Update 17 | March 2019

update

Knightsbridge Wealth

Dear Friends and Colleagues,

The global economy both gives and takes away. So Germany is finding. Its economy is stuttering as demand for its exports falls (manufacturing orders from foreign countries were down over 9% year-on-year in December). And so the UK is finding. Most commentators have been quick to at least partially blame Brexit for any miserable news that emerges – such as Honda closing a major car plant.

However, if this was all about Brexit, Honda might have wanted to wait a mere six weeks to see what Brexit is actually going to mean. It might also not have announced the closure of its Turkish plant at the same time. And it might even have hinted that it would open a plant in a country rather more enthusiastically settled in the European Union's customs union than we are.

The truth is that the global car market is changing (sales are falling, diesel is finally all but dead) and the role of the UK is changing with it. That's not to say that uncertainty over Brexit isn't having an effect on investment in the UK economy, it's just to say that for now at least global shifts are probably having more of an effect.

On the plus side, while the UK looks like it will be losing jobs in the car-manufacturing sector overall, it is doing a pretty good job of creating them elsewhere. The unemployment rate is now a mere 4% – the lowest reading since the mid-1970s. Even better, this tightening of the labour market is finally feeding through into real wage rises – with wages rising at a nominal annual rate of 3.4% and inflation sitting at around 2%, workers' pay packets are at last growing faster than the cost of living.

Stock-markets keep a beady eye on Donald Trump. December's market wobbles have prompted the president to seek a "quick-and-dirty settlement" in the trade war with China. Trump has announced that he will postpone an increase in tariffs on $200bn of Chinese goods set for 1st March.

He said there had been "substantial progress" in trade talks. The US might also drop criminal charges against Huawei (for violating US sanctions on Iran and stealing US technology) as part of a trade deal, says The Wall Street Journal. In return, China could agree to buy large amounts of US products, such as soybeans.

Chinese stocks surged following the announcement, with the CSI 300 index rising to its highest level since July. The S&P is up 11% so far this year. The CSI 300 shed a third of its value as trade tension worsened.

There may well be further gains ahead, even if optimism on the trade front is overdone. The latest data coming from China suggests that credit growth may be accelerating again, and this is positive for equities. Many other emerging markets are largely a play on China, and if China picks up they should too, especially since the balance sheets in emerging markets are strong, and currencies started the year attractively valued.

This does not represent an easy market to give investment advice. GDP growth worldwide is looking weak ; markets are looking quite expensive ; and there is increasing risk of global inflation. With that in mind, it is important to emphasise the value of diversification.

More than ever, people need access to the highest standards of advice and regulation to protect their wealth and assist with financial planning. Despite Brexit, London remains the pre-eminent safe haven for international investors. The UK's brand across the globe remains un-dimmed, and its financial centre has a deserved reputation for quality and innovation, supported by a resilient banking sector.

Whenever Knightsbridge Wealth gives advice, it is UK regulated. Our clients – whether they live in London, Limassol or Libya - recognize the value and security that gives.

We look forward to working with you in the remainder of 2019.

Our strategic partnership with UBS (Union Bank of Switzerland) gives the best of both worlds – personal service and the ability to react in a way that only a small firm can, partnered by one of the world's most prestigious brands.

Market Report

Bonds

Rising interest rates drive values lower

Spreads in most regions have tightened to fair or even slightly expensive levels. Corporate leverage is elevated in the US, whilst less so in Europe. A sharp increase in defaults is unlikely.

Total returns in High Yield Bonds are likely to remain positive, whilst high quality Bonds are likely to fall, as global interest rates edge higher.

The end of the European Central Bank's corporate bond purchase programme has worsened the technical backdrop for the asset class, as new buyers still have to be found.

Only emerging markets have provided a positive return year-to-date, with government bonds gaining 3.3%, and corporate bonds 1.9%.

Equities

Emerging markets favoured

Equity markets has shown signs of recovery after reaching a trough in late December 2018. Economic data is likely to stabalise after last year's deceleration in global growth momentum, supporting global stock-markets.

Emerging markets are looking very attractive on current valuations. Emerging market 'value' stocks have now out-performed growth by 7% year to date, with financials, energy and materials particularly appealing. Key drivers are a pick-up in emerging market growth differential over developed markets and the recovery in commodity prices. Risks include tighter global liquidity conditions derailing the recovery, continued weakness in commodities and a rally in the IT sector.

Commodities

Red metal jumps

Gold prices have behaved as you would expect during the recent uncertainty, rising in value as equities sold off. Market volatility has confirmed that gold remains a safe-haven asset and helps to reduce balance risk in a portfolio at times of downturns.

After plunging by a fifth last year, copper prices have jumped to their highest level in eight months: around $6,500 per tonne. Tight supplies and optimism over global growth boosted prices after President Donald Trump said he would delay an increase in tariffs on Chinese goods. The red metal is found in consumer products, cars and semiconductors. In 2018, global demand reached 23.6 million tonnes. By 2027, it could hit 30 million tonnes, representing an average annual growth rate of about 2.6%, according to Forbes. Electric vehicles use far more copper than their combustion-powered counterparts. Bullish sentiment has offset recent signs of a downturn in China, the main consumer of the metal.

Oil

Asia fuels demand

The production cuts by OPEC and the fall in Russian production, whilst demand remains healthy, has driven up prices. However, supply growth in the rest of the year (from China, amongst others) is likely to continue at a higher pace than demand growth, softening prices.

Longer term, substantial cuts in capital expenditure by energy companies between 2014 and 2016 should constrain supply growth, resulting in a tighter market, whilst emerging Asia will continue to fuel oil demand growth, accounting for half of the world's population but just 25% of global oil demand.

The ongoing improvement in energy efficiency and battery technology is a negative factor for crude oil demand, with electric cars eventually slowing growth.

Hedge Funds

Useful source of stability

Hedge funds are a useful source of return and stability in a multi-asset portfolio, especially during times of market volatility. They can offer superior risk-return compared to many other asset classes and access to uncorrelated investment opportunities, which provides downside protection and diversification benefits.

With potentially tougher times ahead, investors should consider holdings in this asset class. Heightened stock dispersion, volatility, rising interest rates and a maturing cycle more broadly should be conductive of performance. UBS anticipates average annual returns of between 3-6%.

Foreign Exchange

Sterling risk remains

Higher oil prices and recovering Canadian growth is likely to allow the Bank of Canada to hike rates, making it an attractive currency to have exposure to, along with the Norwegian Krone where rates are rising too. The Japanese Yen looks seriously under-valued too.

Sterling is likely to rebound when a Brexit transition deal is passed. However, there is still a significant risk than uncertainty, and therefore Sterling downside risk, is prolonged.

The US economy's momentum has eased and the Fed has switched from autopilot to one rate hike per quarter to data-sensitive mode. The Dollar responded by giving up some of its over-valuation. Markets will monitor Europe's economy and the political risks linked to Italy and Brexit, which are likely to hurt the Euro in the short term.

Brexit nearing

A month before the Brexit referendum in June 2016, the UK Treasury published a report saying that "a vote to leave would represent an immediate and profound shock to our economy." The Treasury set out the gloomiest of forecasts of what would happen if the result went the wrong way. Britain's GDP would nose dive while unemployment jumped, it said—and many agreed. Happily, the impact of voting for Brexit was neither immediate nor profound: the economy has held up better than expected. Yet almost three years on, as Brexit day nears, there are signs that Britain's decision to quit the world's largest trading bloc is beginning to take its toll.

Even the most committed Remainers struggle to portray the aftermath of the referendum as an economic disaster. Average GDP growth in the two years following the vote was only slightly below what it had been in the five years before. And although the Pound's swoon stoked inflation, while failing to generate the export boom that some had expected, Britain continued to attract a goodly share of foreign investment and unemployment kept falling.

But mounting evidence suggests that the economy has taken a turn for the worse. Official data published on February 11th showed that in the fourth quarter of 2018 GDP grew by 0.2%, rounding off the weakest year since the financial crisis. In December, the latest month for which there are hard data, GDP shrank by 0.4%.

Is Brexit to blame, as many Remainers argue? At the end of this month, Britain is currently due to leave the European Union. But other factors complicate the picture. The global economy has slowed, in part owing to trade tensions between China and America, which hurts trade-heavy economies such as Britain's. Italy, another big trader, recently fell into recession. Germany, which enjoys the world's largest trade surplus, may follow. That, rather than Brexit, is likely to explain why British export growth is weak. Consumer confidence in Britain is edging down, but it is doing so in most rich countries.

Still, Brexit does appear to be spooking companies. A paper published in December by Nick Bloom of Stanford University and colleagues shows that the share of businesses reporting that Brexit was their biggest source of uncertainty roughly doubled in the autumn, to 19%. Only 13% say it is "not important", down from over 25% in September 2016.

That is having an impact on investment, which accounts for over 15% of GDP in the short term. In the year to September, gross fixed capital formation fell in Britain while rising in every other G7 country except Japan. Business investment fell in every quarter of 2018.

The Brexit effect seems particularly clear in industries that trade a lot or rely heavily on workers from the EU. Capital spending in the engineering and vehicles sector, also hit by diesel woes, is falling by 9% a year. It is dropping even faster in the hotel and restaurant industry.

Whether Britain gets out of this hole, or digs in deeper, depends on what happens after March 29th. Postponing the date of departure, which looks increasingly likely, would stave off the threat of no deal, but prolong the limbo that the country is now in. Most business people hope for a deal including a transition period, during which existing rules would remain.

Mark Carney, the governor of the Bank of England, speaks of the potential for "upside", "if there's clarity on the deal" soon. In recent years, British companies have built up enormous cash piles, which they could invest when uncertainty ends. Philip Hammond, the Chancellor of the Exchequer, has implied that a livelier economy—and the tax receipts that came with it—would allow him to loosen fiscal austerity.

Yet even then, once the transition period is over, Britain will probably be outside the EU's single market and perhaps its customs union, leaving it in a worse position than it is at the moment.

In the event of disorder, the Bank of England might loosen monetary policy, though perhaps not by much: another fall in the Pound would probably push inflation above target again. Mr Hammond could boost spending or cut taxes to the tune of £20bn without breaking his fiscal rules. Officials are reportedly drawing up a dossier, "Project After", with emergency plans to cut corporation tax and vat if no deal is reached.

Nearly three years after the vote, Brexit is beginning to bite. Investors portfolios need to be constructed to ensure they protect against the risks of Brexit, and able to take advantage of the opportunities.

Feature: Europe

Germany narrowly avoids recession

The once seemingly unstoppable German economy had the slowest growth of any eurozone country except Italy at the end of 2018. Last year, Europe's largest economy only narrowly avoided a recession. Its GDP growth was below the Euro-zone's average at just 1.4% in 2018, down from 2.2% in 2017.

The slowdown has resulted from Germany's reliance on what was once its biggest strength: its exports. Germany is more deeply entwined with the global economy than perhaps any other country. Exports account for 47% of German GDP, according to World Bank data. This compares with 31% in the UK and the US's 12%. As The Economist notes, Germany's talent for producing goods that are desired by emerging economies – especially China – propped up its recovery after the financial crisis. Yet exports are also its Achilles heel, leaving it particularly vulnerable to a global slowdown.

In particular, cars and car parts make up 15% of Germany's exports. In January, Volkswagen reported a 3.4% drop in sales to China. Components manufacturer Continental also noted decreasing demand. Last year China introduced new emissions standards, an area where Germany hasn't shown itself in the best light. However, while China is part of the story, Germany's exports are quite diversified. Sales to China are equivalent to just 2.8% of GDP.

Low water levels in the Rhine have also hit the shipment of some German exports, which is clearly a temporary issue. What's more concerning is that German consumers are spending less, despite solid wage growth, low unemployment, and ultra-low interest rates. Perhaps they are hunkering down for a recession, or maybe it's a result of the nation's ageing population saving for retirement. Either way, they are unlikely to propel growth this year.

By the end of last year, the troubles facing the German economy were being reflected in stock-markets. In the last three months of 2018 the German blue-chip index, the Dax 30, fell by 16%, one of the weakest global performers in a notably bad period. But since the start of this year, the Dax has staged a rally, rebounding sharply. The bad economic news seems to be priced in. Investors are hoping for the silver lining. Exports won't be in free fall forever, and consumers' spending also ought to pick up given solid fundamentals.

The German stock-market now trades on around 12.1 times earnings – similar to the UK and Japan. What's more, Commerzbank reckons €38bn will be handed out in dividends by Dax companies this year, up 3% on 2018. It's certainly possible that the German economy hasn't yet seen the worst. But investors looking for good-value stocks should pay attention.

Italy going from bad to worse

Lorenzo Codogno, the former chief economist of the Italian treasury, recently told The Daily Telegraph that "we are going in exactly the wrong direction,". Italy's anti-immigration, populist government, led by Matteo Salvini of the Northern League and Luigi Di Maio of the Five Star Movement, is dismantling recent pension reforms and introducing a basic income for all.

About one in ten Italians live with serious deprivation, But the Five Star's 'citizens income' risks getting bogged down by its own complexity and the country's famously inefficient bureaucracy. In addition to spending more money it doesn't have, Italy's anti-establishment government has been attacking France on various fronts in recent weeks, exacerbating political tensions in the Euro-zone. According to Politico, 51% of Italian voters under 45 would vote to leave the European Union in a potential referendum.

Italy's leaders have criticised everything from France's role in Libya to its stance during the migrant crisis. Using France as a whipping boy is a helpful alternative to bashing Brussels, which risks rattling investors.

Investors, however, are pretty rattled anyway. Consider the economic backdrop. Italy's GDP has shrunk for two quarters in a row, so it is officially in recession – for the third time in a decade. Industrial production was down by 2.6% year-on-year in November, whilst youth unemployment stood at 32% last year. Rome's interim deal with Brussels over the Italian budget may have averted a dangerous political showdown for now but nothing is resolved. Given all this, concern over the country's debt pile will intensify. Government debt comprises 132% of GDP; without growth there isn't a hope of whittling it down.

Italy's poor GDP has only been a phenomenon for the last decade. Until 2006, Italy's GDP growth was broadly in line with that of Germany. Before it adopted the Euro, Italy tended to let the lira fall, cut interest rates and increase government spending every time it faced a downturn. Under the single currency and Brussels' fiscal regime, these escape routes have been closed off.

Another problem is that the European Central Bank has halted its quantitative easing (QE) programme, whereby it buys government bonds with printed money. That leaves Italy without a 'buyer-of-last-resort 'standing behind its sovereign bonds." This means there is no longer a cap on how high the yields of Italian bonds, and thus implied long-term interest-rates, can go. Expensive money is the last thing a country in debt up to its eyeballs needs. If investors panic and sell off their Italian bonds, the country could fall back into a debt crisis.

Emerging Europe struggling

The Romanian Leu has been the worst-performing emerging-market currency this year. The currency has come under pressure from Romania's widening current-account deficit and concern about new taxes on banks and energy companies that were introduced to address the deficit. Last December, when these measures were first announced, the Bucharest Stock Exchange index tumbled some 12%.

The sinking Leu has prompted declines in other regional currencies, reminding investors that emerging Europe has well and truly come off the boil. Regional year-on-year GDP growth slowed to 1.3% in the fourth quarter. This is partly due to Turkey's recession following its credit bubble. But central Europe (Czech Republic, Poland, Romania, Slovakia and Hungary) is losing momentum too. The trouble is that the region depends on western Europe: almost two thirds of the value of its exports goes to the rest of the EU.

The eurozone's soft patch that began in the late summer has extended over half a year. German manufacturing output has contracted, and the eurozone's economic growth was close to zero at the end of last year.

Capital Economics expects GDP growth of 2.8% and 2.3% in the Czech Republic and Hungary respectively for 2019, down from 4.5% and 4% in 2017. Poland's economy continued to expand at a robust 5% year-on-year at the start of the fourth quarter in 2018, however. Its large domestic market means it is less dependent on exports than its neighbours. But Poland's relative dynamism may not temper the regional equity market decline: the MSCI Eastern Europe index slipped by 5% last year.

Expats struggle to get UK mortgages

Expatriates looking for a mortgage on a property in the UK now have a wider choice of loans. Cambridge Building Society and Tipton & Coseley Building Society have both launched new ranges of buy-to-let mortgages aimed at British people living overseas. Both ranges include fixed and discount deals, available for both new purchases and re-mortgaging.

About five million UK nationals live overseas, and many are keen to hold on to a home in the UK, or to invest in one to rent out. But the available mortgage options are quite restricted – and in most cases, you'll need to get a specialist landlord mortgage. It is possible to secure a standard residential home loan as an expat, but it's tricky to arrange, since lenders will want to see evidence that close family are living in the house. Since most expats work abroad and cannot live in two places, for the majority, a buy-to-let is the more appropriate solution.

You will typically need to seek out a specialist lender: options include Paragon, Saffron Building Society, Market Harborough Building Society, Al Rayan Bank, Skipton International, Natwest International and Kent Reliance. And be prepared to jump through a lot more hoops than for the standard home loan. It can be a difficult process to secure a mortgage when clients are overseas, especially with the tighter lending criteria.

Many lenders like borrowers to work for multinational firms, interest rates tend to be higher, and a deposit of 25% is usually required. Another factor is the European Mortgage Credit Directive, introduced in 2016, which means individuals paid in a foreign currency now come under closer scrutiny when their loan applications are assessed. The underwriting process needs to take account of possible exchange-rate fluctuations, as well as looking at a borrower's overall financial position.

Unsurprisingly, salaried expats have the greatest choice of mortgages. Lenders often exclude the self-employed, on the basis that income cannot be verified to a high enough standard, unless it is audited by a reputable accountancy practice.

Expats face tougher identity checks. Getting a correctly certified passport can be tricky if the borrower lives in a remote area without access to international lawyers, accountants or diplomats. And don't rely on your employer to help out. Big multinational companies will have standard formats for issuing employee references which seldom match the requirements laid down by a lender, who is trying to underwrite on the basis of very specific individual information needs.

It is also easier to get approval for a UK mortgage from certain countries than others. Most lenders have a "restricted" list of countries where they won't lend (for example, countries subject to sanctions or with a weak reputation for regulation). Many African nations and some in Eastern Europe meet this category.

Finally, if you do buy, remember to keep the tax office informed. If you live abroad for six months or more per year, and rent out a property, you'll be classed as a "non-resident landlord" by HMRC – even if you're a UK resident for tax purposes.

Wherever your income is taxed, you'll be required to pay tax on the rent you receive.

'Golden visa' schemes under the spotlight

In a recent report, The European Commission warned EU member states that the "golden visa" schemes used to attract the wealthy to make investments in exchange for residency rights or citizenship, have exposed the continent to corruption and organised crime.

The 28 EU member states have earned about £22bn of foreign direct investment in the last decade from a variety of different offers to wealthy people under which investors can secure the right to free movement in the bloc.

Bulgaria, Cyprus and Malta sell citizenship in return for investments ranging between approximately £800,000 and £1.6m, while 20 member states offer residence permits for cash. Before her murder, the journalist Daphne Caruana Galizia was investigating an alleged abuse of the scheme in Malta.

The UK are currently reviewing 700 Investor Visas issued to wealthy Russians under its scheme. In December, the British government announced it would suspend its Tier 1 (Investor) Visa programme, which provides a fast-track route to settlement for people willing to invest in the UK, while new rules were being formulated. But the government did not follow through on that pledge, and it remains an option for those looking to secure UK residency rights.

Sophie in 't Veld, a Dutch member of the European parliament, who is the Vice Chair of its committee on civil liberties, justice and home affairs, said the EU had been slow to respond to the abuse.

She said: "I welcome the fact the European commission is, albeit belatedly, sounding the alarm. We need a ban on these schemes, which are exploited by organised criminals who often receive limited background checks, and to align rules for acquiring citizenship. After all, by acquiring citizenship of an EU member state, you get EU citizenship automatically. Golden visas and passports are essentially state-facilitated corruption and money-laundering schemes."

The commission's report highlighted the varying standards across the EU in terms of the background checks on applicants. Whilst not having any legal consequence, the Commission has urged governments to adopt common approval criteria and be more transparent about their internal processes.

A long-running court case in Portugal on the alleged abuse of the government's golden visa scheme led to two people being given suspended sentences and two Chinese nationals fined earlier this month. Visas have been offered by the government there since 2012 to wealthy foreigners willing who invest €500,000 in property, make a capital transfer of €1m or create 10 jobs.

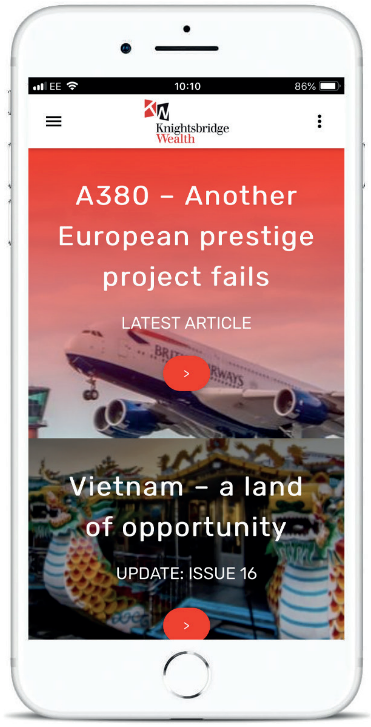
Cyprus has also made changes to its Investment programme. Applicants will now need to declare if they have applied for citizenship in another EU state and, if they have been rejected, they will not be able to apply. In addition to the requirement to invest at least €2m in property, applicants now have to donate €150,000 to government initiatives.

Residency is an important aspect of advice for international clients and Knightsbridge Wealth work with the most experienced immigration advisers to ensure they receive the highest quality of advice in a fast changing environment.

Knightsbridge Wealth launches new app

Knightsbridge Wealth has launched a new app to keep clients and contacts up to date with issues affecting their financial planning. It will evolve and be increasingly used as the core way of issuing bulletins and market news.

Download onto your smartphone or tablet now by clicking on the 'Download app' button on the home page at **www.knightsbridgewealth.co.uk**.



Knightsbridge Wealth's senior team and support staff have over 200 years experience in the world's largest Banks

Alexander Wade

Alexander is one of the most experienced London advisers in the international market, specialising in this field over the last 20 years at HSBC, consistently recognised as one of its most accomplished advisers. He has over 24 years' experience in financial services. He is particularly interested in the Middle East market and understands the specific issues which are relevant there.

Stuart Poonawala

Stuart has worked in financial services since 1998. In 2003, he helped to found HSBC's specialist London arm advising international clients which quickly became one of the bank's most successful UK divisions. In 2009, he launched Kubera Wealth, our sister company, focussing on providing quality advice to the UK market.

Graeme Cowie

Graeme is responsible for building our professional connections with international lawyers and accountants, as well as co-ordinating our relationship with key fund managers at a number of international Private Banks and Discretionary Fund Managers. He has spent over 20 years in financial services and investment management, most recently spending more than six years at UBS where he led the Strategic Partnership team.

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