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Smart[im]: Weekly Market Review

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Smart Investment Management

The week to date as at 12 p.m. Friday (GMT).

Markets and Key Events

Mixed week for markets as US data points to acceleration, whilst Europe remains in the doldrums

Stock markets largely ignored the impending G7 meeting in Canada this coming weekend, which is expected to be fractious, as more countries retaliate against the United States imposition of tariffs on steel and aluminium imports. The Nasdaq Composite index, the US technology index, hit a succession of new highs at the start of the week led by the mega cap stocks. Both Apple and Amazon hit record highs, as positive leading indicators out of the US pointed to a rebound in growth after the soft first quarter. However, the picture for Europe was somewhat different, as industrial data released later in the week pointed to continued weakness.

The US Standard & Poor's 500 Index rose 1.3% over the week up to 12pm London time, Emerging markets rose 1.7%, the Australian S&P/ASX 200 rose 0.9%, Japanese Topix index climbed 1.8%, Hong Kong Hang Seng was up 1.5%. However, despite a promising start to the week, the EuroStoxx 600 fell 0.7%, with the Italian FTSE MIB index falling 3.2% despite the formation of a government last week and the United Kingdom's FTSE All Share fell 0.4%.

The core sovereign bonds of the US, Europe and the UK gave up some of their price gains from last week, however, towards the end of the week sovereign bonds started to rally again as the G7 meeting neared. 10-year US Treasuries were broadly flat for the week, yielding 2.90%, whilst 10-year German bund yields were trading at 0.43%, having been as high as 0.51% following a suggestion from a senior European Central Bank official that the ECB's quantitative easing programme could close by the end of the year. UK 10-Year Gilt yields are trading marginally higher at 1.37%, with yields moving inversely to price.

Escalation in trade war largely ignored, as markets focus on improving US lead indicators

The week began with the third round of trade talks between China and the US coming to an end without a breakthrough, as the US tries to pressure China into opening up its economy to US companies through the imposition of trade tariffs. On Tuesday Mexico unveiled tariffs against the US on agricultural and steel products, including pork, cheese, apples and potatoes. However, markets largely brushed off trade war concerns as the latest data on US services pointed to the US economy having picked up following a weak first quarter. The ISM non-manufacturing index, a leading indicator on the health of the service sector, rebounded in May, coming in at 58.6, with readings above 50 indicating expansion. Historically such a level has been consistent with annualised GDP growth of above 4%.

However, European lead indicators disappoint, despite upbeat comments from the ECB

Europe threatened to have its own version of the 'Taper Tantrum' of 2013 as Jens Weidmann, head of the Bundesbank and an ECB board member, told a conference that market expectations that the central bank could end its bond buying programme before the end of the year were "plausible". This view was leant support by Peter Praet, also an ECB board member, pointing to the "underlying strength" of the eurozone economy. German bund yields jumped from a low of 0.37% to trade as high as 0.51%. However, this was followed by a string of economic data releases pointing to continued weakness in the Eurozone, particularly in Germany. New orders for German manufacturing fell 2.5% in April the fourth month in a row in which orders have fallen, driven by weakness in orders from the Eurozone, whilst new orders from countries outside the region rose by 5.4%. German equities fell sharply on the news whilst bunds rallied, with the 10-year yield compressing back down to 0.41%, currently trading at 0.44%.

Upcoming Brazilian election looms large over currency and stock market

The Brazilian stock market had a torrid week as the Ibovespa equity index fell by as much as 6% intraday on Thursday, before recovering slightly, now trading down 4.4% for the week. This performance has been mirrored by the Brazilian currency, the Real, which is down by about 15% from the start of the second quarter. These levels have not been seen since the political crisis that led up to the impeachment of former president Dilma Rousseff in 2016. This reassessment by markets has been triggered by the introduction of price controls for fuel following a crippling truckers' strike. These have been viewed as a throwback to left-wing policies, whilst extreme candidates from both the left and the right are leading in polls in the run up to the October elections.

Australian GDP surprises to the upside

The Australian S&P/ASX 200 closed 1.1% higher, led by the energy sector, whilst defensive names lagged over the week. Australian GDP grew faster than forecast in the first quarter of 2018, rising 1% over the quarter, versus 0.5% in the previous quarter, driven by an increase in mining exports.

G7 Summit & Kim Jong Un Summit

Markets are adopting a risk off tone towards the end of the week, ahead of the G7 summit. The other keenly anticipated event next week is the summit between President Trump and the Kim Jong Un of North Korea, scheduled for Tuesday.