Wealth Management
Weekly Market Update

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Market Update

Last week, global markets rallied by 2.1% on the back of lower than expected inflation figures. In the US, stocks rose by 2.2% as core personal consumption expenditures, the Federal Reserve's preferred measure of inflation fell by more than expected. The rally also saw a broadening of sectors: all 11 sectors of the US large capitalization stock market increased over the week, in contrast to the past year where returns have been singularly driven by technology. Tech sector growth nevertheless remained strong, and in particular saw Apple reach its all time high share price, and become the first publically traded company to reach a $3 trillion market capitalization. European stocks rose by 2.5% as eurozone inflation was a tick lower than expected, at 5.5% versus a consensus of 5.6%, raising hopes that interest rates could be near their peak. UK stocks also participated in the rally, but rose by a smaller 0.9% as persistent inflation and hawkish statements from the Bank of England weighed on investor sentiment. Bonds moved in the opposite direction to equities as UK gilts fell by 0.1%. Oil prices rose by 2.4% over the week as the Energy Information Administration reported that US crude oil inventories fell by more than expected.

UK Stocks	US Stocks	EU Stocks	Global Stocks	EM Stocks	Japan Stocks	Gilts	GBP/USD
▲ +0.9%	▲ +2.2%	▲ 2.5%	▲ +2.1%	▼ -0.2%	▲ +0.7%	▼ -0.1%	▼ -0.1%

all returns in GBP to Friday close

Macro News

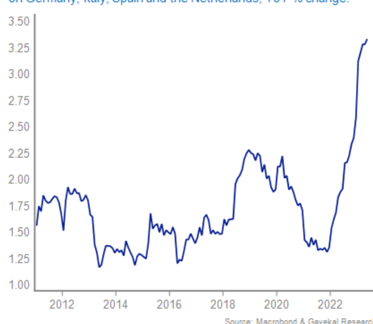
- European inflation was reported to have fallen sharply again in June, down to 5.5% from 6.1% in May. However, core inflation, which strips out the most volatile contributors to inflation such energy and food prices, rose slightly to 5.4%, giving the European Central Bank more room to press forward with additional interest rate hikes. Markets currently anticipate that the ECB will start cutting rates by H2 2024. However Chief Economist at the ECB, Philip Lane, pushed back against this assumption last week, saying "Where I do think the market should ask itself questions is about the timing or the speed of reversal of restrictive policy".
- For a long time, equities have offered the most attractive risk-reward profile, with the acronym TINA (There Is No Alternative) becoming commonplace among investment managers over the last decade. However, the sharp rise in the yields of fixed income securities means that alternative equity classes are becoming increasingly viable.

The Week Ahead

- Investors are awaiting the release of the June ISM Manufacturing PMI which reports on the condition of the US manufacturing sector. Analysts are calling for a mild recovery from May's lows of 46.9, but ultimately expect the US manufacturing to remain within contraction territory.

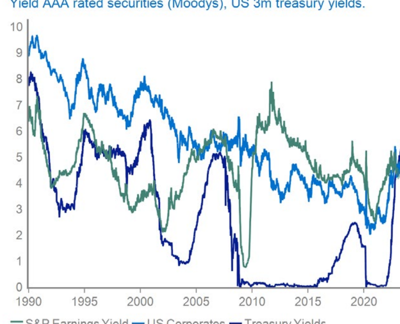
Week in Charts

Wage growth in the Eurozone is accelerating
Eurozone negotiated wages tracker of average wage growth based on Germany, Italy, Spain and the Netherlands, YoY % change.



The ECB will be particularly concerned about a general acceleration in wages, a phenomenon rarely observed in Europe. As wages increase, the risk of second order inflation effects and the possibility of a wage-price spiral, will likely encourage them to continue raising interest rates to curb demand and slow down the economy.

Bonds are back - the end of TINA?
Yields across asset classes, S&P Earnings yield, US Corporate Yield AAA rated securities (Moodys), US 3m treasury yields.



For income focused investors, equities have been able to fill both the requirement for capital return and income generation since the Global Financial Crisis. However, yields across asset classes have broadly converged and sharp rise in government bond yields has provided more attractive risk-return profile for investors with shorter time horizons.

View From the Desk

Last week, central bankers held a conference in Sintra, Portugal. There, they confirmed that inflation remains sticky, and interest rates will thus remain elevated for some time. The central banks keep telling us what they will do. They have been consistent in their fight against inflation. Even when something did break, banks with poor risk management, central banks did help markets, but only through the provision of credit lines. Unfettered money printing or abandonment of interest rate hikes was not an option they would entertain.

Fed's Jerome Powell said that "If you look at the data over the last quarter, what you see is stronger than expected growth, a tighter than expected labour market and higher than expected inflation". Britain's Andrew Bailey, who's facing worse growth, a tighter labour market and higher inflation than his peers, added that "I've always been interested that markets think that the peak will be short-lived in a world [where] we're dealing with more persistent inflation"

Our investment committee member, the learned and insightful Anthony Peters, has reiterated for years that central banks will continue to tighten until they suffocate the economy.

One of the professional quirks in the asset management industry is the "cathedral-sized ego". If markets are efficient, then everything that's in the public sphere is well priced-in. To make 'alpha', they would need to think outside the box. See what others don't. Adding up for twenty or thirty years, the thought "what can I see others don't" easily mutates to "I can see what others can't".

If one's career mostly consists of the last fourteen years, when central banks went out of their way to curb volatility, then it's natural to think that central bankers communicate a hawkish stance simply to lower inflation expectations and exert some control over wages, but at heart, they are market doves. They want low rates and money to flow easily.

In reality, central bankers have long lamented their inability to escape the Zero Interest Rate trap. Very low rates tend to cause pension deficits, an anathema in an ageing society. And they tend to be the source of asset misallocation. If a client is getting 10% returns on a balanced portfolio, why risk their money and waste their time starting their own business for merely double the rate of return?

We doubt that central banks are eager to cut rates soon and return to a an ultra low interest rate regime. They would be happy to avert a systemic crisis through credit lines (the literal job of a lender of the last resort), even pause rate hikes when necessary. But if the market thinks that central bankers are itching to lower rates before they see clear evidence that they are suffocating the economy, they could find themselves surprised, and their ego-cathedrals in ruins.

Sticky inflation means sticky rates. And (high) sticky rates mean market volatility as well as financial and policy divergence. In this world, money managers should remain sanguine about risk and recognise that their best friends in the past decade, central bankers, are not there anymore to bail them out at the first sign of trouble. Where risks are taken, the potential rewards should be worth it. And we would do well to remember that fighting the central bank is folly, not because there are always right, but because they are powerful enough even to remain wrong.

George Lagarias – Chief Economist

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