The Premier Partnership Limited

Your Family Office

Has the World Changed?

Hello again and welcome to our Autumn edition Newsletter. So how has it been for you all in these strange and troubled times? Well, the title of this quarter's newsletter is 'Has the world changed?' We think it has in all sorts of ways. In this edition we would like to review some of the things that we have perceived as change, as well as giving our thoughts on the US Election. We are far from out of the woods as far as Covid-19 is concerned. It may well be the ultimate case that it never completely goes away, but we learn to manage it as we have with such things as AIDS, Ebola and SARS. These viruses are still with us but they are managed. There is no cure yet, but we have to get on with life, re-open the economy and rebuild the economic devastation of the lockdown. We also have to live with the end of furlough, Brexit and the potential rises of unemployment. So it begs the question - Has the world changed? **Let's have a look.**

NewsLETTER

Hell & High Water

Financial Fitness

In lots and lots of ways, yes it has. Is this a permanent change, and is this for the good or bad?

One of the interesting statistics to come out of the last 6 months is the increasing amount of cash that UK households have been putting away in banks and building societies, at a time when interest rates are at record low levels.

On average, the country as a whole saves around £4 Billion per month. This sounds like a big number until you divide it by the 28 Million actual households, and then it boils down to a measly £140 per month, per household.

Then, low and behold, along comes Covid-19 and in March that figure rose to £14 Billion. In April it went even higher at £16 Billion and in May it was £25 Billion. So now, per household, the average savings are £900 per month.

Interestingly, it is not just the UK where this has happened, it's the same story throughout the developed world.

So the big question is why?

Well, let's face it, there was nowhere to go and nothing was open anyway to spend our money on, so generally people built up surplus funds from their monthly income.

Has the pandemic affected not only our ability to spend money - but also our willingness to do so?

Psychologists would point to the fact that when the media and everyone we talk to is slightly worried, then the world becomes very worried. Then stockpiling occurs. Not just in toilet rolls or pasta, but actual cash as well. So people put a bit more away 'for a rainy day', just in case more bad things happen.

Unlike 2008 and the financial crisis, this saving of cash has not coincided with a stock market collapse - yes we had a correction in March - but since then global stock markets have produced solid and positive returns, beating the investment returns from cash deposits and inflation.

Whilst it is absolutely right and proper to set money aside in our often touted, short, medium and long term pots, if the planning overall was being followed, there would be no need to build the cushion of cash even greater. So this money needs, where appropriate, to be invested, provided the basis of the short, medium and long term investment is being followed. To reiterate our mantra:

Short Term - Money you need for 6-12 months of daily living. (Current and deposit accounts)

Medium Term - Capital requirement for major expenditure over the next 2-3 years. (Car change, marriages, university, property refurbs etc.)

(Term deposit accounts, NS&I)

Long Term - Money not required immediately, so beyond 3 years. (Pensions, ISA's, invested funds, stock market based)

This is a basic and simple premise for ongoing financial planning, but never let the perfect be the enemy of the good. Good financial planning is not, and should not be a 'perfect' plan, because such an animal does not exist. Any financial plan should be simple, low cost, flexible enough to be adjusted quickly and easily, and be without tie ins or penalties for adjustment.

Such a plan is not about the size of the overall pot or total estate, and 'good' can be achieved on a small scale really well, providing these simple rules are obeyed. To get physically fit, you may have to go to the gym, play sport, or employ a personal trainer, who don't just tell you what to do, but to make sure you do it via help, encouragement, and advice.

Financial fitness is where financial planners take on the role of personal trainer and provide direct help, advice and guidance where needed.

So review your cash holdings, apply the basic principles above, and start putting in place the plan to meet your own personal goals and objectives, whatever they may be. Early retirement potential is an area we spend a lot of time on, for example. Caution can be good - but planning can be almost perfect.

Understanding Investor Risk

What this year has undoubtedly highlighted is that the end investor rarely considers the term 'risk' as volatility in stock market prices, instead as the actual loss of capital. Covid-19 has returned extreme volatility to stock markets, and this may well have caught a few investors out.

For the seven years to 31 December 2019, the average volatility of the MSCI World Stock Market Index was 12.4% per annum. For the previous 30 years the average was 16% per annum. For the first 6 months of 2020 the average of this index leapt to 24.6%, but since January this index has actually made a gain, and so overall is up on 2020 to date by 1.7%. Therefore when we are defining risk in investment terms, we must also include volatility, or downside/upside movement as well. Therefore, the best way to describe risk is the volatility of an investment fund or portfolio value in negative market conditions. Maximum drawdown is defined as the difference between a fund's highest price/value over a period and its lowest price over a period. If you bought a fund at 100 pence and it fell to 50 pence before recovering to 102 pence, would you be comfortable with that level of volatility. That is not risk, it is volatility. The only risk to your capital is if you consciously choose to dispose fully of the investment at 50 pence (having paid 100 pence for it) thereby crystallising a 50 pence loss.

Investors should always remember that the maximum drawdown of a fund is just two points in time. A fund may have lost value of 20% between two points in time, but recovered a week later to be only down 5%. So when looking at or referring to risk in investments, it is vital to understand what the technical words mean and what is relevant to you. Risk of loss of capital is in the hands of the investor themselves, as they make the ultimate decision to sell an investment at a loss or profit. Volatility is a function of markets that can create decision points, but the old adage of greater risk can provide greater returns, has been proven completely this year, following the strong recovery in market values since the end of March.

Whilst 2012 to 2019 were years when volatility was greatly suppressed by the actions of Central Banks globally, 2020 onwards (the era of disorder?) has brought volatility back to markets like a caged tiger being released, so expect more - not less - volatility to come to portfolios.

The £300 Billion Black Hole

Broadly speaking, £300 Billion is the cost of the Covid-19 pandemic to date, and the amount of money the Government has pumped into the system via a variety of methods including furlough, tax payment deferrals and out and out gifts such as 'eat out to help out'. The problem is that the pandemic is not over yet and so the bill could get higher.

Does this sound like a capitalist Government and society to you? Perhaps you may think it is bordering on socialism and democracy, where the Government pays for and owns everything. Should we even contemplate paying down this debt, which now stands at approx. £2 Trillion in total or 110% of GDP. Or, like the cost of the Second World War, we kick the can down the road and let the future decades erode the debt mountain. Does this even matter, as we only owe the money to ourselves (Bank of England), unlike in the 1970's when we owed vast fortunes to the International Monetary Fund, who demanded repayment of the loans as agreed. All valid points, but as all Central Banks globally, from the Federal Reserve in America downwards have adopted the same approach, are we now witnessing a fundamental and profound change in global economics? Involving a move away from capitalism toward democracy - which is essentially socialist in nature.

I am indebted to the latest long term asset study produced by Deutsche Bank where they put forward the notion of five distinct and defined global eras since 1860. The interesting point they make is point number six.

1. **The first era of globalisation - 1860-1914**
2. **The Great Wars and the depression- 1914-1945**
3. **Bretton Woods and the return to the gold standard - 1945-1971**
4. **The start of the flat money and high inflation - 1971-1980**
5. **The second era of globalisation - 1980-2020**
6. **The age of disorder - 2020-?**

Point number 5 was the era of Reagan/Thatcher and Federal Reserve Chairman, Paul Volker. An era built around Independent Central Banks, aggressive globalisation of supply chains and impressive growth of wealth. Has Covid-19 supplied the coup de grace for point 5? For the last two decades we have existed on debt to an ever greater degree. In contrast, our article on financial fitness proves how attitudes have changed and changed quickly.

The global debt issue is now as great as that created to fight the cost of World War II, and it's not over yet. Critically the pandemic forced global Governments into expansive fiscal policies, to match the expansive monetary policy of the last 20 years, which leads us to only one conclusion - that inflation is about to come back with a bang. This is not a bad thing. Rising inflation will allow Governments to kick the debt can down the road, as inflation erodes debt. This takes the immediate pressure off the introduction of onerous tax rises, which could easily stifle a brittle recovery.

The friction between the USA and China indicates an end to globalisation, which implies greater power for labour over capital. Workers would no longer have to compete against cheaper imports which would lead to wage rises and again inflation.

So where would that leave our long term asset investments, which have prospered under point 5. Long term financial histories are often dismissed as being incomparable between eras, and therefore are meaningless, but I think that is wrong. In the long term, irrespective of era, risk taking is rewarded and we cover the concept of risk in investments in an article in this edition. Irrespective of what could be a fundamental shift in global economies, similar to that seen after World War II, people will get back to work, they will hug and shake hands again, children will go fully to school, and all aided by the biggest Government stimulation packages in history. Because of this we expect the majority of the world's economies to recover quickly. All of which will benefit equity markets. It may take a further 12-24 months, but it will happen. There are still reasons for concern, one is that mobility is still being repressed, and the second is that we have no idea when a vaccine may become available. We can't change that but what we can do is interpret the economic data, apply that to financial plans, invest, monitor and review clients' situations, circumstances and plans, and ensure that we stick with our financial planning through thick and thin.

The US Election

US Elections are far more significant globally than our own General Election. As such they have the power to influence global stock market performance. As we know Joe Biden is challenging Donald Trump and currently the book makers have Biden a marginal favourite at 20/23, against Trump at 20/21 but in the more important move for the Senate, the polls have tightened with the Democrats (Biden) losing what only a month ago had looked like a winning lead against the Republicans. As we know - polls are not always correct. Hilary Clinton was the clear favourite 4 years ago, and we know how that turned out.

Back in 1992, Bill Clinton's political strategist coined a phrase that has become synonymous with US Election victory 'It's the economy stupid', and it's still a truism today.

Since 1950, the only times an incumbent President, running for a second term, has lost, was when there was a recession the previous year. Gerald Ford in 1976, Jimmy Carter in 1980 and George W H Bush Senior in 1992. So history would suggest it is Biden's and the Democrats to lose.

We mention that the Senate Election are also crucial, and we only have to think back to the Obama Presidency to see how a Democratic President can be hamstrung by a Republican Senate (and Vice versa). Having the Senate, and/or Congress on your side, greatly enhances the ability a President has to get legislation and policies through the House.

Traditionally a Democratic President/Senate would be viewed as bad for markets, but a unified Democratic victory may not be all bad as they would ramp up spending and loosen fiscal policy. A Biden Presidency would also be viewed as less confrontational on the world stage (which would not be difficult).

In 2018, US Corporate America received a golden hello from Trump as he slashed taxes for US businesses, a tail wind that still exists today. Biden would look to reverse those changes, so a slight negative. Higher minimum wages, higher taxes for high earners and increased regulation and red tape would also be part of a Biden Presidency. So our overall view is that markets may view a Biden Presidency as negative for 6 months, until we see exactly what he can and cannot get passed into legislation. A Republican Senate would quash most of the above anyway.

A Trump victory on the other hand may well bring more tax cuts, along with infrastructure spend, particularly if he has the Senate with him (current position). So a positive for markets. On the other hand we would get more global posturing and more tension with pretty much anyone who is anyone, along with any major institutions (WHO, NATO, The EU and of course China) worth mentioning.

So this is a flip of a coin Election and on 3 November, America will go to the polls. Key States such as Texas with 38 Electoral college votes (currently Trump) will decide who wins. I for one will be keeping a close eye on the Senate/ Congress Elections, for it is there that the real power lies. We shall wait and see.

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