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Another election and lots of earnings

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"'Elections are won by men and women chiefly because most people vote against somebody rather than for somebody" Franklin Pierce Adams

If 2016 brought us the Brexit referendum and the U.S. Presidential election, then European politics in 2017 is all about the ballots in the Netherlands, France and Germany, with a few Italian, Greek and embryonic Brexit discussions thrown in for good measure. With the first round of the looming French Presidential vote in just a few days, only the snap - and unexpected - announcement of a U.K. General Election on 8 June could even hope to push the fascinating and hugely important race to choose Francois Hollande's successor off the top of the agenda.

If I have opined before that a mainstream candidate - undoubtedly currently Emmanuel Macron - will be the likely next president residing the Elysee Palace after the expected two rounds of voting, then what should we make of Theresa May's decision to hold an early election (she could have waited until 2020) from the rationale that it is the 'Only Way To Guarantee Stability' in the years ahead?

Clearly this is all about the upcoming Brexit discussions and having a bigger parliamentary majority, and a feeling of a popular mandate for what ultimately will be a 'soft Brexit' with clear interim arrangements that extend the whole process by a year or three. Given the twenty-percentage-point odd lead the U.K. government had in a recent opinion poll, little wonder the immediate reaction to the news was a higher pound thrusting above its 200-day moving average.

The pound's move is completely logical to me. A couple of weeks into 2017 I participated in a roundtable meeting with various other market strategist types, and caused a bit of a stir with my favourable view of the U.K. currency and the euro versus the U.S. dollar. I do not believe they are as controversial now. Dust down some half-sensible purchasing power parity analysis and the 1.35 pound-dollar and 1.20 euro-dollar levels I mumbled about in early January no longer seem unreasonable targets.

Back to the U.K. economy specifically. A firmer pound has very clear investment implications, which once again underpin the key portfolio outperformance characteristic in 2017 of concentrating on stock picking / finding alpha rather than focusing on markets going up / beta. That is not to say that some markets will not go up - indeed, due to current global portfolio managers being underweight in the Eurozone and emerging market assets, these markets/regions will continue to outperform, in my view.

A firmer pound is good for the stock selection mix. A little after the election announcement, I saw a report that juxtaposed the strength of the pound and the weakness in the U.K. large cap index. This is perfectly logical given the high excitement towards the non-pound earning sectors, such as energy, mining, pharmaceuticals, and industrials since the Brexit referendum result. Meanwhile the most domestic-oriented sectors and corporates have been much duller performers. A firming pound aids a rotation. I like the

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more domestic U.K. investments here with their sentiment recovery potential. If you want to buy the U.K. anticipating electoral benefits, then look here.

Of course, with another earnings season already upon us, investors intrigued by this increasingly stock-picking friendly epoch will be dusting down earnings to help identify pockets of value. I have talked before about the classic earnings season dance of expectations being lowered in order to allow 'beats' to be made. The trouble is most earnings seasons do not start with even this 'lowered' number pushing around the double-digit percentage growth level. Yes, the absolute bar is higher this time around in many parts of the world. And what sectors are driving this? The five sectors with double-digit plus earnings growth this season are (in order of magnitude) energy, materials, IT, financials, and industrials.

Now this is interesting. With the exception of the seemingly omnipresent (but actually very diversified and specific) IT sectors, these are sectors that typically benefit when bond yields go up (and bond prices go down). And yet... bond yields have recently surprised me by continuing to compress.

We all know markets look forward, but if you want to get another take on why tensions are still apparent below the still almost mirror-like financial markets lake, (historic) earnings are showing strong growth in sectors typically not rotated towards given recent bond yield shifts. Before this sorts itself out in 2018, your conclusion for 2017 is to be an anarchic stock picker. And any populist election fear should be embraced... which brings us back to where we started and the French presidential vote.