FINANCIAL PARTNERS

momentum

Weekly Digest

Week ending **20 September 2015**

The US Federal Reserve (Fed) had an unenviable task last week. Had they increased rates, it is likely that the market would have responded badly on the basis that fragile economies both in the developed and developing world weren't 'ready' for the US tightening its monetary policy no matter how modest a rate rise would have been. Yet the Fed's decision to do nothing was also greeted with negative price action globally, as market participants collectively asked 'what does the Fed know that we don't?' While their inaction seemingly delays the inevitable, on balance the Fed made a sensible, if conservative choice: if action and inaction were both to be greeted badly they may as well opt for inaction over an actus reus that would have been over-analysed for decades to come. As I noted last week, the Fed is desperate to avoid putting up interest rates only to have to cut soon after.

Over the weekend other central bankers added their weight to the Fed's dovish stance, with the European Central Bank's (ECB) Benoît Coeuré suggesting the Fed's decision to keep rates unchanged is "a confirmation of our diagnoses of the existence of risks in the global economy". This sentiment was echoed by his colleague, executive board member Peter Praet, who stated "we share the concerns about the outlook for the global economy". Praet went further by confirming that the ECB would contemplate cutting interest rates where shocks were of such import that they risked lower inflation. In a similar vein, the Bank of England (BoE)'s Chief Economist Andy Haldane warned that the risks to UK growth and inflation mean that the case for a UK rate rise is 'some way from being made'. Indeed, Haldane believes that the balance of risks are skewed 'squarely and significantly to the downside'. Haldane also suggested that the BoE may have to cut rates to combat low inflation: "were the downside risks…to materialise, there could be a need to loosen rather than tighten the monetary reins as a next step to support UK growth and return inflation to target". This view was not universally shared, however, with former Monetary Policy Committee member Andrew Sentance suggesting "Andy Haldane's spouting rubbish here…cutting interest rates from all-time low is unnecessary. Doing so when economy in 7th year of recovery is totally foolish."

Meanwhile, Monday morning's Financial Times reports that "Demand at gilt auctions have fallen to its lowest level since the financial crisis" noting that June's auction of 10-year securities received "bids equivalent to just 1.19 times the amount sold, a six-year low". Perhaps the take up of the auction was low because potential bidders had one eye on expected rate rises but it could also be a sign that buyers of gilts are finding it difficult to justify gilts at today's persistently low yields. If it is the former, it again demonstrates the importance of central banks to manage expectations as effectively as possible whilst there is an elevated level of economic uncertainty. If it is the latter, and gilt buyers are starting to fatigue, this suggests gilt yields should rise. The UK plans to raise GBP 127 billion in gilt sales this year which is a large volume for the market to digest without meaningful appetite. This is likely to also be the case in markets such as the US, which also are in a position of having a low benchmark government bond yield and a likely interest rate rise in the offing. This serves to remind us that safe haven government bonds remain unsustainably expensive at present levels and as a result, we remain lowly allocated to these securities, instead preferring to use parts of the credit market to achieve fixed income exposure.

Sources: Deutche Bank, BBC, Financial Times.

The **Marketplace**

- US Fed holds rates at 0-0.25%
- 1-month US Treasury yielding negative rate
- Equities falter on growth uncertainty
- China's equity market continues to be volatile
- Syriza win re-election in Greece

Market **Focus**

Global

- Global equities added a mere 0.2% as volatility returned to markets. Global emerging markets added 3.5%, however, as US monetary policy remained loose.

US

- US Treasuries added 0.3% while US Investment Grade corporate debt rose by 0.5%. Global government bonds added 0.7%.
- Last week saw the US Federal Reserve make its much anticipated decision on interest rates. The central bank decided to keep rates at their historic low levels of 0-0.25%, in part due to the volatility seen in China and other emerging markets.
- Market expectations of a September rate hike had dampened recently, but the accompanying statement released by the Fed struck an unexpectedly dovish tone, stocking suspicions that the global economic slowdown may be more pronounced than anticipated.
- The rate-sensitive 2-year US Treasury saw its yield fall by 0.13 points on the news; the yield on the 1-month US Treasury turned negative for the first time since June.
- The Vix index of implied volatility, or the 'Wall Street Fear Gauge', had been falling since it spiked in August, but the index rose by 9% after the announcement on Thursday.
- The Fed's own forward looking interest rate projection now hints at a first hike before year-end, although some market participants are looking further ahead and towards January 2016.

Europe

- In Greece, the leftist Syriza party, led by Alexis Tsipras, won re-election after securing a third bailout deal in August and betting that voters would return the party to government. Mr Tsipras has since purged many of the Syriza members that resisted the bailout, but uncertainties about implementation remain.

China

- China's equity market continued to see volatility last week with the Shanghai Composite ending the week having fallen by 3.1%. Global developed markets focused on the Fed's decision, however, rather than reacting to the swings in China.

Commodities

- Brent crude fell by 1.4% while the price of gold rose by 2.8%.

James Klempster, CFA & Scott Gordon

Source: Bloomberg. Returns in US dollars unless otherwise stated.

Asset Class/Region	Currency	Currency returns			
		Week ending 18 Sep. 2015	Month to date	YTD 2015	12 months
Developed Market Equities					
United States	USD	-0.1%	-1.5%	-3.9%	-1.2%
United Kingdom	GBP	-0.2%	-2.3%	-4.9%	-8.0%
Continental Europe	EUR	-0.5%	-2.7%	6.6%	5.1%
Japan	JPY	-1.2%	-5.6%	5.0%	13.0%
Asia Pacific (ex Japan)	USD	3.4%	1.8%	-9.6%	-13.8%
Australia	AUD	2.0%	-1.2%	-0.9%	-0.1%
Global	USD	0.2%	-1.6%	-3.2%	-4.7%
Emerging Market Equities					
Emerging Europe	USD	3.7%	0.3%	-5.3%	-28.1%
Emerging Asia	USD	3.5%	2.7%	-9.0%	-12.6%
Emerging Latin America	USD	2.5%	-3.3%	-24.9%	-40.0%
BRICs	USD	2.9%	-0.4%	-11.1%	-19.8%
MENA countries	USD	-1.8%	-0.9%	-7.9%	-25.5%
South Africa	USD	6.3%	-0.6%	-11.1%	-14.8%
India	USD	3.4%	0.5%	-6.5%	-8.1%
Global emerging markets	USD	3.5%	1.4%	-11.5%	-19.5%
Bonds					
US Treasuries	USD	0.3%	0.3%	1.4%	4.4%
US Treasuries (inflation protected)	USD	0.1%	-0.2%	-0.5%	0.1%
US Corporate (investment grade)	USD	0.5%	1.0%	0.1%	2.3%
US High Yield	USD	-0.5%	0.2%	0.2%	-1.9%
UK Gilts	GBP	-0.4%	0.6%	1.8%	9.7%
UK Corporate (investment grade)	GBP	-0.3%	0.4%	0.5%	5.8%
Euro Government Bonds	EUR	0.3%	0.7%	0.8%	4.5%
Euro Corporate (investment grade)	EUR	-0.2%	-0.1%	-1.1%	0.8%
Euro High Yield	EUR	-0.3%	-0.2%	1.5%	1.7%
Japanese Government	JPY	0.2%	0.5%	0.2%	3.2%
Australian Government	AUD	-0.2%	-0.2%	2.0%	8.3%
Global Government Bonds	USD	0.7%	1.2%	-1.0%	-2.2%
Global Bonds	USD	0.6%	1.1%	-1.5%	-2.7%
Global Convertible Bonds	USD	0.2%	0.5%	-0.1%	-2.8%
Emerging Market Bonds	USD	1.4%	1.3%	2.4%	1.3%

Source: Bloomberg

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Asset Class/Region	Currency	Currency returns			
		Week ending 18 Sep. 2015	Month to date	YTD 2015	12 months
Property					
US Property Securities	USD	3.0%	0.6%	-5.0%	6.7%
Australian Property Securities	AUD	0.7%	-1.7%	3.2%	12.2%
Asia Property Securities	USD	1.0%	-0.6%	-0.6%	-1.9%
Global Property Securities	USD	2.2%	0.3%	-3.8%	0.2%
Currencies					
Euro	USD	-0.4%	1.0%	-6.6%	-12.5%
UK Pound Sterling	USD	0.7%	0.9%	-0.3%	-5.3%
Japanese Yen	USD	0.5%	1.4%	-0.2%	-9.4%
Australian Dollar	USD	1.8%	0.6%	-11.7%	-19.7%
South African Rand	USD	1.8%	0.0%	-13.0%	-16.7%
Swiss Franc	USD	0.1%	-0.6%	2.7%	-3.6%
Chinese Yuan	USD	0.2%	0.4%	-2.5%	-3.4%
Commodities & Alternatives					
Commodities	USD	-1.3%	-2.0%	-16.9%	-31.7%
Agricultural Commodities	USD	-1.7%	-1.2%	-14.4%	-11.4%
Oil	USD	-1.4%	-5.2%	-17.2%	-51.4%
Gold	USD	2.8%	0.5%	-3.9%	-7.0%
Hedge funds	USD	0.2%	-0.1%	-1.1%	-3.6%

Source: Bloomberg

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