



UK Week in Markets

Week ending 20 May 2018

Market Moves

- Global equity markets edged slightly lower over the week with a notable divergence in regional equity returns. Strong US economic data releases and increasing crude oil prices renewed concerns over rising inflation and higher interest rates. Geopolitical tensions prevailed across the globe as, on the one hand, North Korea threatened to pull out of summit talks with the US whilst, on the other hand, Italy's anti-establishment political parties agreed to form a government. The MSCI AC World Index fell 0.2% in local currency terms and 0.1% in sterling terms. Japan was the best performing market in local currency terms (1.2%) as the weaker yen benefitted exporters' stocks. The UK was the best performing region in sterling terms (0.7%). Emerging markets were the worst performing region both in local currency (-1.1%) and sterling terms (-1.7%) as concerns over a capital flow reversal prompted an equity sell-off.
- UK gilt yields rose across all maturities over the week, in tandem with the government bond yields of other major developed markets. The 10 year UK gilt yield rose by 7bps to 1.52% and the 20 year UK gilt yield rose by 5bps to 1.92%. The 10 year US treasury yield touched a seven-year high as it rose by 9bps to 3.06% on the back of decent economic data. European government bond yields rose across the region amid Italian political uncertainty and mixed economic data. German bund yields rose by 3bps to 0.60% and French government bond yields rose by 5bps to 0.84% over the week. Italian government bond yields sharply rose by 31bps to 2.20% as the populist 5SM and far-right League party agreed to form a coalition government. Greek government bond yields rose sharply by 50bps to 4.50%.
- The UK 20 year real yield rose by 4bps to -1.49% and the Over 5 year real yield rose by 2bps to -1.46%. 20 year breakeven inflation was unchanged at 3.34%.
- The US high yield bond spread over US treasury yields rose by 1bp to 341bps over the week. The spread of USD denominated EM debt over US treasury yields rose by 6bps to 328bps. The sterling non-gilt spread over government yields (based on the Merrill Lynch index) was unchanged at 111bps.
- The S&P GSCI rose by 1.0% in USD terms over the week. The energy sector rose by 1.6% as the price of Brent crude oil increased by 1.8% to US\$79/BBL. Industrial metals fell by 0.2% as copper prices decreased by 1.2% to US\$6,784/MT. Agricultural prices rose by 1.8% whilst gold prices fell by 2.7% to US\$1,288/ounce.
- Sterling strengthened against major currencies (except the US dollar) over the week. The US dollar appreciated by 0.6% against sterling, ending the week at \$1.35/£. The euro weakened by 0.9% against sterling, finishing the week at €1.14/£. The Japanese yen depreciated by 1.2% against the US dollar, ending the week at ¥110.69/\$.

Economic Releases

- There was broadly positive economic news flow in the US over last week with a number of upward revisions to previous readings and a few indicators outperforming expectations. Industrial production marginally exceeded initial estimates and increased by 0.7% in April, bolstered by strong growth in the utilities and oil and gas sectors. Moreover, this followed the upward revision of March's reading to 0.7% from 0.5%. Retail sales, meanwhile, matched analyst forecasts and grew at a moderate pace of 0.3% over April as higher gasoline prices cut into consumer spending. While still positive, it marked a slowdown from the upwardly revised 0.8% increase recorded in March. The Philadelphia Federal Reserve Business Outlook index jumped from 23.3 in the previous month to 34.4 in May; the highest reading in over a year. This was driven predominantly by the New Orders sub-index, which rose sharply to a multi-decade high of 40.6 from 18.4.
- Labour market data dominated economic releases in the UK. As expected, the UK unemployment rate held steady at 4.2% in the three months to March. However, recent jobless claims data may signal that the unemployment rate could increase in the future. Jobless claims for April were unexpectedly high, measuring 31,200 from an upwardly revised 15,700 in March. The claimant count rate increased marginally over April, up 2.5% from 2.4% previously, also signaling a possible future increase in the unemployment rate. UK average weekly earnings excluding bonuses rose 2.9% year-on-year in the three months to March, an increase from the previous reading of 2.8% while earnings including bonuses slowed to 2.6% year-on-year down from 2.8% previously.
- In the Eurozone, industrial production data recovered over March, rebounding by 0.5% from a 0.9% decline previously, although it did miss forecasts of a 0.7% increase. However, Germany's GDP increased at a pace of just 0.3% compared to the 0.6% increase recorded in the previous quarter. Economic sentiment indicators were mixed for May with Germany's ZEW survey expectations index remaining at -8.2. The current conditions sub-index eased to 87.4 from 87.9 previously posted. The Eurozone's ZEW survey's expectations index inched higher over May, from 1.9 to 2.4. Economic data in Japan was broadly negative last week. The preliminary reading for GDP growth in Japan indicated the first economic contraction since 2015, as the economy slowed by an annualised 0.6% over the first quarter. The reading was worse than -0.1% forecasted. Over the quarter, private consumption remained flat while business spending fell by 0.1%, undershooting analyst estimates of 0.4% growth. Furthermore, inflationary pressures have seemingly stalled with consumer price inflation slowing to 0.6% in April.
- In China, industrial production for the year to April increased by 7.0%; above the 6.0% previously recorded and 6.4% forecasted. Retail sales decelerated from 10.1% previously to 9.4% while fixed asset investment increased by 7.0% for the year to April; down from 7.5% in the previous month.

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