MARKET REVIEW

Irish Life

AUGUST 2018

Global equity markets rose in August, driven by the US which reached new all time highs as trade tensions eased with progress in NAFTA trade negotiations while economic data generally remained firm. Eurozone sovereign bonds fell however as political tensions in Turkey negatively impacted Italian spreads with uncertainty ahead of upcoming budget discussions also contributing to higher Italian yields.

Sentiment on the trade issue continued to 'see saw' through the month although overall, some progress appeared to be made with risks around global growth perceived as having eased somewhat. The US and China held low level trade talks for the first time in a number of months and while nothing of substance was agreed, immediately afterwards China implemented measures to ease depreciation pressure on the Renminbi which appeases the US. The talks also served to keep communication channels open between the US and China on the trade issue. Elsewhere, the US and Mexico agreed terms on a new trade deal and with growing hopes that Canada would join the agreement thereby enabling a new NAFTA trade agreement, the threat of a trade war on the North American continent reduced. While these measures represented progress, threats by President Trump to impose tariffs on an additional $200bn of Chinese imports as soon as the first week in September and the rejection by Trump of an EU offer for zero tariffs on auto and industrial goods were seen as backward steps at month end.

On the political front, the conviction of President Trump's former campaign manager for financial fraud and the guilty plea of his former attorney to breaking campaign finance laws were seen as increasing the likelihood of a possible future impeachment of Trump although they had little impact on markets. In relation to Brexit, comments by the Bank of England Governor and secretary for International Trade early in the month suggested an increasing probability of no deal with the EU prior to the UK's exit from the EU in March. Later however the EU's chief negotiator suggested the EU is willing to give the UK a partnership deal like none ever offered to any other country suggesting a compromise might be reached in Brexit talks in coming months. In Turkey, a political and economic crisis erupted as the US imposed sanctions in response to the detention of a US citizen in connection with the 2016 coup. Combined with the apparent loss of the central banks independence, large levels of foreign exchange corporate borrowings, a sizable current account deficit, a rising fiscal deficit and evidence of nepotism in government, the Turkish Lira fell almost 25% and contributed to significant weakness in Turkish assets. While these issues were viewed as being specific to Turkey and not necessarily representing a contagion risk to other EM markets, they nevertheless impacted sentiment towards EM assets. Italian bonds were also negatively impacted by these events given the recent political sensitivities there.

There was little of note from global central banks. Minutes from the recent Fed meeting and speeches by Fed members confirmed that the path of gradually rising rates is likely to continue, despite open criticism of this policy by President Trump.

Global macro data generally remained firm. US Q2 GDP growth was revised up to 4.2% annualised while consumer confidence reached a new cycle high although housing data and ISM's were softer. In Europe, sentiment surveys generally improved, consistent with a pick up in growth in the second half. Japanese Q2 GDP moved back into positive territory at 0.5% q/q. Chinese data however continued to be softer with retail sales, industrial production and investment disappointing although as an offset, fiscal policy continues to be loosened.

Over the month the MSCI AC World equity index rose 1.2% (1.4% in €). The US rose 3.3% (3.9% in €), reaching new all time highs as the growth and earnings backdrop remained positive and progress was made in NAFTA trade talks. The UK fell -3.3% (-3.6% in €) as Brexit related uncertainty acted as an overhang. Eurozone >5 year bonds fell -0.7% despite German 10 year yields falling to 0.33% in the flight to safety associated with the political tensions in Turkey and renewed concerns about Italy. Italian 10 year spreads against Germany rose to 291bps as fallout from tensions in Turkey pulled yields higher. The expected confrontation in the upcoming budget discussions with the EU where the Italian government is likely to seek an increase in the fiscal deficit in 2019 also caused Italian yields to rise. The rise in Spanish 10 year spreads was more modest given its better economic and fiscal position and more EU friendly government with 10 year spreads ending the month at 114bps. The Euro traded in a wide range during the month, ending slightly lower at 1.1602 against the US$ as the fallout from the tensions in Turkey and Italy pushed the currency lower. Commodities rose 1.1% (1.6% in €) with WTI oil up 1.5% as inventories fell, supply disruptions were again evident in various regions and markets discounted the embargo on Iran oil exports from November.

Markets in August

	Local Returns	Euro Return
Ireland	-0.8	-0.8
UK	-3.3	-3.6
US	3.3	3.9
North America	3.1	3.6
Europe	-2.0	-1.7
Japan	-0.7	0.8
Pacific	-0.1	-1.2
Emerging Markets	-0.5	-2.1
World	1.2	1.4
EMU Govt Bonds >5yr	-0.7	-0.7
Commodities	1.1	1.6

Markets YTD

	Local Returns	Euro Return
Ireland	-3.8	-3.8
UK	-0.4	-1.3
US	10.1	13.7
North America	9.7	13.0
Europe	1.4	1.7
Japan	-2.8	1.9
Pacific	3.1	1.3
Emerging Markets	-1.4	-3.9
World	5.4	7.1
EMU Govt Bonds >5yr	0.0	0.0
Commodities	7.6	11.1

US Economics and Rates

USA	Latest Value	Prior Value	Change	Survey (Expectation)
Average Hourly Earnings %m/m	0.3	0.1	0.2	0.2
Capital Non-Defense Goods Orders %m/m	1.4	0.6	0.8	0.5
Consumer Confidence	133.4	127.9	5.5	126.6
CPI %m/m	0.2	0.1	0.1	0.3
CPI ex Food and Energy %m/m	0.2	0.2	0	0.3
Durable Goods Orders %m/m	-1.7	0.7	-2.4	N/A
Durables Ex Transportation %m/m	0.2	0.1	0.1	N/A
Existing Home Sales %m/m	5.34	5.38	-0.04	5.4
Factory Orders %m/m	0.7	0.4	0.3	-0.6
GDP US Chained 2009 Dollars %Q/Q	4.2	2.2	2	4
House Prices Top 20 Cities %m/m	0.2	0.4	-0.2	0.3
Industrial Production %m/m	0.11	0.97	-0.86	0.3
ISM Manufacturing PMI SA	61.3	58.1	3.2	57.6
ISM Non-Manufacturing PMI SA	55.7	59.1	-3.4	56.8
New Home Sales %m/m	-1.7	-2.4	0.7	2.2
NFIB Small Business Optimism	107.9	107.2	0.7	108.2
Non-Farm Payrolls (000s)	157	248	-91	195
Personal Consumption %m/m	0.4	0.4	0	0.4
Personal Income %m/m	0.3	0.4	-0.1	0.4
Retail Sales %m/m	0.5	0.2	0.3	0.6
Unemployment Rate %	3.9	4	-0.1	3.8

The minutes for the Fed meeting which was held through the 31st July and the 1st August at which policy was left unchanged highlighted the Fed's ongoing confidence regarding the current strength and outlook for the economy. Economic activity was described as being strong compared to solid in the previous minutes and guidance towards further gradual increases in interest rates was maintained. While risks were viewed as being roughly balanced, the concerns and risks around the trade issues were noted. While there was some debate around the current shape and level of the US yield curve, overall there did not appear to be any great concern regarding the recent flattening of the curve. Some Fed members pointed out that inferring economic causality from any potential inversion of the yield curve was inappropriate. Criticism by President Trump of the Fed's current plan for further rate rises appeared to be ignored by Fed Chairman Powell when he suggested at an economics conference that prudent risk management and review of the output gap and potential excesses in the economy justified the Fed remaining on its current path of gradual rate rises.

European Economics and Rates

Eurozone	Latest Value	Prior Value	Change	Survey (Expectation)
Construction %m/m	0.2	0.3	-0.1	N/A
Consumer Confidence	-1.9	-0.5	-1.4	-1.9
Core Inflation %y/y	1	1.1	-0.1	1.1
Euro Area Business Climate indicator	1.22	1.3	-0.08	1.26
Euro Area Economic Confidence	111.6	112.1	-0.5	111.9
Euro Area GDP Chained 2010 prices %Q/Q	0.4	0.4	0	0.4
Eurozone Composite PMI	54.4	54.3	0.1	54.4
Eurozone Manufacturing PMI	54.6	55.1	-0.5	54.6
Eurozone Services PMI	54.4	54.2	0.2	54.4
Headline Inflation %m/m	0.2	-0.3	0.5	-0.3
Headline Inflation %y/y	2	2.1	-0.1	2.1
Industrial Production %m/m	-0.7	1.4	-2.1	-0.4
Industrial Production %y/y	2.5	2.6	-0.1	2.4
Money Supply Growth M3	4	4	0	4.3
Retail Sales %m/m	0.3	0.3	0	-0.1
Retail Sales %y/y	1.2	1.6	-0.4	1.3
Sentix Business Sentiment	14.68	12.0908	2.5853	13.4
Unemployment%	8.2	8.2	0	8.3
ZEW Survey Expectations	-11.1	-18.7	7.6	N/A

Germany	Latest Value	Prior Value	Change	Survey (Expectation)
Composite PMI	55.7	55	0.7	55.7
Consumer Confidence	10.5	10.7	-0.2	10.6
Factory Orders% m/m	-4	2.6	-6.6	-0.5
GDP growth %q/q	0.5	0.4	0.1	0.3
Industrial Production %m/m	-0.9	2.4	-3.3	-0.5
Retail Sales %m/m	-0.4	-1.4	1	1
Retail Sales %y/y	0.8	-1	1.8	1.5
Unemployment%	5.2	5.2	0	5.2
ZEW Survey Expectations	-13.7	-24.7	11	-21.3

France	Latest Value	Prior Value	Change	Survey (Expectation)
Business Sentiment	105	106	-1	107
Composite PMI	55.1	54.4	0.7	54.5
Consumer Confidence	97	97	0	98
Consumer Spending	0.1	0.1	0	0.6
GDP growth %q/q	0.2	0.2	0	0.2
Industrial Production %m/m	0.6	-0.2	0.8	0.5
Industrial Production %y/y	1.7	-0.6	2.3	1.4

Spain	Latest Value	Prior Value	Change	Survey (Expectation)
Composite PMI	52.7	54.8	-2.1	54.1
GDP growth %q/q	0.6	0.7	-0.1	0.7
Industrial Production %m/m	0.5	1.3	-0.8	1.9

Retail Sales growth %y/y	-0.4	2.6	-3	0.3

Italy	Latest Value	Prior Value	Change	Survey (Expectation)
Consumer Confidence	115.2	116.1	-0.9	113.3
GDP growth %q/q	0.17	0.276	-0.106	0.2
Industrial Production %m/m	0.5	0.8	-0.3	0.4
Industrial Production %y/y	1.71	2.2	-0.49	N/A
Retail Sales growth %y/y	1.5	0.79	0.71	0.05

Minutes for the July ECB meeting showed that members believed that the first half slowdown in economic growth would prove to be temporary. While growth was expected to remain positive, recent trade issues were seen as the greatest risk to growth although their impact to date was seen as muted.

Economic sentiment indicators across Europe began to improve through October suggesting that growth could indeed improve through the second half of the year. Eurozone GDP growth looks to have stabilized in August with the Eurozone Aggregate Composite PMI edging up slightly, to 54.4, a level consistent with 2% growth. While core inflation missed the mark in August, falling from 1.1% in July to 1% last month, the ECB is unlikely to be worried by the figures, as the headline figure, currently at 2%, remains close to its inflation target. This, along with the stabilization in growth, should help the ECB to justify the end of QE at the end of the year.

UK Economics and Rates

UK	Latest Value	Prior Value	Change	Survey (Expectation)
Average Weekly Earnings ex bonuses %m/m	2.4	2.5	-0.1	2.5
CBI Reported Sales	29	20	9	15
CBI Trends Selling Prices	15	13	2	N/A
Claimant Count Rate	2.5	2.5	0	N/A
Composite PMI	53.6	55.2	-1.6	54.9
Construction Output %m/m	1.4	2.9	-1.5	-0.4
Construction PMI	52.9	55.8	-2.9	52.8
Consumer Confidence	-7	-10	3	-9
Core CPI y/y	1.9	1.9	0	1.9
CPI m/m	0	0	0	0
CPI y/y	2.5	2.4	0.1	2.5
GDP UK Chained 2009 %Q/Q	0.4	0.2	0.2	0.4
Halifax House Price Index %m/m	1.4	0.9	0.5	0.2
Headline Retail Sales %m/m	0.7	-0.5	1.2	0.2
Industrial Production %m/m	0.4	-0.2	0.6	0.3
Mortgage Approvals	64.768	65.374	-0.606	65
Retail Sales ex Auto Fuel m/m	0.9	-0.6	1.5	0
Services PMI	53.5	55.1	-1.6	54.7
UK Business Investment %q/q	0.5	-0.4	0.9	0.4
UK Labour Force Employment Change q/q	42	137	-95	93
Unemployment Rate %	4.13	4.23	-0.1	N/A

The Bank of England raised rates by 0.25% at its meeting towards the end of July. Given its forecast for future unemployment and the level of the output gap, it appeared to suggest that more rate increases might be forthcoming than the two rate rises discounted by the market over the next three years. The general assumption in the market however was that the next rate rise was unlikely to occur before greater clarity was evident in relation to the outcome of Brexit negotiations. It was rumoured that Bank of England Governor Mark Carney might extend his planned departure date beyond June 2019 to promote a smooth path around Brexit and provide continuity through any subsequent negotiations or upheaval. This was subsequently confirmed in early September.

The summer recess in parliament meant little progress was made in Brexit negotiations. The probability of no deal being agreed between the UK and the EU prior to the UK's official exit in March was seen as having increased in the view of Mark Carney and UK International Trade secretary Liam Fox. Investors' perceptions appeared similar as sterling experienced renewed weakness. There was some counterbalancing of the growing pessimism towards month end when Michel Barnier, the EU's chief Brexit negotiator indicated the EU was willing to offer the UK a partnership like none ever proposed to another country.

Asian Economics and Rates

Japan	Latest Value	Prior Value	Change	Survey (Expectation)
Bank Lending Growth %y/y	2	2.1	-0.1	N/A
Capital Spending Growth %y/y	12.8	3.4	9.4	3.1
Composite PMI	51.8	52.1	-0.3	N/A
Construction PMI	52.5	52.3	0.2	N/A
Consumer Confidence	43.3	43.5	-0.2	43.8
Core CPI %y/y	0.3	0.2	0.1	0.3
Economy Watchers Current Reading	46.6	48.1	-1.5	48
Economy Watchers Outlook Reading	49	50	-1	49.9
Exports %y/y	3.9	6.7	-2.8	6.3
GDP Annualized %Q/Q	1.9	-0.9	2.8	2.7
Headline CPI %y/y	0.9	0.7	0.2	1
Household Spending %q/q	0.7	-0.2	0.9	0.7
Imports %m/m	14.6	2.6	12	14.2
Industrial Production %m/m	-0.1	-1.8	1.7	0.2
Leading Index	104.7	106.9	-2.2	103.5
Machine Orders %m/m	-8.8	-3.7	-5.1	-1
Retail sales %m/m	0.1	-1.7	1.8	0.2
Services PMI	51.3	51	0.3	N/A
Tertiary Index %m/m	-0.5	0.2	-0.7	-0.3
Unemployment Rate %	2.37	2.47	-0.1	N/A

China	Latest Value	Prior Value	Change	Survey (Expectation)
Caixin Composite PMI	52.3	53	-0.7	N/A
Caixin Manufacturing PMI	50.6	50.8	-0.2	50.9
Caixin Services PMI	52.8	53.9	-1.1	N/A
Exports CNY %y/y	6	3	3	5.55
Fixed Asset Investment Growth %y/y	5.5	6	-0.5	6
GDP SA q/q	6.7	6.7	0	
Imports CNY %y/y	20.9	6	14.9	12.5
Industrial Production %y/y	6	6	0	6.3
Industrial Profits %y/y	16.2	20	-3.8	N/A
Loan Growth CNY bn	1450	1840	-390	1275
Official Manufacturing PMI	51.3	51.2	0.1	51.3
Retail Sales %y/y	8.8	9	-0.2	9.1

Japanese GDP returned to positive growth in the second quarter, rising at a strong 1.9% q/q annualised, indicating that Japan's economy has recovered somewhat from the brief slump it experienced at the start of the year. The solid GDP figure was driven by higher consumer spending and capex, the two central components of domestic demand. This trend appears to have continued well into Q3, with capital spending growth rising 12.8% year-on-year in August.

The recent acceleration of growth in employee compensation is also worth highlighting. Wage growth at the end of the second quarter was running at a solid +3.6% year-on-year. This should eventually exert some upward pressure on the inflation rate which is currently at 0.9% for headline and 0.3% for core, with improvement in the underlying trend already visible since the start of the year.

Irish Economics

Ireland	Latest Value	Prior Value	Change
Composite PMI	56.8	58.1	-1.3
Consumer Confidence	107.63	102.13	5.5
CPI %m/m	0.4	0.1	0.3
CPI %y/y	0.8	0.4	0.4
GDP SA q/q	-0.6	-0.6	0
Imports %y/y	-1.1	-1.1	0
Industrial Production %m/m	2.9	-8.8	11.7
Live Register Level SA (000s)	217.7	219.9	-2.2
Manufacturing PMI	57.5	56.3	1.2
Monthly Seasonally Adjusted Trade Surplus	4053.5	5222.2	-1168.7
Property Prices %q/q	1.1	0.7	0.4
Retail Sales %m/m	6.5	-1.55	8.05
Services PMI	57.4	59.5	-2.1
Unemployment %	5.6	5.8	-0.2

Irish GDP data show that GDP fell by -0.6% in the first quarter but grew 9.1% year-on-year. Capital investment exhibited an increase of 0.6% q/q while Personal Consumption expenditure increased by 2.7% year-on-year. Exports decreased by 5.8 per cent in Q1 2018 compared with Q4 2017, which, when combined with an import decrease of 2.5 per cent meant overall net exports for the quarter declined by 13.2%.

Official figures released this month showed that in the year to June, residential property prices (houses and apartments combined) at a national level rose by 12.0%, down from a year-on-year rise of 12.4% in May. In Dublin, residential property prices increased by 9% in the year to June. Dublin house prices increased 8.4% whereas apartments rose 12.8% in the same period. Residential property prices in the Rest of Ireland were 15.2% higher in the year to June.

An Exchequer deficit of €277 million was recorded to end-July 2018. This compares to a surplus of €3,366 million in the same period last year. When adjusted for the impact of the AIB share sale in June 2017, the Exchequer balance shows an underlying annual decrease of €210 million. This decline in the Exchequer balance was primarily due to an increase in expenditure (both voted and non-voted), albeit somewhat offset by increased tax revenue. Tax revenues of €29,689 million were collected to end-July 2018, an increase of 5.5% or €1,555 million on end-July 2017. This was in line with profile, up 0.6% or €174 million.

Bonds

The Merrill Lynch Eurozone Government bond index >5 years posted a loss of 0.65% in August giving a flat return for 2018 of 0.0% so far. A crisis in Turkey following US trade sanctions resulted in a large sell off in the Turkish Lira with spill over into other EM countries and Eurozone bond markets.

A spat between the US and Turkey over the arrest of an American pastor in Turkey resulted in the US implementing trade sanctions on Turkey. As a result the Turkish Lira sold off by about 50% which together with question marks over the independence of the Turkish Central Bank caused a risk off rally in most markets. 10 year German bond yields dropped to 0.28% while even 10 year US Treasury yields reached a low of 2.8%. In the Eurozone the Italian bond market was at the receiving end of the risk off mode especially as at the same time doubts about the 2019 Italian budget remained. The 10 year Italian Government bond yield spread over Germany widened to 288bps with 10 year Italian bonds yielding in excess of 3%.

During the last week of August positive news emerged from NAFTA negotiations with the US agreeing new terms with Mexico and looking close to an agreement with Canada. At the same time leading indicators such as PMI's and the German Ifo reinforced a message of ongoing good economic growth. With the Turkish issue fading into the background and the US Federal Reserve affirming its path of gradual rate hikes bond yields started to rise into month end with 10 year German bond yields temporarily back up at 0.4% but finishing the month at 0.33%.

Emerging Markets

Emerging markets slipped -0.5% (-2.1% in €), continuing the trend seen throughout most of the year that seemed to pause last month. Despite a strengthening in economic data and a strong Q2 earnings season, markets remained influenced by developments in Turkey and Argentina. Risk aversion due to fluctuating trade rhetoric also weighed on EM equities throughout August. Brazilian markets also fell -11.3% during the month as election jitters set in, compounded by the aforementioned Turkish and Argentinian woes. Latin American markets were the worst performing region with a fall of -8.8% over the last month, followed by Emerging European Markets at -7.8% and Asia at -1%.

Corporate Bonds

The Bloomberg Barclays Euro Aggregate Corporate Index generated excess returns of -44bp in August, bringing year-to-date excess returns to -123bp. August total returns were +1bp. Top-performing sectors were: Construction Machinery, Chemicals and Technology. Bottom-performing sectors were: Transportation, Insurance and Electric Companies.

Commodities

Commodities rose 1.1% (1.6% in €) with WTI oil up 1.5% and Brent up 5.6%. Energy saw an upbeat month with WTI crude up 1.5% and Brent up 5.6%. The first half of the month saw energy prices correct by approximately 4%, but later in the month news on weaker US weekly inventories and reduced Iranian crude shipments helped prices rebound. Industrial metals were down -3%, pulled back by EM weakness, a stronger dollar and rising trade tensions. Precious metals also underperformed with gold prices falling for the fifth month in a row, decreasing by -1.7% to $1,201/oz. amidst a modestly stronger dollar. Agricultural prices fell -3.5% with grains down up -3.2%. Livestock prices fell by -0.5% during the month.

Source: ILIM 5th September