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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?

Rate cut hopes fuel optimism.

Despite global uncertainty, with wars in Europe and the Middle East and government elections, notably in the UK and US, record-breaking equity market levels confirm that investor confidence has returned.

Alongside this, interest rates are losing dominance over global markets which are now also focusing on corporate earnings results which have been very positive, especially in the US.

Even so, this more upbeat mood does not mean the global economy is about to surge as several risks remain, including that market valuations are high and may have already accounted for all the positive signs.

Inflation is thought to be under control in developed countries and stands at a lower-than-expected 3.4% in the UK, 3% in the US and 2.6% in Europe. The move down to the Bank of England's (BoE) 2% target level may be harder to achieve as service sector inflation remains stubborn even though goods inflation has fallen.

Strong wage growth in the developed world has supported consumer spending, even though savings during the Covid-19 pandemic have largely been spent.

"Inflation is thought to be under control in developed countries."

The asset classes – a quick round-up

EQUITY MARKETS

Equities started 2024 confidently as the momentum behind interest rate cuts led to greater faith in company earnings. This is important because although markets will still move on interest rate speculation, this will also be founded on more durable and tangible valuations based on company performance.

A buoyant US is still driving global stock markets, closely followed by Japan where the weaker yen and consistent inflation has propelled the main index past its 1989 highs. Some economists fear the current rise could be due to stocks, especially in US technology, being overvalued.

The UK has drifted slowly higher but is less influenced by the technology sector and is more likely to move ahead if the UK economy is clearly improving.

In comparison, European markets have done well, recovering some of the ground lost when recession looked likely at the end of 2023.

Asian stocks have also picked up slightly, mostly in India, Korea and Taiwan as China's difficulties are taking time to resolve, although there are early signs that this is happening.

FIXED INTEREST

Bond markets have surprisingly struggled after a strong end to 2023 when expected US interest rate cuts reduced returns. Most economic commentators still believe interest rates will be cut throughout 2024 although on fewer occasions.

Investors are now more in line with central banks which have calmed the feverish rate cut expectations at the end of last year. The BoE has kept rates at 5.25% and governor, Andrew Bailey, said a cut is likely but not imminent as wage growth and service price inflation are too high.

Government bonds had a poor start with gains last year largely eroded, particularly in the UK.

Credit markets continue to do well and US demand for corporate bonds has soared to record highs as investors rush to 'lock-in' the highest yields in years, ahead of anticipated rate cuts.

Risks include that the central banks may mistime reductions, which could drive inflation below target and cause a recession.

If rates fall, bonds will become more attractive, and several fund managers predict this may be a rare chance to capitalise on falling rates. Emerging market debt may also offer opportunities as several countries are already lowering rates.

We see volatility ahead as investors move assets from cash into other products to maintain returns. Potential hazards also include the Middle East and Ukraine conflicts and possible game-changing US and UK elections.

ALTERNATIVE INVESTMENTS

Due to equity markets' strong performance, attention has drifted away from alternatives and some areas have struggled. Expectations of interest rate cuts, which would benefit property and infrastructure, have been delayed, probably until summer, so the momentum behind assets sensitive to rates has slowed.

Property has struggled with offices still a concern. Supply chain crises have hit transport and logistics, but warehousing has proved resilient, partly due to rising demand from operators outside logistics wanting to hold large volumes of stock as part of a 'just-in-case' strategy.

Continuing e-commerce growth has also helped logistics, and retail demand is expected to creep up in 2024 after warehouses acquired during the pandemic are absorbed and online sales continue to rise. European office space still looks strong compared to the US where it underperformed compared to much of the rest of the world in 2023.

While there are many areas where caution is advised, we are in the early stages of growth in new sectors that could generate very attractive long-term returns.

China's persistent obstacles, including a property crisis, added to concerns about global energy consumption.

Meanwhile, the rapid expansion of renewables and low heating requirements during the mild winter slashed natural gas demand in North America and Europe, lowering prices as a result.

Oil may well be a barometer for commodity growth in 2024 as will weaker Gross Domestic Product (GDP) data from China, which is usually a benchmark for industrial metal prices including copper, aluminium, and nickel.

RSMR Global round-up

- Purchasing managers' index (PMI) surveys showed that eurozone goods and services output almost stabilised in March.
- After recession in December, the UK economy grew slightly, by 0.2%, in January (source ONS).
- Norway's central bank kept its policy rate unchanged at 4.5%.
- US economic growth was 3.3% in the final quarter of 2023, well ahead of other G7 economies.
- The eurozone composite PMI rose to a nine-month high of 49.9 from 49.2 in February.

- China's property investment fell by 9% in January and February compared to a year earlier.
- India is Asia's second largest economy and is benefitting from the economic reforms of 2017.
- Latin American central banks have started acting independently of politicians and introducing inflation targeting.
- Japan's short-term outlook looks good for equity investors and could benefit from any recovery in Asia and China.

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SO, WHAT'S NEXT?

Central banks' indications of interest rate cuts later this year confirm a realistic basis for the optimism which has boosted equity markets. While rates will remain crucial for investors, the renewed focus on company valuations and investment potential, is likely to continue.

As ever, there are potential hazards, including possible overvaluations, especially in the US.

A broadening market outlook from a few stocks and sectors would send investors a stronger signal that global economic growth can last, and that inflation is under control.

As investors become more confident, investment should encompass the mid and small cap stocks that have lagged in recent years.

Some countries are still struggling, including China, but its economic growth is still higher than the west.

Investor focus should not just be on equities, as the forecasted rate cuts also suggest a positive future for bond holders.

There are many encouraging signs: global economic growth is improving, and higher interest rates have helped stem the post pandemic inflationary surge without creating a recession.

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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