02 June 2017

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INVESTMENT MANAGEMENT

WEEKLY INVESTMENT UPDATE

Election Jitters Hit Pound

KEY MESSAGES:

President Trump's pull out of the Paris Climate Accord dominated the headlines this week. Key central bank meetings coming up on both sides of the Atlantic. While markets are pricing in a high probability of a June hike by Fed. The slowdown in euro area inflation is expected to bolster ECB's confidence in delaying the withdrawal of monetary stimulus.

USD fell to the lowest level since November. GBP weakened, hurt by conflicting projections of the general election outcome schedule June 8.

US stocks pushed to fresh records, 10-year Treasury yielded 2.16%. WTI crude oil dropped 1.1% to $47.81 per barrel. Gold closed at $1,277.10 per ounce.

Market developments during the week

The British pound was the stand-out mover amid muted moves in many markets, weakening on the prospect of a hung parliament in next week's UK election and handing a boost to stocks. Sterling dropped as a poll showed Theresa May's Conservative Party may fall short of a majority. The currency's weakness lent a hand to British equities, and the FTSE 100 Index rose as miners and energy companies weighed on the broader European gauge. However, uncertainty about the reliability of polling seems to have helped contain the pound's retreat, but the moves are a reminder of the potential risks surrounding a series of national elections in Europe this year. Meanwhile, with key central bank meetings next month on both sides of the Atlantic, investors focused on this week's slew of economic data to gauge both the strength of the global economy and the path for interest rates.

Trump administration continued to hit the headlines this week, the major one being the US withdrawal from the Paris Climate Accord. President Trump announced the decision to quit the Paris accord and is being widely condemned by world leaders and domestic business leaders. The German, Italian and French governments all reacted individually within an hour of the announcement, before putting out a joint statement condemning the withdrawal. However, this won't happen overnight. Under the terms of the Paris accord, Trump must wait until November 2019 to formally submit his intention to withdraw. At that point, the US enters a one-year waiting period before it's formally removed. The decision could be reversed by the next president, or even Trump himself. As a result, the issue will be front and centre during the 2020 presidential election campaign. President also indicated his openness to negotiate a new climate agreement. He also said he's open to renegotiating the deal on terms more favorable to America. The American exit is unlikely to have an immediate effect on global efforts to address climate change. Almost 200 countries remain in the pact, which remains in effect regardless of the US position.

Regarding update on tax cuts, President Trump said this week that the tax bill is moving along in Congress soon after announcing that the US would pull out of the Paris climate deal. But no tax bill has been introduced, or even circulated, and Republicans who strongly support Trump and are desperate to advance some kind of tax bill, fret that the White House is falling far behind. The White House's only public contribution to the debate has been a one-page outline released in late April that included trillions of dollars in individual and corporate tax cuts that would explode the deficit and lacked details on how to pay for them.

Also another concern is the reaching of debt ceiling by US Government. President Donald Trump's chief economic adviser stated that Congress has no choice but to vote to raise the government's borrowing authority, and that the White House will

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consider spending cuts or other riders to avert an unprecedented default. The US government is expected to reach its debt ceiling by as soon as August. If Congress doesn't act to raise the ceiling, the government would default for the first time in its history.

Given the recent strength in global growth, economic fundamentals trump political risk. Likewise, the Federal Reserve is expected to look past political clouds if there's no knock-on impacts to the real economy. US growth is expected to bounce back above 3% in the second quarter, and financial conditions are actually easier today relative to when the Fed resumed its rate hike path back in late 2016.

As the next meeting of Federal Reserve policy makers in mid-June draws near, investors are putting the chances that they'll raise interest rates at nine in ten. Wall Street did keep an eye on the jobs report which was expected to support the June rate hike path. However, the US labor market gave mixed signals in May, with a decline in the unemployment rate to 4.3%, a 16-year low contrasting with below-forecast hiring and wage growth, Labor Department figures showed. Payrolls rose 138k (est. 182k rise) and March-April revisions subtracted 66k jobs. Average hourly earnings rose by 0.2% m/m and climbed 2.5% y/y. Wage growth remains slower than peak of previous expansion. Cooler hiring may partly reflect the challenge of finding skilled and experienced workers amid a tightening job market. It may also be a sign that businesses are reluctant to expand their workforce until they see more evidence the new administration's plans are translating into legislation that'll reduce taxes and spur growth. This jobs report likely won't deter the Federal Reserve from increasing interest rates in two weeks as the economy continues to grind higher even as Washington shows few signs of moving forward with tax and spending reforms.

The Federal Reserve's preferred price measure rose 1.7% in April from a year ago, down from 1.9 % in March and 2.1% in February, Commerce Department figures showed. Core inflation also slowed to the weakest annual pace since 2015 easing to 1.5% in April from 1.6% in March in spite of a slightly bigger-than-expected 0.2% month-over-month rise. A rebound anytime soon looks unlikely, with prices kept in check by an ongoing oil glut, an overstocked auto market and a rising supply of apartments to rent. Fed policy makers forecast in March that inflation would end the year at 1.9%, just below their 2% goal for the personal consumption expenditure price index. Inflation looks likely to end the year shy of the Fed's forecast. While the shortfall isn't expected to prevent central bankers from raising interest rates next month, a sustained stall would make it more difficult for Chair Janet Yellen and her colleagues to follow through with another hike later in the year, as their March projections indicated. Federal Reserve Governor Lael Brainard said soft inflation could cause her to reassess the path forward for monetary policy should it linger, even as the global economic outlook brightens and US growth looks poised to rebound. She said her baseline expectation is that "it likely will be appropriate soon to adjust the federal funds rate" and start shrinking the balance sheet.

On trade update, US demand for foreign-made goods climbed and exports declined, causing the trade deficit to widen in April, which may restrain the pace of economic growth this quarter, Commerce Department data showed. Gap increased 5.2% to $47.6b from a revised $45.3b in March. Merchandise-trade deficit climbed to $68.4b, the second-widest in two years. Trade contributed little to first-quarter growth after subtracting 1.82 percentage points in the final three months of 2016, according to the government's figures on gross domestic product.

Other indicators showed the housing market remains tight and consumer sentiment is relatively strong.

Currencies

The Bloomberg dollar index fell to the lowest level since November retreating 0.4%. It's down by the same amount in the week.

GBP added 0.7% this week to $1.29, while the euro strengthened 0.9% for the week to $1.13. Sterling slipped after a YouGov poll in the Times showed Prime Minister Theresa May's party may fall short of an overall majority by 16 seats, and face a hung parliament.

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The yen lost 0.7% this week closing at 110.5 per dollar, after falling 0.5% on Thursday.

China's offshore yuan jumped the most in four months as funding costs surged amid speculation policy makers were supporting the currency in the wake of a surprise sovereign rating downgrade.

Equities

US stocks pushed to fresh records with the S&P 500 climbing 0.6 % to 2,430. The Dow Jones Industrial Average rose above 21,200 for the first time, while the Nasdaq Composite Index extended its record. The Russell 2000 Index jumped more than 1%. Technology indexes extended all-time highs.

European stocks were little changed. The Stoxx Europe 600 Index increased 0.2%, to cap a 0.3% advance in the week.

The FTSE 100 Index closed at 7,549.

Asian equities were set to cap a second week of gains as Japanese stocks advanced to the highest in 21 months, with sentiment boosted by a slew of economic data that was better than expected and after US equity benchmarks closed at record highs. Japan's Topix index breached the 1,600 mark and the Nikkei 225 Stock Average surpassed 20,000 for the first time since December 2015 closing at 20,177 as the yen weakened for a second day. The Shanghai Composite rose 0.2%, after an earlier gain of 1.1% on better-than-expected Chinese factory data.

Global equities have advanced more than 10 % this year.

Bonds

The 10-year Treasury yield touched the lowest level of the year following wage growth and hiring that was below forecasts falling nine basis points to 2.16. It touched the weakest level of the year immediately following the jobs report.

The UK benchmark yield dropped three basis points to 1.04%.

Yields in France and Germany fell with 10-year German bunds yielding 0.28%.

Commodities

WTI crude oil dropped 1.1% to $47.81 a barrel. It's on course to fall almost 5% this week as US crude production expanded to the highest level since August 2015, countering a slide in stockpiles. US crude exports rose to average about 1 million barrels a day in April, according to Bloomberg calculations of US Census Bureau data. Data suggests that OPEC's efforts to rebalance the market need more time. Oil futures have lost 8% since the OPEC and its allies agreed on May 25 to keep output constrained through the first quarter of 2018 in a bid to clear a global glut. Within the organization there is pressure too, as data show Iraq's oil production hit a 2017 high in the run-up to the deal to extend production cuts.

Gold reversed a slide of 0.3% to trade higher by 0.5% at $1,277.10 an ounce.

Copper dropped 1.9%, leading industrial metals lower

Major economies:

Euro area

A Purchasing Managers' Index rose to 57 in May from 56.7 the previous month, as per a report by IHS Markit, confirming a May 23 flash estimate. Employment jumped the most in the survey's 20-year history and expanded in all countries covered for the first time since November indicating euro-area manufacturers are hiring at a record pace as growing export and domestic demand push output to the highest level in six years.

On the other hand, euro-area inflation slowed more than economists forecast, giving ammunition for European Central Bank policy makers who are due to meet next week and consider it's too early to commit to an exit from monetary stimulus. Consumer-price growth decelerated to 1.4% in May, the weakest reading this year, from 1.9% a month earlier, Eurostat said. Core inflation fell to 0.9%, also weaker than expected. In a separate release, the European Union's statistics office said unemployment declined to 9.3%, its lowest level since March 2009. IHS Markit, which publishes a monthly activity index, last week captured the disconnect between weak price growth and a strengthening economy where companies are stepping up hiring to meet demand.

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ECB's Mario Draghi stressed on Monday in Brussels that "downside risks to the growth outlook are further diminishing," highlighting one of the key signals that the ECB could send next week. Some policy makers have said they now consider risks to the economy's outlook as broadly balanced. Ahead of ECB's meeting next week, the inflation data gives actual proof that price trends remain weak should help Mario Draghi hammer home the message that the central bank has to remain patient and quell the urge of some of his colleagues to take more decisive steps.

French inflation figures also joined the euro-area trend slowing slowed in May as it became the third major euro-area economy to record weaker-than-forecast price growth. The rate declined to 0.9% from 1.4%, undershooting the median estimate of 1.1 %. Spain and Germany also posted readings this week that fell short of predictions.

Italy's jobless rate fell in April to an almost 5-year low, pointing to improved growth prospects for the rest of this year. The unemployment rate was 11.1%, down from a revised 11.5% in March, statistics agency Istat said. Italy is facing renewed political pressures as it moves towards an early vote as the country's main political parties near a deal on a new electoral law. Italy's biggest parties are considering a proportional system similar to the German model with a 5% cut-off for smaller parties, and lawmakers are due to discuss a first draft of the new law early next month. An agreement would remove any hindrance to snap elections, eliminating the need to wait for scheduled elections in early 2018. Former Prime Minister Matteo Renzi is among those making the case for an early ballot as he seeks a political comeback from the referendum defeat that led him to resign in December. Italian markets shuddered at the emerging prospect of early elections. Italians dumped stocks and government debt after ruling Democratic Party's Matteo Renzi signaled the possibility of a vote in September or October. Italian bonds have been the worst performers in Europe this week following Renzi's comments. Since Monday the yield on Italian 10-year bonds has risen nine basis points to 2.19%, pushing the yield spread over German bunds to 189 basis points. Italy's FTSE MIB benchmark index was down 0.7% on Tuesday, with banks leading losses.

Italy is also struggling to fix a crisis legacy of about 360 billion euros of soured loans in its banks' balance sheets that is holding back credit and weighing on the country's weak recovery. Italian authorities are trying to prop up Banca Monte dei Paschi di Siena SpA and two banks in the northern region of Veneto, using a provision in the EU's bank-failure rules that allows governments to provide state aid. European Union and Italian officials agreed on a plan to restructure Banca Monte dei Paschi di Siena SpA, allowing Italy to inject capital to rescue the world's oldest bank. Competition Commissioner Margrethe Vestager and Italian Finance Minister Pier Carlo Padoan reached "an agreement in principle" on a deal that paves the way for a precautionary recapitalization of the lender, according to a statement on Thursday. The deal, following "intensive" talks between Italy, the EU and the ECB, still requires formal approval. The comments weighed on the euro, with the common currency already not helped by the prospect of earlier-than-expected Italian elections.

After it was considered that Trump's five nation visit last week was not completely positive, German chancellor Angela Merkel has signalled that Europe can no longer count on the US as a reliable partner, reflecting a new transatlantic rift. President Trump's announcement of withdrawal from the Paris Climate Accord further adds fuel to the fire. During the trip to Europe, Mr Trump also took aim at Germany for its trade surplus with the US. The US president also clashed with European heads of state berating them for not meeting a target to spend 2% of gross domestic product on defence.

Canada

Canadian real GDP rose 3.7% annualized in Q1, while nominal GDP rose 8.3%, marking the best three-quarter streak in almost seven years. The household sector has contributed most to growth, due in large part to a hot housing market. Still, exports appear to be gaining momentum heading into the second quarter of the year.

Preliminary data showed policy-induced soft market conditions in the GTA and GVA extended into May, bringing the durability of Canada's growth prospects into question.

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Low interest rates will likely continue to support consumption amid a cool down in activity in Canada's largest housing markets, providing upside potential to our 2017 growth forecast. Higher interest rates in 2018 should bring about a cooling in consumption and real estate.

China

Official manufacturing data showed that growth in China is holding up, despite worries that a leverage crackdown would feed through to investment providing a short-lived market bounce. The manufacturing purchasing managers index remained at 51.2 for a second straight month, beating estimates. Non-manufacturing PMI rose to 54.5.

While some early indicators for May suggested a slowdown in growth is taking hold, the PMI data signal continuing momentum that gives policy makers more room to rein in financial risks.

One place that the deleveraging campaign is apparent is in the government bond market, with the nation's 10-year security falling for the second month in a row. China's debt market has been hit especially hard by the campaign to reduce the level of borrowing, with both sovereign and corporate yields surging. This was worsened by last week's Moody's Investors Service downgrade of China's credit rating. The 10-year yield has advanced 17 basis points so far in May to 3.65%. That follows an increase of 18 basis points last month.

UK

Election jitters hit GBP this week, as the UK currency was being buffeted by conflicting projections of the general election outcome, bearing the brunt of increasing market tension before next week's vote. GBP first dropped to a more than 5-week low on Wednesday after a YouGov Plc study showed Theresa May's Conservative Party may fall short of a majority, a contrast from just a few weeks ago when a victory was seen as a foregone conclusion. The currency later rallied after the release of a Panelbase poll showing a 15-percentage point lead for the Tories, even though that survey was carried out more than a week ago, before erasing the day's losses as a Kantar study showed a 10 point advantage. A separate Times/YouGov poll Wednesday night showed the Conservatives leading Labour by three points. Jeremy Corbyn, the leader of the British Labour Party, continues to increase his appeal among UK voters ahead of next week's election, with his approval rating doubling since April. While the opposition leader is still unlikely to win the election, the momentum he is achieving against the struggling Theresa May is keeping markets alert to another British electorate June surprise.

On the economy, the picture remains mixed, with IHS Markit's Purchasing Managers Index coming in at 56.7 in May, while home prices fell for the third month in a row for the first time since 2009.

UK manufacturing activity maintained its momentum in May and confidence rose as strong domestic demand buoyed orders. IHS Markit's Purchasing Managers Index was at 56.7 in May, better than estimates, after reaching 57.3 the previous month, which was the highest in three years. Domestic demand helped manufacturing sustain growth momentum. One pressure point for the UK is accelerating inflation, which is hitting households. The factory report showed that while measures of both input costs and output charges eased in May, both remain elevated, with the latter close to a record high.

UK house prices fell for a third month in May, the worst streak for the market in eight years, according to Nationwide Building Society. Values fell 0.2% from the previous month, taking the annual rate of change down to 2.1%. That's the weakest year-on-year growth since 2013. Multiple reports are pointing to a housing slowdown, with the Bank of England saying on Wednesday that mortgage approvals fell to a seven-month low in April, though Britons are continuing to take advantage of low interest rates to take on unsecured debt. Mortgage lending grew £2.7 billion, the least since April 2016. But consumer credit rose £1.5 billion, little changed from the previous month, pushing annual growth to 10.3% from 10.2%.

The UK construction figures show an increase in May rather than the expected decline.

The Markit/CIPS construction purchasing managers index climbed from 53.1 in April to 56, the highest level since December 2015, helped by a pickup in housebuilding. Analysts had been forecasting a dip to 52.7.

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Jason Granite
Chief Investment Officer
02 June 2017

Contact us
T: 020 3793 7424
T: 0161 886 8000
F: 0161 886 8002
www.frenkel topping.co.uk

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Frenkel Topping Investment Management's ("FTIM's") Safety First performance

	2016 Performance	2017 Performance	Volatility* 04/01/16
FTIM Safety First 2	1.53%	0.11%	2.41%
FTIM Safety First 3	3.26%	0.34%	2.70%
FTIM Safety First 4	4.38%	0.68%	3.51%
FTIM Safety First 5	5.63%	1.19%	3.87%
FTIM Safety First 6	10.10%	2.20%	5.32%

Date:02 June 2017
Source: FTIM / FE Analytics

Safety First Portfolio strategies were launched on 29/04/16. All figures are on a bid - bid, total return basis and are quoted net of underlying fund charges, our DFM fee of 0.6% including VAT and a platform fee of 0.2%. Advice charges would depend on the charges made by your independent financial adviser. The deduction of these charges would reduce the performance shown. Actual Past Performance Data is from 29/4/16 only as the models only launched on this date and therefore 5-year performance data is not available and 12-month performance figures are not able to be shown. Pre - launch performance from 4/1/16 – 29/4/16 is Simulated Past Performance. The figures represent performance of a model portfolio; individual account performance may differ if your account does not follow the model. Past performance is not a reliable indicator of future performance. Investment values can go down as well as up and may be affected by exchange rate variations.

*Volatility is a measure of the movement in the price of an asset around its average return. The higher the volatility the more risk involved in the investment.