

(CDX 125 @ 59 // +1)  
(CDX HY - pts @ 108.66 // -0.154)  
(S&P 500 @ 1960 // -0.04%)  
(Brent Oil^ @ 112.55 // -0.66%)  
(Gold^ @ 1327 // +0.83%)  
(10 yr Treasury^ @ 2.52 // -1 bp)  
^ - Change from previous day's 5:30 GMT to 05:30 GMT

Macro Strategy (J. Reid, N. Burns, A. Ip)

I'll be honest and say that yesterday's EMR was a bit of a daze. I had a belated party for my 40th on Saturday and spent virtually the entire Friday night awake with my builders trying to put a house back together that has been owned by the builders for 8 months. I had 15 people there until 4am Friday night with 3 of them working non-stop until the first guests arrived at 230pm. Never have I been so stressed and tired. So all day Sunday and Monday morning were a bit of a daze. Sadly I'm now back living with builders again as they finish things off after the party. It was blissful for the few hours we were apart. At least we've moved out of the kitchen where we were living and sleeping for nearly 5 months before last week. Hopefully by the time the second half of the year ends I'll never have to see a builder again.

Anyway, the second half has now begun for markets and in our H1/Q2/ June performance review today we show that most assets have had a positive year so far. So much so that if the year eventually goes to penalties it will end up being a very poor second half showing in line with many of England's in recent years!! We briefly review the numbers at the end but all the data and charts are in the pdf of this document. Its pretty rare to have almost all main global assets in positive territory this far into a year. Central bank liquidity continues to drive markets in our opinion which has helped this synchronised uplift in valuations. However we can't help sensing that there's less joy over these returns than might be expected. Investors are worried about valuations in numerous assets and worried that the Fed might become more hawkish soon. There's little chance of the ECB following suit anytime soon though and European Government bonds have had a very good 2014 so far.

Over the last month we've again highlighted how many European Government bond markets have hit multi-century, all time yield lows. Well yesterday it was the turn of the Dutch 10 year yield to go through it's all time low again. The Dutch series is where we have our longest history of any government bond market with data going back to 1517 spanning almost half a millennia. The graph is in the pdf today and further shows just how unique the current situation is. The level of uncertainty about how this all ends must by definition be very high given this.

So as we start H2, Asian markets are trading with a stronger tone this morning helped by a solid start to the global manufacturing PMIs. The official Chinese manufacturing PMI printed at 51.0, in line with consensus and at a six month high. The final HSBC Chinese manufacturing PMI came in at 50.7, slightly below the flash reading of 50.8, but this is also the highest print of the year. The PMIs for other Asian bellwethers including Indonesia and Taiwan were also up on a month-to-month basis. The Nikkei (+1.2%) is the clear outperformer today, on decent volumes and despite a drop in the Japanese Q2 tankan manufacturing index to 12 from 17 previously and 15 expected. The capex component of the Tankan survey was above expectations however (+7.4% vs 6.0%) expected, which is strongest rate of growth since 2007. This has helped USDJPY (+0.1%) today. Outside of Japan, activity has been subdued with Hong Kong markets shut for July 1st holidays. The Indonesian rupiah is poised to record its strongest three-day rally in about fourth months – spurred by comments last week from the Bank of Indonesia that the country's trade balance returned to surplus in May. The AUDUSD is also poised for a solid gain (+0.25%) after the RBA maintained its neutral tone in today's policy meeting.

The last trading day of 1H14 failed to bring with it any volatility associated with month-end and half-end portfolio rebalancing. Indeed, yesterday's S&P 500 volumes were about half that compared to the last trading day of 1H13. Adding to that, the S&P 500 closed virtually unchanged at -0.04%, and for the record the last time we saw a gain or loss of more than 1% in the index was April 16th. One theme to note though was the continued underperformance of European banks across the equity and credit spectrum. Yesterday's underperformance was sparked by a 17% fall in the stock of Banco Espirito Santo which is Portugal's largest bank. The price action was dictated by reports that regulators were concerned over corporate governance between the bank and other related companies and there were also reports that Luxembourg justice authorities had launched an investigation into one of the bank's holding companies (Reuters). Portuguese securities regulator banned naked short selling on the bank's stock for one day. The news weighed on Portuguese bond yields which added 8bp, and also on European banking stocks in general (-0.75% vs Stoxx 600 - 0.09%). Peripheral bank credit traded about 3-5bp wider yesterday - and the European senior financials index (+2bp) underperformed Main (+1.375bp). The two credit indices were trading flat to each other in the middle of June but the recent underperformance of banks has pushed the basis back to nearly 6bp. We still think its likely that Fin Senior will trade through Main in H2 though.

Across the Atlantic, there was focus on the Chicago PMI and home sales data, following which treasury yields spiked up briefly before retracing the move to be largely unchanged on the day. The US Chicago PMI was slightly below expectations 62.6 (vs 63.0 expected) and also below last month's 65.5. Still, our economists note that the PMI was consistent with a large snapback in growth in Q2, and they noted the three-month to June average was 63.7 which is the