FINANCIAL PARTNERS

Weekly Digest

Week ending **24 April 2016**

The US is testing all-time highs: time to worry?

While positive headlines on the equity market were few and far between last year, they have made a welcome return in 2016. Nevertheless, as long term, valuation driven investors, the key question for us today is whether this positivity remains appropriate given how far the markets have come, the pressure on corporate profits and the apparent reliance on this uniquely accommodative period of monetary policy to prosper. There is a growing anxiety with respect to US corporate profitability which is not captured in the headlines and a feeling that, while the US is in reasonable shape, it may be a bit pricey today. With respect to the former assertion according to Thomson Reuters (as reported in the FT), analysts expect S&P 500 companies' earnings to fall 7% in Q1 2016 compared to the same time last year. Putting the valuation into context, the S&P currently trades at a Price-Earnings ratio (P/E) of over 19 times; this is not an exceptionally high level, but it is certainly not cheap; for example, according to Bloomberg the average quarterly trailing P/E valuation is 16.4 since March 1954. The relentless grind up of returns, combined with continued positive headlines and stretching valuations does give cause for some concern over the US market.

The US stock market is on a roll. It has rallied strongly out of the post financial crisis trough and remained resolute, compared to other developed markets, in the face of market turmoil that was experienced in the second half of 2015. Indeed, according to the FT dated the 25th April 2016, the S&P is poised for its second longest bull run in history. This could be achieved on Thursday as the current run would eclipse the 2607 days of the 1949-56 rally. Then this current bull market would be second only to the period between 1987 and 2000 which had a bull run of 4,494 calendar days. A bull market is defined as a period of stock price movements that does not see a fall of 20% from any fresh peak.

The run is a testament to a number of factors. Firstly, it confirms that if investors have the nerve to buy a market when it has fallen substantially and is significantly out of favour with investors, there is a good chance of achieving strong returns as the market rebounds. It also demonstrates that while there have been bumps on the way, sticking with an asset class while its prospects remain good can be a rewarding strategy. For example, while there have been sources of shocks such as the taper tantrum and last year's broad based sell off, companies listed in the US have been profitable and fairly- or under-valued as the market rose; investors who had been spooked by the early volatility would have missed out. Finally, it underlines the effectiveness of Quantitative Easing and other extraordinary monetary policy as a tool for central banks. Keeping interest rates low provided a fillip for corporate profitability because they were able to finance themselves cheaply in the debt market. Furthermore, the relative unattractiveness to investors of the price of debt in the market continues to provide a ready source of buyers in the equity market.

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

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The **Marketplace**

- US manufacturing index lowest for over 6 years
- Dollar hits weakest level since June 2015
- Japan reports the largest trade surplus since October 2010
- Oil proves resilient after failed Doha talks
- Iron ore at 15-month high

Market **Focus**

US

- The US manufacturing purchasing managers' index for April printed 50.8 on Friday, declining from 51.5 last month and failing to meet consensus forecasts of 52.0. This latest level is the lowest since September 2009, suggesting that this particular area of US economy is not performing as well as broader figures suggest.
- The US dollar fell on Tuesday the 19th April 2016 to its lowest level since June 2015, according to Bloomberg's trade weighted dollar index. This represented a fall of 6.7% from its January high, before rallying 1.1% to the end of the week.
- The NASDAQ 100 index – of predominantly tech stocks – had its worst week since the 6.0% fall in the first week in February, falling 1.5% over the week.

Japan

- Japan reported the largest trade surplus since October 2010 in March, after imports declined substantially more than exports. Imports fell 14.9% year-on-year, beating the expectation of a 16.6% fall, while exports declined 6.8%, marginally beating an expected 7.0% drop.

Commodities

- After falling 6.7% when the markets opened at the start of the week on news that no production freeze agreement was reached in Doha, Brent crude oil recovered into Monday's close (the 18th April 2016) to finish down just 0.4%. Oil proceeded to rise 4.7% over the week to a price of USD 45.11 per barrel on Friday. The recovery can be attributed to US Energy Information Administration reporting that inventory levels were lower than expected the previous week, as well as talk of another potential OPEC meeting next month with freezing production on the agenda.
- Iron ore rallied 17.6% over the week, reaching the highest level since January 2015. This is due to a rise in Chinese steel demand, alongside hints of lower output levels from major producers of iron ore, including BHP Billiton and Rio Tinto.

James Klempster & Jonathan Adamson

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Asset Class/Region	Currency	Currency returns			
		Week ending 22 Apr. 2016	Month to date	YTD 2016	12 months
Developed Market Equities					
United States	USD	0.5%	1.6%	2.8%	0.8%
United Kingdom	GBP	-0.3%	2.6%	2.8%	-7.1%
Continental Europe	EUR	1.8%	3.7%	-3.7%	-12.2%
Japan	JPY	3.4%	4.5%	-8.1%	-11.3%
Asia Pacific (ex Japan)	USD	0.3%	1.6%	3.5%	-15.3%
Australia	AUD	1.5%	3.0%	0.2%	-6.0%
Global	USD	1.0%	2.4%	2.1%	-3.7%
Emerging Market Equities					
Emerging Europe	USD	2.3%	3.1%	17.9%	-8.8%
Emerging Asia	USD	-0.4%	0.5%	2.5%	-18.6%
Emerging Latin America	USD	-0.7%	1.9%	21.4%	-14.4%
BRICs	USD	-0.4%	2.7%	4.1%	-23.2%
MENA countries	USD	1.0%	4.5%	1.6%	-18.7%
South Africa	USD	0.4%	2.2%	16.3%	-18.6%
India	USD	0.4%	1.2%	-1.0%	-10.5%
Global emerging markets	USD	-0.1%	1.1%	6.9%	-17.3%
Bonds					
US Treasuries	USD	-0.8%	-0.5%	2.9%	2.2%
US Treasuries (inflation protected)	USD	-0.4%	-0.7%	3.9%	0.0%
US Corporate (investment grade)	USD	-0.1%	0.8%	4.8%	1.7%
US High Yield	USD	1.1%	3.1%	6.6%	-1.8%
UK Gilts	GBP	-1.4%	-1.3%	3.8%	3.3%
UK Corporate (investment grade)	GBP	-0.6%	-0.1%	2.9%	1.2%
Euro Government Bonds	EUR	-0.7%	-0.9%	2.5%	0.1%
Euro Corporate (investment grade)	EUR	0.2%	0.5%	3.0%	1.0%
Euro High Yield	EUR	1.0%	2.2%	4.3%	2.0%
Japanese Government	JPY	0.3%	1.3%	6.0%	7.2%
Australian Government	AUD	-0.4%	-0.7%	1.8%	1.6%
Global Government Bonds	USD	-1.2%	-0.4%	6.3%	5.4%
Global Bonds	USD	-0.8%	-0.3%	5.4%	4.2%
Global Convertible Bonds	USD	-0.1%	0.7%	0.5%	-2.7%
Emerging Market Bonds	USD	0.1%	1.5%	7.6%	5.5%

Source: Bloomberg

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Asset Class/Region	Currency	Currency returns			
		Week ending 22 Apr. 2016	Month to date	YTD 2016	12 months
Property					
US Property Securities	USD	-1.9%	-2.4%	3.3%	2.7%
Australian Property Securities	AUD	-0.5%	0.3%	5.8%	6.7%
Asia Property Securities	USD	1.4%	4.2%	5.1%	-4.5%
Global Property Securities	USD	-0.8%	0.0%	4.9%	-1.0%
Currencies					
Euro	USD	-0.6%	-1.4%	3.4%	4.6%
UK Pound Sterling	USD	1.4%	0.3%	-2.3%	-4.2%
Japanese Yen	USD	-2.7%	0.7%	7.6%	7.8%
Australian Dollar	USD	-0.2%	0.7%	5.8%	-0.6%
South African Rand	USD	1.2%	2.6%	7.5%	-15.1%
Swiss Franc	USD	-1.1%	-1.7%	2.4%	-0.7%
Chinese Yuan	USD	-0.4%	-0.9%	-0.2%	-4.8%
Commodities & Alternatives					
Commodities	USD	4.2%	6.7%	5.8%	-18.9%
Agricultural Commodities	USD	3.9%	5.3%	5.0%	-1.4%
Oil	USD	4.7%	13.9%	21.0%	-28.1%
Gold	USD	-0.1%	0.0%	16.1%	3.8%
Hedge funds	USD	0.4%	0.6%	-1.5%	-7.5%

Source: Bloomberg

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