AMR Financial Market Review

Summer Report July 2018

AMR
FINANCIAL MANAGEMENT

Review – Equities & Bonds

In January, good economic data continued, and Fed minutes showed members' uncertainty as to the effects of the Trump tax cuts and stuck to the mantra of gradual rises and peaking at a lower level than in previous cycles. Q4 reports from UK retailers were mixed, with Tesco and Next ahead of expectations, but profit warnings from Debenhams and Mothercare. The oil price continued its rally up to $70. The ECB meeting minutes showed that stimulus is close to being wound down in the face of improving data, and the Euro reached 3yr highs vs other currencies. It was a poor month for UK outsourcers, with Carillion entering administration, and a profit warning from Capita. Toward the month end, Treasury yields began to rise more persistently to the highest levels since 2014 leading to a broad market sell-off. Market weakness continued through February, with mixed UK corporate results. Vodafone's Q4s were poorly received, while Unilever's were upbeat and Royal Mail impressed with an agreement on pensions reached with trade unions. Reckitt Benckiser fell sharply on disappointing earnings, while resources companies BP and Rio Tinto demonstrated good cash generation through focus on costs and better commodity prices. HSBC results were overshadowed by provisions for write-downs of loans to Carillion and Steinhoff. Macro developments dominated markets in the month, with strong US job creation and announcement of 2.9% year-on-year wage growth driving 10-year Treasury yields close to the key 3% level. Economic data remained upbeat elsewhere, so markets were volatile as investors focused on the prospect of rising rates. In March, market volatility continued as rate concerns preoccupied investors despite data showing moderating US wage growth. Trade concerns then came to the fore as Trump announced the prospect of swingeing tariffs on Chinese steel and aluminium exports. This was swiftly met with the introduction of tariffs on US imports by the Chinese leading to fears of a trade war that could affect up to $50bn of flows and triggered one of the poorest one day falls in US indices since 2014. In the UK, Micro Focus warned on profits, while Hammerson was the recipient of a £4.9bn bid from Klepierre. Facebook fell sharply after announcing a large-scale misuse of users' data by Cambridge Analytica in the US election. Toward the month end, the Fed increased rates by 0.25% as widely expected.

The oil price rose sharply in April following sanctions on Russia and Allied military action in Syria. This drove good performances in Oil stocks and equity indices were generally higher on good Q1 results and reduced trade war fears. Whitbread was stronger following an announcement that Costa Coffee was to be demerged, and Lloyds and Barclays performed well following good results. Glaxo fell following disappointing results, affected by stronger Sterling. It was a busy month for M&A, with Sainsbury to buy Asda for £7.3bn, T Mobile bid $59bn for Sprint and US oil group Marathon bid $36bn for peer Andeavor. Bonds were slightly weaker in this more 'risk-on' environment. The oil price rally continued through May as Trump withdrew from the Iran nuclear deal. Bond yields in Italy rose sharply and European equity indices fell following the general election and resultant uncertainty over key political appointments. In contrast, safe haven bonds rose. Asia and Emerging market indices fell on an escalation of trade war fears, while UK indices outperformed, driven by the Oil sector.

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Key Indicators

Equity Market Indices	*30/06/18*	*29/12/17*	*% change six months*	*30/06/17*	*% change one year*
UK – FTSE 100	7636.92	7687.77	– 0.7	7312.72	+ 4.4
UK – FT ALL Share	4202.25	4221.82	– 0.5	4002.18	+ 5.0
UK – FT Mid 250	20830.97	20726.26	+ 0.5	19340.15	+ 7.7
UK FT Small Cap	5876.82	5911.89	– 0.6	5584.96	+ 5.2
USA – Dow Jones	24271.41	24719.22	– 1.8	21349.63	+ 13.7
USA – S&P 500	2718.37	2673.61	+ 1.7	2423.41	+ 12.2
USA – Nasdaq	7040.80	6441.42	+ 9.3	5646.92	+ 24.7
Japan – Nikkei 225	22304.51	22764.94	– 2.0	20033.43	+ 11.3
Europe – FT Europe ex UK	203.19	209.99	– 3.2	201.28	+ 0.9
Asia – FT Asia Pacific ex Japan (£)	621.46	644.37	– 3.6	597.95	+ 3.9
Emerging – FT Emerging (£)	584.73	620.58	– 5.8	567.66	+ 3.0
Global – FT AW World (£)	374.61	371.89	+ 0.7	350.83	+ 6.8
Currencies					
£ / $	1.32	1.35	– 2.4	1.30	+ 1.7
£ / Euro	1.13	1.13	+ 0.0	1.14	– 1.1
£ / Yen	146.20	152.11	– 3.9	146.35	– 0.1

Sources: FE Analytics, returns shown in local currency unless otherwise stated, income withdrawn.

It is important to remember that the value of investments and the income from them can fall as well as rise. Past performance is not necessarily a guide to future performance. Investors may not get back the amount invested.

In M&A news, Shire agreed a $62bn bid from Japanese peer Takeda. Weakness in Asia and Emerging markets continued in June as trade war fears dominated, with Chinese shares entering a 'bear market'. Other global indices were also lower, although the leading US technology stocks touched all-time highs during the month. The US Federal Reserve announced a quarter point increase in interest rates, while the ECB guided that rates would be held until the middle of 2019 at least. The Bank of England also held rates, citing uncertain data in the first quarter. The Bank of China announced a reduction in bank reserve requirements, coinciding with the introduction of US tariffs, injecting up to $100bn into the Chinese economy. In contrast to Amazon's record profits, profit warnings were seen at John Lewis, Debenhams, House of Fraser and Dixons Carphone.

Outlook

After a prolonged period of benign market conditions for both equity and fixed interest, characterised by rising indices and low levels of volatility, we have entered a phase of greater uncertainty. With valuations of many markets considered high in relative historical terms at the year end, a period of consolidation was perhaps to be expected given the emerging political and economic environment. As we begin the second half, corporate results are expected to show strong growth, but the tone of companies' outlooks will be scrutinised for their views on future growth and how it may be affected by factors such as trade tariffs, input costs pressures and how they are reacting to an uncertain political environment.

The Trump administration has triggered an escalation of a trade dispute on a number of fronts, primarily affecting China and Europe, but also drawing in other countries such as Canada and Mexico. This has taken the form of tariffs on an ever-growing list of imported materials and finished goods which will raise costs for companies which use these goods as part of their production, as well as raising costs for consumers. This has the effect of reducing profitability for companies and reducing consumer purchasing power at a time where real wage growth has remained surprisingly anaemic given high levels of employment, with these factors potentially combining to reduce demand in economies globally.

As the initial limited round of tariffs only came into effect in early July, it will be some time before they manifest in corporate results and economic data, and the evolving nature of the trade dispute makes the eventual scope and magnitude and hence effects hard to predict. In the meantime, investors have reduced holdings in regions they see as likely to be affected by the trade dispute, hence Emerging markets and Asia Pacific indices have declined. However, this presents opportunities in as much as many companies which operate in these regions are not dependent on global trade, with Asia in particular a centre for technological innovation.

The political environment in Europe is also presenting a challenge for investors. We are now less than ten months away from the UK's exit from the EU and still with limited visibility of how the UK's trading relationship with our key trading partner will look. It is therefore unsurprising for UK based companies to be talking of how this uncertainty is impacting on investment decisions and this may in turn limit economic growth. Politically, there is a minority government in the UK, the German coalition remains unstable and the new Italian government has an anti-EU stance. This has added to relative underperformances of the Euro and European stocks, which again presents opportunities to acquire shares in European companies operating globally at more attractive valuations.

A number of positive themes remain in place; economic growth remains robust, monetary policy globally remains accommodative and although the US is further down the road of interest rate rises, rates are still expected to peak at much lower levels than historical norms. The effects of the Trump tax cuts have been positive and although much of the benefit has been felt by the US stock market in terms of buybacks and record levels of Mergers and Acquisitions activity, there is evidence that some of the additional post tax profit is being passed on through higher wages and increased investment.

Technological development continues, and whilst some 'old economy' sectors such as Retail are suffering disruption, these long-term dynamics are exciting and present opportunities for companies and investors. Regions such as Asia Pacific are strong beneficiaries of a shift away from low value-added export led growth to internal consumption. It is therefore important for investors to look through economic and political 'noise' with its resultant volatility and focus on the attractions of the underlying positive investment themes.

Key Indicators

Equity Market Indices (£ Total Return)	*% change six months*	*% change 2017*	*% change 2016*	*% change 2015*	*% change 2014*	*% change 2013*	*% change 2012*
UK – FTSE All Share	+ 1.69	+ 13.10	+ 16.75	+ 0.98	+ 1.18	+ 20.81	+ 12.30
UK – FTSE 100	+ 1.68	+ 11.95	+ 19.07	– 1.32	+ 0.74	+ 18.66	+ 9.97
UK – FT Mid 250	+ 1.90	+ 17.78	+ 6.66	+ 11.17	+ 3.66	+ 32.27	+ 26.11
UK – FT Small Cap	+ 1.01	+ 18.15	+ 14.29	+ 9.17	+ 0.89	+ 32.77	+ 27.82
USA – Dow Jones IA	+ 1.38	+ 17.02	+ 38.96	+ 6.02	+ 16.89	+ 27.25	+ 5.40
US – S&P 500	+ 4.88	+ 10.62	+ 32.67	+ 6.58	+ 20.02	+ 29.10	+ 10.16
US – Nasdaq	+ 10.58	+ 19.22	+ 29.86	+ 13.16	+ 21.88	+ 37.52	+ 12.29
EU – FTSE Europe ex UK	– 1.07	+ 17.12	+ 16.32	+ 9.54	– 0.92	+ 26.00	+ 19.11
Japan – Nikkei 225	+ 2.10	+ 12.64	+ 24.62	+ 13.29	+ 0.10	+ 26.90	+ 4.59
Asia – FT AW Asia Pac ex Japan	– 1.58	+ 24.45	+ 26.88	– 3.52	+ 9.74	+ 1.51	+ 15.90
Emerging – FT AW Emerging	+ 4.48	+ 21.06	+ 35.43	– 10.31	+ 7.87	– 5.29	+ 12.76
Global – FT AW World	+ 2.14	+ 13.84	+ 29.56	+ 4.04	+ 11.30	+ 21.03	+ 12.00
Unit Trust Sectors (Retail, £ Total Return)							
Mixed Inv 0%-35% Shares	– 0.55	+ 4.51	+ 8.28	+ 0.20	+ 4.98	+ 4.17	+ 6.20
Mixed Inv 20%-60% Shares	– 0.40	+ 6.95	+ 9.90	+ 1.12	+ 4.82	+ 8.57	+ 8.12
Mixed Inv 40%-85% Shares	+ 0.43	+ 9.78	+ 13.11	+ 2.31	+ 4.76	+ 13.77	+ 9.60
Flexible Investment	+ 0.50	+ 10.61	+ 13.54	+ 2.04	+ 5.00	+ 14.43	+ 10.02
UK All Companies	+ 2.74	+ 13.74	+ 10.71	+ 4.86	+ 0.46	+ 25.96	+ 14.96
Uk Equity Income	+ 1.63	+ 11.05	+ 9.05	+ 5.18	+ 2.81	+ 25.18	+ 13.61
UK Smaller Companies	+ 5.34	+ 26.63	+ 7.70	+ 14.68	– 1.89	+ 37.17	+ 22.08
Asia Pacific ex Japan	– 1.58	+ 24.45	+ 26.88	– 3.52	+ 9.74	+ 1.51	+ 15.90
Europe Excluding UK	– 1.07	+ 17.12	+ 16.32	+ 9.54	– 0.92	+ 26.00	+ 19.11
Global Emerging Markets	– 5.50	+ 24.47	+ 31.71	– 10.47	+ 2.37	– 4.06	+ 12.64
Japan	– 0.35	+ 17.45	+ 23.88	+ 16.08	+ 0.66	+ 26.20	+ 3.37
North America	+ 5.13	+ 9.47	+ 31.15	+ 4.64	+ 17.63	+ 30.41	+ 6.32
Global Equity Income	– 0.47	+ 11.07	+ 22.51	+ 2.11	+ 6.97	+ 20.74	+ 10.55
Global	+ 2.19	+ 14.04	+ 22.27	+ 3.09	+ 6.99	+ 20.68	+ 10.24
Technology & Telecoms	+ 11.95	+ 23.83	+ 25.05	+ 8.15	+ 14.40	+ 28.32	+ 10.60
Property	+ 1.82	+ 5.67	+ 5.54	+ 5.25	+ 12.01	+ 5.94	+ 9.61
Targeted Absolute Return	– 0.71	+ 2.86	+ 0.02	+ 2.66	+ 3.01	+ 6.32	+ 3.09
Sterling Corporate Bond	– 1.53	+ 4.86	+ 8.55	– 0.41	+ 9.25	+ 0.48	+ 12.82
Sterling High Yield	– 1.42	+ 6.20	+ 9.81	– 0.45	+ 1.40	+ 6.49	+ 19.08
Sterling Strategic Bond	– 1.53	+ 4.63	+ 6.91	– 0.43	+ 5.76	+ 3.32	+ 13.67
Money Market	+ 0.12	+ 0.13	+ 0.25	+ 0.04	– 0.02	+ 0.08	+ 0.15
UK Gilts	+ 0.55	+ 1.48	+ 10.03	– 0.36	+ 12.62	– 4.96	+ 1.65
UK Index-Linked Gilts	– 1.18	+ 1.85	+ 21.64	– 1.32	+ 17.31	– 0.43	+ 0.09
Global Bonds	– 0.84	+ 1.55	+ 12.69	– 1.30	+ 4.08	– 2.86	+ 6.06
Global Emerging Market Bond	– 4.23	+ 3.76	+ 23.95	– 3.71	+ 4.59	– 9.58	+ 12.10

Sources: FE Analytics, returns in Sterling unless otherwise stated, net income reinvested.

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