Market Insights: Monthly Market Newsletter
Global equity markets bounced back

March 2014 (covering February 2014)

Global overview

Encouraging news over China's growth prospects and waning emerging market tensions aided by currency stabilization led to an improvement in global equity market sentiment for much of the month. Nonetheless, emerging equity markets lagged developed equity markets, further impacted by the political instability in Ukraine in the final days of February. Developed equity markets were the beneficiaries of this unease as the economic recovery in the US, UK and Europe continued to gain ground. In the US, equity markets reversed the losses that had been incurred during what was their worst January since 2010. The strength of the US economy continued to be reflected in Q4 2013 company earnings announcements, the majority of which exceeded market expectations. Early in the month, the House of Representatives voted to raise the US 'debt ceiling' until March 2015.

In the UK, the Bank of England (BoE) raised its 2014 forecast for UK gross domestic product (GDP) to 3.4% from 2.8%. This was its fourth consecutive upgrade to growth and the biggest run of upgrades to UK growth expectations since the BoE was made independent in 1997[1]. At a press conference, the Governor of the Bank of England, Mark Carney, said that any adjustments to interest rates would be gradual and limited. One of the reasons cited for this relaxed attitude was new guidance regarding the amount of spare capacity in the labor market.

The European Central Bank (ECB) left interest rates on hold in February, with President of the European Central Bank, Mario Draghi, stressing that ECB is ready and willing to act if needed. Meanwhile, the small rise in the European Commission's economic sentiment indicator (ESI) in February provided an indication that the economic recovery has built up a little momentum since the start of the year. The increase in the headline index, from 101.0 to 101.2, was a touch better than expected and was the 10th consecutive monthly gain.

Elsewhere, Asian equity markets bounced back in February, although some mixed macroeconomic data saw continued divergence between equity markets with strong gains for Indonesia and the Philippines, while Taiwan and China ended the period with only small positive returns. In Japan, the TOPIX index ended the period lower in local currency terms as some mixed macroeconomic data more than offset the positive impact of a corporate earnings season where results were largely ahead of, or in line with, market expectations.

In the global bond market, prices and yields were relatively stable in February. Broadly positive economic data in the major developed markets pointed to rising growth and modest inflationary pressures. While investment grade credit spreads were little changed, corporate bonds outperformed core sovereign bonds due their higher yields. Spreads on high yield bonds and peripheral Eurozone sovereign bonds continued to tighten.

- S&P 500 index closed the month at a new all-time high
- Consumer spending and consumer sentiment improved
- The 'debt-ceiling' was raised until March 2015

US

During February, US equity markets reversed the losses that had been incurred during what was their worst January since 2010. Weakness in the emerging equity markets, the Ukraine crisis and the continuing adverse weather conditions were seemingly brushed off, as the S&P 500 index breached 2013 December's all-time high to close February at a new all-time high of 1,859. Having done so, the S&P 500 index returned 4.3% for the month (in US$, price return terms). In sector terms, all but the telecoms sector ended the period in positive territory, with materials and healthcare sectors amongst the strongest. Indeed, the latter has led the way both for the year thus far, and over the last 12 months.

In economic news, the Commerce Department announced that consumer spending, which accounts for circa 70% of the US economy, rose by more than expected in January. This was also reflected in improving consumer sentiment. The University of Michigan's survey of consumer confidence sentiment rose from 81.2 to 81.6 in February. In addition, some of the major US retailers indicated that they foresee improving business conditions, after the adverse weather experienced in January.

[1] Source: Financial Times 12 February 2014

Manufacturing data was also positive as the Institute for Supply Management's purchasing managers index (PMI) rose to 53.2 in February, from 51.3 in January. The housing market continued to show signs of improvement. While data showed that existing home sales fell 5.6% in January compared to December 2013, there was a sharp rise in new home sales, which rose 9.6% to their highest level since July 2008.

In the employment market, it was announced that 113,000 jobs were created in January, which was fewer than the 150,000 expected. However, this helped the unemployment rate decrease to 6.6%. New US Federal Reserve (Fed) Chairman Janet Yellen stressed that there would be a continuity of current monetary policy, with forward guidance remains unchanged. The Fed has stated that it will likely "maintain the current target range for the federal funds rate well past the time that the unemployment rate declines below 6.5%".

Elsewhere, ahead of the 27 February deadline, the House of Representatives voted to raise the US 'debt-ceiling' until March 2015. This allows the US Treasury Department to borrow to meet its obligations. Legislation was passed without conditions, and was in contrast to the last-minute political brinkmanship that has characterized debt-ceiling discussions in recent years.

- European equity markets moved higher in February
- European sentiment indicator registered 10th consecutive monthly gain
- German business climate IFO index rose to 30-month high

Europe

European equity markets moved higher in February as macroeconomic data continued to show an improving trend while the Q4 2013 earnings season remained mixed. Towards the end of the month, focus intensified in the Crimean Peninsula, as the anti-government protests in Ukraine led to the president leaving the capital. The European Central Bank left interest rates on hold in February, with Mario Draghi stressed that the ECB is ready and willing to act if needed. European equity markets were positive across countries with France performing the best. On a sector basis in Europe, it was healthcare, utilities and energy sectors leading the way while telecoms proved to be the laggards.

In macroeconomic news, the small rise in the European Commission's ESI in February provided an indication that the economic recovery has built up a little momentum at the start of the year. The increase in the headline index, from 101.0 to 101.2, was a touch better than expected and was the 10th consecutive monthly gain.

The Spanish Ministry of Employment reported a reduction of 1,949 unemployed people in February, which compares very positively to the 57,000 people average increase seen in February over 2004-2012 and the 22,000 increase expected, for the month, by the market. Spanish final Q4 GDP revealed that the economy expanded by just 0.2%, a touch weaker than the initial estimate of 0.3%. However, the breakdown showed that both household spending and investment rose for a second quarter running. Elsewhere, German GDP rose by 0.4% in Q4 2013, while Swiss GDP was up 0.2%.

The German business climate IFO index rose to a 30-month high in February, the index was up moderately at 111.3 (110.6 the previous month) and better than expected. While the assessment of the current situation rose markedly (114.4 vs. 112.4 in the previous month), expectations fell slightly (108.3 vs. 108.9 in the previous month), though they remained higher than in the previous 33 months preceding January. Both components were better than the consensus expected.

In Italy, a new Prime Minister, Matteo Renzi (of the center-left Democratic party), was sworn in 10 months after his party colleague, Enrico Letta, formed a coalition after an election stalemate. During his first Senate meeting since Letta's resignation, Renzi pledged to implement a double-digit cut to 'the tax wedge' and stated Italy needed to put its public debt in order; and revealed his intention to reform the country's justice system. One of the additions to his new cabinet, Pier Carlo Padoan – a former OECD (Organization for Economic Co-operation and Development) Chief Economist, has the task of implementing these structural changes and reducing payroll taxes in order to revive Italy's competitiveness.

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- UK equity markets moved higher in February
- Forecast for 2014 UK GDP growth raised to 3.4%
- BoE referred to significant spare labor-market capacity

UK

The FTSE All-Share index returned at 5.2% signaled a good recovery for the UK equity market as concerns regarding the possible impact of emerging market turbulence the previous month subsided. Parallels could be drawn between the performance of the UK equity market, the strength of sterling and the direction of UK economic growth.

The Bank of England (BoE) raised its 2014 forecast for UK GDP to 3.4% from 2.8%. This was its fourth consecutive upgrade to growth and was the biggest run of upgrades to UK growth expectations since the BoE was made independent in 1997[1]. At a press conference, when discussing such forecasts, the Governor of the Bank of England, Mark Carney, said that any adjustments to interest rates would be gradual and limited. One of the reasons cited for this relaxed attitude to interest rates was new guidance regarding the amount of spare capacity in the labor market. One way the BoE is measuring this is the rising number of those in part-time work that would prefer to work full time.

Within the UK equity market, tobacco and oil equipment services were among the strongest performers at the sector level, while aerospace and defense were the biggest laggards. The banking sector also had a difficult month with a few major banks reported significant losses.

- Asian equity markets bounced back
- Mixed economic data from China
- Japanese equity markets continued to lag the broader market

Asia Pacific

Asian equity markets bounced back in February, although some mixed macroeconomic data saw continued divergence between equity markets with strong gains for Indonesia and the Philippines, while Taiwan and China ended the period with only small positive returns.

In China, official survey data released at the start of the month indicated that the pace of manufacturing expansion would slow, with the HSBC/Markit manufacturing PMI pointing towards further contraction. However, trade data for January appeared to contradict the view that China's economy is slowing with exports increasing 10.6% year-on-year (y-o-y) from 4.3% the month prior, while imports grew 10.0% y-o-y from 8.3%, leaving China with a trade surplus of US$31.86bn. There was also a sharp fall in the renminbi towards the end of the month, following what many market participants viewed as intervention by the Peoples Bank of China (PBOC) to increase two-way volatility in the currency and discourage speculative flows.

The region's best performing equity market was Indonesia, where improving trade and foreign exchange reserves data provided a positive catalyst for its equity market and its currency to rally. The Philippines' equity market also made strong gains driven by better-than-expected Q4 2013 corporate earnings in the property and consumer sectors, with further support from robust economic data. The Australian equity markets also bounced back strongly despite mixed corporate earnings, while the Australian dollar appreciated over the month as the Reserve Bank of Australia left interest rates unchanged and removed the quantitative easing bias from its commentary. Taiwan had the worst performing equity market in the region impacted by mixed global economic data and the Ministry of Finance's tax reform proposals.

In Japan, the TOPIX index ended the period lower in local currency terms as some mixed macroeconomic data more than offset the positive impact of a corporate earnings season where results were largely ahead of, or in line with, market expectations. Data showed that Japan's trade deficit had risen with increased consumption ahead of the sales tax increase, the weaker yen and higher demand for imported energy all contributing to the increase. The rise in imports also had a negative impact on GDP with weaker-than-expected preliminary estimates for Q4 2013, although the domestic components of GDP (private consumption, housing and public consumption) were all higher. Elsewhere, industrial production grew 4.0% month-on-month in January.

[1] Source: Financial Times 12 February 2014

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The Bank of Japan surprised the market by maintaining its expansionary monetary policy, signaling its resolve to support Prime Minister Abe's reflationary stance. They announced an extension of special loan facilities by one year and doubled the size of funds available to banks.

- Emerging equity markets rebounded in February
- The gains were led by emerging European countries, except Russia
- Unfolding events in Ukraine pushed oil prices higher

Emerging markets

Emerging equity markets rebounded with improving sentiment aided by currency stabilization and encouraging Chinese trade data that eased concerns of a slowdown in the world's second-largest economy. From a regional perspective, Europe, Middle East & Africa (EMEA) led the gains, followed by emerging Asia and Latin America. Instability in Ukraine and events in Crimea dominated the news flow towards the end of the month. Concerns over energy supplies prompted a rise in Brent crude oil and natural gas futures.

The Greek equity market was the standout performer in EMEA, drawing support from a strong equity rally in European peripheral markets. Polish and Czech equity markets also registered healthy gains although Russian equity market came under selling pressure as unfolding events in Ukraine hurt confidence. The South African equity market had a good month as mining companies and other exporters benefited from the rand's fall to a five-year low. The Turkish equity market finished higher as the lira appreciated by over 2%. In terms of sector winners within the EMEA region, consumer discretionary and utilities led the gains.

Sector performance in the Latin American equity market was more varied with the financial sector coming out on top. Telecom services and energy were the only two sectors to fall into negative territory. At a country level, Chile, Colombia and Brazil equity markets all registered gains while Mexico equity market was the exception. Economic data from Brazil was mixed. Although 30,000 new jobs were created in January, the unemployment rate increased to 4.8% from 4.3% in December 2013. The country's current account deficit widened to US$11.6bn last month but was still better than consensus estimates. The Brazilian central bank increased the Selic interest rate to 10.75% from 10.5%, in line with expectations. By contrast, Chile's central bank cut interest rates by 25 basis points (bps) to 4.25%, as widely expected.

The rally in emerging Asian equity markets were broad based, with strong gains being registered in Indonesia and the Philippines' equity market. Chinese stocks also bounced back from weakness in January, drawing comfort from upbeat macroeconomic data. February's non-manufacturing PMI came in at 55.0 versus 53.4 from the previous month. In an unexpected move, China's central bank drained the equivalent of US$7.9bn from money markets to signal its concern about the boom in lending at the start of the year.

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- Global bond market yields relatively stable
- Improved economic data in the Eurozone and the UK
- High yield and peripheral sovereign bonds boosted by spread tightening

Fixed Interest

Global bond market prices and yields were relatively stable in February. Economic data in the major developed markets continued to be broadly positive, pointing to rising growth and modest inflationary pressures. While investment grade credit spreads were little changed, corporate bonds outperformed core sovereign bonds due to their higher yields. Spreads on high yield bonds and peripheral Eurozone sovereign bonds continued to tighten.

US treasuries displayed slightly higher volatility than other core government bonds. Longer-dated treasury yields rose early in the month as the unemployment rate fell to 6.6% (just above the 6.5% level at which the Fed would consider a higher interest rate, according to its forward guidance) and investors awaited the outcome of Janet Yellen's first Fed meeting and testimony to Congress as the Chairperson. The Fed, as expected, announced another cut of US$10bn per month in its asset purchase program but gave no other indication of a more hawkish outlook and Yellen's testimony was judged marginally more dovish than expected. Yields fell back. In the final days of February they fell further in reaction to the political instability in Ukraine.

In Europe, economic data showed some positive momentum. While consumption remains weak, business sentiment is pointing to a strengthening in GDP growth from the very modest levels we have seen in recent quarters. January's PMI data was the strongest seen since 2011. The Ifo survey of German business confidence and the Eurozone economic sentiment indicator, later in the month, added to the evidence of improvement. Revised UK Q4 2013 GDP data showed more growth than previously estimated coming from investment and less from consumption, a balance commentators saw as more sustainable.

The net result of US treasury market moves intra-month was a rise of just 0.4bps in the 10-year yield for February as a whole. According to data from Merrill Lynch, US treasuries had a total return for the month of 0.3%. Returns were similarly low for Gilts (0.2%) and Bunds (0.1%) in local currency terms. Sterling investment grade corporate bonds returned 0.5%, their aggregate spread over Gilts 2bps tighter at 140bps. European high yield bonds returned 1.6%, the aggregate yield of the market falling 26bps to 4.66%. Peripheral Eurozone sovereign bonds all saw spread tightening over bunds, with Italian bonds returning 1.7%, aided by the formation of the new Renzi political administration. The strengthening UK economic recovery is putting some upward pressure on the pound. In February, sterling rose by 1.9% against the dollar.

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Global equity and commodity index performance – figures to 28 February 2014

	1 Month	3 Months	6 Months	YTD	2013
Global US & Canada					
MSCI World (US$)	5.1%	3.4%	14.9%	1.2%	24.7%
MSCI World Small Cap (US$)	5.3%	5.8%	18.8%	3.4%	32.9%
MSCI Emerging Markets (US$)	3.3%	-4.7%	4.9%	-3.4%	-2.3%
FTSE World (US$)	4.9%	2.7%	14.0%	0.8%	24.7%
Dow Jones Industrials	4.3%	2.1%	11.5%	-1.1%	29.7%
S&P 500	4.6%	3.5%	15.1%	1.0%	32.4%
NASDAQ	5.2%	6.4%	20.7%	3.4%	40.1%
S&P/ TSX Composite	3.9%	6.9%	14.0%	4.8%	13.0%
Europe					
FTSE World Europe ex-UK (£)	5.4%	2.8%	11.3%	2.3%	25.2%
MSCI Europe	4.8%	4.0%	14.0%	3.0%	20.5%
CAC 40	5.8%	2.9%	12.8%	2.6%	22.2%
DAX	4.1%	3.1%	19.6%	1.5%	25.5%
Ibex 35	2.3%	4.8%	25.7%	2.7%	30.0%
FTSEMIB	5.3%	7.6%	23.4%	7.8%	20.5%
Swiss Market Index (capital returns)	3.5%	2.6%	9.4%	3.3%	20.2%
Amsterdam Exchanges	3.3%	0.8%	10.5%	-0.5%	20.7%
HSBC European Smaller Cos ex-UK	6.2%	9.4%	24.1%	8.0%	34.0%
MSCI Russia (US$)	-2.4%	-10.9%	-3.0%	-12.3%	1.4%
MSCI EM Europe, Middle East and Africa (US$)	2.0%	-9.7%	0.1%	-7.2%	-3.9%
UK					
FTSE All-Share	5.2%	3.9%	8.8%	2.0%	20.8%
FTSE Small Cap ex Investment Trusts	2.9%	10.2%	18.1%	6.2%	43.9%
Asia Pacific & Japan					
Hong Kong Hang Seng	3.7%	-4.3%	5.9%	-2.0%	6.6%
China SE Shanghai Composite (capital returns)	1.1%	-7.4%	-2.0%	-2.8%	-6.7%
Singapore Times	2.8%	-1.7%	3.3%	-1.7%	3.0%
Taiwan Weighted (capital returns)	2.1%	2.8%	7.7%	0.3%	11.9%
Korean Composite (capital returns)	2.0%	-3.2%	2.8%	-1.6%	0.7%
Jakarta Composite (capital returns)	4.6%	8.5%	10.1%	8.1%	-1.0%
Philippines Composite (capital returns)	6.4%	3.5%	5.8%	9.1%	1.3%
Thai Stock Exchange	4.3%	-3.0%	3.4%	2.3%	-3.6%
Mumbai Sensex 30	3.1%	2.1%	14.5%	0.1%	10.9%
Hang Seng China Enterprises index	0.7%	-13.6%	1.1%	-8.6%	-1.5%
ASX 200	5.0%	2.6%	7.6%	1.8%	20.2%
Topix	-0.7%	-3.6%	10.5%	-6.9%	54.4%
MSCI Asia Pac ex Japan (US$)	4.6%	-2.0%	7.6%	-0.7%	3.7%
Latin America					
MSCI EM Latin America (US$)	1.9%	-10.0%	-2.1%	-7.8%	-13.2%
MSCI Mexico (US$)	-3.7%	-8.9%	0.6%	-10.0%	0.2%
MSCI Brazil (US$)	3.6%	-11.6%	-1.5%	-7.3%	-15.8%
MSCI Argentina (US$)	19.4%	-16.4%	22.5%	-9.1%	66.2%
MSCI Chile (US$)	8.4%	-6.4%	-6.4%	-5.0%	-21.4%
Commodities					
Oil - Brent Crude Spot (US$/BBL)	0.6%	-1.9%	-5.8%	-1.2%	0.2%
Oil - West Texas Intermediate (US$/BBL)	5.5%	11.2%	-4.7%	4.8%	6.9%
Reuters CRB index	6.8%	10.0%	3.9%	8.0%	-5.0%
Gold Bullion LBM (US$/Troy Ounce)	6.7%	5.8%	-5.2%	9.8%	-27.3%
Baltic Dry index	13.3%	-30.9%	11.1%	-44.8%	225.8%

Source: Thomson Reuters Datastream, total returns in local currency unless otherwise stated.
Data as at 28 February 2014.