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'Some Place Else'

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The widely expected decision for the Federal Reserve and the Bank of England to pause rate hiking for a second successive month was the reported reason for the welcome rally in risk assets last week. In reality though, the lower-than-expected Treasury appetite for longer duration bonds and US employment data signalling the mighty US economy is slowing were more influential. However, the nature of last week's price action indicates that investors were caught short by marginally better news, but better news it was.

With bond yields stepping back, the question becomes whether we have arrived at peak rates and, if so, when can we expect rate cuts. (Futures markets indicate 100 bps by the end of 2024). Following their markup, risk assets need inflows to consolidate, and it remains too soon to know if we are at such a turning point. Public balance sheets remain in structural deficit, and policymakers want to resist the temptation to restart QE (or QE-like measures), fearing the return of inflation. Higher for longer monetary policy has damaged the US economy far less than the rest of the world, and fears remain that it could still take higher rates to tame.

However, encouragingly, for non-US economies, the US economy is showing signs of slowing. It can still execute the improbable soft landing. At least the seat belt signs are on, and the engine speed has slowed. But we must wait to find out whether its undercarriage is fully down and its glide path sufficiently shallow to land gently. Harder, bumpy or even emergency landings remain in the set of possible outcomes. We are not there yet.

Meanwhile, Germany is leading the Eurozone into recession, leaving the UK between the red-hot US and a colder, darker Europe. While lacking America's superpowers, the UK does have more optionality than other economies; the Netherlands, for example, is tied into Eurozone structures such as a one-size-fits-all monetary policy.

City economist and Times columnist Simon French argues that whatever you make of the UK's economic performance over the last seven years, evidence is growing that it is "firmly in the middle of the G7 pack." But over the same period, the UK has, as he puts it, "been put on the naughty step" by bodies such as the IMF, impacting the UK's standing among global investors. As Alyx Wood of Kernow Asset Management noted, the UK, which on most measures is the 6th largest economy in the world, was last year ranked 67th in global political stability, reflecting precisely the type of uncertainty that alienates long-term investment flows.

How the UK transitions to a new government by 2025 will be a critical test. Good governance, the proper execution of management change, is vital for companies and national economies. But global investors need more than just cheap valuations to buy UK equities. They need crowding in by reliable natural buyers of UK-listed shares. Gone are the days of the UK pension funds and insurance companies allocating significant proportions of their AUM to UK equities. The Edinburgh Reform and Mansion House Compact offer hope that the upcoming Autumn Statement, later this month, will offer new policies to change this and improve the allocative efficiency of the UK markets and source new long-term owners for the overwhelming number of cheap UK companies.

If interest rates have peaked, we get politicians who can deliver fiscal restraint; global dollar liquidity will flow again, and the UK should receive more than its fair share. If into this mix, we can add some exogenous productivity gains, re-accelerating economic growth; well, happy days are back, and we can one day afford to dream again of lower rates for longer. Central bankers might not be even thinking about thinking about lower rates, but as equity investors, we can.

In the last issue of CI, we looked at the developments in satellite launch technology, offering a glimpse of one aspect of powerful potential growth. Last week, PM Sunak hosted world leaders at historic Bletchley Park to discuss another, AI. And the keynote guest was the "out-of-world" leader, Elon Musk.

While much policy and media attention focus on the technology's threats, AI offers potentially game-changing economic benefits. Capital Economics has undertaken one of the more sober and wide-ranging assessments of the economic benefits of AI, and they see it as a "general purpose technology" (GPT) able to enhance economic performance like the development of steam power, electricity, and the internet. However, an economy's ability to benefit from AI depends on first how well it innovates in the underlying technology, next how well it can diffuse this technology across sectors, and finally, the economy's ability to cope with the inevitable disruptions AI will cause. Could you handle not having to work?

Given the relative resilience the UK has demonstrated in the face of Brexit, the pandemic, inflation and all our years cast out onto the naughty step of investability, the indicators are there that the UK should be at least in the middle of the pack when handling the positive exogenous shock of AI. We are by no means there yet. But as Yogi Bera, the great baseball philosopher of life, said, if you don't know where you're going, you'll end up someplace else. It could be better for us all.

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10/11/2023	Value	YTD (%)
FTSE 100	7423.97	-1.72
FTSE 250	17660.00	-9.46
S&P 500	4137.23	6.22
Gold $/lb	1997.40	4.7
Brent Oil $/bl	85.05	8.25
Copper $/lb	3.63	-7.13
UK 10 yr yld	4.33%	18.5
US 10 yr yld	4.62%	19.1

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JACKSON'S CHART - BTCUSD (MONTHLY)

An analysis by Jackson Wray

Source: BTCUSD Trading View

EXPLANATION

Bitcoin is an asset class (to some, not all) that divides opinion, but all the same, it is approaching a fascinating technical price point. The fall from its all-time high ($69,000) to the low ($15,500) represented a 77% drop in value, from which there has been a recovery. This recovery cleared previous resistance at $25,000 and subsequently entered a 7-month range between this and $31,750, with multiple attempts to break out. In October, BTC breached this and moved to the next resistance at the diagonal trend-line. Beyond the $38,000 zone lies the most critical area of all, the previous lower high (blue circle) at $48,250, from which a change in the long-term structure will be challenged. In a period of great euphoria, it is crucial to identify the higher time structure and areas of importance, as any reversal from here could draw price action to the lower trend line at $20,000 once again. The psychological battle is not yet over; while the price has rallied strongly, the downward structure is yet to be changed.

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FURTHER READING & LISTENING

- Why Invest in the UK? Simon French, Alyx Wood & Laurence Hulse
- Can Apple keep on delivering for investors?
- Special episode: AI and the global economic order
- Politicians need to show how artificial intelligence can transform economies

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