Market Commentary for the Period 1st July 2016 – 30th September 2016

Global equity markets delivered strong returns over the quarterly period, recovering from the aftermath of the EU referendum result. The IMF downgraded global growth in both 2016 and 2017 citing that the UK's decision to leave the EU had 'thrown a spanner in the works'. Changes in the political landscape was a clear theme for the period. This included developments ahead of the US election in November, a new Prime Minister in the UK, the failure to form a majority government in Spain, an incumbent win in the election for the upper house in Japan and the official removal of President Temer in Brazil after being found guilty of fraud. Towards quarter end, OPEC members agreed to limit oil production marking the first agreed deal in 8 years. Fixed income markets posted attractive returns, particularly in sterling bonds following the changes announced by the Bank of England.

US equity markets delivered modest returns over the period despite growing uncertainty over the US election. Markets dropped early in September as presidential candidate Hillary Clinton was reported as being treated for pneumonia after fainting at a 9/11 ceremony in New York. This raised questions over why she didn't disclose her health conditions earlier and led to concerns over her ability to proceed with the campaign. Later, Donald Trump was victim to anonymously leaked tax returns which revealed how he used aggressive accounting tactics to avoid tax. The US Federal Reserve agreed not to raise interest rates at their most recent meeting. The central bank acknowledged that the case to raise rates had strengthened but yet still wanted to wait for further evidence of progress towards their objectives. US second quarter GDP rose to 1.4% q/q annualised driven by exports and the first gain in business investment in 3 quarters. Inflation rose to 1.1% y/y in August driven by rising shelter and medical costs. US unemployment remained at 4.9% in August, unchanged from the previous month.

UK equity markets performed strongly, rebounding from the dip experienced following the result of the EU referendum. After the resignation of David Cameron, Theresa May was appointed as the UK's second female Prime Minister, marking one of the shortest campaigns in British history. The Bank of England announced an array of measures designed to support growth and achieve a sustainable increase in inflation. The members agreed unanimously to cut the bank rate from 0.50% to 0.25% marking a record low in the central bank's 322-year history. The bank also announced an increase of asset purchases of government bonds as well including corporate bond purchases. At their most recent meeting, the bank added that the majority of members would be supporting a further rate cut in November, if the outlook then is consistent with projections. UK second quarter GDP rose to 0.7% q/q encouraged by household spending and fixed investment. Inflation remained at 0.6% y/y in August. Transport prices rose further and the cost of food fell at a slower pace, although lower prices for housing and clothing weighed on inflation. UK unemployment remained at 4.9% in July while the employment rate was the joint highest since comparable records began in 1971.

European equity markets posted decent returns, despite the central bank disappointing on its announcement on potential monetary stimulus. The European Central Bank left interest rates and its stimulus program unchanged at its recent meeting. President Mario Draghi commented on the resilience of the European economy amid global and political uncertainty, but reiterated that, on balance, risks were tilted to the downside. In the Spanish election, Prime Minister Rajoy failed to form a majority in a hung parliament. It is possible that a new election will have to be held on Christmas day, should the political leaders not succeed in forming a government. Eurozone second quarter GDP fell to 0.3% q/q as investment stalled and an inventories drag weighed on growth. Inflation remained at 0.2% y/y in August as price rises in restaurants & cafes and fruit & vegetables were offset by declines in transport fuels and heating oil & gas. Eurozone unemployment was unchanged at 10.1% in August, remaining the lowest rate since July 2011.

Asian equity markets experienced large gains following better than expected market data and accommodative stimulus across Australasia. Chinese second quarter GDP remained at 6.7% y/y. This marginally beat market expectations driven by a greater increase in industrial output, retail sales and new loans. Chinese trade data was also encouraging with imports and exports improving in August. Australia and New Zealand cut interest rates to 1.5% and 2% respectively. Both central banks commented on low inflation being a key reason to reduce rates, with New Zealand in particular citing that a decline in its exchange rate was needed.

Japanese equity markets were strong over the period as markets took positively to a win by Japan's incumbent leader. Japanese Prime Minister Shinzo Abe claimed a major victory in an election for the upper house of parliament. This re-affirmed confidence in Abe's plans for aggressive financial stimulus. Later in the period, the Bank of Japan increased its equity purchase program and doubled lending to local companies. The bank then approved a ¥13.5 trillion fiscal package which would be invested into projects such as infrastructure including a new magnetic levitation railway line from Tokyo to Osaka. In a later meeting the bank adjusted its quantitative easing program to allow for more control and also committed to carry out necessary policy to meet the inflation target. Japanese second quarter GDP fell to 0.2% q/q. Although lower than the previous quarter, this was announced higher than expected boosted by private consumption and public investment. Inflation fell to -0.5% y/y in August marking the sixth consecutive month of deflation driven by the falling cost of housing and transport as well as lower food price rises. Japanese unemployment rose to 3.1% in August, surpassing the previous month and expectations.

Emerging markets performed strongly over a period of mixed events. Early in the quarter, over 300 people were killed and thousands injured in Turkey as an army faction attempted to overthrow the government in a fight for democracy. The Brazilian senate voted to impeach President Dilma Rousseff following accusations of fraud. This saw her removed from the Workers Party and interim President Michel Temer staying in power until the end of 2018. The Russian and Saudi Arabian energy ministers agreed to work together to stabilise the oil market following a G20 summit in China. This marked a historical moment given their positions as the world's largest oil producers as well as being OPEC and non-OPEC members. Later, OPEC members agreed to limit oil production following an informal meeting at the International Energy Forum. This was the first agreed deal in 8 years and led to a sharp rise in the oil price. The Russian central bank cut interest rates to 10% signalling potential further cuts in 2017 in its assessment of inflation risks.

In fixed income markets, sterling corporate and high yield bonds outperformed demonstrating higher risk appetite over the period. Yields fell across sterling denominated bonds leading to higher prices following the decision by the Bank of England to cut interest rates and buy bonds through its quantitative easing program. Comments from the US Federal Reserve that the case to raise interest rates strengthened had a negative initial impact to bond prices. Yields on the UK, US and German 10 year bond ended the quarter at 0.65%, 1.60% and -0.12% respectively.