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INVESTOR INSIGHT

A look at the markets by RSMR

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Welcome to the latest edition of our 'Investor Insight' which provides high-level commentary on the global markets and how these might be affecting your investments.

Ken Rayner, CEO, RSMR

The global economy: What's going on?

Challenges threaten favourable outlook.

Despite some volatility, equity markets, apart from Japan, ended the last quarter looking positively ahead, prolonging a buoyant year. Volatility was triggered by investor concerns about a possible US economic slowdown, but these faded during the summer as the economy maintained its strength and several markets responded by reaching all-time highs. Emerging markets, which have been subdued for some time due to concerns about the Chinese economy, surged late in the quarter as the Chinese government announced an economic stimulus package.

In August, the Bank of England (BoE) cut interest rates by 0.25% to 5% and the Federal Reserve (Fed) followed with a significant 50 basis points reduction the following month. In contrast, the Bank of Japan (BoJ) raised rates in July to 0.25% and is expected to raise them again by the end of the year.

Although central banks have started cutting rates as inflation falls, they are monitoring inflationary pressures to confirm that it has been defeated as service sector inflation, especially the UK, remains too high.

Think tank, the Organisation for Economic Cooperation and Development (OECD), noting falling inflation, forecasted weaker price pressures and global growth stabilising. The next challenge is to bring down debt.

> "In August, the Bank of England (BoE) cut interest rates by 0.25% to 5%."

The asset classes – a quick round-up

EQUITY MARKETS

Equity markets were the main impetus for returns but momentum stalled as concerns about the global economy increased. This was most conspicuous in August when central bank policy moves in Japan and the US, as well as lower-than-anticipated US job numbers, resulted in volatility in many indices.

Even the US tech giants, which had been driving markets, were affected and, while a such a market correction was not desirable, it was not surprising given the variation between this narrow band of stocks and the rest of the US stock market. It may have been a bubble waiting to burst but most of these stocks are large, profitable businesses, not speculative like those which led to the 2000 dotcom boom and bust.

Although there was higher volatility, the US market still managed to hit an all-time high and the Chinese market sprang back to life after the government announced an economic stimulus package which will also help some emerging markets.

In local currency terms, the main equity markets remained positive, building on gains so far this year. Japan, which has just called a snap election, was the exception where the market struggled to recover from August's decline.

Euphoria about the outlook for artificial intelligence (AI) and its uses has been central to the US tech giants' success. How beneficial AI becomes, and to whom, remains to be seen, but managers are working the breadth of the market to find ways to broaden its application.

Meanwhile, the UK economy has continued to improve, with gross domestic product (GDP) growth up in the last six months.

FIXED INTEREST

Returns fell during the summer as the long-awaited interest rate cuts, signalled by Fed chair, Jay Powell, some time ago, finally happened but the Fed is monitoring inflation as it also has a mandate covering employment. The US 10-year Treasury yield fell in the last few months from around 4.4%, falling to about 3.79% as the quarter closed.

Investors are ruminating on the direction of monetary policy, especially after the Fed's 50-basis point cut. As previously mentioned, falling rates are an opportunity for investors to capitalise on rising prices as returns fall. Corporate bonds are favoured by some managers.

Central banks in emerging markets had increased interest rates faster and higher than developed markets. They are well placed to reduce rates having had a higher starting interest rate, making selective emerging market debt compelling.

ALTERNATIVE INVESTMENTS

Both property and infrastructure benefited from falling interest rates, reflecting their market sensitivity. Further reductions will help but both are also benefitting from larger investment imperatives including renewable energy infrastructure and AI which will require dedicated data management centres.

Offices have continued to struggle due to the rise of hybrid working, although there are signs that some companies are reverting to a greater office presence, notably Amazon which is insisting on staff working in their office five days a week from January.

Precious metals responded enthusiastically to the Fed's rate cut with gold trading at record highs in dollar terms and silver rising, although not to the peaks of 2011. Wider commodities, including iron ore, copper and steel reacted positively to China's stimulus, anticipating increased demand.

Oil's sensitivity to global economic concerns and recession risks was evident as crude oil prices fell. Saudi Arabia was also prepared to lift its unofficial price target in a sign that lower prices may be here for some time. Despite this, oil prices recently rose in response to the Middle East's escalating hostilities. If this rise persists, it may create global inflationary pressures.

RSMR Global round-up

- Based on August's data, UK inflation is at 2.2% with services inflation at 5.6%.
- August's US Consumer Price Index (CPI) showed inflation fell for the fifth consecutive month to 2.5%.
- Concerns persist about China's consumer and property markets.
- The European Central Bank (ECB) continued to reduce rates with a further 25 basis points cut to 3.5%
- The Bank of Russia raised interest rates to 19% in September to tackle inflation above 9%.
- The EU is likely to introduce tariffs on electric vehicles from China to protect the EU automotive industry.
- Thailand, Asia's second largest economy, launched an economic stimulus package in which cash will be distributed to its citizens to help offset benign growth.
- Argentina's interest rate has fallen to 40%, from a 126% peak, as president Javier Milei works to combat high inflation.
- Mexico has a worsening budget deficit with the focus on how the forthcoming budget by its first female president, Claudia Sheinbaum, addresses this.

"Concerns persist about China's consumer and property markets."

> The US presidential election is the most curucial this year in terms of its geopolitical and economic implications and will be closely watched by investors.

SO, WHAT'S NEXT?

Overall, the global economy appears in quite good shape, although challenges must be navigated for this to continue. In the UK, the detail of the new Labour government's first budget on 30th October will clarify how the chancellor will address the party's election manifesto commitments and the UK's precarious financial position.

Geopolitical risks have increased with the escalating Middle East conflict, which is now a year old. The oil price, which had been falling, has risen in response. Meanwhile, Russia's invasion of Ukraine continues.

Kings College London estimated that in 2024, 1.5bn people in more than 50 countries would vote in government elections and the most crucial in terms of its far-reaching geopolitical and economic implications, will be November's US presidential election, the outcome of which will be closely watched by investors. Regardless of who wins, concern remains that the US will enter recession in 2025 as the Covid-19 economic fiscal stimulus washes through. However, the depth and duration of any economic slowdown will be more important to investors than recession itself.

The need for a diversified portfolio, holding different asset classes, is as relevant as ever. For equity investing, especially in the US, broader market exposure is warranted to dilute concentration in the mega cap companies. In fixed income, although rates are declining, prudence is still required about the types of bonds an investor holds.

About RSMR

Independent specialist research.

RSMR was formed in 2004 to meet a growing demand from financial advisers for specialist and impartial investment research.

The RSMR team is made up of individuals with expertise from across all areas of the financial industry – from asset management, strategy and fund research through to business development, strategic planning and market research.

We are best known within the financial industry for our 'R' fund ratings – this rating is given to investment funds that meet our stringent research criteria. We don't limit ourselves to just looking at performance – we also look carefully at the people, processes and capabilities that are required to make effective investment decisions.

We work in partnership with your financial adviser, providing the benefit of our broad industry insight and rigorous research. This quarterly market summary is designed as a 'snapshot' of the more thorough and lengthy commentary that we provide to your adviser on a quarterly basis.

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