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Markets Update: 25th August 2015

- Global equity markets have fallen -9.7% in local currency terms over the last four trading days to the close of markets on Monday 25th August. The fundamental cause of the fall in markets has been concerns over the growth outlook in China and its possible implications for global growth while selling pressure has been exacerbated by hedge funds reducing exposures.

- While growth in China has been slowing since last year, concerns were raised further over the extent of the slowdown when on August 10th the Chinese authorities allowed the Chinese currency, the renminbi, to devalue by approx. 3%. As a result of the devaluation, investors became overly focused on the possibility that China was seeking a lower currency to boost growth and exports because growth was slowing much more rapidly than expected and thus viewed it as a signal of a deteriorating Chinese economy. Given that China has been one of the principal drivers of global growth in recent years, a significant slowdown could have negative implications for the global growth outlook and equity markets.

- The Chinese authorities have introduced a number of fiscal and monetary stimulus programmes in recent years to support growth and further stimulus measures are expected. While growth has slowed from the 8%+ pace evident in previous years even using unofficial as opposed to official estimates growth remains relatively strong and the authorities remain determined to avoid a hard landing in the economy.

- Outside China, developed market growth has remained more resilient and leading economic indicators suggest growth is running around 2%-2.5% in the US, 2.5%-3.0% in the UK and 1.5%-2.0% in the Eurozone.

- Even with lower growth in China, risks of a significant global slowdown or recession are low and thus recent moves in equity markets appear overdone. If global growth were to show signs of slowing, policy responses would be expected from authorities which would be supportive of economies and markets. In particular, additional monetary stimulus could be expected from the ECB and the Bank of Japan while the US Federal Reserve and the Bank of England could also be expected to delay anticipated interest rate increases.

- Equity markets have become more volatile over the last 12 months, reacting to various stress points which arise from time to time. Currently, markets are experiencing such a bout of increased volatility and uncertainty relating to concerns over Chinese growth. While growth is slowing, available data does not suggest China is about to experience a hard landing and thus it would appear markets have overreacted to developments in Chinese economic news flow and movements in its currency. While possibly remaining volatile in the short term, some stabilisation and ultimate improvement in markets should be evident as investors' confidence in the growth outlook for the Chinese and global economies improve.

- Overall, we believe recent markets falls have been an overreaction to the Chinese news flow and while some volatility could remain, ultimately markets should reverse the moves seen over the last few days and in fact European and US markets have opened up strongly today, August 25th.

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