The agony and the ecstasy

We live in strange times with markets 'risk on' one day, and 'risk off' another, all because of one seemingly off-the-cuff tweet from the Potus. Markets swing from sheer euphoria of a Federal Reserve rate cut (surprisingly against a background of strong job creation and low inflation, but that's another story) to near depression over faltering US trade negotiations with China.

What are we to make of these violent mood swings? A few pivotal events help explain the market's schizophrenic behaviour as it is pushed and pulled between macro events like interest rates and Chinese tariffs and micro stock-specific developments.

1 WeWork and the death of the unicorn. The failure to float and the subsequent collapse of WeWork's valuation from $47bn to $8bn killed the unicorn and exposed it for the mythical creature that it is. Positioned as a digital disruptor, WeWork was suddenly seen as an old-fashioned office rental business with old-world issues of high costs and low margins that crashed and burned under the weight of its own debt.

As an aside, it was amusing to see it change its well-known branding from WeWork to WeCompany or WC for short, which sounded like a call of nature or a lavatory cubicle. Unfortunately, it's where the billions of dollars disappeared.

2 Woodford and the end of active management. The suspension of Neil Woodford's flagship Equity Income fund and subsequent collapse of his investment empire focused investors' minds on the cult of the star manager. How much of a fund manager's performance is down to sheer luck and how much superior judgement?

The consensus is that success comes from sticking to your knitting and in Woodford's case that would have been investing in high dividend payers, like tobacco and big pharma, rather than punting in bio-tech and hi-tech start-ups where failure is common and where he lacked an edge or special expertise.

As another aside on branding, naming Woodford's fund Equity Income lacked intellectual honesty as most start-ups don't have a top line let alone a bottom line, so where was the income or dividend stream coming from? Sadly, nowhere is the answer.

3 Lloyds Bank and the cost of 'doing the right thing'. Following the 29 August 2019 deadline, the PPI mis-selling scandal has now cost UK banks £50bn in consumer compensation and Lloyds Bank the most, with close to £22bn. Like BP's Deepwater oil spill in the Gulf of Mexico, which cost £60bn in US fines, Lloyds compensation bill is precious cashflow that has been diverted from growing the business at the expense of the shareholders.

4 Negative interest rates in the eurozone and the loss of risk-free returns. For the first time in history, some eurobanks are offering a paltry 0.1% for one-year fixed term deposits and many others are charging customers for safekeeping of their cash deposits. Indeed, unimaginably, $16tn of debt is now attracting negative interest rates.

5 The FAANGS, the taxman and the regulator. With the FAANGs (Facebook, Amazon, Apple, Netflix, Google) representing the biggest transfer of value in history from established businesses to digital disruptors, the challenge now is for them to become respectable citizens, to pay their fair share of taxes and respect customer privacy. Many believe that they have contributed to the demise of our communities through the collapse of the high street (Amazon), the local pub, the local newspaper and even church attendance (Facebook).

As I'm fond of pointing out, just as Shakespeare's comedies end in marriage, so bull markets end in M&A (mergers and acquisitions). Despite the traditional summer lull in corporate activity in 2019, we saw two takeovers in the run-up to the August bank holiday weekend – pub operator Greene King by Hong Kong tycoon Li Ka-Shing, and Peppa Pig entertainment company EOne by toy company Hasbro.

These two deals followed a string of takeovers that defined the first nine months of 2019 with bids for 11 other companies, including Manx Telecom, KCom, Inmarsat, Tarsus, BCA, Merlin, EI, Refinitiv, Just Eat, Cobham and Sophos.