FE Investments

WEEKLY MARKET COMMENTARY BY ROB GLEESON

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CUTTING THE US OUT OF NEGOTIATIONS MAKES SHORT TERM SENSE BUT LONG-TERM PROBLEMS REMAIN

This week markets were calmed by the prospect of a deal to reopen the Strait of Hormuz. The price of oil fell and UK gilt yields dropped slightly as the prospect of higher inflation faded. Hopes of a deal added to equity market positivity following some strong tech earnings updates, although there are still some concerns about the scale of AI investment. However, America has been excluded from the talks between Iran and Oman. This may help secure a short-term agreement but the US is further from its goals than ever and has shown its willingness to return to hostilities.

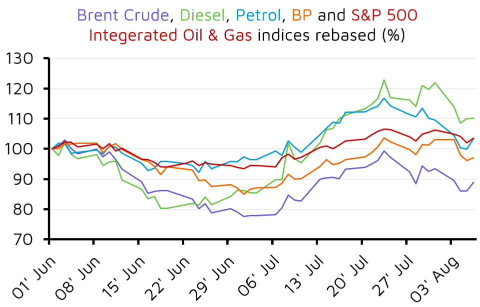
Meanwhile, the US Treasury's interference in the currency markets is a big departure from its usual behaviour. The decision to prop up the yen is motivated by self-interest, rather than altruism. It wants to avoid any further upwards pressure on US government bond yields if the Bank of Japan sells some of its huge stock of Treasuries to fund its defence of the yen. In the meantime, the Federal Reserve's policy of no communication with bond markets risks running against the Treasury's efforts as US Treasury yields creep higher.

THE MARKETS THIS WEEK

FTSE 100	S&P 500	Nikkei 225	STOXX 600	Hang Seng	US 10 Yr	UK 10 Yr	Brent Crude	Gold	Copper	GBP USD
-0.83%	+3.17%	+3.03%	+0.71%	-0.77%	+0.02%	-0.02%	-3.03%	+5.80%	+3.36%	-0.04%

ENERGY: OIL DROPS ON HOPES OF A DEAL TO REOPEN STRAIT OF HORMUZ

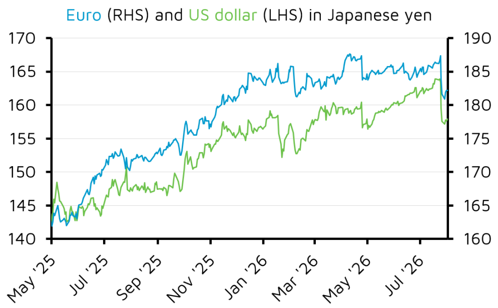
The price of Brent crude oil fell below $80 as markets assess the chances of Gulf oil and gas exports resuming. The US halted air strikes on Iran to allow room for negotiations. Despite no direct talks with the US, Oman and Iran have been trying to find a short-term deal to reopen the Strait of Hormuz. News of the negotiations helped government bonds to rally as fears of persistent inflation have faded.



BP, ExxonMobil and Chevron are the latest energy giants to announce record profits due to high oil and gas prices in the second quarter. BP's quarterly profits were up 144% on last year as it announced plans to sell its North Sea operation. Chevron and Exxon reported profits of $12bn and $14bn, respectively, drawing criticism from US President Donald Trump due to the high cost of petrol and diesel in the US. Meanwhile, the surge in demand for electricity due to AI is being reflected in markets with US coal-fired power stations back in favour and US nuclear generator Westinghouse preparing for a stock market listing.

JAPAN: A WEAK YEN IS AN AMERICAN PROBLEM

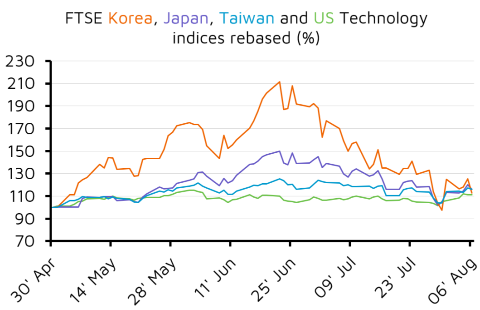
Japan and the US intervened in currency markets to protect the Japanese yen. Japanese interest rates are still just 1%, far below other major economies, which gives investors little reason to hold yen. By late July the yen was at its weakest against the dollar since 1986, pushing up the cost of imported food and fuel. The Bank of Japan bought yen to steady it, with little lasting effect. Surprisingly, the US Treasury then bought yen, the first time the two have acted together since the late 1990s.



Japan is the largest foreign owner of US government debt, holding roughly $1tn. If the BoJ sold those bonds to fund its defence of the yen, American borrowing costs, already the highest since 2007, would have risen further. The yen has since regained some ground and both sides promise to act again if necessary. But intervention delays the problem rather than solving it. Lasting strength needs higher Japanese rates, which markets now expect from October. Until then, currency and bond markets are likely to stay unsettled.

TECH: STRONG UPDATES RESTORE INVESTOR CONFIDENCE IN AI

Technology shares experienced more volatility, but strong company results helped support a broader rally in global equity markets. Palantir's second-quarter results beat expectations, with US sales rising 23%. AMD also delivered record quarterly revenue of $11.5bn, up 50% from a year earlier, as data-centre microchip sales doubled to $6.7bn. However, its shares fell as investors focused on the pace at which future AI investment will translate into earnings.



Amazon's profits increased more than threefold, supported by growth in its cloud business. SoftBank also beat expectations due to gains in its technology investments. SpaceX released a positive first update with earnings higher than expected, but shares fell as it announced a big increase in its investment in AI. The positive earnings news improved investor sentiment after recent selling of tech stocks. Asian markets rebounded particularly strongly, led by semiconductor and AI-related companies, but US and European shares also gained.

Data sourced from FE Analytics and Investing.com