Wealth Management
Weekly Market Update

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Market Update

Following a tumultuous start to the week, global equities rallied to finish in positive territory. The decision by OPEC+ to increase production contributed to markets selling-off on the Monday, with energy the worst performing sector for the week, while most other sectors recovered to finish up or almost flat. In particular telecoms, IT and consumer discretionary did well, benefitting from another week of falling yields. US equities saw the largest gains, up +2.1% in Sterling terms. European and UK equities gained +1.5% and +0.3%, with UK equities lagging due to their large weighting to energy stocks. Emerging market and Japanese equities were down -2.0% and -1.1% respectively. Currency movements were limited, with Sterling up marginally against the Euro and the Yen, but down marginally against the US Dollar. Oil finished the week up +0.6% and gold down -0.5% in US Dollar terms.

UK Stocks	US Stocks	EU Stocks	Global Stocks	EM Stocks	Japan Stocks	Gilts	GBP/USD
▲ +1.5%	▲ +2.1%	▲ +1.5%	▲ +1.7%	▼ -2.0%	▼ -1.1%	▲ +1.1%	▼ -0.1%

all returns in GBP to Friday close

Macro News

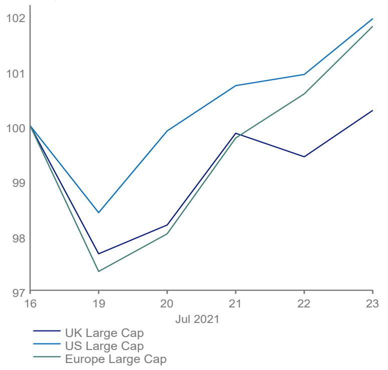
- Concerns around the Delta variant and slowing growth came to a head for equity markets last Monday. The main concerns are whether the Delta variant could lead to more restrictive measures and whether economic growth will be sustainable without ultra-loose monetary policy. This contributed to the c.2% fall we saw in developed equity markets on Monday, which was however short-lived as by the end of the week European markets rebounded to previous levels and US equities even went on to make new highs.
- Bond prices have continued to defy both gravity and analysts' expectations, as US treasury yields (which move inversely to bond prices) have moved lower. The low was reached on Monday when concerns about Covid-19 and the prospects for economic growth reached a peak, and the yield on the 10-year US treasury fell to 1.18%. The move lower in US Government bonds has been attributed to technical factors including pension fund purchasing, but market watchers are wary of dismissing such a move as the bond market often portends the direction of the economy and wider capital markets and this move recommends a cautious stance.

The Week Ahead

- We will see US Federal Reserve Chair Jay Powell give a press conference on 28 July and investors will be watching for any signs of plans to taper QE operations.
- Q2 GDP data will be released for the US and the Eurozone which will confirm whether those economies rebounded as analysts have expected.

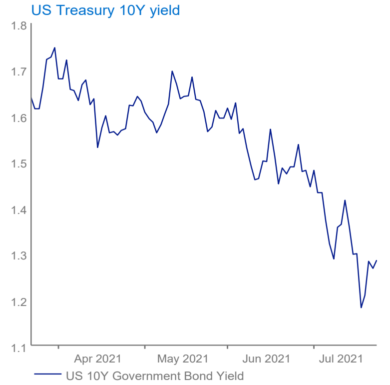
Week in Charts

Volatile, but not for long
Large cap equities, one week performance



The volatility in equity markets was very brief and this brevity is widely attributed to investor realisation that central banks can step in to support asset prices at any point.

Bond yields are not sticking to the script
US Treasury 10Y yield



The continued fall in US Treasury yields has bucked the consensus view that bond yields ought to continue to rise as economic growth rebounds and the case for tapering QE and raising interest rates grows. The question is, which is right, the US equity market making new highs or the bond market foretelling gloom?

View From the Desk

Last week featured a quick market correction on Monday which looked inconsequential by Friday when the market completely bounced back. The result was even higher equity prices (further supported by another very good earnings season with 88% positive surprises) and even higher bond prices. The rebound was relatively narrow, however, with tech stocks leading the charge a week ahead of their own results announcements.

There are three points after last week for investors:

1) Despite the bounce, the Delta variant is still advancing and weakening supply chains in developing economies, pushing inflation up and potentially undermining the growth rebound. Equity prices may not presently reflect that.

2) It is very rare for stocks to correct during a robust earnings season. It is not uncommon that they do so once positive catalysts are less potent.

3) Investors need to keep an eye at the balance between inflation and central bank accommodation. Any comment, no matter how insignificant, towards hawkishness could significantly unnerve markets in the next few months.

The issue for portfolio managers is less about equities, which are primarily supported by an abundance of cheap money looking into a limited opportunity set and more about bonds. If inflation creeps in, central banks may have to slash accommodation.

There are three reasons to hold bonds at such low yields: diversification and risk management (which still works), a mandate (plenty of pension funds have a mandated allocation to fixed income) and the certainty that no matter how expensive the asset is, someone will be willing to take it off your hands at a higher price. That last part, primarily affecting 'fast' trading money which has been contributing to falling yields for some time, is important. If central banks taper asset purchases and find themselves behind the inflation curve, the hit on a bond market conditioned for a decade to rely on government support could be material. If inflation persists, asset allocators have to make sure their sources of income are diversified and that their choices prepare them for a re-rating of the world's largest investment asset class.

David Baker, CIO

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