Macro and Market Review

June 2014

MACRO AND MARKET REVIEW

MACRO REVIEW

In June, aside from mounting tensions in the Middle East and in Ukraine, the attention of financial markets was dominated by:

- **Mixed global macro-economic data**. In the US, despite a better employment situation there was the substantial downward revision of the first quarter GDP figures to -2.9%. In Japan growth data were revised higher, while in Europe there are more signs of a pause in the recovery. The contrast in activity between Europe and the US has not been so pronounced for a while. The UK economy continues to grow at an above-trend pace with no signs of slowing. In China, growth has stabilized. In Emerging Markets, growth remains below trend.

- **Key diverging policy moves from Central Banks**. The Governor of the BOE surprised the markets when he announced that UK interest rates could rise sooner than expected. Conversely, in order to fend of the risk of deflation and to stimulate growth, the **ECB launched a number of measures, such as an unprecedented policy of negative deposit rates**, down to -0.10%, and plans to expand its balance sheet via long term refinancing operations with the banking sector in order to stimulate lending. In the US, the FOMC announced a cut of another USD 10 billion from its QE program, a move consistent with the FOMC's earlier guidance on the tapering of QE. In Asia, the Japanese government announced the specific policies making up the third arrow of Abenomics to revitalize the domestic economy.

Of note, global M&A activity reached a 7-year high, with a global deal volume reached USD 1.75 trillion, up 75% for the same period a year ago. Aside from cheap financing, corporates are taking advantage of their strong stock prices and ample cash reserves.

MARKET REVIEW

Equity and credit markets did well, while volatility fell close to all-time lows. Valuations across many markets remained supported by a mixture of low interest rates and steady, yet low growth.

- **Global equity markets were mixed**. The MSCI Europe (-0.63%) declined while many major equity markets extended their rally in June. The Nikkei rose +3.62%, while the **S&P 500 (+1.91%) reached record highs levels**. The MSCI World (+1.65%) and the MSCI EM (+2.25%) did well. On a sector basis, Energy outperformed, while Utilities and Healthcare did well. Financials were the worst performing sector, whilst Industrials and Information Technology also underperformed the broader market. Global convertible issuance was strong, although lower equity volatility further weakened the valuation of bonds which are favored by traditional convertible arbitrage players.
- **In fixed income, performance was mixed.** The yield on the 10-year German Bund fell further to 1.25% from 1.36% whilst the yield on the 10-year US treasury bond rose to 2.53% from 2.48%. The US yield curve flattened. In the UK, fixed income weakened as the yield curve moved higher and flattened. **Credit spreads, especially in high yield, continued to tightening.**
- In currencies, the **EUR (+0.42%)** and the **GBP (+2.09%)** gained against the USD, with the GBP reaching a 6 year high.
- **In commodities, with the exception of crops, prices were stronger, led by precious metals and energies** driven by oil prices climbing amid continuing violence in Iraq, impacting hopes for future supply increases from this key exporter. Crude oil (WTI) was up +2.59%. Gold (+6.21%) did well.

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