Monthly Market Commentary

May 2024

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Good Problems and Data Dependence

As the global economy continues to improve, it's becoming clear that many of the challenges we face are a result of our own success.

The strength of labour markets across the developed world underpins household resilience and broader economic growth. The manufacturing sector appears to be exiting a drawn-out period of retrenchment and even housing activity has started to level out. While the pessimists will point to the lingering risks from higher interest rates, investors will take solace from an improvement in economic data.

Central banks face a delicate balancing act as they argue for monetary prudence in the face of sticky inflation and robust job markets. The Federal Reserve has maintained data dependence and removed promises of rate cuts in 2024, while the Bank of England and European Central Bank are likely to cut rates gradually.

Corporate Earnings in Focus

Continued economic strength is a good problem for risk assets as we approach a turn in corporate profits. Exposure to risky assets, such as equities and high yield debt, is warranted given the backdrop of improving profits and financial conditions.

At the midpoint of the US reporting season, 77% of companies have reported a positive EPS surprise, with earnings growth for the first quarter standing at 3.5% and revenue growth at 4.0%. Analysts project earnings growth of 11% and revenue growth of 4.9% for 2024. The strong performance is led by Communication Services, Utilities, and Information Technology companies, highlighting the resilience of these sectors in the face of economic challenges.

Elevated expected returns

Investors must carefully select which regions and sectors to include in their portfolios while remaining vigilant and prepared to adjust holdings as global economic and market conditions evolve.

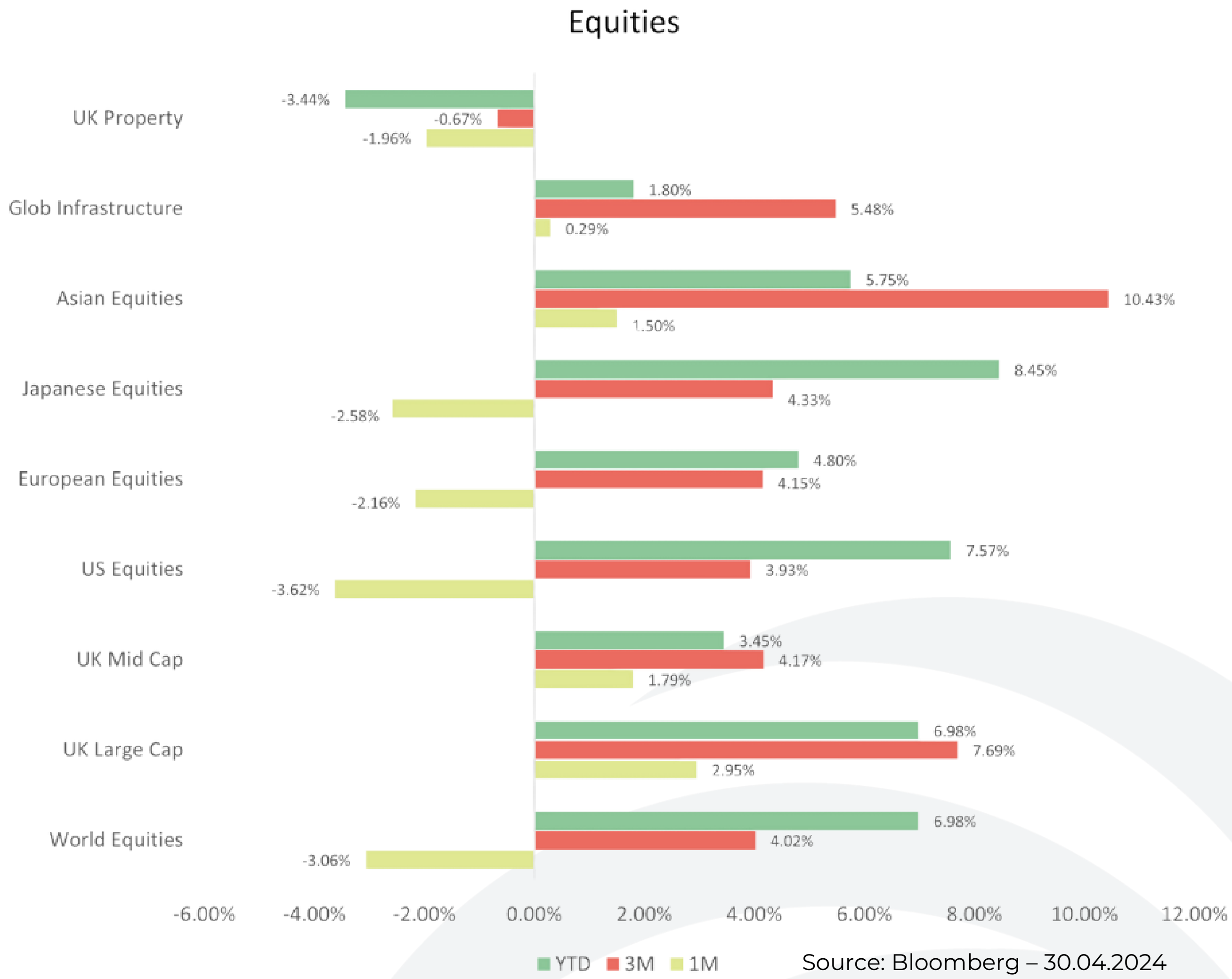
Fixed income assets have experienced a setback over the last month as economic growth has remained strong and progress on inflation has stalled. As government bond yields have moved higher, high yield and corporate bond funds have experienced setbacks. The good news is that yields across fixed income now provide attractive risk adjusted returns to investors. Patient investors are being paid to wait in fixed income assets and multi-asset investors benefit from the diversification these holdings provide. Monetary policy should allow an orderly decline in inflation, even if it takes slightly longer than anticipated.

Equity markets were down 3% over the month. US, European and Japanese equities fell as investors reassessed the risk to corporate profits from higher interest rates. UK large and mid-cap equities were notable gainers over the month as investors sought the safety of higher dividend yields and cheaper valuations. Asian equities also rallied as better economic data buoyed the case for the region.

Conclusion

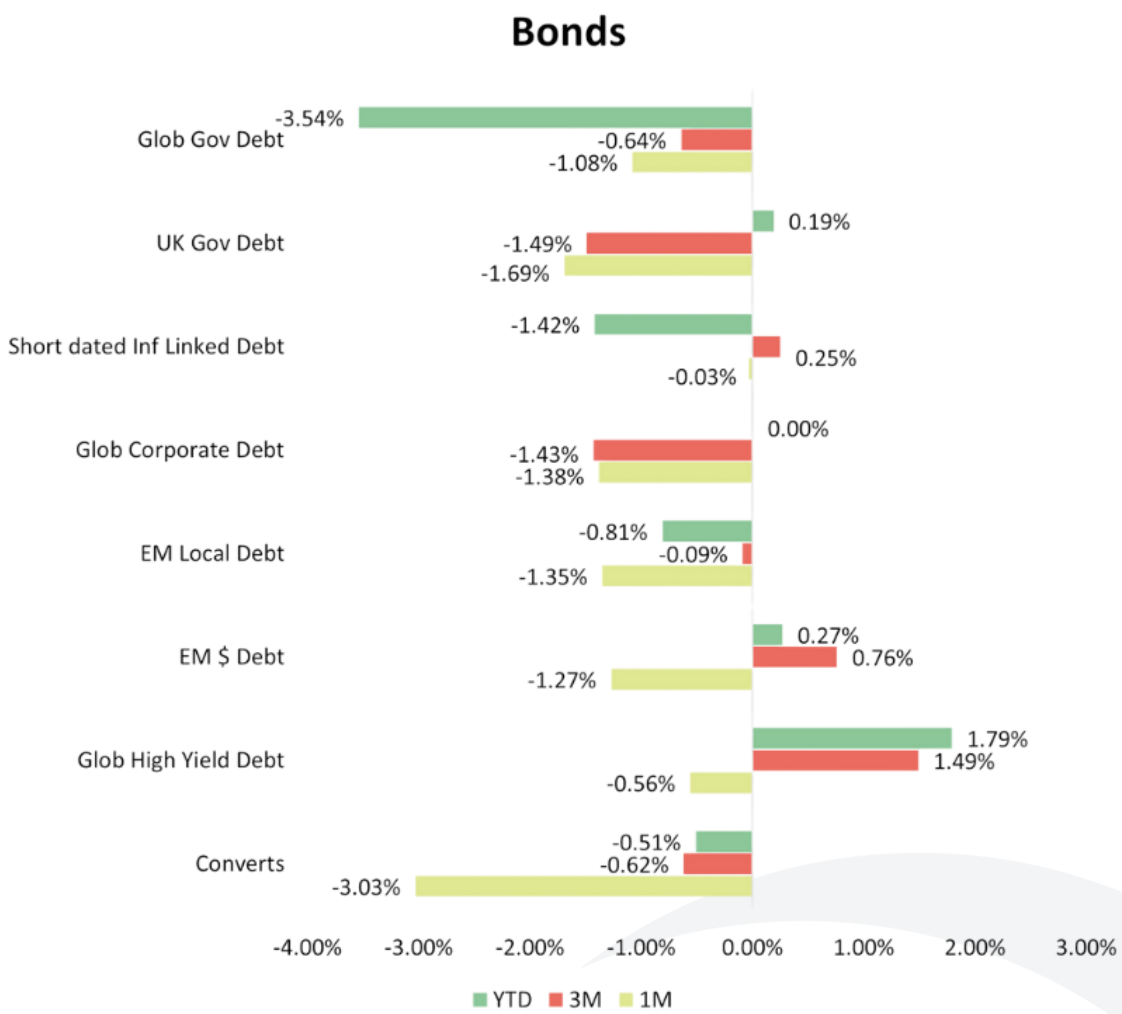
We started 2024 with a focus on expected returns and a need to broaden our equity market exposure to include smaller companies. Our first step in this direction was in February and we envisage an additional step later this month. We will continue to monitor corporate earnings and incoming economic data to assess portfolio risks and will make changes if required.

Asset Class Performance:



Source: Bloomberg – 30.04.2024

Past performance is not a guide to future performance



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