

SEPTEMBER 2023

MONTHLY COMMENTARY

During the month of September central banks took centre stage with their “higher for longer” message for interest rates leading to a wobble across financial markets.

Global equities, as measured by the MSCI World, finished down 4.3%, while global bonds, as measured by the Bloomberg Global aggregate index, also falling 2.9% for the month. In the US, Fed (Federal Reserve) chairman Jay Powell kept interest rates unchanged at 5.25%-5.5%. However, his forward guidance was clear “any relief from high borrowing costs will be neither swift nor generous.” Meaning that the resilience of the US economy might require further rate adjustments. Furthermore, the Fed dot plot projections – a survey of the 19 policymakers of future interest rate projections – pointed to a median estimate of 5-5.25% for year-end 2024. A significantly higher prediction to the 4.5-4.75% dot plot median in June. US macro data was mixed with August annual headline consumer price inflation (CPI) rising to 3.7% from 3.2% in July due to higher energy prices. While the closely watched core CPI which strips out food and energy trended down to 4.7% from 4.3% in July with shelter costs still stubbornly high.

US jobs growth continues to be softer with non-farm payrolls adding 180,000 jobs for the previous month and the growth numbers for August and July were also revised down. While the unemployment rate edged higher to 3.8% and wage inflation remained elevated at 4.3%. Furthermore, leading indicators of growth such as the manufacturing purchasing manager’s index remain below the 50-level indicating contraction for the US economy may lie ahead. Digesting the trend of data over the last few months would suggest the probability of a soft landing in the US from a recessionary viewpoint has increased. However, the lagged effects of higher interest rates are perhaps yet to be felt.

In the UK, the Bank of England avoided raising interest rates for the 15th consecutive time keeping deposit rates unchanged at 5.25%. An unexpected fall in inflation to 6.7% in August couple with a cooling jobs market were the key contributors for no change. Additionally, the UK house prices fell for the fifth month in a row down 4.6% in August.

Chinese growth remains a concern. The property market continues to falter with Country Garden – one of the country’s largest real estate companies - just avoiding default on payments. The sector accounts for nearly a quarter of economic growth for the second largest economy in the world. Consumption remains subdued and youth unemployment so high that the government have cancelled publication of the data.

ASSET CLASS

In September, all equity sectors were down except for energy. Oil production supply cuts by Organization of the Petroleum Exporting Countries (OPEC) continue to support oil prices and profit taking in outperforming sectors such as technology and communication services was taking place too. But while global equities came off, their high's developed market equity indices are still up above 10% for the year.

This year, names such as Microsoft, Apple, Nvidia, Amazon and Google have contributed to over 70% of the S&P 500 index performance (the index is up 21%!). The key driver has been the buzz around artificial intelligence (AI) with language learning models such as Chat GPT (part owned by Microsoft) & Bard (Google owned) the key players.

Defensives sectors such as consumer staples and healthcare continue to lag the broader market, but our view is for these sectors to outperform in the near term if increased market volatility occurs.

Bond volatility also increased, exacerbated by the hawkish tones of central banks shifting the yields across the US government bond curve higher. The 10-year treasury yield rose by almost 0.5% to 4.75% while the shorter maturities e.g., the 1-year treasury yield rose by 1% to 5.4%. As yields rise bond prices fall.

Within commodities, West Text Intermediate (WTI) Crude and Brent crude rose 8.6% and 9.7% respectively for the month. Copper prices fell on Chinese growth concerns while Gold fell 5% on higher interest rate projections. The world food price index was little changed up 1.3% in June on rising prices for vegetable oils and a significant decline in sugar price index, declines in vegetable oils, dairy and meats were offset by a surge in sugar and maize prices.

Strong moves across currencies particularly on Cable - the slang term used for the price of British pound (GBP) against the Dollar (USD). Material sterling weakness caused the currency to drop from 1.27 to 1.21 versus the dollar.

While the consensus appears to be for a soft landing in the US and recessions in Europe and the UK, inflation remains above the 2% target and the Fed, at the minute expects rates to be higher for longer. The lagged effects of the monetary tightening are yet to be felt by the consumer and we remain cautious on risk assets from an asset allocation perspective.

The London & Capital mantra of high-quality investments shines ever brighter. Our asset allocation for multi asset balanced portfolios is defensive with an overweight to fixed income versus equities. Bond yields are extremely attractive, and our focus is on major corporations and systematically important financial institutions while our equity exposure focuses on high quality global brands with resilient cash flow generation across defensive sectors and structural growth sectors.

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