HYMANS ROBERTSON

Market brief

July 2024

July highlights

- Data indicated that US GDP growth rebounded in Q2 to an above-forecast annualised pace of 2.8%, due to a reacceleration in domestic demand. The eurozone economy also grew more quickly than expected in Q2.
- The J.P. Morgan Global Composite PMI, while still consistent with solidly expanding activity, suggests global economic growth eased for the second month running in July as manufacturing slowed.
- US composite purchasing managers' indices (PMI) quickened in July as services seemingly grew more quickly than expected, while manufacturing activity slipped back into contraction. Equivalent survey data pointed to a robust post-election acceleration in the UK, while surveys suggest the eurozone economy stalled in July.
- US headline and core CPI fell more than expected in June, to 3% and 3.3%, respectively. Equivalent UK CPI measures remained unchanged at 2% and 3.5%, respectively. Flash releases showed eurozone annual headline CPI rose unexpectedly to 2.6% in July, while core CPI was unchanged at 2.9%.
- Amid general progress on inflation, market-implied interest rates fell, with markets moving to price in at least two 0.25% pa interest rate cuts from the US Federal Reserve (Fed) and Bank of England (BoE) in 2024.
- As a result, sovereign bond yields fell, while credit spreads were little changed. Investment- and speculative-grade credit markets delivered similar total returns, as falling yields benefited longer-duration markets.
- Equity markets rose modestly. Stocks sensitive to interest rates outperformed at the expense of technology stocks, which gave back some of their year-to-date gains. Investors took profits and grew sceptical about the potential future returns from the huge capital expenditures on AI-related infrastructure.
- Gold rose a further 4.1% amid heightened tensions in the Middle East and concerns over a global slowdown. Oil prices fell as weak demand from Asia outweighed supply concerns.
- The trade-weighted Japanese yen rose 4.1% in July, the biggest monthly gain since 2016, as the Bank of Japan unexpectedly raised interest rates at its July meeting. Meanwhile, expectations of interest-rate cuts elsewhere grew.

Market performance to end July 2024

UK	Jul 24	Q2 24	2024
EQUITIES	3.1	3.7	10.8
BONDS			
Conventional gilts	1.7	-0.9	-0.8
Index-linked gilts	1.9	-2.1	-2.0
Credit	1.6	-0.1	1.5
PROPERTY**	n/a	1.7	2.3
STERLING			
v US dollar	1.6	0.1	0.8
v euro	0.6	0.8	2.9
v Japanese yen	-5.0	6.4	7.5

GLOBAL	Jul 24	Q2 24	2024
EQUITIES	1.3	3.5	14.8
North America	1.5	3.9	16.2
Europe ex UK	0.7	0.6	10.9
Japan	-0.7	1.4	19.6
Dev. Asia ex Japan	2.1	0.6	6.0
Emerging Markets	1.1	6.9	12.6
GOVERNMENT BONDS	1.8	-0.9	0.1
High Yield	1.8	1.4	5.2
Gold	4.1	5.1	17.3
Oil	-6.7	-1.1	3.8

Percentage returns in local currency ($ for gold and oil). All returns to 31/07/2024, *apart from property and hedge fund data 28/06/2024 Source: DataStream and Bloomberg. FTSE Indices shown: All Share, All World, North America, AW Developed Europe ex-UK, Japan, AW Developed Asia Pacific ex-Japan, Emerging, Fixed Gilts All Stocks, Index-Linked Gilts All Maturities, iBoxx Non-Gilts, S&P GSCI Light Energy, Crude Oil BFO, ICE BofA Global High Yield, Gold Bullion LBM, MSCI UK Monthly Property and BBG Aggregate Government Total Return.

Fixed income markets

Sovereign bond yields fell and inflation expectations eased slightly

Benchmark US 10-year bond yields fell 0.4% pa to 4% pa on the back of June's softer inflation data and weakness in the labour market. This heightened expectations of interest-rate cuts by the Fed. Equivalent UK and German yields also fell by 0.2% pa to 4.0% pa and 2.3% pa, respectively. Japanese 10-year yields were little changed, at 1.0% pa, despite declines in yields elsewhere, following the BoJ's decision to increase its policy rate and announcement of its intentions to reduce the pace of Japanese government bond purchases.

Ten-year implied inflation, as measured by the difference between conventional and inflation-linked bonds of the same maturity, eased 0.1% pa in the UK, US, and eurozone, to 3.5% pa, 2.2% pa, and 1.9% pa, respectively.

Falling yields supported total returns in fixed income markets

Investment-grade credit spreads were little changed over the month: US and UK credit spreads stayed at 1.0% pa and 1.1% pa respectively, while their European counterparts declined 0.1% pa to 1.1% pa. Speculative-grade credit spreads were also little changed, with US and euro speculative-grade credit spreads remaining around 3.3% pa and 3.7% pa, respectively. Despite the higher income in speculative-grade credit markets, investment- and speculative-grade credit markets delivered similar total returns in July as falling yields benefited longer-duration investment-grade markets.

A weaker US dollar contributed to positive emerging market sovereign debt returns

Hard-currency debt, as measured by the J.P. Morgan EMBI Global Diversified Index, returned 1.9% pa in dollar terms, as income and decline in underlying treasury yields more than offset a rise in spreads. Local-currency emerging market debt, as measured by the J.P. Morgan GBI-EM Global Diversified Traded Index, returned 2.3% pa in dollar terms, as yields fell 0.2% pa and index currencies, in aggregate, strengthened against the US dollar.

Global equities

Sectors sensitive to interest rates outperformed, and 'growth' stocks trailed value

Amid a decline in sovereign bond yields, the more interest-rate-sensitive sectors of the economy, such as small-cap stocks, outperformed as the FTSE All World Total Return Index rose a modest 1.3%. Utilities, which are often seen as a bond proxy, were the best-performing sector. Financials were the second best-performing sector and industrials, consumer staples, telecoms and healthcare also outperformed, in that order, as did energy stocks, albeit very modestly. This broad sector outperformance has come at the expense of technology stocks, which gave back some of their year-to-date gains as investors took profits. Though big US technology companies generally delivered decent Q2 earnings, investors grew more sceptical over potential future returns on investment related to huge capital expenditures on AI infrastructure. Consumer discretionary was the only other sector to underperform the broader index in July. As a result of this sectoral performance, value stocks outperformed growth stocks by a wide margin.

UK stocks outperformed and, to a lesser extent, so did North American equities

Above-average exposure to financials and consumer staples will have helped the UK outperform, while robust PMIs and a better-than-expected Q2 GDP reading pointed to an improving domestic economic environment in the UK. North American equities were the only other region to outperform, although very modestly. More than a half of US companies reported Q2 earnings and, while technology stocks suffered a setback, more than two-thirds have beaten analysts' expectations, which contributed to the broadening of performance across sectors and drove US equities higher in July.

Japanese and European ex-UK equities underperformed

Japanese equities fell 0.7% in July, partly reflecting weaknesses in global technology stocks and pressure on overseas earnings from the rapidly strengthening yen. European ex-UK equities also underperformed, delivering a modest return of 0.7%. Disappointing PMIs coming out of the eurozone tempered optimism around the region's nascent economic recovery, while political uncertainty weighed on French stocks. Emerging market and Asia ex-Japan also mildly underperformed. Chinese economic data released in July pointed to ongoing challenges in the real estate sector and the broader impact on the economy, prompting policymakers to further loosen financial conditions.

Currencies, commodities and property

The Japanese trade-weighted yen appreciated 4.2% in July, the biggest monthly rise since 2016, as the Bank of Japan unexpectedly raised interest rates at its July meeting while expectations of interest rate cuts at other major central banks grew. Those expectations led to a 0.3% in the trade-weighted dollar, while positive economic data releases in the UK supported a 1.1% rise in the equivalent sterling measure. Oil prices fell 6.4% in July as weak demand from Asia outweighed supply concerns owing to heightened tensions in the Middle East. Those deepening geopolitical tensions and concerns about broader economic activity perhaps helped gold prices rise by 4.1%.

The MSCI UK Property Total Return Index rose 0.7% in June as aggregate capital values continued to increase for the third consecutive month. The 12-month return to end-June was 1.0%, as income growth of 5.9% more than offset a 4.7% fall in capital values. Capital values continued to fall in the office sector, down 14.2% year on year, though the pace of decline slowed in recent months. Monthly capital values in the retail sector have plateaued in recent months, though they are still down 5% compared with the same period 12 months ago. Industrial capital values have also stabilised in recent months and are slightly higher on an annual basis. Aggregate annual nominal rental growth has slowed to around 3.6% pa in June, unchanged from May. However, given the steeper falls in inflation, real rental year-on-year growth rose. Structural demand continues to support rental growth in the industrial sector, but it remains much weaker in the office and retail sectors.

The global economy

Preliminary Q2 GDP data indicated that the US economy grew at an annualised rate of 2.8%, surpassing economists' forecasts of 2.0% and up from Q1's 1.4% rate. The increase in real GDP primarily reflected an increase in consumer spending, business inventory and capital investment. Monthly data suggest the UK economy continued to grow more quickly than expected, expanding 0.4% month on month in May. The eurozone economy grew 0.3% quarter on quarter in Q2, unchanged from Q1 and above expectations of slightly slower growth. Meanwhile, the Chinese economy expanded 0.7% quarter on quarter in Q2, down from an increase of 1.5% in the previous quarter and below expectations. The latest data release was the softest since Q2 2023 and points to ongoing weakness in the property sector and a spillover effect on the domestic economy.

The timelier J.P. Morgan Global Composite PMI survey data suggest that global economic growth eased for the second month running in July as the manufacturing sector slipped back in to contraction, and output and new orders expanded at slower rates. While the composite reading is still consistent with a solid rate of expansion, and jobs growth was sustained for the third successive month, business optimism dipped to its lowest level since last November amid heightened geopolitical uncertainty and slower growth of new business.

Divergence between ongoing expansion in the service sector and weaker manufacturing activity was also apparent in most of the key regions. An expansion in US private-sector activity owed entirely to an acceleration in service-sector activity as manufacturing grew very marginally. Eurozone PMI data disappointed in July, dropping to a five-month low, and signalling near stagnation in private-sector activity as demand deteriorated, particularly in the manufacturing sector. UK survey data were a relative bright spot amid an apparent post-election bounce in activity. In contrast to other regions, UK surveys suggest private sector activity accelerated in both the manufacturing and service sectors.

At a global level, input price inflation accelerated to a 10-month high in July, with the rate of increase in service-sector costs reaching its quickest pace since March, and above that signalled for manufacturing for the twenty-seventh successive month. However, the rate of selling price inflation eased to the weakest pace since October 2020, suggesting that producers and service providers may be struggling to pass on rising costs amid softer demand.

Year-on-year US CPI fell more than expected to 3% in June, its slowest pace since June 2023. The annual core CPI, which excludes volatile food and energy prices, also fell more than expected to 3.3%. UK headline year-on-year remained at the BoE's 2% target in June, while equivalent core CPI was also unchanged at 3.5%. Meanwhile, flash releases for year-on-year eurozone headline inflation unexpectedly edged higher in July, to 2.6%, up from 2.5% in June and against forecasts of modest decline. The equivalent measure of eurozone core CPI stayed unchanged at 2.9%, above expectations of slight easing.

Amid progress on inflation, market-implied interest rates generally fell, with markets moving to price in at least two 0.25% pa interest-rate cuts from the US Fed and BoE in 2024. The BoE subsequently delivered on the first of these expected interest-rate cuts on 1 August, reducing the base rate by 0.25% pa from its 16-year high of 5.25% pa. The US Fed left interest rates unchanged at a two-decade high of 5.25–5.5% pa at its July meeting, but hinted that recent progress in lowering inflation could soon facilitate an interest-rates cut. The ECB also held its deposit facility rate steady at 3.75% pa, after delivering a widely expected 0.25% pa cut in June. In contrast to the other major central banks, the BoJ unexpectedly raised its benchmark interest rate to 0.25% pa as Japan's core inflation has stood at or above 2% for over two years. The BoJ also outlined plans to halve its monthly bond purchases by Q1 2026 to pursue a more normal monetary policy to narrow an interest-rate gap that has driven record yen weakness.

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Additional Notes

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