Wealth Management
Weekly Market Update

Blog - LinkedIn - Twitter
Publications - Web
Contact Us

Published 21 June 2021

Market Update

Global equity markets fell last week in local terms, selling-off on hawkish comments from the Federal Open Markets Committee that suggested two interest rate hikes in 2023. Further hawkish comments from FOMC members, including the possibility of a tapering of asset purchases, were also seen as contributing to weak equity performance. What was surprising given the Fed comments was that 10Y US Treasury yields fell due to central bank purchases and technical factors. However 10Y Gilt and Bund yields did fall 4bps and 7bp respectively, with UK 10Y yields at 0.752%. Sterling fell -2.1% vs the US Dollar and -1.7% vs the Yen, so that in Sterling terms these equity markets were up +0.2% and +1.2% respectively. However UK and European equities were down -1.6% and -0.7%. Cyclical stocks were the worst hit, with materials and energy selling-off the most globally, while bond proxies such as IT and healthcare held up relatively well. Gold also fell -6.0% in USD terms.

UK Stocks	US Stocks	EU Stocks	Global Stocks	EM Stocks	Japan Stocks	Gilts	GBP/USD
▼ -1.6%	▲ +0.2%	▼ -0.7%	▲ +0.1%	▲ +0.6%	▲ +1.2%	▲ +0.2%	▼ -2.1%

all returns in GBP to Friday close

Macro News

- UK inflation jumped in May, accelerating to 2.1%, on higher prices for clothing, fuels, and meals in restaurants and bars. The increase was above economists' forecasts and the BoE's target. Governor Andrew Bailey said last month that he would not hesitate to tighten monetary policy if the inflation rate consistently exceeded the BoE's target. UK payrolls rose for a sixth consecutive month, driven by hiring in the hospitality industry, while the unemployment rate averaged 4.7% in the three months ended April 30.
- Japan's exports rose 49.6% year-on-year in May, the highest growth since 1980. The jump in exports largely reflected a rebound in shipments from last year's plunge in the wake of the pandemic shock. The highest export growth was to the US, driven by cars and auto parts, while exports to China were also strong, led by chip production equipment and hybrid cars.

The Week Ahead

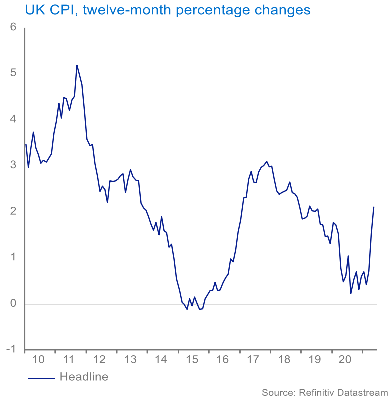
- The Bank of England's Monetary Policy Committee will meet this Thursday. Although the meeting is unlikely to result in any major change in monetary policy, it will be watched closely for any hawkish shift in tone after the US Fed signalled plans to bring forward interest rate hikes amid rising inflation.

Week in Charts

Japan's exports highest since 1980
Japanese trade

Japan's exports rose at the fastest pace since 1980 in May, helping the world's third largest economy offset sluggish domestic demand as Covid-19 vaccinations boost business activity in key markets.

UK inflation surges
UK CPI, twelve-month percentage changes



The UK inflation rate jumped to 2.1% in the year to May, the highest for almost two years, as the easing of lockdown sparked a rise in consumer spending. The rate is now above the Bank of England's 2% target for inflation.

View From the Desk

Last week featured a rarity: a hawkish Fed. The Federal Open Markets Committee (FOMC), the Fed's rate setting body, suggested two interest rate hikes in 2023, up from none at the last projection in March. Chair Powell also indicated that the committee had initiated discussions about tapering asset purchases, although he said that they are ways away from that point.

To no one's surprise, investors' Pavlovian instincts kicked in and they quickly wrapped up the 'reflation trade'. Gold dropped -5%, the Dollar rebounded, value lost ground to growth and US equities saw their worst day in more than a month. 5-year inflation expectations in the US dropped to 2.3%, down from a 2.7% high a few weeks ago, and bonds rallied.

We believe that this may have been the overreaction of a market that has been moving sluggishly for the past two months.

First, in many instances in the past, the Federal Reserve had indicated potential rate hikes without following through. Between now and the next 730 days many things can happen. Conditions are volatile enough, the economy has a lot of slack and there's little visibility of what the post-Covid world will look like. Additionally, the market is holding its breath in anticipation of Mr. Biden's stimulus plan.

It is possible that the Fed wants to communicate rate hikes. It is equally possible that it wants to have all the bases covered in case it finds itself behind the curve in the event of record fiscal stimulus by the new President.

Second, less than one percent rates in two years' time is hardly considered tightening. Markets often confuse tightening cycles with rate adjustments. We would expect the Fed to communicate a 'cycle' well in advance.

The reaction really serves to highlight how important monetary accommodation still is for risk assets. This can, however, change. Instead of exhaustingly dissecting every word the Fed says, investors might be best served to also think about the implications of a rise in long-term inflation and growth as governments are becoming more active in stimulating growth.

David Baker, CIO

mazars