WHY ITS TIME TO REVIEW MONETARY POLICY INDICATORS

This week the world has been focused on those two hardy perennials, Trump and Brexit. The former for being racist and the latter for parliament acting to contain the new prime minister. At this point however, these events hardly qualify as news. Instead we've been taking a closer look at the finer points of monetary policy. Following the Fed Chairman's admission that the link between economic growth and inflation might not be what it was, we find multiple instances of central banks rethinking their approach. The European Central Bank is looking at revising its 2% or below rule to be more accommodating of above target inflation, while there is also speculation a Labour government could increase the BofE's 2% target in the future.

While the acknowledgement that perhaps an overzealous approach to inflation has been detrimental is welcome, New Zealand have gone a step further and dropped GDP as a measure of the economy in favor of a happiness and wellbeing index. While this isn't strictly monetary policy, it is another sign that the economic orthodoxy of the 20th century is coming to an end. Old models of rates and inflation, if not broken already, will need to be scrapped.

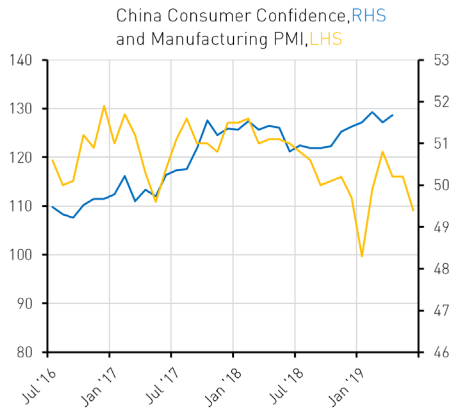
THE MARKETS THIS WEEK

FTSE 100	S&P 500	Nikkei 225	Euro Stoxx 50	Hang Seng	US 10 Yr	UK 10 Yr	Brent Crude	Gold	Wheat	GBP USD
+0.46%	-0.16%	-0.82%	+0.43%	+1.03%	-0.08%	-0.09%	-7.32%	+2.08%	-7.23%	-0.40%

CHINA: IS SLOWING GDP GROWTH BAD NEWS?

Much attention has been paid to China's recent slowdown, growth in Q2 slipped to 6.2 per cent, with many commentators attributing falling growth figures to the impact of the trade war. This is too simplistic however; Chinese growth was expected to slow before Donald Trump was even elected. It has been transitioning from export orientated growth model to one of nurturing a burgeoning domestic economy over the few decades. While growth is at its lowest level in close to thirty years, maintaining this rate for the rest of the year would add $1.4tn to the $13.2tn economy – equivalent to the size of all the Scandinavian economies combined.

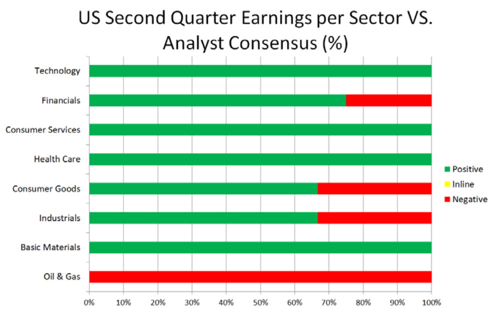
Even so, the question remains as to whether domestic growth can continue to offset export woes. So far, a growing middle class (400m) with increasing spending power have helped boost retail sales and consumer confidence remains high. However, trade tensions have started to bite. Both imports and exports have been declining on a quarterly basis and foreign demand looks set to be weak in the second half of the year.



US: WILL WE SEE AN EARNINGS RECESSION THIS QUARTER?

The big banks this week kicked off this quarter's earnings season and so far, the results have been fairly positive. Goldman Sachs and the Bank of America both beat expectations with the formers strong showing in the equities and lending divisions helping to offset the drag in the fixed income division, the latter benefiting from higher retail lending figures. In addition, Morgan Stanley profited from rising markets with its wealth management division beating analyst expectations by $60m with revenues last quarter from its investment arm coming in at $839m.

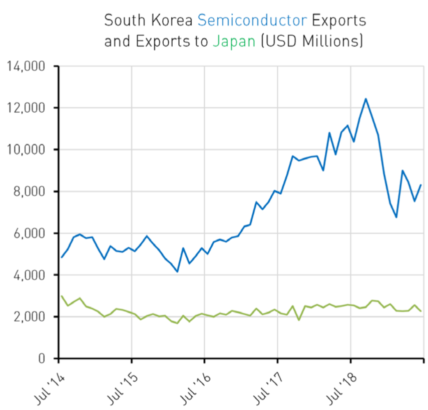
Only JP Morgan suffered, as low interest rates slashed away at lending margins. But with possible upcoming rate cuts, those banks whose income primarily derives from interest income (JPM, BoA, Wells Fargo) will most likely have to revise profit forecasts for 2019 downwards. Market sentiment towards corporate earnings remains cautious given the current weak outlook and a consecutive quarter of falling profits would lead to the first earnings recession since mid-2016.



ASIA: JAPAN-SOUTH KOREA TRADE WAR IS NOT ALL ABOUT CHEMICALS

A new trade war is brewing between two of the US's closest allies, Japan and South Korea. Tensions kicked off when Japan restricted the exports of certain chemicals to South Korea over "national security concerns" leaving the likes of SK Hynix and Samsung who require the materials for memory chip production in trouble. Memory chips accounts for a fifth of South Korea's exports and an extended embargo would squeeze the nation further. As a result, the central bank has moved for the first time in three years to cut interest by a quarter percentage point to 1.5%.

In reality, the row has nothing to do with national security concerns but is caused by a longer running dispute. South Korea feel that Japan haven't atoned enough for its occupation of the country between 1910-1945. Last year South Korea ordered Japanese companies to pay $90,500 to each forced labour worker. Japan believe the compensation issue has already been resolved in the 1965 treaty when it provided $300m in economic aid and further loans totalling $800m.



Data Sourced from FE Analytics, and Bloomberg Finance LP