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# Smart[im]: Weekly Market Review

**13 July 2018**
**Smart Investment Management**

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

## Markets and Key Events

Despite global equity markets falling briefly midweek, aggravated by trade fears, investors attempted to look beyond mounting trade tensions between the US (United States) and China in anticipation of earnings season. Markets got off to a moderate start but were derailed on Wednesday when the Trump administration began the process of imposing tariffs on a further $200 billion of Chinese imports. However, by Thursday and Friday morning, global stocks recovered, as attention now turns to the release of second quarter corporate results. Later this week, JPMorgan Chase & Co. and Citigroup Inc. are among the largest companies due to give reports.

As of 12pm London time most major markets finished in positive territory, with the S&P 500 gaining 1.39%, the FTSE All Share up 0.92% and the Eurostoxx 600 higher by 0.81%. Emerging and Asia markets also fared better this week as the MSCI Emerging Markets index increased by 0.97%, and the Shanghai Composite also rallied higher by 3.06%.

In other economic news, US inflation reached its highest level since 2012, as headline CPI (Consumer Price Index) showed prices were 2.9% higher year on year. This is also higher than last month's annualised reading of 2.8%. The strong reading has strengthened expectations that the Federal Reserve will continue to tighten its monetary policy 'gradually'.

*Europe and the UK*

Political moves dominated headlines in the UK, after Brexit secretary David Davis resigned over disagreement with Prime Minister Theresa May's Brexit plan. More pressure was put on the Prime Minister, as the Foreign secretary, Boris Johnson, also resigned on the same day. The proposals for the terms of departure from the EU were criticised by both ministers for making too many concessions to the EU. The consequent uncertainty over the leadership of the Conservative party prompted a volatile reaction in the domestic currency. Sterling declined as much as 0.7% to a low of $1.3188 after the ministers' resignations.

In Europe, stocks considered particularly exposed to China declined after the announcement of tariffs from the US. Industrials and mining stocks suffered, though the market overall rebounded in line with global equities by the end of the week. Economic news flow has been quiet otherwise, though May's Eurozone industrial production climbed by a seasonally adjusted monthly reading of 1.3%, reversing April's revised decline of 0.8%.

*Asia Pacific*

Notably this week, data revealed China's monthly trade surplus with the US widened to a record monthly high for June, of $28.97 billion, up from $24.58 billion in May. Exports to the US climbed to $42.62 billion, also a record high, and this result could further escalate the trade dispute with the US, who cite the imbalanced trade relationship as the underlying root of ongoing tariffs. June data also suggested a sudden rise in volumes as a result of exporters rushing to make shipments before tariffs went into effect. However, analysts expect a less favourable trade balance for China going forward, as export duties and tariffs start to take their toll.

The Australian S&P/ASX 200 closed the week marginally lower, down just 0.1%. Miners such as BHP Biliton and Rio Tinto were lower after a plunge in base metal prices this week. The Australian Dollar came under pressure, given the economy's exposure to Asia and its fallout from an escalating trade conflict; the currency declined 1.2% on Thursday against the US dollar to as low as 73.65 US cents, before finishing the week trading at 73.40 US cents.

*Commodities*

As alluded to earlier, base metal prices dropped sharply midweek, amidst escalating global trade tensions. Copper, Nickel and Zinc, all widely consumed and processed by China, declined in price significantly, as Copper fell 3% to its yearly low of $6,317 a tonne. Nickel and Zinc dropped as much as 3% and 6% respectively. Brent crude oil also had a very volatile week following its biggest one-day drop in more than two years, also reflecting the widespread weakness in commodity markets. The commodity was not helped after Libya's internationally recognised state oil company said it was reopening four key export terminals, suggesting additional supplies to meet rising global demand. Brent crude finished the week trading at $73.93 per barrel.

*Fixed Income*

Yields, which move inversely to their bond prices, were mostly unmoved for core government bonds. US 10-year treasury yields moved just 2 basis points higher over the week, whilst equivalent 10-year Bund yields also rose 4 basis points. UK 10-year Gilts however, declined by only 2 basis points.

## *Changes to the portfolios.*

Across all Smartfunds, we removed our exposure to Morgan Stanley Cube Equity 8 asset, which has had a tough time of late, despite us holding it as a defence equity. In its place, we have introduced exposure to healthcare and increased our allocation to energy companies. We believe the healthcare sector will be relatively insulated from any global trade wars, whilst our preference to increase our allocation to energy is not necessarily a bet on the oil price. Rather, integrated oil companies continue to generate higher free cash flows after a programme of cost cutting since the oil price collapsed to under $30 a barrel in 2016.

In Smartfund Growth, we introduced a small position to Emerging Market Debt in both hard currency sovereign debt and local currency sovereign debt. Despite recent underperformance of Emerging Markets driven by the recent strength of the US dollar, many emerging economies continue to experience a trend of moderating inflation and falling interest rates, which is beneficial for fixed income. We already have these positions in Smartfund Cautious and Balanced and have not added to these.

In addition, we also reduced our absolute return exposure, which has also suffered in the recent volatility, and reinvested the proceeds into US TIPS (Treasury Inflation Protected Securities), and limited positions in Gold and Commodities. Inflationary protected US Treasuries act as a hedge for the potential risk of inflation in the US, which could occur from Trump's trade war, whilst Commodities also typically outperform other sectors in a rising inflationary environment later in the economic cycle. The position remains small as we appreciate that a global trade war could cause commodity prices to retreat. Meanwhile Gold, which has fallen in price since December, is typically negatively correlated to interest rates. The precious metal will benefit should the Federal reserve fail to raise interest rates in line with inflation.

For Smartfund Balanced, we have reduced our exposure to Sterling short duration credit and diversified into longer dated Sterling credit, European High Yield and US short duration High yield, where these asset classes have sold off recently and thus look relatively attractive again. Similarly, for Smartfund Cautious, we have also reduced exposure to Sterling short duration credit in favour for global investment grade credit and European High Yield.