

MARKETS RALLY AS FED PAUSES RATE HIKES

This week the most impactful story came out of the US, when the Federal Reserve announced it was keeping interest rates steady. This is significant, because while official guidance is for three rate hikes in 2019, many believe the Fed is overly optimistic in its estimate of the strength of the US economy and needs to back off. The market was convinced this move was coming; now it's arrived a significant risk of disappointment has been removed. The impact is yet to be determined, monetary policy takes about 18 months to have an impact on the real economy.

Elsewhere the Brexit saga rumbled on. While there were a number of developments in parliament, none of them really mean anything and we expect to be back here again in two weeks' time. Fundamentally there is one basic choice to be made; leave Northern Ireland behind, or accept some sort of customs union. Without making this choice, no-deal is the default. We expect Theresa May to eventually push her deal through, but that ultimately just means this choice is delayed to the end of the transition period.

THE MARKETS THIS WEEK

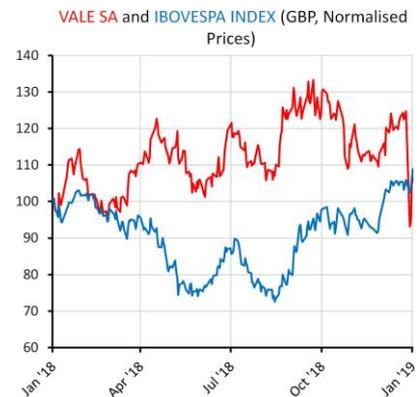
FTSE 100	S&P 500	Nikkei 225	Euro Stoxx 50	Hang Seng	US 10 Yr	UK 10 Yr	Brent Crude	Gold	Wheat	GBP USD
+2.73%	+2.34%	+0.07%	+0.01%	+1.31%	-0.13%	-0.08%	-1.26%	+1.38%	-0.29%	-0.72%



COMMODITIES: VALE UNDER SCRUTINY FOLLOWING SECOND DAM DISASTER

At the time of writing 99 people have died and a further 259 remain unaccounted for in what has been described as the worst labour disaster in Brazil's history, after a dam holding back iron ore by-product collapsed in a Vale facility last Friday. Around £15bn was wiped off market cap and share price plunged 24.5 per cent following the news. To compound matters class action lawsuits are already starting to filter through, while Brazilian prosecutors have quickly moved to seize £2bn in assets to ensure Vale pays for damages caused.

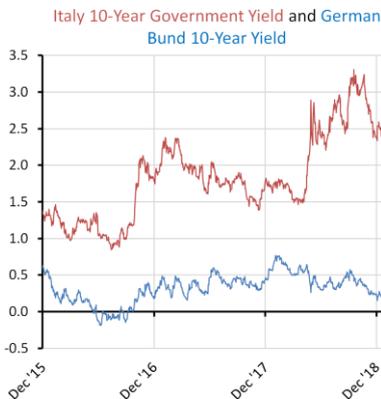
This isn't the first time the company has been hit with a disaster, four years ago a similar dam collapsed in Mariana, wiping out a village and killing 19 people. Vale has since grown to become the world's fourth largest mining company with revenues of around \$34bn (2017). In response to the crisis, Vale has cut production by ten per cent and a further ten dams will be temporarily shut down to prevent future collapses.



EUROZONE: ITALY FALLS INTO RECESSION

Italy capped off an abysmal 2018 by falling into its first technical recession in five years. Political unrest, an ongoing standoff with the EU over increasing public spending and with spiralling borrowing costs all played a part in slowing the economy. Output in Q4 contracted by 0.2 per cent following a decline of 0.1 per cent in Q3. Cyclical stocks that are sensitive to economic swings like banks were affected, with Banco BPM and Poste Italiano the worst performing stocks falling by -3.6 per cent and -3.3 per cent respectively.

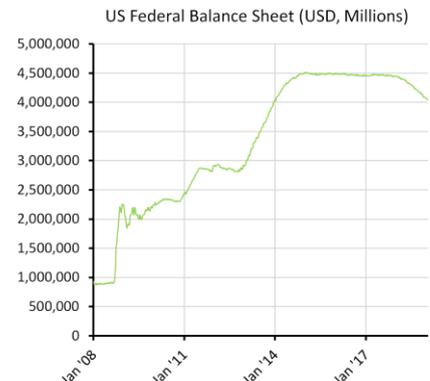
This heaps further pressure on a coalition government already fraying at the edges. Deputy Prime Minister Salvini is being urged by his party (League) to call an early election this year to split with anti-establishment party Five Star Movement. News of the recession also cranks up further pressure on the ECB. President Draghi had hoped to enter a period of expansion following the decision to end quantitative easing last year but forecasted Eurozone growth this quarter is expected to be sluggish. Draghi has admitted "risk to the downside has increased" signalling a cut in growth forecasts when policymakers next convene in March.



US: FEDERAL RESERVE PIVOTS TO RISK MANAGEMENT OVER RATE HIKES

The Federal Reserve performed a U-turn this week deciding to hold rates steady – a stark contrast from last month's bullish stance of not yielding to market pressure to pause hikes. This time, chairman Jerome Powell struck a dovish tone as "cross-currents" caused by growth slowdown in China, ongoing Brexit noise, US-China trade tensions as well as the partial government shutdown led to the Fed adopting a wait and see approach, before deliberating on further increases this year. Global markets reacted positively with S&P 500, FTSE 100 and Hang Seng index all up by 2.34, 2.73 and 1.31 per cent respectively.

Another key factor that drove momentum was the Federal Open Market Committee acknowledging that it could slow its quantitative tightening (QT) programme which began at the end of 2017. This program aims to shrink the size of the FED's balance sheet, removing some of the additional liquidity it pumped into the market after the financial crisis.



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