market analysis: May 2011

6 June 2011

May has been a difficult month for equity markets with poor economic data from the US and the UK and fears that a second round of bailouts will be required in the Eurozone. The largest losses were seen in Europe, with the EuroStoxx 50 index down 5%. Reports suggest that a second bailout of Greece is now highly likely in the coming months, whilst analysts are keeping an eye on the situation in Spain and Italy.

Looking at market performance over a longer period, equities have continued to be volatile and provide gains one month followed by losses the next. The FTSE 100 and EuroStoxx 50 are both at similar levels seen at the end of 2010, whilst the Dow Jones is up over 8% and the Nikkei 225 is down over 5% compared to the 2010 year end.

In the US and UK, a variety of economic data released last month suggested that the recovery was not proceeding according to plan. In the US, unemployment rose and manufacturing output fell, whilst in the UK independent analysts cut their growth estimates for the economy in 2011, with some suggesting a figure of 1.2% was likely, a full 0.8% below the 2% forecast by the Bank of England.

According to recent data, both the UK and US economies appear to be struggling. The respective governments in the UK and US have adopted different policies in order to aid the recovery; In the UK the cuts have been deep and immediate, whilst in the US there have been some cuts but on the whole the policy has been to continue spending in order to prop up the economy.

One effect of the possibility of a further Eurozone bailout was an increased appetite to hold US Dollars, the world's traditional reserve currency, with the Euro down against the US currency by over 3%. Most commodities fell in value, with the price of a barrel of oil down over 9% as a result of diminishing global growth prospects.

Key Data	29 April	31 May	+/(-)%
FTSE 100	6,069.90	5,989.99	(1.3)
Dow Jones	12,810.54	12,569.79	(1.9)
EuroStoxx50	3,011.25	2,861.92	(5.0)
Nikkei 225	9,849.74	9,693.73	(1.6)
Hang Seng	23,720.81	23,684.13	(0.2)
MSCI EM	1,204.03	1,167.97	(3.0)
Crude Oil	$113.35	$102.70	(9.4)
£ = $	1.671	1.645	(1.6)
Euro = $	1.484	1.438	(3.1)
£ = Euro	1.126	1.144	1.6

Interest Rates	
Bank of England Base Rate	0.5%
ECB Refinancing Rate	1.25%
US Fed Funds Target Rate	0.00% -0.25%

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UK

The latest inflation figures saw the Consumer Price Index (CPI) rise to a 30 month high of 4.5%. This latest rise has been blamed on increases in the cost of tobacco, alcohol, air and sea travel. Despite its mandate of keeping inflation at 2%, the Bank of England expects inflation to top 5% before the end of 2011, with rises anticipated in the price of utility bills.

EUROPE

Despite worries about some of the Eurozone countries requiring bailouts, economic growth in the Eurozone has actually accelerated at a faster pace than in the UK and US, powered primarily by strong results from Germany. GDP growth in the first quarter of the year was 1.5% in Germany and 1% in France, whilst even Greece returned a positive growth figure of 0.8% (more than the UK's 0.5% over the same period). Overall, GDP growth in the first quarter across the Eurozone was 0.8%.

US

One of the most important economic indicators in the global economy is the monthly unemployment data from the US. May was a disappointing month for unemployment figures, with the overall rate up to 9.1% and the fewest number of new jobs started in eight months. With unemployment remaining stubbornly high, there is a danger that any recovery will not affect the general population.

ASIA/PACIFIC

Given the tragic events in March, the news that Japan had slipped back into recession following negative GDP growth in the last quarter of 2010 and first quarter of 2011 was perhaps unsurprising. GDP fell 0.9% in the first quarter, more than twice the estimate of many economists. Initial calculations of the cost of the damage sustained during the earthquake and tsunami vary between $196 and $306 billion and the government is likely to finance much of the rebuilding cost.

EMERGING MARKETS

One commodity not usually widely reported but which can have a devastating impact, especially in emerging markets, is the price of basic foodstuffs. The most widely consumed foods are maize and rice and the price of both can be greatly affected by drought or crop failure in just one major supplier. The general price of most foodstuffs has been rising over the last 12-18 months adding to inflationary pressures in every economy with many global analysts expecting the trend to continue as the global population increases.