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INVESTMENT

View from the Front

5th February to 11th February 2018

Front and centre of our thoughts this week include

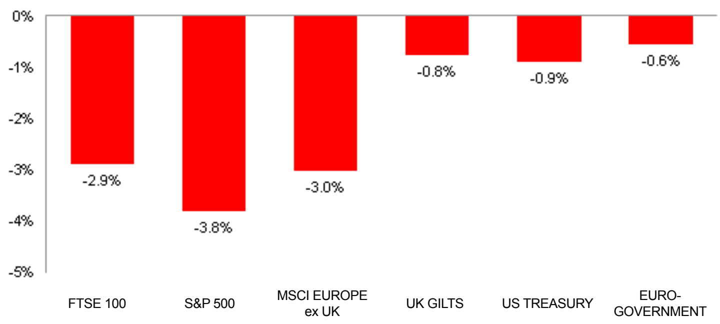
- The highlight of the week will be the Bank of England (BoE) Monetary Policy meeting where it is expected that the BoE will make no changes to policy and leave interest rates at 0.5%. In a speech last week at the House of Lords, Governor Mark Carney painted a relatively upbeat picture of the UK economy and it will be interesting to see if this is reflected in the central bank's assessment of the economy in its latest quarterly Inflation Report. We expect the BoE to upgrade their forecasts for growth due to the strengthening global growth backdrop and the better-than-expected performance of the economy over the fourth quarter of 2017. Similarly, declining spare capacity and the recent increase in the price of oil is likely to see inflation forecasts revised higher. If both growth and inflation estimates are revised higher as expected, it will likely reinforce expectations of another interest rate rise in May.
- Sticking with central banks, Jerome Powell will be sworn in as new Chairman of the US Federal Reserve (Fed) in a private ceremony today. Additionally a number of Fed officials are scheduled to give speeches this week including monetary policy voting members Bill Dudley and John Williams. The speeches will be closely watched to see how much of an impact the recent increase in wage growth in the US will have on central bankers' forecasts for interest rate rises this year.
- Central banks aside, it is a relatively quiet week for economic data with the service sector business confidence readings from across the globe being the focus of attention. The service sector accounts for over 70% of growth in most developed and over 50% in the majority of developing economies. As a result the release of the confidence readings for this sector are an important gauge into the underlying health of the global economy. We expect the readings to follow a similar pattern to the manufacturing sector surveys and indicate a broad-based strengthening in global growth.
- In regards to politics, the US Congress has until Thursday to approve another short-term spending bill to avoid a partial shutdown in government. Another short-term extension of funding is expected to be approved this week which will give Republicans and Democrats more time to reach a deal on the issues preventing a long-term funding agreement from being agreed – notably protection rights for immigrants and border security.
- On the corporate front we are halfway through the fourth quarter of 2017 US earnings updates, and despite this quarter's numbers being distorted by the recent tax reforms in the US, the results have been encouraging. Of the 250 companies in the S&P 500 that have reported earnings so far, close to 80% have beaten analysts' estimates for earnings and revenues according to Thomson Reuters data. This week sees a further 94 S&P 500 companies set to report, including General Motors, Walt Disney and AIG.

In the rear view mirror of last week we saw

- As was widely expected, Janet Yellen's final Fed monetary policy meeting produced no change in policy. The Fed's post meeting statement indicated a fairly upbeat outlook for the economy and set the stage for a further rate rise in March (20-21st) when the Fed are next scheduled to meet.
- The US employment report for January certainly supported the case for an additional rate rise. The US economy added more jobs than expected in January (200k) and the unemployment rate held steady at 4.1% - a 17 year low. The most eye-catching aspect of the report was the increase in average hourly wages which increased at an annual rate of 2.9% - a potential sign that inflationary pressures are beginning to build in the economy as employers respond to a tightening labour market by raising wages.
- It was another positive week for Europe as data showed the Euro area economy grew at its fastest rate in a decade in 2017 with the economy growing 2.5% last year. Despite the robust growth, inflationary pressures continue to remain subdued with initial estimates showing annual consumer prices rose 1.3% in January, a slowing from the 1.4% rate in December. If inflation continues to trend lower it may persuade the European Central Bank to extend their quantitative easing programme beyond the current September end date.
- The manufacturing sentiment surveys for January, on balance, continued to signal that growth in the sector remains robust. Both the US and Japan reported an increase in manufacturing companies confidence while European and Chinese sentiment remained broadly unchanged. UK manufacturers were the exception and reported a slight dip in sentiment although the decline was from historically high levels of business confidence.

In the side view mirrors of corporate activity we notice

- It was another difficult week for the UK outsourcing sector, following the collapse of Carillion, outsourcing group, Capita issued a new profit warning which resulted in its share price falling over 40%. New Chief Executive, Jonathan Lewis, who took charge of the business in December, said the company had become too widely spread and relied too much on acquisitions for growth. To strengthen the company's balance sheet Mr Lewis announced a cost restructuring programme which includes the sale of non-core businesses (ParkingEye and Constructionline), a dividend suspension and a £700m rights issue.
- It was a mixed set of results for technology heavyweights Alphabet, Amazon and Apple, who all reported fourth quarter earnings last week. Alphabet's profits were lower than expected as the company had to spend more money ensuring Google is the default search engine on products like the iPhone while Amazon and Apple both beat expectations. Apple's profits were helped by sales of the new iPhone X exceeding expectations while a surge in on-line spending over the holiday season boosted Amazon's profits.



Source: Bloomberg. Figures are for the period 29th January to 4th February 2018. Where the index is in a foreign currency, we have provided the local currency return.

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