Market Watch

January Review 2018

Latest monthly commentary from the Investment Markets Research team at BT.

Led by US and Asian markets, world markets roared into the New Year, although late in the month, caution crept back into markets after one of the best starts to a year in recent history. It was the best start to a year for the broad US benchmark, the S&P 500 index, since 1987. The story driving the markets continued to be improving company earnings and synchronised global economic growth. On the back of this outlook, January saw significant boosts to growth forecasts for 2018.

Developments in Financial Markets

Australian Shares
In Australia, the S&P/ASX 200 Accumulation index eased 0.4%, although its Resources sub-index managed a 0.8% gain. Slicing and dicing the sectors and capitalisation levels, the only other sub-category to record a gain was the S&P/ASX Mid-Cap Industrials Accumulation, which returned 0.1%.

In contrast, the S&P/ASX 200 Industrials Accumulation shed 0.7%. The S&P/ASX 200 Accumulation A-REIT (real estate industrial trust) index dropped 3.3% for the month.

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International Shares

Markets reacted enthusiastically to the improving outlook. On a total return basis, the Dow Jones Industrial Average surged 5.9% in January, while the S&P 500 Index gained 5.7% and the technology-heavy Nasdaq Composite Index surged 7.4%. In Europe, the Euro Stoxx 600 index was up 1.7%, the DAX in Germany was up 2.1% and, on a price basis, the CAC 40 in France ended 3.2% higher. London’s FT 100 index went against the trend, shedding 2.0%.

In Asia, Japan’s Nikkei index added 1.5% in total return, and the Hang Seng Index in Hong Kong powered to a 9.9% price gain, its biggest monthly jump since April 2015. The Hang Seng China Enterprises index, which tracks the performance of mainland stocks listed in Hong Kong, climbed over 16% in the year to January.

On the mainland, the Shanghai Composite Index gained 5.3%. South Korea’s KOSPI index added 4.0%.

Fixed Interest

US and European yields rose substantially as bonds were sold off on anticipation of the end of stimulus from major central banks. The yield on the key 10-year US Treasury bond hit a four-year high at 2.75%, before closing the month 30 basis points (bps) higher at 2.71%. The US two-year yield rose by 26 bps to 2.14%, while the 30-year yield added 20 bps to 2.94%.

In Europe, German 10-year yields climbed 27 bps to 0.69%, while the German 5-year yield turned positive, to the tune of 0.002%, for the first time since December 2015. The French 10-year yield gained 19 bps to 0.97%, while its UK counterpart increased by 32 bps to 1.51%. The Japanese 10-year yield reached a seven-month high of 0.095% toward the end of January.

Currencies

The Australian dollar gained 3.1% against the greenback, which also lost ground against the Euro, the Yen and the Pound. News of a record high in the UK employment rate pushed sterling to a post-Brexit referendum peak against the US dollar, rising through US$1.40 towards month-end.

The ICE dollar index, which measures the US dollar against a basket of six other major currencies, posted its worst January in three decades, losing 2.6% and sinking to a three-year low by the end of the month.
Commodities

On the commodities markets, Brent crude oil gained 3.3% and West Texas Intermediate (WTI) rose by 7.1% in January, in oil's strongest start to a year in five years. Gold appreciated by 2.8% in US dollar terms, while iron ore added 1.2% to $US71.61 a tonne, and copper eased by 3.2%. The Bloomberg Commodity Index was 1.9% higher for the month.

Global Economic Outlook

Australia

Australian households became more confident in the economy in January, with the Westpac-Melbourne Institute Consumer Sentiment Index reading jumping from 103.3 in December to 105.1 in January. (A number above 100 indicates the number of consumers who are optimistic exceeds the number of consumers who are pessimistic). The long-term average reading for the Index is just over 101. Whether measured by the Westpac-Melbourne Institute survey or the ANZ-Roy Morgan survey, Australian consumer confidence is at its highest level in more than four years. Part of the explanation for the improving confidence lies in the labour market. The Australian economy posted its fifteenth consecutive month of employment gains in January, as the December employment estimates by the Australian Bureau of Statistics (ABS) showed employers boosting both full-time and part-time positions.

The streak equals the 15 months of job gains the economy achieved between May 1993 and July 1994. The total number of people employed in Australia (in either full-time or part-time work) increased by 34,700 in December, well ahead of market expectations for 15,000 new jobs.

The Westpac-MI Leading Index jumped to its highest level in more than a year in December, pointing to the likelihood that Australian economic growth would accelerate sharply in the first half of 2018. The index’s six-month annualised growth rate, a guide to the likely pace of economic activity looking three to nine months into the future, rose to 1.41%, from 0.66% in November. At that level, it suggests Australian economic growth is likely to be 1.41 percentage points above its trend level, which is seen as about 2.75% a year. The Ai Group’s Australian PMI came in with a positive result at 58.7 points in January, up 2.5 points from the level reported in December.
United States

The National Retail Federation (NRF) trade group said that by its measure, which excludes sales from autos, gas and restaurants and includes non-store sales like those from catalogues, US holiday spending rose a stronger-than-expected 5.5%, to $US691.9 billion ($887 billion), the biggest increase since the 5.2% gain in 2010. Online shopping, which was included in the NRF figure, surged by 11.5%, to $US138.4 billion ($177 billion). Spending for November and December combined was the strongest since 2005, according to economic and financial data compiler IHS Markit. The IHS Markit US Manufacturing PMI came in at 55.5 in January, compared to 55.1 in December (a figure above 50 shows expansion). The Composite PMI (which includes services) was 53.8, down from 54.1 in December, but recorded its 23rd consecutive month above 50.

The US economy expanded at a 2.6% annual rate in the fourth quarter of 2017, to grow 2.3% for the year, up from the 1.5% growth in 2016. The IMF lifted its forecasts for US growth from 2.3% to 2.7% in 2018, and from 1.9% to 2.5% in 2019.

Asia

The National Bureau of Statistics’ official Purchasing Managers’ Index (PMI) for the Chinese economy declined from 51.6 to 51.3, an eight-month low, but still above the 50-point level that divides growth from contraction. However, the non-manufacturing side of the Chinese economy appears to be holding up, expanding for a third consecutive month on the back of a pick-up in service sector growth. China’s final official GDP growth figure for 2017 was 6.9%, which beat Beijing’s target of 6.5%. Beijing will release its 2018 growth target next month. Japan’s factory output grew by 1.8% in the December quarter, rising for a seventh straight quarter. The country’s manufacturing sector’s strong momentum carried through into 2018, growing at its fastest pace in almost four years in January. The Nikkei-Markit Japan manufacturing PMI rose to 54.8 in January from 54.0 in December, as new order growth rose for a third consecutive month. South Korea’s manufacturing PMI returned to expansion in January.

Europe

The Eurozone economy ended 2017 with the strongest growth in almost seven years, with gross domestic product (GDP) rising by 0.8% for the December quarter, to make 2.5% annual growth, well ahead of the 1.8% posted in 2016. The December quarter saw the strongest factory output increase in Europe since 2000, helped by a steep increase in service sector activity and a near-record expansion of manufacturing production. Eurozone growth was stronger than in the US and well ahead of the UK, which recorded growth of 1.8%, Britain’s weakest annual rate since 2012. A particular highlight was the French economy, long a laggard in Europe, reporting its fastest growth in six years in 2017, expanding by 1.9%. Meanwhile the largest Eurozone economy, Germany, grew by 2.2% in 2017, also marking its fastest rate of expansion since 2011.