The cut and thrust of markets

The MSCI All Countries World index closed 1.63% up over the week, for a marginal loss of 0.49% for the year-to-date, compared to global bonds as measured by the Bloomberg Barclays Global Aggregate index, which rose 0.10%, for a return of 1.22% for the year-to-date. Events in Syria early in the weekend pushed all other news to one side. During the lead-up to that, market talk regarding trade had morphed, with President Trump now prepared to reconsider his Administration's terms for membership of what was previously the 'Trans-Pacific Partnership', in addition to being prepared to proceed with NAFTA talks. The S&P 500 index rose a fraction under 2% over the week, after profit-taking in Wall Street banks following result 'beats' from JPMorgan, Citi, and Wells Fargo (the latter's announcement was spoiled by the likelihood of a $1 billion fine for the mis-selling of insurance and mortgages). At the close of trade on Friday, the S&P was down 0.65% for the year-to-date. Encouragingly, the VIX index closed at a very moderate-looking 17.41. US equity indexes gave back some gains around mid-day on Friday after CNBC and others reported the US was considering attacking targets in Syria. Elsewhere, crude oil had an excellent week (with Brent closing 8.15% higher, at $72.58), and had been climbing before the Syria news, although not purely on geopolitics alone. Needless to say, Energy stocks did well. So overall stocks were very resilient during what was a very interesting week – now we need to know what happens in the aftermath of the Syrian events. Through all this the Fed minutes from their last policy meeting became lost in the background, as did the potentially significant announcement from Paul Ryan, the popular Republican Speaker in the US House of Representatives, that he was intending to retire after the mid-term elections. Also in the mix was that Trump's personal lawyer was placed under criminal investigation for his personal business dealings. In bonds, the yields on US 10- and 2-year Treasuries rose, by five and nine basis points respectively, to 2.8267% and 2.3566% - making that yield curve flatter over the week (to 47, from 51 basis points). US 'core' consumer prices as measured by the Bureau of Labor Statistics increased to 2.1% year-on-year in March (from 1.8%), although please note this data series is running about 0.3% higher than the 'core' PCE series that the Fed prefers. **Federal Reserve Chairman, Jerome Powell, has already said they expect inflation to increase, and to above 2% year-on-year, prior to their targeted 2% rate being more conclusively met.**

"If not already done, establish a hedge position in gold"

In FX markets, the dollar gave back 0.34% on its index (DXY), to 89.800. The minutes of the Federal Reserve's March meeting contributed to market participants revising upwards (by perhaps 8 basis points) their expectations of where the Fed funds rate might be in two years' time (i.e. about 2.54%, vs. 1.69% currently). We still expect the Fed to move a total of three times this year (i.e. two more). The euro was 0.41% firmer vs. the dollar, despite signs that Eurozone growth has come off the boil. Cable was just over 1% higher over the week, at $1.4238; our Global Markets colleagues believe it can trade up to $1.50 by the year-end as the Brexit discount falls. Overall, the dollar is just about 'hanging in', with a two-day close above about 91 on the DXY needed to suggest recovery. In commodities, further than just reflecting Middle Eastern geopolitics, sentiment was helped by the International Energy Agency noting that global crude stockpiles had fallen quite sharply, inferring that OPEC and NOPEC may well have achieved a rebalancing of the crude market. Saudi officials are talking of crude with an $80 price handle, and we would agree with this, certainly by year-end (we have our $70 upside limit and the trading range under review). Non-commercial players (hedge funds) are already very long, yet could become even more enthusiastic. The physical market has tightened, given that global demand has been good, and unexpected supply curtailments would have a greater effect. Turning to gold, the yellow metal was $13.77 higher over the week, at $1,346.20/oz. Depending on extra hedging/investment demand materializing in Asia as you read this, there is a chance that a break-out to the upside (a two-day close above about $1,366 would likely confirm) may occur. We are not yet suggesting readers go overweight for a trade - rather, please make sure diversified portfolios contain sufficient gold exposure for hedging purposes. The FAB Asset Allocation Committee meets later this week, and is sure to discuss whether current hedging exposure in the models is adequate. **Known holdings of gold by gold ETFs have been a good proxy for investment demand, and these have been steadily increasing.**

"Singapore reflects many of the positive aspects of the Asia-Pacific region"

This week will see the latest assessment of the outlook for global GDP growth from the IMF. We know that global growth momentum has slackened during the year-to-date, although it remains to be seen whether the IMF will actually need to reduce its forecasts, as they were already looking quite conservative (i.e. not too demanding) at the time of their January update. Economic data coming out of the Eurozone has been poor lately (witness the steep fall in the Citi

Eurozone Economic Surprises index) which tracks how data has compared to consensus expectations. China's growth has slackened, although we had already allowed for that (their desire for 'better-quality' growth, which was always going to cause growth to moderate further - although it still compares well globally - when we wrote 'Outlook 2018'. The main underperformer the IMF will point to is likely to be the Eurozone. Having said that, Japanese consumer spending has been restrained, and wage growth there has not picked up despite low unemployment and rising vacancies; that country's fundamentals continue to be very difficult. The IMF will underline recent warnings that trade protectionism could impact the global economy (the World Trade Organisation has already said this has begun to be the case). The IMF in January forecast 3.9% growth for the global economy this year. In terms of our 'Tilt to Asia-Pacific (ex-Japan)' recommendation in Outlook 2018 (further to investment policy from last year), we believe this is still very much on track as a theme. In our article we used Singapore as the location that is probably the best economic barometer in the region i.e. it is exposed to many of the positive aspects of it. Singapore's central bank tightened monetary policy for the first time in six years late last week, saying they expected to see steady economic expansion throughout 2018. By adjusting the slope of the Singapore dollar's managed policy band upwards slightly from zero they are allowing their dollar to strengthen - thus underlining their expectation of solid economic growth (with manufacturing in the vanguard). **Real growth in Singapore grew 4.3% year-on-year in the first quarter, meeting the Reuters consensus forecast; growth for 2017 as a whole was 3.6%.**

"A concern in the background for Trump last week was that more Republicans might follow Paul Ryan"

INVESTMENT SUMMARY:

POLITICS: (1) Trump could be becoming more pragmatic on trade - with November's mid-term elections in mind, and not wanting other Republicans to follow Paul Ryan's example; (2) As Ryan's successor, House Majority Leader, Kevin McCarthy is more popular than House Majority Whip, Steve Scalise, although it arguably comes down to party fund-raising ability in each case.

ECONOMICS: (1) The minutes of the Federal Reserve's 20th-21st March policy meeting showed a "strong majority" saw downside risks for the U.S. economy from retaliatory actions on trade; (2) The ECB may find that Italy's political difficulties (no government yet), as well as pushback on Macron's reforms in France means extending the time horizon for full monetary normalization; (3) The ECB could easily (and justifiably) say they will reassess reversing asset purchases at the year-end, and say they might raise rates in 2019; (4) Chinese data showed March exports fell 2.7% from a year earlier - it was seasonal, and follows an exceptionally strong period.

MARKETS: (1) Stocks rose sharply on Thursday after the market thought Trump might be hanging-back on acting in Syria - so we might see quick equity weakness early on Monday; (2) If stocks do fall in reality it will be too late to do anything, and in any case we certainly don't recommend selling as a reaction to events last week; (3) On EM equities: investors increasingly like EM as a way forward for the medium-to-long term; they know they must invest in China and India despite the inevitable speed-bumps; (4) …we agree - the EMs are developing into 'Emerging Developed', of course! (4) We have argued the return of normal volatility in markets (so far only in equities) is a good thing within limits; (5) If global growth ***is*** adversely affected by trade factors, central banks will not be able to remove monetary accommodation at the rate they wanted to… (6) …and relatively low rates for longer would be supportive of elongating the cycle, and quality bonds and risk assets would benefit; (7) Wall Street banks are now able and willing to take more risk in markets - we believe this will actually make markets more stable within ranges; (8) Bank of America, Goldman Sachs and Morgan Stanley have results this week; higher rates, lower tax, and a return to normal volatility in markets are all positive for investors in them; (9) …we now await a lending recovery assisted by lighter regulation and less onerous prudence ratios, with the multiplier effects that should result as full capitalism gets re-established; (10) Soon it will be time to decide whether to take some money tactically off the table for the 'Sell in May' season, and leading into thinner summer markets; (11) **Since global growth is slackening in the short-term, we expect the offset of more slowly rising rates, at least for the time being; this will be supportive of risk assets; we still believe in the 'long-cycle'.**

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