ALPHA
PORTFOLIO MANAGEMENT

The need for speed

 The clock is ticking down.....no, not to the Scottish independence vote but to the supersonic car speed test. The British **Bloodhound Supersonic Supercar** is a **Bristol based project** and reminds us how fortunate we are in the South West of England to have some excellent manufacturing and technology businesses nearby. We like investing in locally based businesses but particularly ones which have either ground breaking technology or leading global operations.

We wish the Bloodhound Supersonic team every success in their attempt to beat the world speed record and for our part can offer some useful bits of local knowledge. Careful if you test the supercar in our area as the council are considering turning the speed cameras back. Do not bother using the M32 after 5pm weekdays as a test track as you will be lucky to hit 10mph let alone 1000mph. Finally, be careful where you park, as someone might steal the wheels and leave the car chocked up on bricks (something I have sadly suffered!).

The supersonic supercar also reminds us that the **equity market has a need for speed**. Valuations are generally high and need company earnings to accelerate yet currency headwinds are currently acting as a brake on forward momentum.

What are we watching this week?

The hot, dry weather spell has temporarily come to an end but what do you expect with both the Glastonbury Festival and Wimbledon? If only the stock market was as predictable although market volumes remained subdued with many key decision makers out of the office. This week football and tennis are joined by the most famous two-wheeled road race, the Tour de France, starting in Yorkshire! Those in their office continued to monitor developments in Iraq with oil holding around the $113 level.

 In the **UK, bid activity** moved from big pharma to the oil sector and for strategic logic and earnings enhancement rather than for tax reasons. **Kentz** which had received opportunistic approaches last summer from AMEC and M+W announced a recommended 935p per share cash offer from Canadian engineering and construction company, SNC-lavalin valuing it at £1.16bn. **New issue indigestion continued** with the **AA** going to a discount in first day trading. **Currency headwind profit warnings continued with Croda the latest casualty** flagging a £19m adverse hit to profits from both translation and transaction. Elsewhere, the banking sector came under pressure due to a worse than expected trading update from **Standard Chartered** while **Barclays** announced it was being sued by the New York State Attorney General.

Mark Carney's earlier, more hawkish, comments on UK interest rates have exacerbated the currency head wind but has also affected sentiment towards UK domestic earners. However, at this week's Treasury Select Committee **the central message to investors from the BoE was to focus on economic data** and not on every comment from MPC members. On this basis, given labour market data showed that wage pressure remains subdued and slow to feed through to inflation that there is still no immediate need for the BoE to take action. The BoE also suggested that **the timing of the first interest rate hike was not that important as long as investors understood that the upward path of rates would be gradual and would not lead back to previous peaks**. In its June Financial Stability Review the BoE implemented two measures to mitigate the risk of excessive household mortgage debt but **said that it did not see an imminent threat to stability from household debt. Sterling remained firm at $1.70 with the market still assuming a more hawkish UK interest rate cycle.**

Political risk has also added to uncertainty. The Labour Party has indicted that it wins the next general election that it intends to review the Work Programme which could have ramifications for a number of UK outsourcing businesses. This adds to its UK business hit list of energy prices, minimum wage, housing land availability/rent control and railways. As if to underscore political driven risk, **Ofgem announced the UK energy market is to face a full investigation by the Competition and Markets Authority** creating further uncertainty for the likes of **Centrica and SSE**.

European PMIs continued to present a mixed picture with the **region still in expansion territory but whereas Germany continued to expand, France has struggled**. The overall output PMI for June dropped back to 52.8. Encouragingly, new orders hit a four year high while the rate of decline at which prices charged is moderating provided some relief on the deflation front albeit the ECB has taken action here. However, as we suspected last week there were voices from the German Bundesbank raising concerns about QE.

In the **USA**, the Markit manufactured goods reading for June was 57.5. Housing data was also encouraging with existing home sales in May the highest level since last October. One slight 'fly in the ointment' is the **US Congress problem to meet the shortfall in the Highway Trust Fund** which historically has funded over half of the USA's key road and rail infrastructure projects. US corporates have become alarmed as there has been talk of tax rises for businesses to fund the shortfall. The potential for delayed reimbursements has already led to some state departments of transportation to slow down their work or delay future projects.

The main surprise from the USA however was the **shock downward revision to Q1 GDP to a decline of minus 2.9% the largest adjustment on record**. Consumer spending was reduced by lower healthcare spending due to the roll out of Obamacare. However, given markets are generally forward rather than backwards looking **the focus is now on Q2 where the growth estimates range from +3% to +4%.**

Data from The World Trade Organisation (WTO) suggested anaemic growth in world trade during the first quarter of 2014. This should not come as a major surprise after the severe winter weather in the USA and sluggish trading environment in Europe and Asia. The WTO had been expecting growth in trade in developed economies to be about 4.7% this year but this feels optimistic given the first quarter growth was 2.2% and just 1.5% in US Dollars. This pretty much ties in with **our assumption of sub trend global recovery** and the continued need of central banks globally to retain an accommodative stance.

Many economists now expect the BoE to increase UK interest rates as early as November 2014. Even within the BoE, they would appear to be struggling to agree what the "normalised" future level of rates are likely to be. To what extent the UK consumer could stomach further increases above this initial hike is questionable. If interest rates were eventually to move up to 3% it is estimated that it would nearly double the amount of interest households would pay on their mortgages. **The UK economy is still imbalanced and the strength of Sterling is not helping UK manufacturing.**

Finally, always remember Alpha-Bites..... but not like Luis Suarez!

If you wish to discuss any aspect of this newsletter, please do not hesitate to contact us.

Further information about Alpha Portfolio Management, our products and services, please visit www.alpha-pm.co.uk or email info@alpha-pm.co.uk. Alternatively, you can call us on 0117 203 3460.