Monthly Markets Update

29 February 2024

FUTURE PLANNING

- Strong US earnings support rally
- Pivot expectations now more realistic
- Geopolitical risks acute

Key points

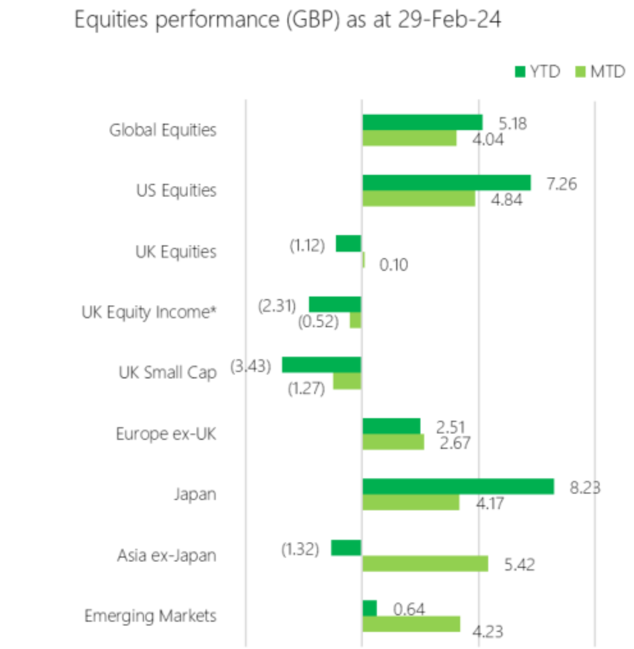
1. Strong US earnings and corporate outlook supports markets..

2. Bond markets have adjusted to a more realistic expectation as regards the timing of rate cuts.

3. Geopolitical risks – in Ukraine, Middle East and Taiwan – combined with upcoming US and UK elections remain acute and could destabilise markets and/or rekindle inflation.

Equities

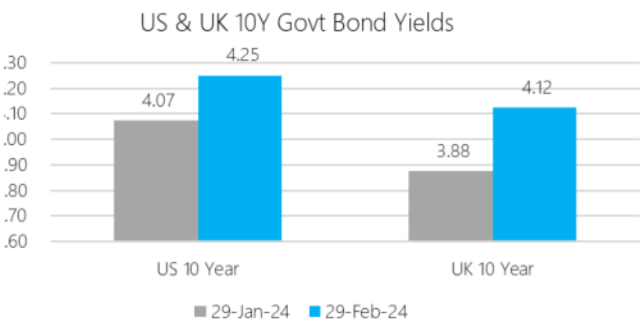
Global Equities closed the month +4.04% MTD and +5.18% YTD. US Equities returned +4.84% MTD and +7.26% YTD, while UK Equities were down -1.12% MTD and +0.10% YTD, all in GBP terms.

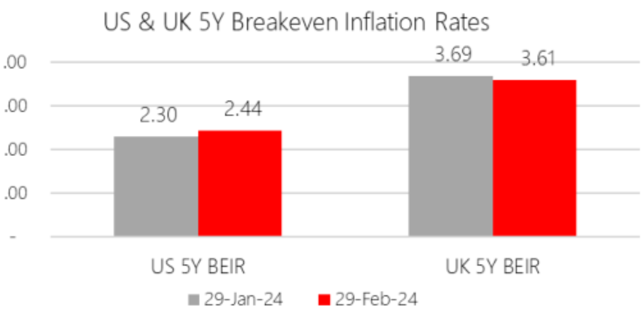


*Elston Indices

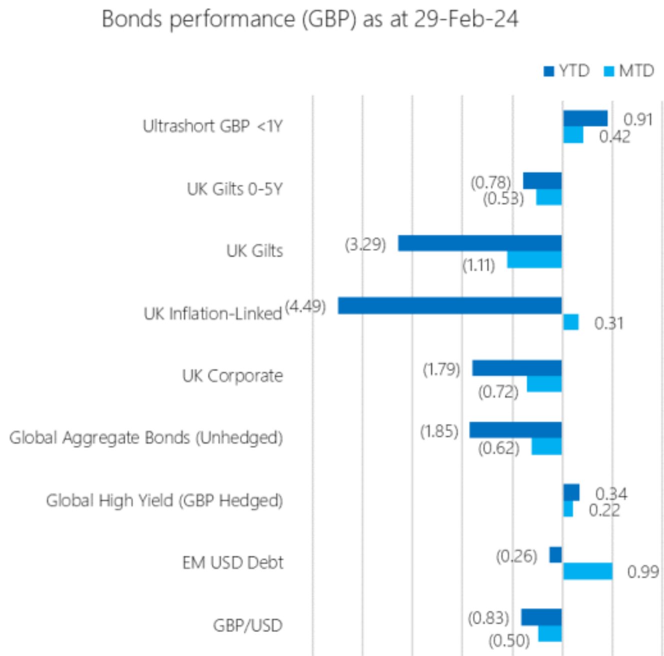
Bonds

US 10-year yields closed the month slightly higher at 4.25%. UK 10-year yields ended higher at 4.12%. The US 5-year market-implied Break-Even Inflation Rate "BEIR" closed the month slightly higher at 2.44%, whilst the UK 5-year BEIR slightly decreased to 3.61%.



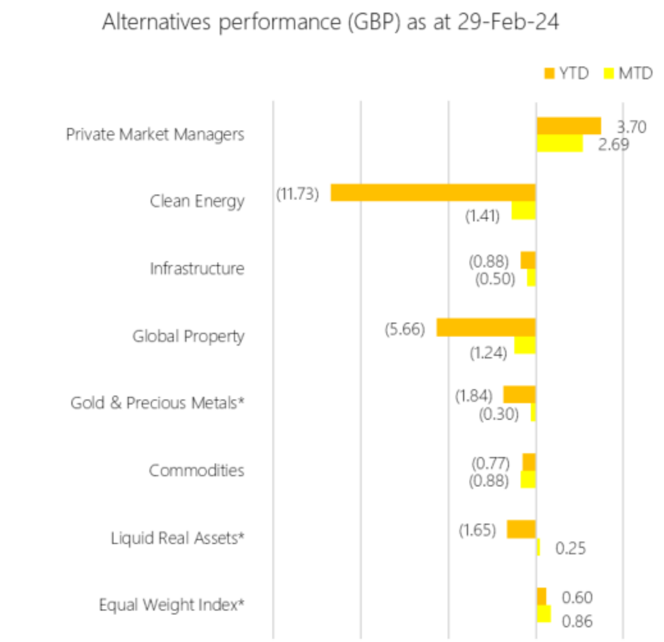


Elston research, Bloomberg data



Alternatives

Alternative Assets had mixed performance during the month. Liquid Real Assets was the best performing alternative asset, up +0.25%. Clean Energy Infrastructure was down -1.41%. Within **Alternative Strategies,** an Equal Weight 4-asset strategy was up +0.86% for the month, and +0.60% YTD



*Elston Indices

Currency

Sterling was a touch down against the Dollar: £1 buys $1.2625, from $1.2668 last month (-0.50% MTD, -0.83% YTD change.)

Month in review

We summarise key drivers and data points in the last month for markets, the economy and geopolitics.

Markets

Markets continued to rally supported by strong earnings and continued high valuations of those earnings in the US tech sector. US Equities continued to rally with S&P500 crossing through the key 5,000 level to new highs. Despite lofty valuations the technology sector, hence the US, and hence world equities have been powering ahead. Strong earnings and ahead-of-estimate guidance from chipmaker NVidia contributed to the surge, along with stronger corporate earnings for large cap US equities. AI is seen as reaching a "tipping point", similar to the transformative adoption of the internet and the tech sector will benefit.

Following resilient relative performance during the inflation shock, UK equities are lagging once again, causing consternation in the City around the valuation multiple discount relative to the US. We think it's wrong to blame UK pension funds for deallocating from UK equities: the problem is the lack of successful growth companies listed or planning to list in London.

European stocks joined the global rally on a more optimistic economic outlook having missed expectations for the past eight months.

Japan's Nikkei stock index reach its 1989 record high driven by Japanese tech manufacturers, weaker yen supporting exporters and the impact of corporate governance reforms. Global funds' renewed interest in Japan after a multi-year absence if supporting flows. Japanese bond yields increased to the highest level since 2011 on expectations that the central bank might abandon its negative-interest-rate policy in coming months. Higher yields would be positive for the Yen and further support Japanese equities.

China market opened after Lunar New Year with modest gains, despite government stimulus plans, including a ban of short-selling large-caps.

Within the bond market, the realisation that Central Banks would not pivot to cut interest rates in the first quarter, but would more likely be in the second half of the year, sent bond yields up (and so bond values down).

Economy

Growth: Economic indicators suggest the US economy remains on solid ground. US GDP continued to show strength as it grew at a strong 3.2% in Q4,2023 driven by strong consumer spending. Growth of 2% is expected for 2024 - ahead of expectations for UK and Europe. UK GDP declined -0.3% in the fourth quarter, compared to -0.1% estimate. As this is the second successive decline in quarterly GDP, it means that the UK was technically in recession in 2h23.

Inflation: US inflation for Jan-24 came in at +3.1%yy vs +2.9%yy estimate. Core US inflation came in at +3.9%yy vs +3.7%yy estimate. UK inflation for Jan-24 came in at +4.0%yy vs +4.1%yy estimate. Core UK inflation came in at +3.9%yy vs +3.7%yy estimate. Expectations are for inflation to trend towards the bank's 2% target in coming months.

Rates: Stickiness in US inflation is one of the reasons that expectations for a US Fed rate cut have been pushed back to the later half of 2024. With the UK now confirmed as having been in technical recession, UK inflation moderating and the Bank of England Governor stating it was not imperative to reach target inflation before cutting rates, we think that we are also closer to a potential BoE "pivot" in mid- to late 2024. Perfecting the pivot is one of the key themes from our 2024 Outlook.

Geopolitics

US Elections: Trump continues to succeed in the primaries and is likely to remain the Republican's front runner despite the mounting number of legal challenges.

UK Elections: The Conservatives were severely defeated in two by-elections, whilst in Rochdale, veteran anti-war hard-left campaigner George Galloway won a protest vote after Labour pulled its candidate. The upcoming Budget is unlikely to rescue the Conservative's slump in the polls.

China/Taiwan: the death of two Chinese citizens when their boat overturned being pursued by Taiwanese coastguards has added to already sour relations.

Ukraine/Russia: President Zelenskyy replaced his military top brass replacing the popular and potential political rival General Zaluzhnyi with the less popular General Syrskyi. US aid funding deal remains in limbo. In the meantime, Russia is making territorial gains having captured the fortified stronghold of Avdiivka. Comments from Macron indicated consideration of putting NATO troops on the ground – subsequently denied by other NATO members. A leaked call from Germany's top-brass suggested that for specific functions (e.g. missile operations), some may already be there.

Middle East/Gulf: the Gaza crisis could broaden following outrage over the shooting by the IDF of civilians gathering round an aid convoy. Houthis continued their attacks on commercial shipping, the US and UK continued with military strikes. Shipping freight costs remain elevated as cargo re-routes which could add to inflationary pressure.

.

Bottom Line

Markets have remained strong in February. A potential policy rate pivot remains data dependent. Potential downside risks include a China/Taiwan escalation that jeopardises AI chipmaking supply chains and a broader Middle East conflagration that could lead to an oil price shock, and associated inflation.

What does this mean for portfolios?

While portfolios should have clear long-run strategic allocation to match a given risk profile, adapting portfolios to align to changing market and economic conditions can help mitigate near- to medium-term risks and help navigate the markets.

Getting in touch

If you would like to find out more or discuss any of the above, please contact your financial adviser.

Contact us

For more information, please contact your financial adviser.

FUTURE PLANNING