Weekly Stock Market Report

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US

Unemployment near three-year low

- Wall Street stocks rose for a fifth consecutive week as data suggested the economic recovery is gathering momentum. The Dow Jones returned 1.6%, while the broader S&P 500 was up 2.2%. The tech-biased NASDAQ gained 3.2%, taking it to its highest level since the collapse of the dotcom bubble 11 years ago.

- The optimistic mood was driven by encouraging economic news. Friday's employment report showed that the economy added 243,000 jobs in January, the most since April 2011 and well ahead of expectations. The unemployment rate fell to 8.3%, the lowest since February 2009.

- Manufacturing data was also encouraging, with the Institute for Supply Management's index of manufacturing activity rising to 54.1 in January from 53.1 in December. A reading above 50 indicates expansion rather than contraction. In the underlying data, the new orders, inventories and prices paid components all rose, though the production and employment components declined.

- Overseas manufacturing surveys added to a picture of strengthening global production, lifting commodity prices and benefiting materials and industrial stocks.

- Homebuilders underperformed the broader market on disappointing data. The housing market remains a notable weak spot in the recovery, with home prices falling in November as foreclosures and forced sales depressed values.

- Technology stocks were boosted by news that social networking company Facebook had filed papers with the US Securities and Exchange Commission for a USD 5 billion initial public offering (IPO). The filing disclosed for the first time the financial details of Facebook's business, revealing that revenue jumped by 88% in 2011 to USD 3.7 billion.

- Social game developer Zynga surged after the filing showed that Zynga accounted for 12% of Facebook's 2011 revenue. Rival social network LinkedIn and retail discounts website Groupon also gained on news of the IPO.

- The financial sector was the best performer in the S&P 500 as Morgan Stanley rose sharply after securing the lead underwriting role in the Facebook IPO and concerns over eurozone debt continued to ease.

- The fourth-quarter earnings season is nearing its end, with three quarters of the S&P 500 by market capitalisation now having reported. Although earnings growth is down sharply from the previous quarter, positive surprises have come at a similar rate (if financial stocks are excluded), supporting the strong performance of US equities in recent weeks.

EUROPE

Xstrata and Glencore announce GBP 50 billion merger

- European stock markets continued to push higher last week amid hopes that the eurozone debt crisis was easing and that global growth was strengthening. The MSCI Europe Index rose 3.1%.

- Among the major markets, Germany's DAX climbed 3.9%, the French CAC 40 gained 3.3%, Italy's FTSE MIB was up 3.1%, the UK's FTSE 100 rose 2.9% and Switzerland's SPI ended 2.1% higher.

- At the beginning of the week the latest European Union (EU) summit ended with 25 out of 27 EU governments agreeing in principle to sign up to tight restrictions on spending to try to prevent a repeat of the current debt crisis. Investors were also reassured by a commitment to bolster the eurozone's bailout funds.

- The launch of the new EUR 500 billion European Stability Mechanism (ESM) was brought forward by a year to July 2012, meaning the ESM will now run in parallel to the existing European Financial Stability Facility. With these facilities in place investors are becoming increasingly confident that the European authorities have enough firepower to bail out Greece, Portugal and Ireland and also to stop contagion to Spain and Italy. Spanish and Italian bond yields fell sharply, making it cheaper for both governments to service their existing debts.

- Meanwhile, the decision by the European Central Bank (ECB) to support Europe's commercial banks through its long-term refinancing operation (LTRO) continues to have a positive impact on sentiment. Much of the EUR 490 billion lent to the banks in December was new money created by the ECB, which it is hoped will eventually be used to lend to businesses and consumers. Another LTRO auction is scheduled for 29 February.

- On the markets, resources stocks were lifted by the announcement of a merger between UK-listed miner Xstrata and its biggest shareholder, the commodities trader Glencore. The all-share deal is expected to be worth more than GBP 50 billion.

- Economic data was mixed. UK growth forecasts were revised higher following a surge in January's manufacturing purchasing managers' index (PMI). The UK services PMI also rose sharply, while the eurozone manufacturing PMI managed a slight improvement, but eurozone consumer spending dropped in the fourth quarter of 2011.

- The reduction in sovereign debt concerns suggest that the rally in European stock markets may have further to run. The new EU fiscal rules and the ECB's intervention have bought time for peripheral governments to tackle the structural reforms that are vitally needed to boost competitiveness within the eurozone.

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- There are risks on the horizon, however. Many of these crucial structural reforms are opposed bitterly by vested interest groups, so there are doubts whether fundamental change is possible – particularly given that governments in Greece and Italy lack democratic legitimacy. The EU's new fiscal rules are also threatened by the upcoming French presidential elections, where frontrunner Francois Hollande has committed to renegotiate the fiscal pact and to introduce generous government spending plans.

PACIFIC

Australian retail sales fall unexpectedly in December

- The MSCI Pacific Index fell 0.3% last week, held back by losses in Japan and Australia.
- Japan's TOPIX dropped 0.1%. Exporters fell amid further yen strength and disappointing company profit announcements, with printer company Ricoh reporting a fourth-quarter loss, camera maker Fujifilm announcing worse-than-expected fiscal third-quarter results, and motorbike maker Yamaha cutting its 2012 profit forecast. Consumer electronics firm Sharp tumbled after predicting record losses for its current fiscal year.
- Economic data was positive, as Japan's industrial output rose 4% in December. However, the rebound was driven by a recovery from floods in Thailand, which had hit Japanese manufacturing supply chains in November. The outlook for Japanese manufacturers remains uncertain given the challenging global backdrop and the strong yen, which hit three-month highs against the US dollar during the week.
- In Australia, the All Ordinaries fell 0.7%. Australian retail sales unexpectedly declined 0.1% in December, the first drop in six months. Weaker consumer demand could convince the Reserve Bank of Australia to cut interest rates for the third successive month at its meeting later this week.
- In contrast, Taiwan's TAIEX surged 6.1%, as investors returned from the Lunar New Year holiday in optimistic mood on hopes for greater economic cooperation with mainland China.
- Hong Kong's Hang Seng was up 1.2%, supported by encouraging Chinese manufacturing data, while Korea's KOSPI rose 0.4% and Singapore's Straits Times was up 0.1%.

EMERGING MARKETS

China fears continue to abate on positive PMI

- Receding fears of a hard landing in China boosted risk appetite last week, contributing to a 2.1% gain for the MSCI Emerging Markets Index.
- China's official manufacturing purchasing managers' index (PMI) remained above the 50 line that separates expansion from contraction in January, versus expectations that it would fall back. The MSCI China rose 1.5%.
- India's Sensex added 2.2% to reach a three-month high as hopes that inflation is coming under control continued to improve sentiment on the market. Last week, the deputy governor of the Reserve Bank of India signalled a definitive end to the central bank's tightening cycle, indicating that policymakers will cut interest rates once they are confident that price rises will continue to slow.
- Central European markets gained as eurozone leaders signed a new fiscal compact and the intervention of the European Central Bank continued to ease contagion in the debt crisis. The Czech PX was up 4.3%, the Polish WIG rose 3.1% and Hungary's BUX returned 2.0%.
- Natural resource-rich markets such as Russia's RTS (+3.8%) and Brazil's Bovespa (+3.7%) benefited as strong PMI data from around the globe lifted commodity prices. Brazilian stocks were also boosted by expectations of further rate cuts after the head of Brazil's central bank, Alexandre Tombini, said that further reductions were achievable without jeopardising the goal of bringing inflation towards 4.5% this year.
- The Mexican Bolsa rose 2.4%, helped by positive economic data in the US, Mexico's largest trading partner. Domestic data was also encouraging, with Mexican consumer confidence rising to the highest level since July 2011 in January.

Source for information: J.P. Morgan Asset Management, Bloomberg, FactSet, Financial Times.