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Eden Park | HRIS

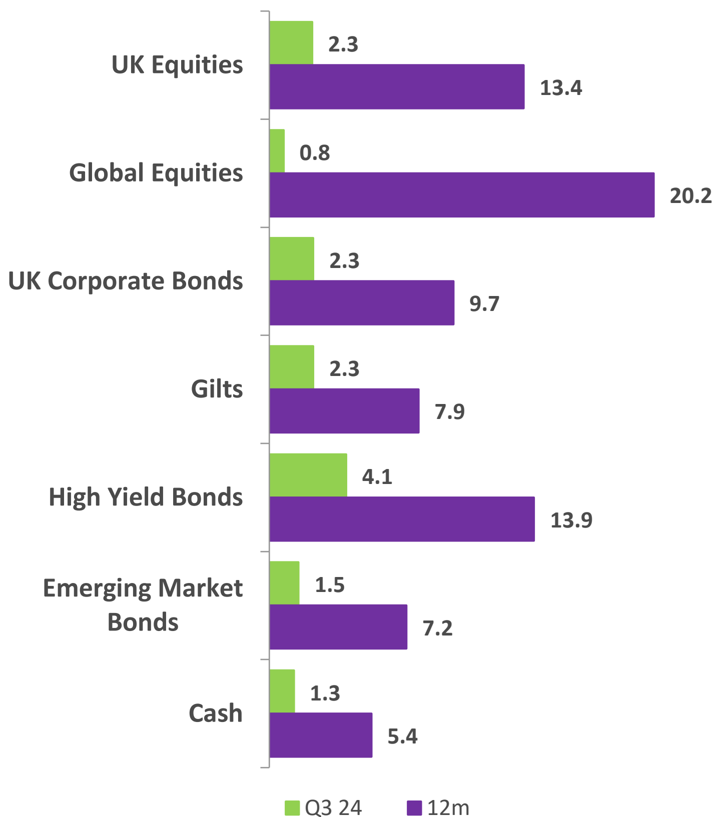
Market Digest

Q3 2024

Quarterly Highlights

- Equities and bond markets both delivered positive returns to portfolio performance. Emerging market equity was the best performing region, driven by China's stimulus announcement.
- The Bank of England and the US Federal Reserve cut their target interest rates, this helped drive the positive bond performance over the quarter.
- On page 3 of this document, we provide market commentary to cover the 12 months to 30 September 2024.

Asset class returns (%)



Source: Morningstar. Figures to 30 September 2024. Returns in sterling terms except High Yield Bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.

Market summary

- Our model portfolios typically invest in a combination of the asset classes shown in the left-hand chart.
- Weak economic data in the US fuelled slowdown concerns at the start of the quarter. The small market sell-off and heightened volatility from these data releases demonstrated the shift in investor focus, away from inflation data and towards growth data.
- The Federal Reserve (Fed) announced a cut of 0.5% to their target interest rate range in September. The cut was larger than expected and greater than the Bank of England's (BOE) 0.25% cut made in August.
- Global equity markets ended the quarter up 0.8%. US markets were broadly flat over the quarter, with valuations of the large US technology companies, such as Nvidia, coming into question. Despite two Japanese market sell-offs, following the announcement of a rate hike in July and the surprise victory of Shigeru Ishiba as the ruling party's leader in September, Japanese equities ended the quarter up 0.7% (in sterling terms). Emerging markets returned 4.6% over the quarter after the announcement by the Chinese government of a fresh stimulus package bolstered the Chinese stock market.
- Bonds performed well over the quarter following the central banks' interest rate cuts. The economic outlook for the UK also improved which left gilts up 2.3% over the period.
- At a portfolio level, bonds tended to outperform equities resulting in lower risk portfolios producing greater returns than higher risk portfolios over the quarter.

Outlook and topical market themes

- Escalation of the conflict in the Middle East has been pushing oil prices up, with fear of an impact on global supply lines increasing.
- A volatile quarter shows how quickly the global interest rate picture can change. Markets now expect the Bank of England (BoE) to cut the rates by 0.9% and the Fed to cut rates by 1.2% by 31 March 2025.

Geopolitical tensions increase

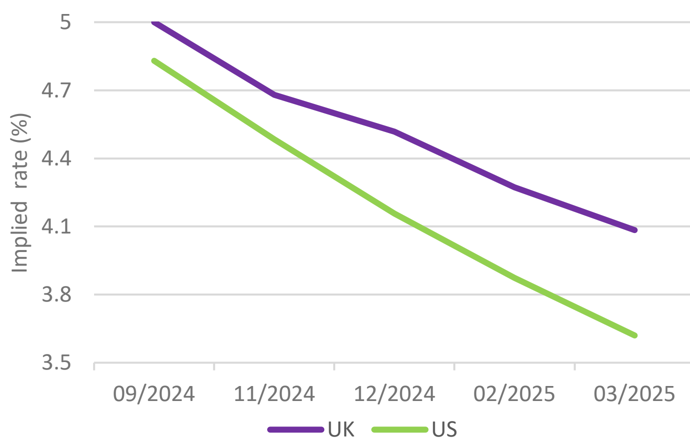
The conflict in the Middle East escalated in September. Brent crude oil jumped to a high of $81 dollars a barrel in early October, gaining almost 20% over a few weeks. This (at least in part) is thought to be driven by concern that Iran's energy and oil infrastructure could be attacked in the future, thereby impacting supply lines. With Iran estimated as 3% of the world's oil production, there are concerns we could see some inflationary pressures come back into supply chains. However, it is worth remembering there is scope for other countries to up oil production, for example from the US shale sector. There are also signs that developed markets are now less reliant on oil, using alternative sources of energy, to generate growth than in the past. The IMF estimates the amount of barrels of crude oil needed to generate $1m in economic growth was 3.5 times higher in 1973 than in 2022. It is thought these can help reduce the impact of any oil price shock on broader economies.

Central bank rate cutting cycles begin

The major developed market central banks have now started to cut interest rates, with the Fed being the last to announce a rate cut, in September. Although the long-awaited first cuts have been well received by investors, the paths of different central banks base rates could vary moving forward.

In September, the Fed moved more aggressively in cutting rates, given their 0.5% cut versus the BoE's 0.25% cut in August. The reaction to the US jobs report data over the quarter demonstrated how market sentiment can change very quickly and impact the outlook that the central banks are faced with. The July jobs reports undershot expectations and caused investors to question again whether the US might enter recession. The August report sparked little reaction, but the September data showed that 254,000 jobs had been created over the month, far exceeding expectations. On the back of this, investors revised their interest rate expectations for the Fed, shifting back towards believing a 'soft landing' for the US is possible. This is the situation where inflation falls back to target without the higher interest rates causing a significant economic slowdown. Perhaps unexpectedly, the post-quarter interest rate paths for the Fed and the BoE now look similar with cuts expected to be slow and steady. This quarter showed how quickly the picture can change. The challenge for central banks will be to continue to focus on the long-term signals, with growth becoming a larger concern than inflation. However, the volatility of the short-term data may lead to dramatic shifts in investors' expectations along the way, even if the Fed is more focused on the totality of the data. The Fed will also be closely monitoring the upcoming US election result as, despite the Fed being an independent body, the successful party's economic policies will inevitably have some impact on the Fed's future decisions. See discussion around market implications of the US election result in our latest article.

Chart of the month – Implied rate cuts to continue into 2025



The chart shows the implied path of central bank interest rates in the US and UK to March 2025, determined by the futures market.

Markets expect the BoE to cut the rate by 0.9%, implying at least 3 cuts of 0.25% whilst they expect the Fed to cut the rate by 1.2%, implying at least 4 cuts of 0.25% by the end of March 2025.

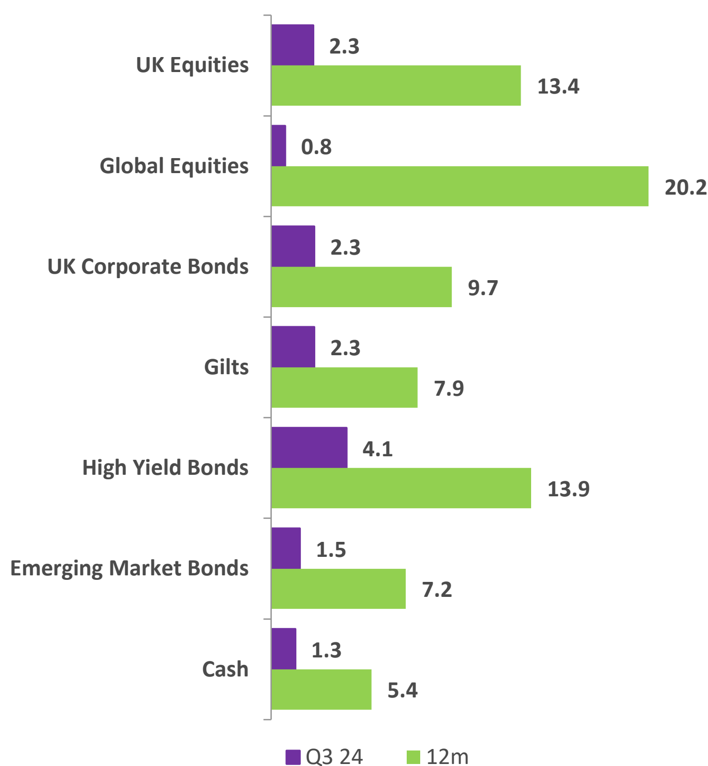
Source: HRLLP as at 4th October 2024

Daniel Kowalewicz
Wealth Investment Associate

Annual market summary- covering the 12 months to 30 September 2024

Throughout this 12-month period, the US economic growth story gave mixed signals. Recession doubts dwindled for most of the period before a below expectations job report, amongst other data points, brought it back into question. The UK started the period with a technical recession, having shrunk again in Q4 2023. However, the UK is expected to have grown since then with estimated GDP figures of 0.6% in Q1 24 and 0.7% in Q2 24, putting deeper recession fears to bed.

Central banks began to cut rates over the 12 months. The Bank of England held the rate at 5.25% until August 2024 when they cut it to 5%. The Fed followed in September 2024 with a 0.5% cut. The rate cuts were well received by investors with equity and bond prices both increasing. Further rate cuts have been priced into markets for the next 12 months into 2025. The pace of future rate cuts has now become a key talking point for investors with the macroeconomic backdrops far from straightforward. In the UK, headline CPI briefly fell back to the BoE's target of 2.0%. Services inflation caused some caution and was a factor in the BoE deciding to cut just the once over the period. Over the 12 months, UK inflation fell from 6.7% to 2.2%, while interest rates fell from 5.25% to 5.0%.



Source: Morningstar. Figures to 30 September 2024. Returns in sterling terms except High Yield Bonds which are hedged. EM bonds are 50% local currency denominated and 50% US dollar denominated bonds.

Geopolitical risk in the Middle East grew, as conflict in Israel and Palestine broke out into Lebanon. The region's importance to global trade and energy markets meant the price of oil increased towards the end of the period. The threat of a reversal in the disinflationary process experienced over the last 12 months was brought further into question.

Bond performance was mixed over the period as expectations on inflation and interest rates were ever changing. Q3 24 saw key central bank rate cuts boost bond markets, ending the 12-month period strongly. Equity markets performed even better, with large US technology driving markets for most of the 12 months. China's announcement of fresh stimulus boosted sentiment for emerging markets, leaving the global equity market with strong returns over the 12-month period. The US market was the best performing region, benefitting from a heavy tech exposure and several companies that gained from exposure to stocks that gain from the growth of Artificial Intelligence, such as chipmaker Nvidia. Emerging Markets and the UK both lagged the global market, with growth prospects looking weak in the first 9 months of the period. They recovered to some extent in Q3 24 as fresh stimulus in China, and the controlling of inflation in the UK, contributed positively to their respective economic outlooks.

Risk warning

The value of your investments and the income from them may go down as well as up and neither is guaranteed. Investors could get back less than they invested. Past performance is not a reliable indicator of future results. Changes in exchange rates may have an adverse effect on the value of an investment. Changes in interest rates may also impact the value of fixed income investments. The value of your investment may be impacted if the issuers of underlying fixed income holdings default, or market perceptions of their credit risk change. There are additional risks associated with investments in emerging or developing markets. The information in this document does not constitute advice, nor a recommendation, and investment decisions should not be made on the basis of it. The material provided should not be released or otherwise disclosed to any third party without prior consent from HRIS.

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