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Portfolio Management

CAERUS Market Commentary – April 2017

Market overview

Global equity markets (ex-UK) were relatively sanguine in April, gaining between 1% and 3% in local currency, once sterling volatility was removed. As can be seen below, the strength of sterling post the election announcement has detracted from that performance for UK Investors, while the market has repriced large cap UK companies for the reverse currency translation that saw them perform so well, post-Brexit. Despite a variety of fundamental data points, both good and bad, reported last month, politics remains the attention grabber and is likely to continue to focus the attention for the foreseeable future.

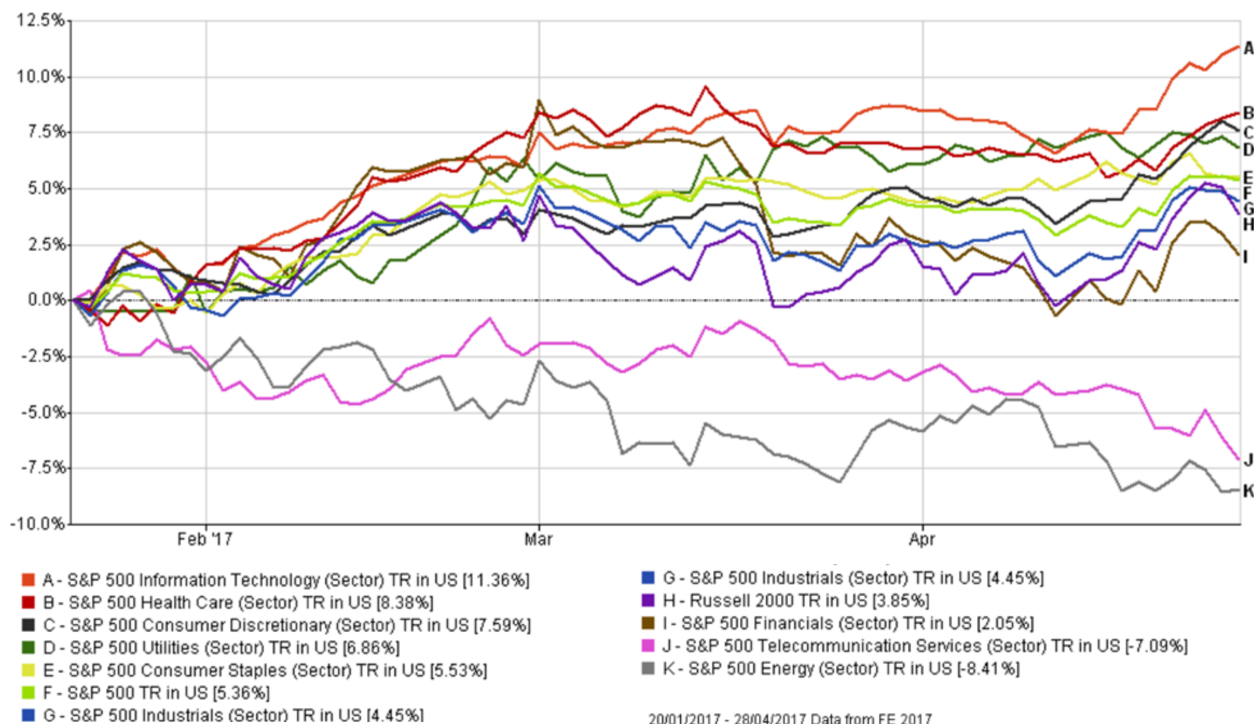
April Indices

Index	April Return (£ base)	April Return (Local ccy)
FTSE World Index	-1.78%	1.31%
FTSE USA TR GBP	-2.32%	1.06%
FTSE Europe ex-UK TR GBP	0.85%	2.84%
FTSE Japan TR GBP	-2.15%	1.28%
FTSE 100	1.33%	-1.33%
FTSE all share	0.37%	0.37%
FTSE EM	1.48%	1.72%

*Past performance is not an indication of future returns. The value of Investments and any income from them is not guaranteed and can go down as well as up.

United States

As we pass the self-imposed 100-day point for reflection on the success of Trump's change agenda it's fair to say the market is viewing his potential with far less blinkered 'animal spirits'. The middle of March was the reflection point for the stock market and April continued with this mild exhalation of confidence, the S&P and Russell 2000 similarly up a mere 1% in local currency (down 2.5% in GBP).



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What may be of greater interest is the sector returns which, for the most part, continue the theme observed since the inauguration, that faith in Trumps reflationary strategy seemed to be waning far sooner than his failure to appeal Obamacare. Since Trump took seat in the White House, the worst performing sectors of the S&P 500 in local currency terms have been Energy (-8.4%), Telecom's (7.1%), Financials (2.1%) and industrials (4.5%). These are predominantly the sectors that would most obviously benefit from 'Trumpflation'. Equally, the domestically orientated Russell 2000 is up comparatively less at 3.9%. On the flip side, we have seen the bond proxy Utilities up 6.9%, healthcare up 8.4% with IT driving returns, up 11.4%.

This is mirrored more acutely in the bond market where the spread between the 10yr and 2yr Treasury yield has completely reversed all the gains accumulated post the election. Specifically, this graph implies that the medium term growth and inflation expectations that the election result encouraged have been fully unwound, with the inauguration date a mere 6bp off the high for this spread at 1.28%, and the end of April matching the pre-election rate of 1.01%.

Looking at fundamentals, we saw a disappointing Q1 GDP estimate, implying a mere 0.7% growth, well short of the 1.3% consensus and 2.1% seen in Q4, 2016. This was exacerbated by some disappointing retail sales and CPI data. Having said that, while consumer confidence dipped slightly, the April release continues to show that confidence remains high and this coincides with positive employment data and an improving employment cost index. Taken together, it suggests there is still some momentum behind the consumer, but that we need to be aware of potential trap doors such as personal debt levels.

United Kingdom

Surprise as politics takes centre stage once again! A snap election from Theresa May caught us all unawares given her prior rhetoric, allowing the pollsters another chance to embarrass themselves. The opportunistic timing with her approval rating nicely up since her elevation to PM, leads markets to tilt towards the delivery of a strong mandate from the election result. This manifests itself to a stronger sterling under the premise that Theresa will have less need for a hard Brexit to appease hard line backbenchers. Markets have subsequently been driven by this currency reaction with the FTSE 100 down on currency translation and the FTSE 250 up on domestic prosperity improvements.

Politics largely overshadowed a less than positive April on the economic front. Q1 forecast GDP came in at a lower than expected 0.3%, as spending in retail and hospitality was hurt by rising inflation. UK consumer confidence in disposable incomes has fallen to its lowest level in three years as the imported inflation from a weak currency has acted to erase any real wage growth. While one-time hits to inflation from revaluations, like that seen to the pound last June, eventually roll out of the data, the danger of the impact on consumers' ability to spend at a point when debt is high and savings are falling, could be quite detrimental to the minimal growth currently existing in the economy.

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Europe

Despite a wobble prior to the first round of the French election, the FTSE Europe index maintained a positive return for the month while other developed markets struggled. Fundamentals have been strong with persistent business confidence, continued purchasing manager's strength (both manufacturing and services) and signs that inflation will finally make an appearance. On the 23rd, the electorate determined that the final leg of the presidency race would be fought between the far-right Marine le Pen and the more centralist Macron. At one point, there was a strong possibility that Melenchon might join Le Pen, leaving a choice between far-right and far-left but as sense prevailed equities rallied adding almost 4% to the index, turning a deficit on the month into a 3% gain. (In the event, Emmanuelle Macron took the laurels). If Europe can negotiate the coming months' elections without deteriorating the Union's status further, then the positive economic momentum should continue to benefit underlying companies.

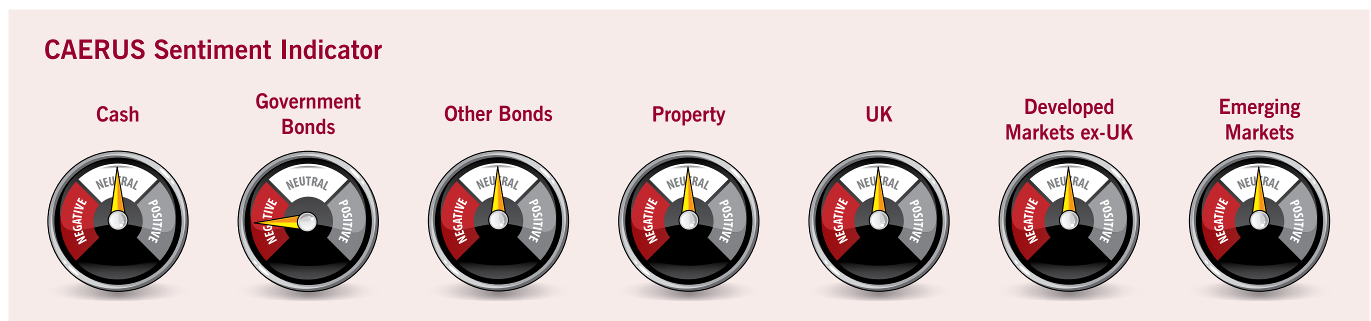
Japan

Japan's labour market reached its tightest in 26 years, last month. However, weakness in wages and consumer spending led to a continuation of stagnant prices. The ratio of open jobs to applicants rose to 1.45x, the highest since 1990 and within a fraction of the peak hit during Japan's bubble economy of the 1980s. The BOJ's target of 2% inflation appears far off, however, as consumer prices ex-fresh food were up a modest 0.2% year on year. The central bank will continue its massive stimulus programme, buying $720bn worth of government bonds annually while capping the 10yr yield at 0% under the hope of inspiring inflation. Equities reacted with a gentle slide upwards over the month in local currency, in line with many other developed indexes.

Emerging Markets

Emerging Markets added to gains they accumulated YTD, as a gentle rise in local currency equity performance permeated across most major equity markets. Last month, the FTCR Association of Southeast Asian Nations (ASEAN) Economic Sentiment Index showed a tick upward for Q1, indicating increasing optimism among ASEAN consumers about the economic outlook. Mexico also had some good news with an unexpected uptick in growth for Q1 coming in at 0.6%, confirming the market overreaction to the weakness expected. On the flip side, an independent survey of China's manufacturing sector indicated business activity grew at the slowest pace since last September as sluggish demand dragged on production.

** All performance data quoted in this article is derived from FE Analytics*



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