The Week in Perspective

22 February 2019

Market Roundup

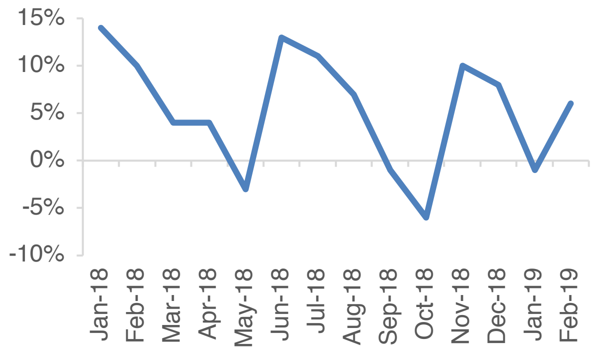
Large-cap UK equities battled the dampening effect of a stronger pound this week, as the currency has responded to reports about an increased chance of a Brexit deal. The more domestically-focused FTSE250, which is not as exposed to currency pressures, consequently enjoyed a better week. The FTSE100 fell slightly on Monday, retreating from the four-month high it hit the previous week. The blue-chip index finished down by 0.2%, while the FTSE250 rose by 0.7%. The US market was shut for President's Day but there were reports that progress was being made in the trade talks between the US and China, which buoyed sentiment. Tuesday was another negative day, with the pound rising and the FTSE100 falling by 0.5%, even as data emerged showing unemployment remaining at a record low and wage growth at its highest since the financial crisis. Equities rose on Wednesday, with the FTSE100 up 0.7% at 7,228. The solid gains came despite the competition regulator voicing concerns about proposed merger between Sainsburys and Asda. Sainsbury shares fell 18.5% on the news. The FTSE100 had another down day on Thursday, losing 0.85% to close at 7,167, but the FTSE250 closed up by 0.18%. Once again, a resilient pound acted as a drag on the FTSE100. In early trade on Friday both the FTSE100 and FTSE250 were heading up.

Company Focus: BAE Systems

BAE Systems warned on Thursday that Germany's ban on arm sales to Saudi Arabia could hit its Saudi contracts for Eurofighter Typhoon jets. Announcing the defence company's full-year results, chief executive Charles Woodburn said it was "working closely with the UK government to minimise the risk of any such occurrence and the impact it would have on financial performance, the supply chain and relationships." The German government has tried to halt weapons exports to Saudi Arabia due to the killing of Saudi journalist Jamal Khashoggi in the Saudi consulate in Istanbul last October.

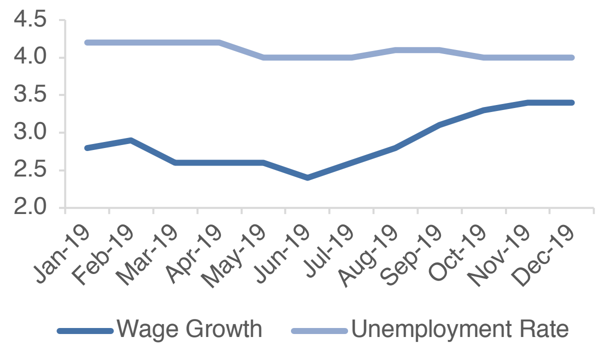
Britain's government has urged Germany to exempt big defence projects. Woodburn told journalists the commercial problem was currently minimal, but "could become more difficult". However, he emphasised that Saudi Arabia represented less than 15% of group earnings and that "it is not a cliff edge". The company's annual results showed an £8bn boost to orders to £28.3bn in the year to the end of December 2018. The company's order backlog grew from £38.7bn in 2017 to £48.4bn last year. Net debt rose to £904m and operating profit was up from £1.4bn to £1.6bn, but revenue shrank from £17.2bn to £16.8bn.

Chart 1: CBI Manufacturing Orders Survey



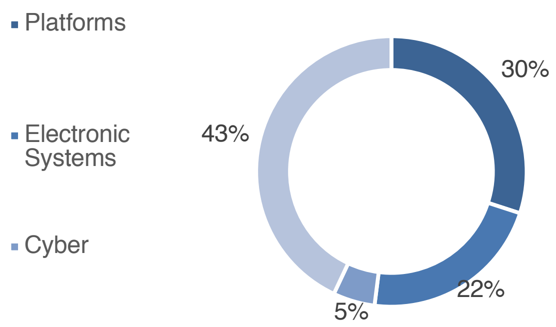
Source: Refinitiv Data at 21/02/2019

Chart 2: UK 3-months Wage Growth and Unemployment Rate



Source: ONS Data at 21/02/2019

Chart 3: BAE Systems – Revenue by division



Source: Brewin Dolphin client note Data at 21/02/2019

Economic Roundup

Britain's labour market continues to defy the seemingly endless gloomy news headlines about job losses. Just 24 hours after Honda said it would be closing its car plant in Swindon, the Office for National Statistics (ONS) released data showing that there were 167,000 more people in work in the final quarter of 2018 compared to the previous quarter. The employment rate, at 75.8%, remains at a record high, and wage growth continued at a healthy 3.4%, almost double January's inflation rate of 1.8%. The unemployment rate for the three months to the end of December was 4.0% but dipped below the 4% mark for women for the first time ever. However, this is likely to be because of the increase in the women's state pension age, which is making more women stay in work for longer. Nevertheless, taken together, the data suggests that the economic uncertainties surrounding Brexit are having less impact on employment decisions than was initially thought, even though business investment has been falling. This apparent contradiction is puzzling many experts, although some have speculated it is easier to reverse a hiring decision than it is to reverse a big investment such as the purchase of industrial machinery.

Separately, this strong wage growth is helping housing affordability improve more quickly than at any time since 2011, according to new analysis. Rapidly rising wages combined with a slump in house price growth is allowing earnings to slowly catch up with house prices, says Rightmove, the property group. Its latest monthly index shows that advertised prices were just 0.2% higher than a year before, the slowest growth since 2009. With wage growth of 3.4%, wages are outstripping house price growth by the biggest margin in eight years, bringing more property within reach of more buyers.

The UK manufacturing sector appears to be holding up relatively well as data this week suggested a rebound in February from the previous month. The Confederation of British Industry's (CBI) Industrial Trends Survey of 366 manufacturing firms revealed that a positive balance of +6% of companies said their order books were better than normal compared to those saying they were below normal. It is a substantial improvement on the negative -1% balance reported in January. However, commentators are still cautious. Anna Leach, the head of economic intelligence at the CBI, said that "UK manufacturing activity has moderated at the same time as headwinds from Brexit uncertainty and a weaker global trading environment have grown." Others said that one months' data did not indicate a trend. The report was released on the same day as the Make UK, a manufacturing body, said a no-deal Brexit would be "catastrophic" for the sector and could see many firms disappear overnight.

In good news for government finances, and appearing to back up the manufacturing survey, the Office for National Statistics said that the UK hit a record public sector surplus for January of £14.9billion. Samuel Tombs of Pantheon Economics said the data suggested the economy had not lost as much momentum as many surveys seemed to imply, posing more questions for analysts to ponder about what is really happening beneath the statistics.

Company announcements that caught our attention this week

Date	Company	Comment
20/02/2019	**Lloyds Banking Group**	Lloyds' chief executive expressed confidence in the UK's economic prospects as the bank announced plans to hand £4bn to shareholders. Britain's largest bank signalled its optimism by unveiling a £1.75bn share buyback and a 5% increase in its total dividend to 3.21p per share. The announcement came as Lloyds reported profit after tax of £4.4bn in 2018. This was up 24% on the year before but below analyst expectations. Operating costs fell even though the bank, which owns Halifax and Bank of Scotland as well as Lloyds, set aside £750m for PPI mis-selling claims. Lloyds confidence about the UK economy contrasted with rivals HSBC and Barclays, which also released their full-year results this week and sounded a more cautious note.
19/02/2019	**BHP**	BHP reported an 8% drop in underlying attributable profit to US$3.7bn (£2.8bn) in the second half of 2018 as the group's results were affected by several unplanned outages. The company revealed a $385m hit in the six months to December related to an iron ore train derailment in Western Australia, unplanned production outages at its Olympic Dam facility in South Australia and fires at its Nickel West smelter in Western Australia and Spence plant in Chile. The world's biggest listed miner announced it had cut its forecast for productivity gains to flat for the financial year, down from previous guidance of $1bn. The company declared an interim dividend of 55 cents a share, the same pay-out as a year earlier. BHP also said it was on track to generate $9bn of free cash flow in 2019, based on current commodity prices.

Key Company Diary Dates

Mon 25 Feb	**Bunzl**	Full-year results
Tue 26 Feb	**Croda International**	Full-year results
Wed 27 Feb	**Metro Bank**	Full-year results
Thu 28 Feb	**Rolls-Royce Holdings**	Full-year results
Fri 01 Mar	**WPP**	Full-year results

Economic highlights over the next week

Wed 27 Feb – Euro Area Business Climate Indicator – The business confidence index for the euro area tumbled to a two-year low of 0.69 in January from 0.86 in December.

Thu 28 Feb – Gfk Consumer Confidence – In January the consumer confidence index was stable at -14 as wider economic prospects continued to weigh on the overall score.

Fri 01 Mar – Manufacturing PMI – The latest reading of the Markit/CIPS UK Manufacturing PMI, an important indicator of confidence in the sector, was the second weakest since July 2016.

Index Movements*

Index	Value	%Change
FTSE 100	7,167	-0.41%
FTSE 250	19,237	1.79%
AIM	909	-0.31%
Dow Jones	25,851	1.62%
S&P 500	2,775	1.06%
Hang Seng	28,630	0.70%
Nikkei 225	21,464	1.54%

Currency Movements*

Currency Pair	Value	%Change
£:$	1.31	2.24%
£:€	1.15	1.59%
£:¥	144.59	2.19%

Best & worst performing sectors (rel. to FTSE 350)*

Sector	%Change
Technology	3.22%
Basic Resources	1.66%
Insurance	1.59%
Chemicals	1.34%
Financial Services	0.26%
Oil & Gas	-0.77%

Best & worst FTSE 100 performing stocks*

Company	%Change
Micro Focus Intl.	8.86%
OCADO GROUP	7.23%
Antofagasta	7.15%
RIGHTMOVE	-11.63%
Centrica	-13.12%
SAINSBURY J	-17.76%

*Weekly movements up until close of business Thursday