

August 2017

Market Bulletin

Downton & Ali Associates



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This update comes to you from
T. Rowe Price

August's biggest story was the strength of global economy, which surprised on the upside.

China's official Purchasing Managers' Index (PMI) figure was at 51.7 for the month, exceeding expectations (any reading above 50 indicates expansion, while a number below 50 indicates contraction). Business activity also remained robust in the US and the Eurozone, albeit slowing slightly in the latter's case. This is unusual: since the global financial crisis, there have only been a few occasions when the three major drivers of the global economy have simultaneously shown strong growth momentum.

The apparent robustness of the global economy is particularly interesting given the volatile nature of geopolitics at the moment. Growing anxiety over North Korea's nuclear capability, which might be expected to unsettle investors, has so far had negligible impact on growth and financial markets. This is probably because large-scale central bank asset purchases have left most investors holding a lot of cash on their balance sheets. At times like these, investors tend to buy quickly at any signs of a slowdown, ensuring

sell-offs are short-lived and maintaining macroeconomic stability.

Will it last? We have our doubts. Chinese growth is likely to slow towards the end of the year as the authorities ramp up their efforts to regulate the financial system once the 19th Party Congress has taken place in November. A slowing China will negatively impact the Eurozone, while Federal Reserve tightening and the prospect of policy gridlock could dampen US growth.

Indeed, developments in the US are likely to be the major story of the autumn. The beginning of Federal Reserve balance sheet contraction, although widely-anticipated, will need to be managed carefully to avoid a repeat of 2013's 'taper tantrum' (when reports of Fed tapering caused investors to flee bond markets, sending yields soaring and prices plummeting). At the same time, Congress has an enormous September to-do list, including finding agreement over proposed tax reforms, increasing the debt ceiling and passing a new budget plan – while simultaneously channeling aid to the victims of Hurricane Harvey. If negotiations don't go well, the prospect of a government shutdown and the US defaulting on its debt has the potential to cause widespread panic in markets.

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So while the overall growth picture is positive and the markets remain calm – for now – North Korea, internal political developments in China and the US have the potential to cause turbulence over the next few months.

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