FINANCIAL PARTNERS

Weekly Digest

Week ending **08 May 2016**

Worries over Trump, Brexit and wobbly markets

The developed world has its fair share of political contention to deal with this year: the UK's in/out referendum on EU membership is fast approaching and the US election looks poised to provide an extraordinary contest between polar opposites Donald Trump and Hilary Clinton. On an individual level political change can be an important factor: a person who is neglected by one political regime may be pandered to by another; likewise one group may do well to be in the European Union whereas others are disadvantaged by it. As a result individuals rightly worry about the likely outcome of general elections and referenda. But the key question is whether these polls help or hurt the ability to generate the requisite returns for clients.

With respect to the UK, while we are seeing news flow intensify regarding the upcoming in/out referendum it is difficult to discern how much of the supposed costs and benefits of a particular outcome are based in hard fact and how many are founded on, shall we say, political expediency. This could continue to be the case right up to the end of the campaign, with the only difference being that the coverage of the information will likely become increasingly shrill. Today's instant gratification culture does not lend itself to pouring over nuanced and balanced comment and the worry is that the competing arguments of the in / out vote will end up looking more like a Punch and Judy sketch than a measured weighing of the collective pros and cons. A surprise result will cause volatility but surely, for longer term investors, this is quintessential market 'noise'? Important noise, no doubt, but for people able to hold or even add to risky assets as risk aversion rises, it could be a great opportunity. This is because the UK's main board is home to world class businesses. This is both in the sense of their management and operations but also, pertinently, in terms of their outlook. We all know that the majority of these firms' revenue is not generated in the UK, but rather the UK index is a suite of global companies that happen to be listed in the UK. To assume that all of them, on average, would be helped or hurt by a vote one way or another is, to my mind, difficult to justify. Sure, if there is change, there will be some winners and some losers, some firms may even relocate away, but surely whichever way public opinion falls will not materially impact, in aggregate, the ability of these one hundred or so global corporate behemoths to generate returns for shareholders? It may seem difficult to imagine today given the amount of time dedicated to the topic but, as an investor rather than an individual, we could look back twenty years from now and laugh about the non-event that was the Brexit referendum of 2016.

A similar case can be made for the US election. Even though the economy has stuttered from time to time, corporate America has prospered through a variety of political regimes with different combinations of power in the lower and upper house. Well-run corporations exist to thrive for their shareholders through thick and thin, and while different political environments provide their own unique challenges the majority of investors (who are optimists at heart) must surely believe that, in aggregate, US listed companies will find the means to thrive regardless of the political challenges they face. There will be winners and losers along the way, no doubt: some major firms have disappeared from view over the years while others have seemingly come from nowhere, but the headline returns for the market will smooth these impacts out. The good news with respect to the Presidential election, unlike the UK referendum, is that should the 'wrong' result prevail the nation will have the chance to put it right in four years, whereas the UK referendum could have ramifications that last for a generation or more.

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

The **Marketplace**

- US dollar falls to near 1-year low
- Risk-off sentiment leads to Treasury yields falling
- Various US employment measures disappoint unexpectedly
- UK PMI data dips to 3-year low in April
- Oil price stumbles at start of week

Market **Focus**

USA

- At the start of the week the US dollar trade weighted index hit its lowest level since May 2015, having declined 6.2% year-to-date. It recovered some ground subsequently, and the index ended the week having gained 1.5%.
- On Tuesday (3 May 2016), the 10-year US Treasury yield fell by 0.08 percentage points (this was the second daily decline of such a magnitude in two weeks) signifying the risk-off sentiment in markets, currently. The yield fell 0.05 percentage points over the week.
- The US payrolls number released on Friday came in at +160,000 jobs, significantly below the market's expectations of a 200,000 rise. This lead to the unemployment rate staying steady at 5.0%; had the expected number been accurate, a fall to 4.9% would have occurred. Also unexpected was a 0.2 percentage point fall in the labour force participation rate, to 62.8%.
- The US Institute for Supply Management (ISM) released mixed data last week, with their manufacturing index falling one point to 50.8 in April, while the equivalent services index rose 1.2 points to 55.7. Market expectations were for a smaller fall and gain, respectively.

UK

- The UK manufacturing purchasing managers' index for April reported at 49.2, falling 1.5 points from March; the expectation was for 51.2. The index has not been below 50 for three years.

Europe

- The EuroStoxx 600 banks index fell by 6.5% over the week. This came after poor earnings announced by UBS and Commerzbank in particular.

Commodities

- Oil had a poor week. Brent crude fell 7.6% to the end of Wednesday (4 May 2016) due to increased OPEC output expectations and rising stockpiles in the US. The price did however bounce 1.7% following the drop, over news that Canadian wildfires could cause a significant drop in production from the region.

James Klempster & Jonathan Adamson

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Asset Class/Region	Currency	Currency returns			
		Week ending 06 May 2016	Month to date	YTD 2016	12 months
Developed Market Equities					
United States	USD	-0.4%	-0.4%	1.2%	0.4%
United Kingdom	GBP	-1.8%	-1.8%	-0.2%	-8.8%
Continental Europe	EUR	-2.6%	-2.6%	-8.2%	-12.5%
Japan	JPY	-3.1%	-3.1%	-15.2%	-16.4%
Asia Pacific (ex Japan)	USD	-3.1%	-3.1%	-1.4%	-18.4%
Australia	AUD	0.8%	0.8%	1.3%	-2.6%
Global	USD	-1.6%	-1.6%	-0.4%	-5.4%
Emerging Market Equities					
Emerging Europe	USD	-5.7%	-5.7%	11.7%	-18.4%
Emerging Asia	USD	-3.0%	-3.0%	-2.4%	-20.8%
Emerging Latin America	USD	-5.7%	-5.7%	19.0%	-18.5%
BRICs	USD	-4.2%	-4.2%	-0.6%	-25.4%
MENA countries	USD	-2.1%	-2.1%	1.0%	-20.3%
South Africa	USD	-9.1%	-9.1%	7.8%	-24.6%
India	USD	-1.7%	-1.7%	-2.9%	-7.6%
Global Emerging Markets	USD	-4.1%	-4.1%	1.9%	-20.7%
Bonds					
US Treasuries	USD	0.3%	0.3%	3.6%	4.5%
US Treasuries (inflation protected)	USD	-0.4%	-0.4%	4.7%	2.5%
US Corporate (investment grade)	USD	0.0%	0.0%	5.4%	4.4%
US High Yield	USD	-0.9%	-0.9%	6.4%	-1.9%
UK Gilts	GBP	1.6%	1.6%	5.6%	7.3%
UK Corporate (investment grade)	GBP	1.2%	1.2%	4.4%	4.6%
Euro Government Bonds	EUR	0.6%	0.6%	2.9%	4.0%
Euro Corporate (investment grade)	EUR	0.4%	0.4%	3.1%	2.3%
Euro High Yield	EUR	-0.4%	-0.4%	3.6%	1.6%
Japanese Government	JPY	0.5%	0.5%	6.3%	8.1%
Australian Government	AUD	1.5%	1.5%	4.1%	6.4%
Global Government Bonds	USD	0.4%	0.4%	8.4%	7.6%
Global Bonds	USD	0.2%	0.2%	7.1%	5.5%
Global Convertible Bonds	USD	-0.9%	-0.9%	0.1%	-3.7%
Emerging Market Bonds	USD	-0.5%	-0.5%	7.4%	6.2%

Source: Bloomberg

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Asset Class/Region	Currency	Currency returns			
		Week ending 06 May 2016	Month to date	YTD 2016	12 months
Property					
US Property Securities	USD	4.7%	4.7%	8.1%	13.1%
Australian Property Securities	AUD	2.2%	2.2%	10.8%	12.6%
Asia Property Securities	USD	-3.9%	-3.9%	0.2%	-9.4%
Global Property Securities	USD	0.8%	0.8%	6.3%	2.5%
Currencies					
Euro	USD	-0.4%	-0.4%	5.1%	0.5%
UK Pound Sterling	USD	-1.1%	-1.1%	-2.1%	-5.4%
Japanese Yen	USD	-0.7%	-0.7%	12.3%	11.5%
Australian Dollar	USD	-3.2%	-3.2%	1.1%	-7.5%
South African Rand	USD	-4.3%	-4.3%	4.1%	-19.1%
Swiss Franc	USD	-1.3%	-1.3%	3.1%	-5.7%
Chinese Yuan	USD	-0.3%	-0.3%	-0.1%	-4.5%
Commodities & Alternatives					
Commodities	USD	-2.6%	-2.6%	5.6%	-22.4%
Agricultural Commodities	USD	-1.6%	-1.6%	3.2%	-3.5%
Oil	USD	-5.7%	-5.7%	21.7%	-33.1%
Gold	USD	-0.4%	-0.4%	21.3%	8.0%
Hedge funds	USD	-0.5%	-0.5%	-2.2%	-7.3%

Source: Bloomberg

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Important notes