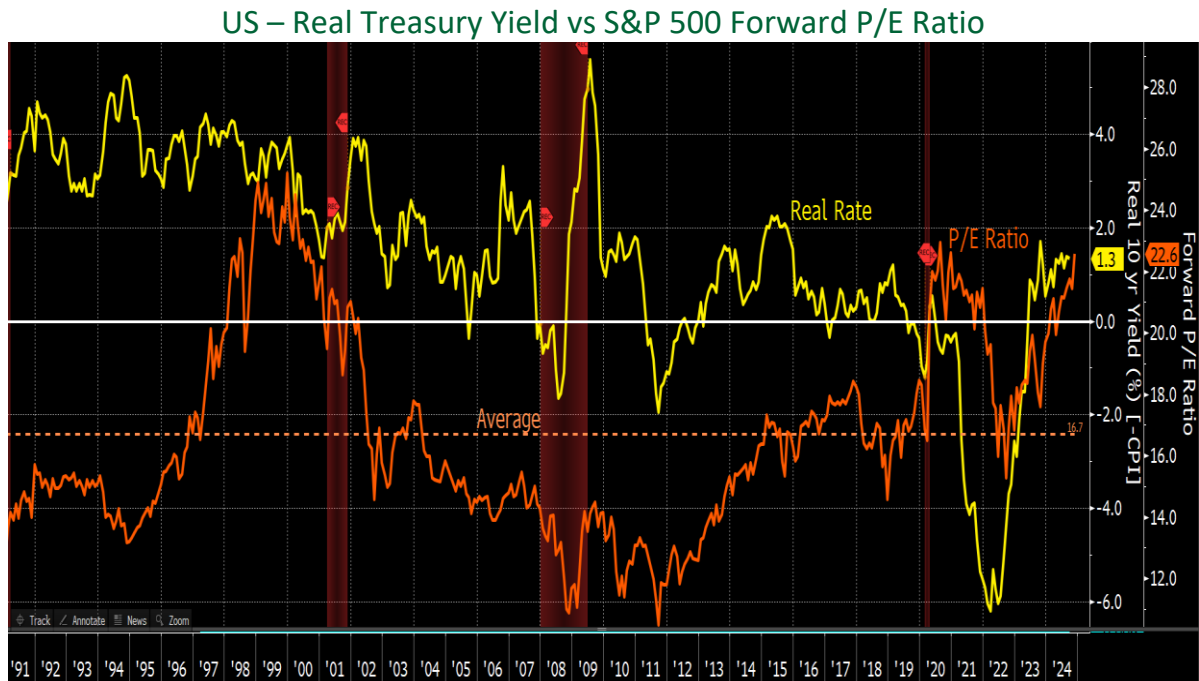
US – Services PMI Index vs Consumption Growth (%)



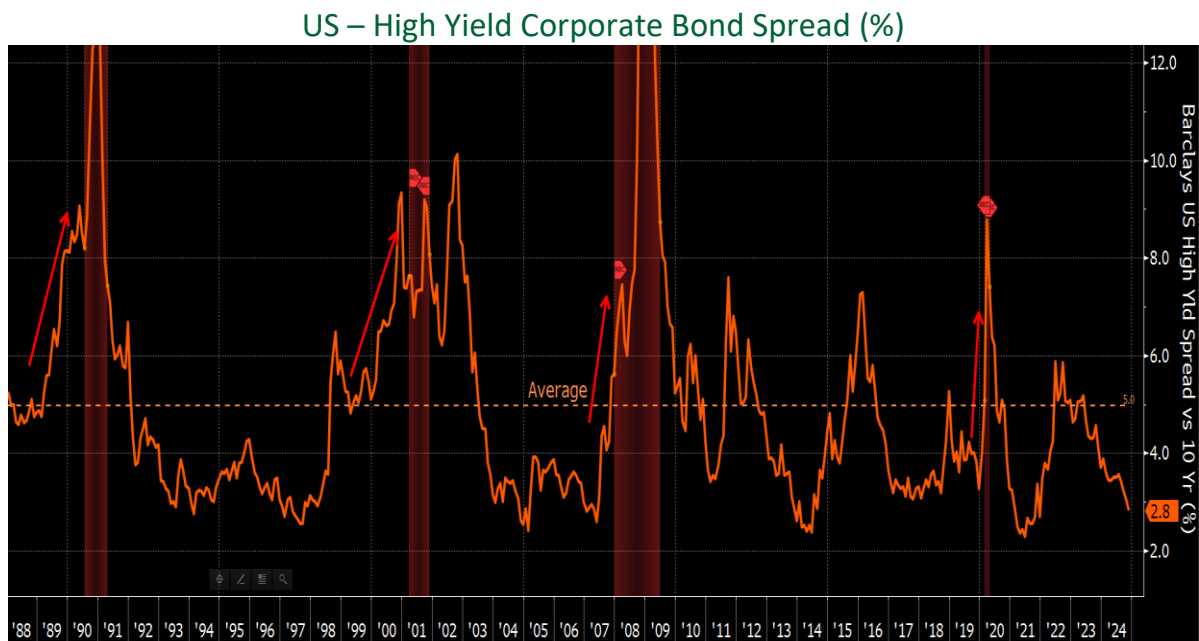
The Manufacturing PMI Index remains weak (not reflected in the chart), whilst the Services PMI Index continues its strong recovery. Seeing the much larger relative weight of the latter in the US economy and Consumption currently growing at 5%, one is inclined to remain constructive.

2. US INTEREST RATE INDICATIONS

It is striking that the ten-year Treasury Yield is currently above 4% and in a rising trend, whilst inflation is dropping. Chances are that this reflects a more resilient economy than what many may have previously thought.



Further to the above comment, the real Treasury Yield is also in a rising trend, back at post Financial Crisis highs. It has historically dropped prior to recessions. These are economically constructive indications. Along with this, stock market valuations also usually drop in the run-up to recessions. It currently remains in a rising trend.



The High Yield Corporate Bond Spread is currently in a downwards trend, at a value of 2.8%. This is close to historic low levels. The combination of the trend and the absolute level reflects a healthy economy.

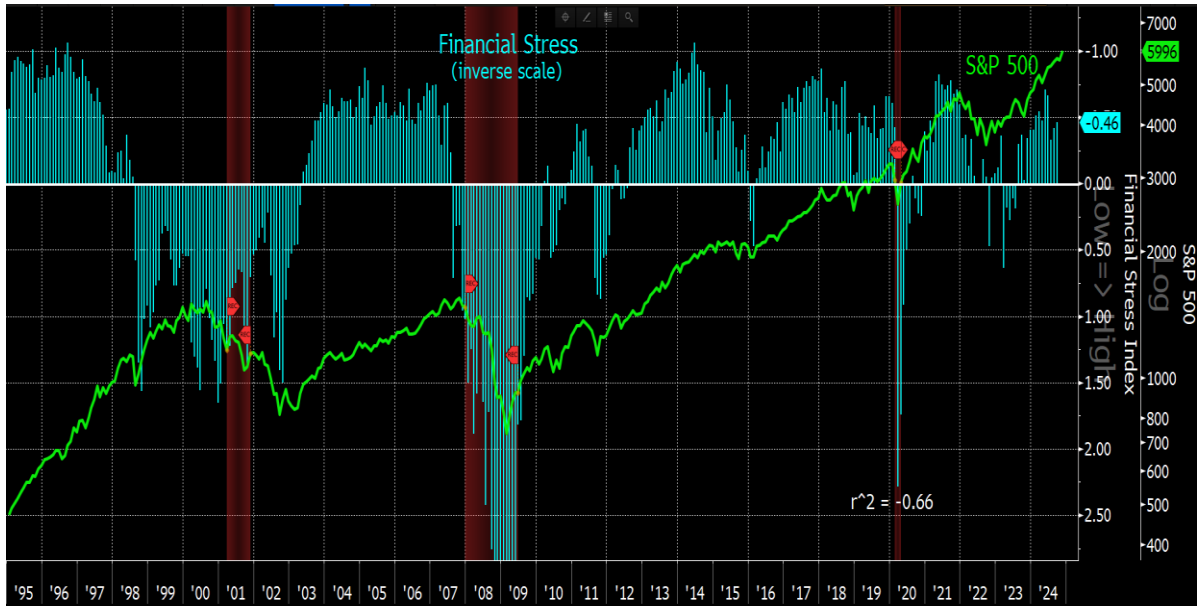
Whilst these are constructive indications, the Yield Curve's opposite indication should be closely monitored. The new administration's economic policy may be a determining factor.



3. FINANCIAL CONDITIONS

The following charts reflect the overall conditions in the regions' financial industries.

US – Kansas Federal Reserve Financial Stress Index vs S&P 500



The above Stress Index is presented on an inverse scale to illustrate its high (negative) correlation with the stock market. Very low (negative) readings indicate risk of excesses in the stock market after an extended period at those levels. Whilst a build-up is in process, the current (low) absolute level is not yet at an extreme and may further support the US stock market.

Bank of America Merrill Lynch (BoA ML) Global Financial Stress Index vs MSCI World Index

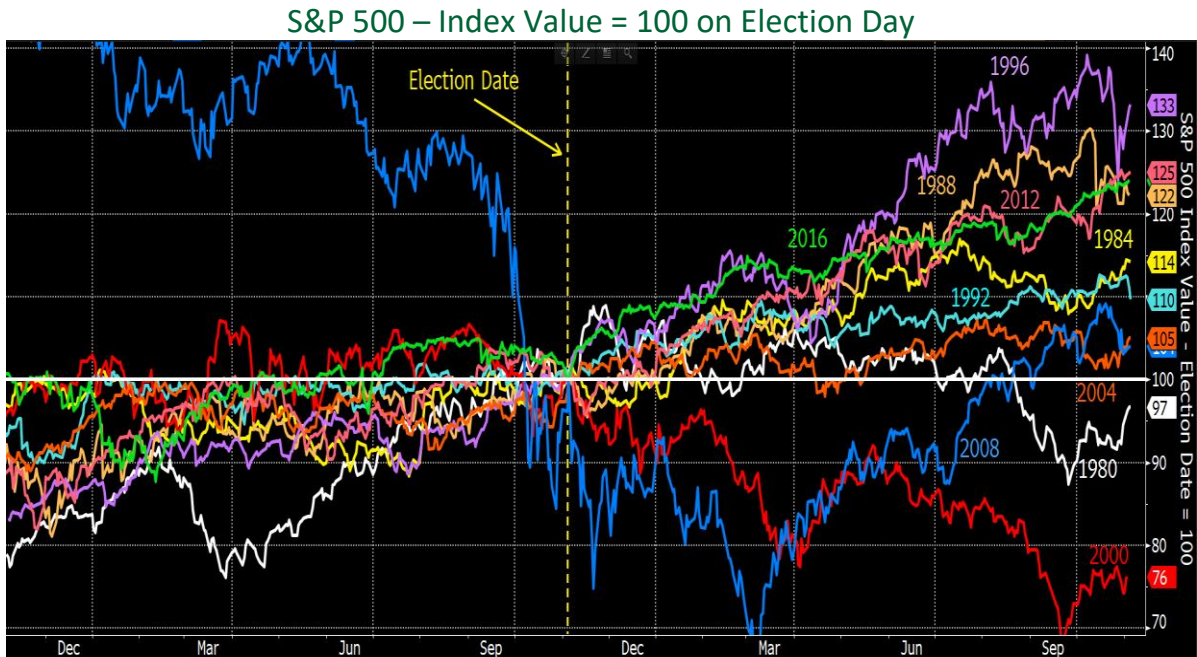


The above Stress Index from Bank of America reflects similar data for global financial markets. It has a similarly strong correlation with the MSCI World Index and reflects support for the stock market. It seems, though, to be in an earlier phase than the US Index, and therefore may potentially offer extended support.



4. US ELECTION

The following chart reflects stock market returns in the 12-month run up to respective US elections since 1980, and the subsequent 12-month performance:



In most cases the stock market increased over the twelve-month periods building up to the elections and delivered well over the subsequent twelve-month periods. The only negative performances following the elections were with the 1980 election (only marginally negative) and with the Dot Com bubble (the red line).

The following chart reflects the stock market returns following US elections along with the stock market valuations since 1990:

S&P 500 12 Month Return Following Presidential Elections & S&P 500 Forward P/E Ratio

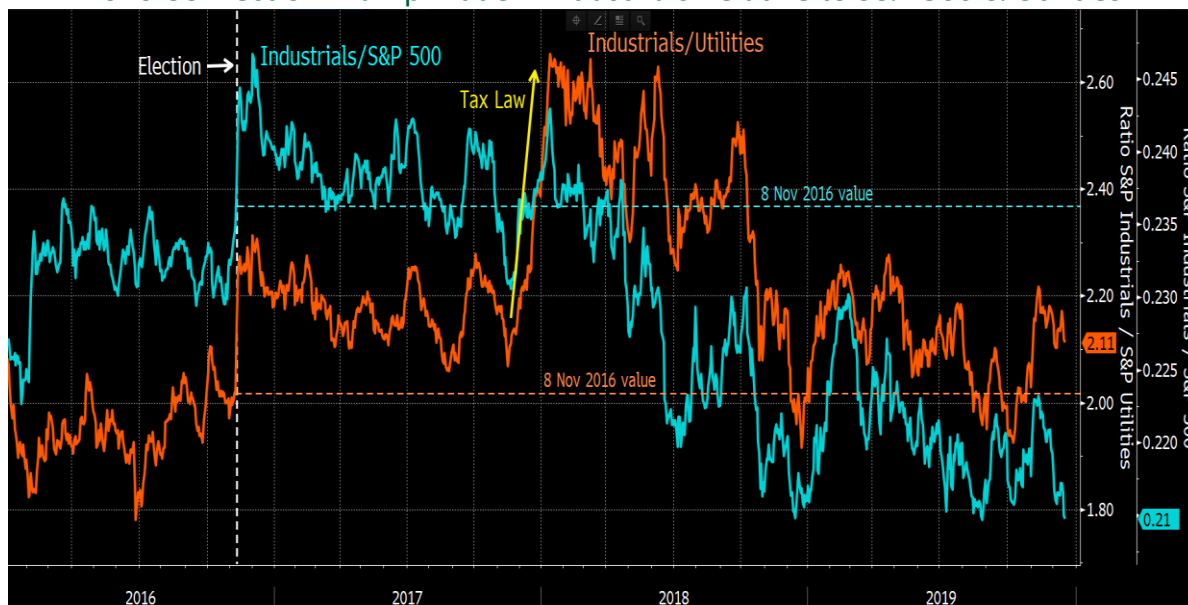


The shaded areas indicate the year-periods following the respective elections, with the green line the rolling one-year returns. The yellow line reflects the stock market valuation.



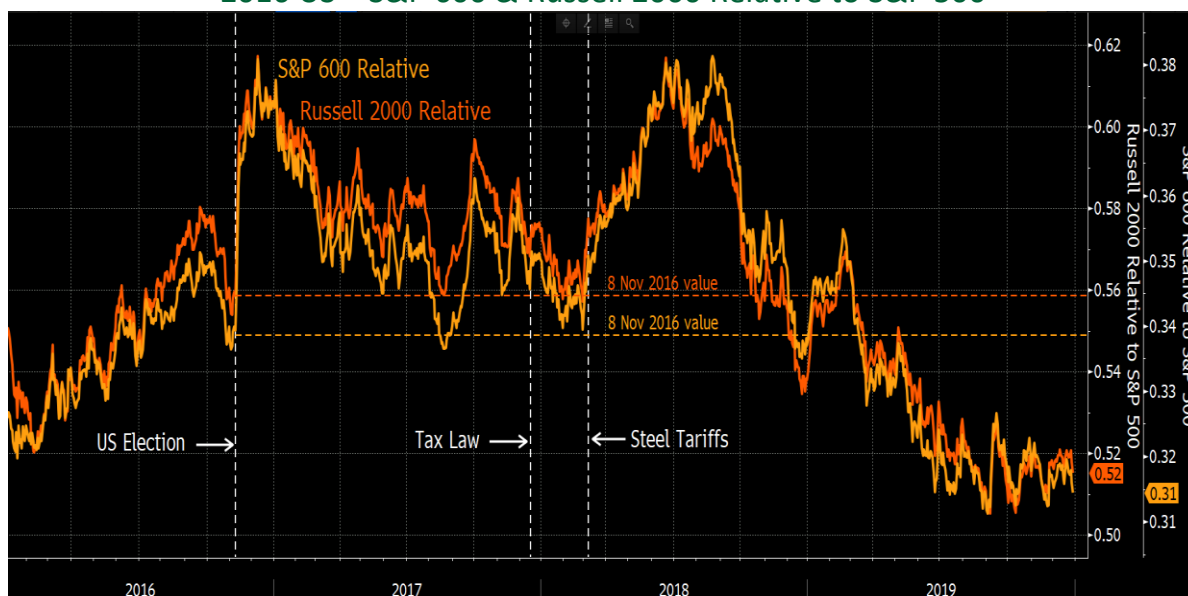
Over the previous eight elections since 1990, the stock market has generally delivered strong returns over the following twelve months. In five cases it returned well in excess of 20%, in two cases around 10% and one case delivered a negative return. George Bush Jnr then inherited a stock market in the process of derating into a recession. With his previous stint, Donald Trump inherited a stock market on a lower return base than currently, and in the process of rerating. This time the stock market base and the valuation level are both higher.

2016 US Election Trump Trade – Industrials Relative to S&P 500 & Utilities



Following Donald Trump's previous win, the Industrial Sector immediately outperformed against the S&P 500 Index and Utilities (as a conservative benchmark), but quickly reverted, losing all outperformance within a year. It again outperformed with his Tax Law, and again reverted performance relatively soon. On this basis, investors should tread carefully.

2016 US – S&P 600 & Russell 2000 Relative to S&P 500



Smaller capitalisation stocks had a similar favourable response on the 2016 election, but did not react similarly on the Tax Law. They did, though, respond well on the steel tariffs for a few months, but soon lost their lustre. Investors should, therefore, on this basis, also tread with caution.

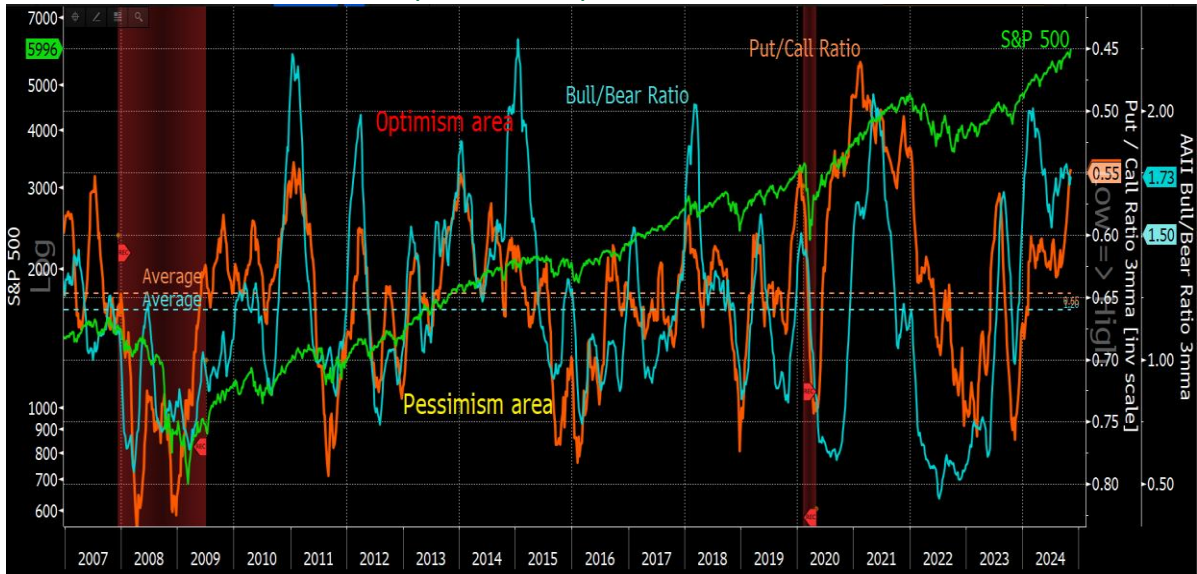
Donald Trump has quite similar stances on the US economy this time. The difference, from an investor perspective, is that he now has more reason to focus on the economy while he inherits higher valuations but, fortunately, and contrary to last time, now has the Federal Reserve easing cycle on his side.



5. TECHNICAL PICTURE

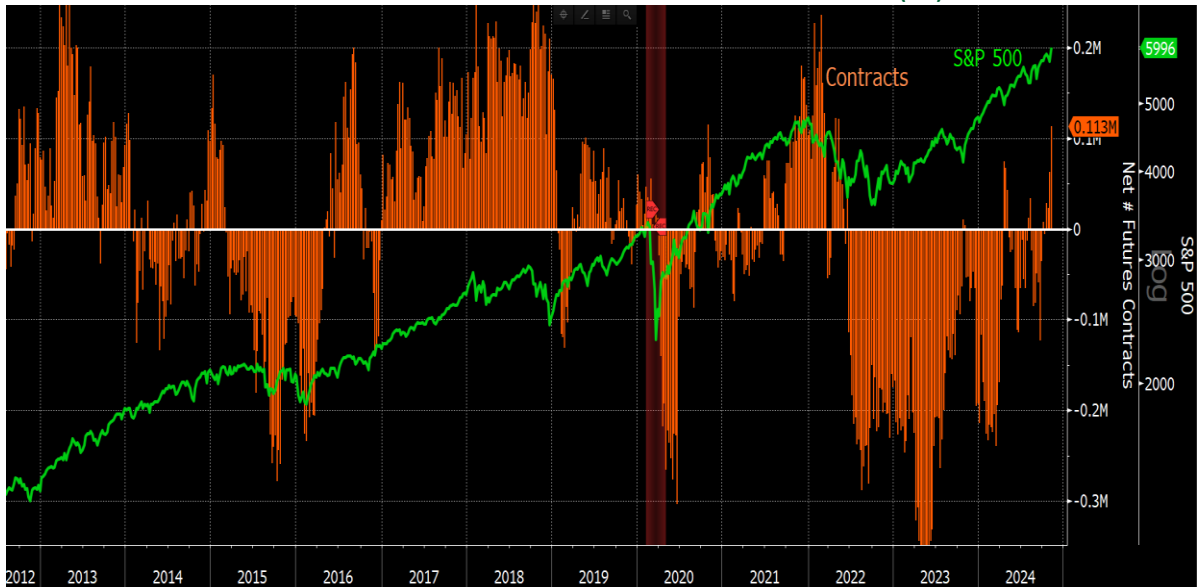
The general S&P 500 technical picture is healthy with early signs of optimism.

AAll Bull/Bear & Put/Call Ratios vs S&P 500



Both the Put/Call and Bull/Bear Ratios in the chart (respectively reflecting Institutional and Retail interest in the stock market) are currently at quite extreme levels, indicating overall optimism. This should be monitored for potential exuberance.

S&P 500 vs Net Number of Futures Contracts (m)



The net number of futures contracts has just gone positive following a long period of being in negative territory. This does not yet indicate investor exuberance.

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