It is Looking More Like Japan

- **A flat equity market and a bond yields tumbling – its Japan**
- **Infrastructure spending no panacea for growth**
- **No backing down on trade wars by President Trump – it's not politically important…yet**
- **China puts up more barriers to overseas property purchases**
- **UK Brexit – another crucial week**

Sometimes it is good to sit back and take a look at the broader picture. For all noise in the markets, global equities and the US equity market have gone nowhere in a year. Quite frankly, the more this goes on, the more that the western markets look like they are going through their Japanification. In a year, global equities are largely unchanged, and the US 10-year government bond yield down 136bps at 1.50%. Most eurozone bond markets have slipped into negative. The Japanese JGB 10-year yield didn't go negative until 2016, 25 years after the start of the economy's problems.

Western governments are even starting to sound like the Japanese. The thought is slowly creeping into their collective heads that a round of infrastructure spending is in order. After all, many of them can borrow money at negative interest rates. However, beware infrastructure spending is no panacea. A study by Ronald Utt showed that Between 1992 and 2000, Japan implemented ten separate spending stimulus packages in which public infrastructure investment was a significant component. Over that same decade, the equity market fell by a third. At the end of last year, Japan was still trying to use infrastructure spending to boost the economy; the government announced 3 trillion Yen of spending over three years. However, year to date, Japan is yet again the worst performing major equity market.

Policymakers are going to have to do much more to arrest the collective global malaise. To be honest, it appears that the only short-term fixes are in the hands of the American President. Unfortunately, his current policy playbook is destructive of global growth. He continues to bet that his America First mantra played out through his trade war stance will win him the next Presidential election. Opinion polls are very mixed. The most recent opinion poll on the handling of the economy by President Trump has 47% approve-51% disapproval, although other polls have shown much higher disapproval. A head-to-head of Trump against Biden would have Biden winning by 16 percentage points however the approval-disapproval rating of the Democrat-led Congress has a net 49 percentage point disapproval rating. There is little comfort that polls will have President Trump shifting his policies anytime soon.

Chinese industrial confidence data continues to slip, although not dramatically. Indeed, while the manufacturing sector remains under pressure, the non-manufacturing sector showed a very modest uptick in confidence. The manufacturing sector confidence indicator from the National Bureau of Statistics fell to 49.5 in August down from 49.7 in July slightly below expectations of 49.6. Any reading below 50 implies a contraction of activity. The survey has been below 50 for six out of the last eight months. The service sector indicator, by contrast, remains above the 50 level of 53.0. Early Monday a further Chinese industrial confidence survey from Caixin showed a modest uptick in industrial confidence.

Chinese measures to restrain overseas real estate purchases

The recent slide on the Yuan against the dollar appears to have encouraged the Chinese authorities to impose further capital controls. The yuan hit an 11-week low against the dollar. To be fair, the dollar has been in the ascendency against most currencies in recent weeks with the trade-weighted dollar at a 17-year high. The changes mainly target Chinese individual and corporate investors in real estate.

The new capital controls can only further weaken the investment flows of Chinese money into global real estate. Chinese investor purchases of overseas real estate fell 63% in 2018 to $15.7 billion. The US, Australia and the UK were the primary beneficiaries of the previous buying spree. In 2016 Chinese buyers accounted for 25% of real estate deals in the US and Australia and 25% of all central London commercial deals.

Precious metals still favoured

Against the backdrop of a challenging global economy, we have a high conviction in a positive view of both the price of gold and silver. The gold price may have paused last week but silver more than made up for it with a 5.5% gain. Judging by the scenes in some of the precious metals retail stores in Singapore, there remains robust retail demand. We witnessed long queues to trade, and some customers bringing their own trolleys to whisk the metal away to savings! Demand for gold ETFs remains very strong. Aggregate holdings of gold by ETFs has risen to 78.7m very close to the previous peak of 82.5m in 2012.

Another crucial week in London

It is yet another critical week for the UK. MPs return from a summer recess on the 3rd September with a deadline of the 9th for the suspension of parliament. **If MPs wish to stop Prime Minister Johnson in his tracks, they will most likely have to move this week**. Should the opposition call a vote of confidence and win then there are two potential outcomes; either they vote in a new government that commands a majority, or it is left to Boris Johnson to announce the timing of a general election to be held in the next three months. There could be a move to collect behind a new prime minister with a mandate to achieve just two things- extend the Brexit deadline with the EU's blessing and hold a general election. Ken Clarke and Margaret Beckett are seen as the potential candidates as interim prime minister. Sterling will remain under pressure in the lead up to that date with the only risk to the upside being Commons' success in passing legislation to order the government to extend the Article 50 deadline yet again and Mr Johnson deciding to comply. That combination still looks implausible as the clock ticks down.

Parliamentary time will be short this week as the government is due to unveil the annual autumn budget for 2020/21 on the 4th September. The budget will have in mind that the UK will leave the EU and hence the Conservative party will position it as part of its agenda for the election manifesto.

If Prime Minister Johnson is still in place by September 9th, then he is expected to barrel on with his threat of a no-deal exit. Boris Johnson has, at least, started to talk to his EU partners but so far there has no real evidence of 'new thinking' by London which might signal horse-trading is getting underway. It does appear as if the Prime Minister is no longer aiming for a comprehensive re-working of the Draft Withdrawal Agreement with all efforts focused on the Irish backstop. Unfortunately, no solution seems in sight that will simultaneously deliver, for the British, the blessed trinity of an independent customs area, no hard border in Ireland and no border in the Irish Sea. The EU simply won't give ground on its insistence that the single market is protected and that there will be no hard border in Ireland. London's hopes for compromise look likely to be mostly disappointed. Parliament is expected to return on the 14th of October. October 17th is a date to keep in mind as another epic EU summit.

Bottom line the UK situation looks as clear as mud. On a three-five year view, UK sterling and the asset markets look cheap, but we doubt it pays to be brave.

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