CENTRAL BANKS SIT ON THE FENCE IN THE FACE OF CONFLICTING SIGNALS

This week investors may be forgiven for feeling slightly wrong-footed by the latest economic data. Several indicators appear to contradict what is going on with consumers in the UK and the US. May retail sales in the UK fell by 2.7% from April and consumer borrowing on credit cards increased noticeably. However, consumer sentiment has improved, with expectations about personal finances notably better. The picture for the US is similarly muddled as consumer confidence jumped from the record low seen in April and May, but retail sales fell far more than expected.

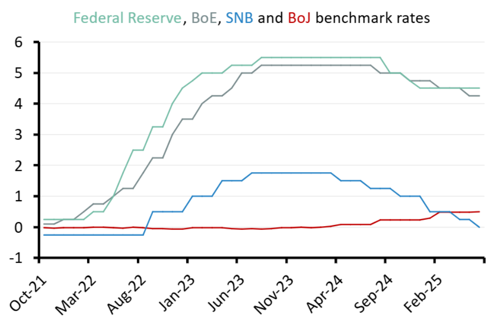
Meanwhile, inflation in the UK cooled as CPI slowed to 3.4%. The decline was caused by a decline in some services prices, which have been pretty robust – but there was an increase in the price of many non-food goods. This is a reversal of the last two years where services have been the driver of high inflation, as goods prices moderated. Against this backdrop many central banks have decided that the best course of action, in the short term, is do nothing and wait for the picture to become clearer.

THE MARKETS THIS WEEK

FTSE 100	S&P 500	Nikkei 225	STOXX 600	Hang Seng	US 10 Yr	UK 10 Yr	Brent Crude	Gold	Copper	GBP USD
+0.01	+0.79%	+1.42%	-0.97%	-1.60%	+0.06%	+0.03%	+4.18	+1.39	+1.74%	-0.48%

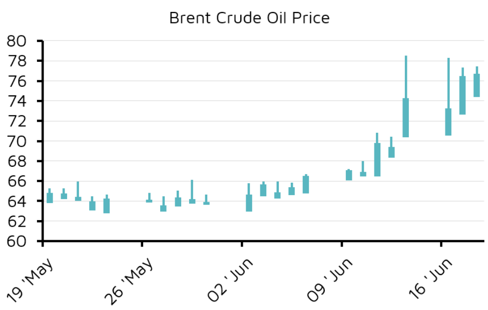
RATES: CENTRAL BANKS FACTORING US TARIFFS INTO RATE DECISIONS

The Federal Reserve held its interest rate steady this week, worried about US tariffs' potential to push up inflation. Chair Jerome Powell expects GDP growth to slow to 1.4% this year, in tandem with a rise in unemployment from 4.2% to 4.5%. The Fed expects its favourite inflation measure, PCE which tracks household expenses, to move up from 2.1% to 3%.



US tariffs are also being factored into other central bank decisions. The Bank of England held rates as UK inflation remains above target, and it deemed its quarter-point cut in May as sufficient to counter rising tariffs. The Swiss National Bank delivered a 0.25% cut, to bring its benchmark rate to zero, to alleviate pressure off the Swiss franc which has rallied recently due to its haven status. Swiss inflation has turned negative. The Bank of Japan held short-term rates at 0.5% but has had to slow its withdrawal of economic stimulus by buying Japanese government bonds following high volatility in global bond markets.

ENERGY: OIL SPIKES ON FEARS OF MIDDLE EAST SUPPLY DISRUPTION

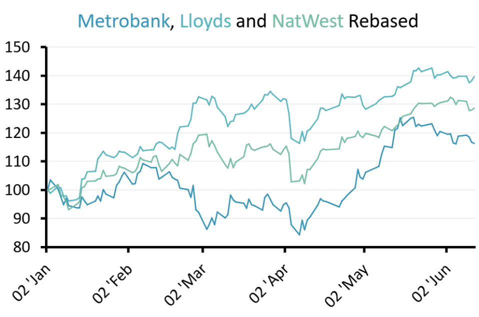


Crude oil prices were volatile as traders gauged the probability of US involvement in the Israel-Iran war. A particular concern is closure of the key shipping route through the Strait of Hormuz, through which a quarter of the world's oil flows. Brent crude spiked 8% to as high as $78 per barrel following Israel's surprise attack on Iran last Friday. The world's largest publicly-listed oil tanker company, Frontline, immediately suspended taking contracts to sail into the Persian Gulf. Insurance premiums have jumped over 60% for ships on this route and a collision between tankers in the Gulf of Oman, right out of the strait, fuelled fears of electronic interference with ships' navigation systems.

The Brent crude price has been volatile but moves this week have been more moderate after the initial spike from $66 at the start of last week. An increase in production may be keeping a lid on price movements. The International Energy Agency expects global production to outstrip demand by 1.1m barrels per day this year.

BANKS: UK MID-LEVEL BANKS ATTRACT TAKEOVER INTEREST

The UK banking sector is experiencing a pick-up in M&A activity. Spanish bank Sabadell is looking to offload its UK operation TSB as it tries to fend off a hostile takeover approach from Spanish rival BBVA. Barclays has apparently expressed an interest in its smaller UK rival and Santander is also tipped as a potential buyer. Shares in Metro Bank surged higher following reports of a takeover bid from US private equity firm Pollen Street Capital. Pollen Street owns UK-lender Shawbrook which has previously expressed an interest in a merger. The rumoured takeover approach pushed shares up Metro Bank up 15%. Metro Bank is continuing its turnaround since it was forced to raise emerging funding in 2023 and its shares are up more the 250% over the last 12 months.



Meanwhile higher interest rates have generally helped support earnings and profits among UK banks. Following years of underperformance, rising interest rates since the Covid epidemic have helped boost bank profits.

Data sourced from Investing.com, Bank of England, Bank of Japan, Federal Reserve and Swiss National Bank