CARTLIDGE MORLAND
INDIVIDUAL WEALTH MANAGEMENT

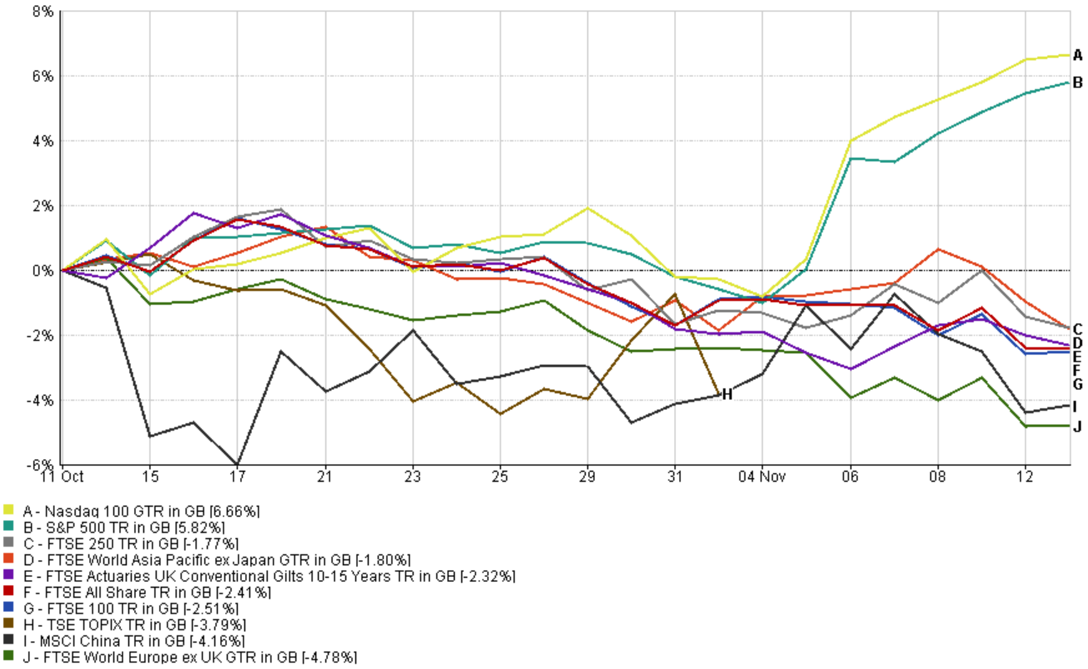
INVESTMENT COMMENTARY

13 NOVEMBER 2024

OVERVIEW

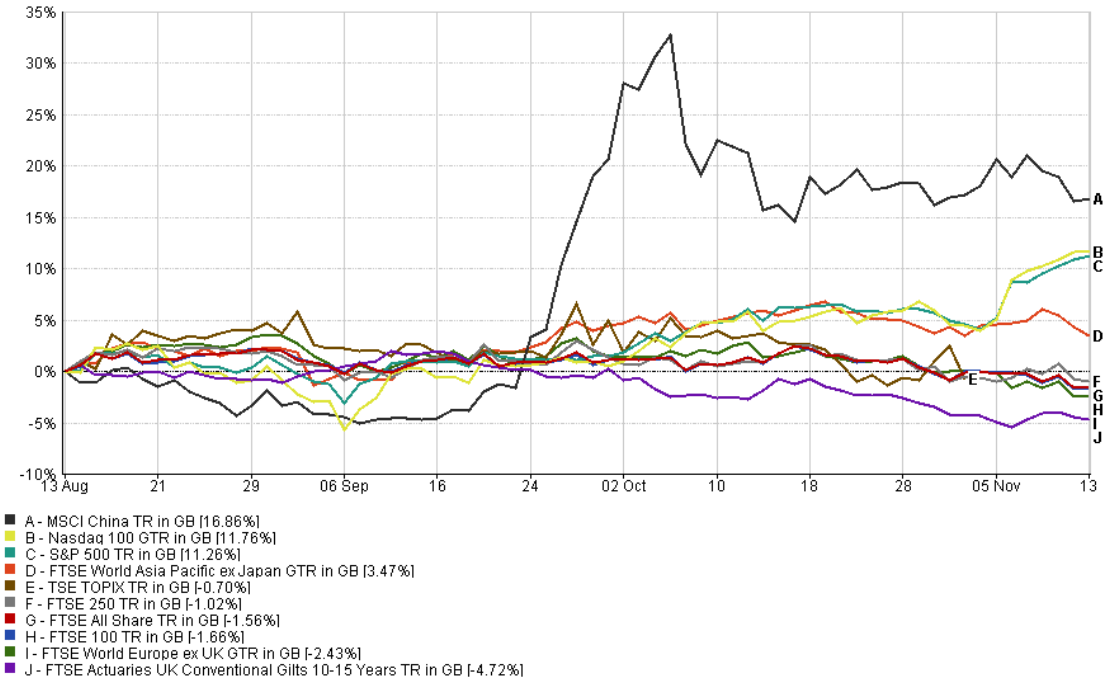
A different news story dominated investment markets over the past month – the US Presidential Election. Central Bank actions took a back seat to some extent. The emphatic presidential election victory of Donald Trump was unexpected and with it Republican control of Congress too. There has been a definite short-term reaction to the election with the US equity market rising rapidly since 6 November, but it remains to be seen when and to what extent the expected fiscal and trade policies to drive markets will be implemented.

ONE MONTH NVESTMENT MARKETS STERLING TOTAL RETURNS



11/10/2024 - 13/11/2024 Data from FE fundinfo2024

THREE MONTHS INVESTMENT MARKETS STERLING TOTAL RETURNS



13/08/2024 - 13/11/2024 Data from FE fundinfo2024

US equity markets have reached record highs whilst the US bond market fell in value in recent days as the possibility of trade tariffs, deregulation and tax cuts drove investor sentiment. President-elect Trump's policy book is likely to support corporate earnings, stoke inflation and possibly lead to interest rates remaining higher for longer.

European equity markets fell as the prospect of US trade tariffs weighed on investor sentiment. Despite a series of interest rate cuts, the European economy is struggling and if a trade war ensues, any nascent signs of economic growth could be quashed. Political uncertainty in Germany after the collapse of the coalition government and fresh elections in February 2025 has also led to investor caution.

The UK equity market has seen lacklustre returns as the Budget at the end of October led to investor concern about the longer term benefit of the Chancellor's borrowing and spending plans. This more negative sentiment outweighed the near term news of inflation falling below the Bank of England's 2.0% target to 1.7%.

The Japanese equity market has experienced heightened volatility of late. Larger exporting companies had benefited from weakness in the Yen. The snap election called by the new leader of the Liberal Democratic Party (LDP) saw the ruling LDP lose its majority. The unsettled political situation had been priced in ahead of the election and in its aftermath, investors became a little more positive as the new government is likely to continue with growth-oriented and investor-supportive policies.

After a sharp recovery in the early Autumn as a result of monetary stimulus measures and the prospect of complementary fiscal stimuli, the Chinese equity market has retreated as the fiscal measures announced have been not as significant as expected and trade tensions with the US are set to increase. The fiscal stimulus packages aimed at improving household consumption disappointed. The measures allow local governments to restructure their infrastructure and property-related debts which have been a drag on the Chinese economy, so lowering finance costs. They do not go far enough in redressing the domestic housing slump. Perhaps further measures will be introduced in the future to counter-balance potentially increased US trade tariffs.

In the wake of the US election result, the US Federal Reserve (Fed) cut interest rates by 0.25% to a range of 4.50-4.75%. The Fed commented that the US economy was growing at a "solid pace" and that the jobs market had continued to ease over the past year. Inflation remains above target at 2.60%. The US economy grew by 2.70% in the third quarter down from 3.00% in the second quarter. Against this backdrop, the Fed has to determine how quickly to lower interest rates to a “neutral” setting, in which the rates neither boost nor decrease demand. Jay Powell, the Chair of the Fed, stressed that the Fed would proceed “carefully” and “patiently” in their interest rate moves. It is likely that there could be a further cut in December but the pace of cutting may then slow – particularly as the new Trump administration’s policy priorities become clearer.

The Monetary Policy Committee (MPC) of the Bank of England (BoE) met earlier this month, a week after Chancellor Reeves’ first budget. The measures in the Budget including greater borrowing, more government spending and increased employer National Insurance Contributions are likely to be inflationary. The MPC cut Bank Rate to 4.75%, as expected, but indicated that a further cut is unlikely before early 2025. Andrew Bailey, the BoE Governor, commented that inflation needed to stay close to the BoE’s 2.00% pa target so reductions in interest rates would have to be undertaken at a moderate pace and level. Inflation fell to 1.70% in September, the first time it had fallen below target since 2021, although it is predicted to rise again in coming months. The BoE will have to weigh up the impact of the Budget and probably adopt a cautious approach. It is expected that inflation will take longer to return to target in the wake of the Budget. The possible introduction of trade tariffs by the US may also add to inflationary pressures.

The European Central Bank (ECB) has continued to cut interest rates – by 0.25% to 3.25% at its latest meeting in October – in the face of weak economic growth. Christine Lagarde, President of the ECB, commented that the Central Bank was on track to meet its 2.00% inflation target. She said that future decisions would be data dependent. The concern for the ECB is that inflation may undershoot target as it fell to 1.70% in September, so there are potentially further rate reductions likely in December 2024 and January 2025.

The Bank of Japan (BoJ) made no changes to monetary policy at its meeting on 31 October 2024. As with other major central banks, the BoJ has said that future interest rates decisions would be dependent on market and economic developments. The difference with the other central banks is that the next move is set to be up.

Yields on UK gilts have increased on the back of the Budget announcement of an additional £28bn a year government borrowing and a £40bn tax increase. Increased supply of gilts would see prices fall (yields rise), whilst the Budget measures are deemed to be inflationary - so interest rates are likely to fall at a far slower pace than previously anticipated. Similarly, President Trump’s economic plans are also likely to be inflationary which has resulted in US Treasury yields increasing. Again, the Fed may not be able to reduce interest rates as quickly as expected.

OUR VIEW

Compiled by Angela Cooper, MD - Investment Services.

Angela runs Cartlidge Morland's Investment Management team, with over 30 years' experience in investment research working for investment companies, leading UK national IFAs and wealth managers. Angela graduated from the London School of Economics and is a Chartered Insurance Practitioner.

In the UK, the new Government's recent Budget cast a pall over financial markets – as the costs to business of increased taxes (employer NICs) and further employment legislation sank in. The business community is doubtful the Chancellor's Budget will boost long term economic growth.

More positively, the government is promising massively increased investment in infrastructure and innovation, using public funds alongside private investment – leading to the classic Keynsian 'multiplier effect'. The latter will depend on how wisely and effectively the public funds concerned are committed, so to what benefit remains questionable. Optimistically, such investment should improve the economy's short term growth rate at the very least. Through pension reforms, the government also hopes to 'unlock' billions of pounds in additional institutional investment. If the UK can indeed break the cycle of low business investment, the economy will benefit over the long term. The system of capital allowances radically improved by the previous government is supported by the Chancellor.

Higher salaries in the UK's burgeoning public sector should boost private sector consumption but potentially at the cost of reduced private sector investment and in due course, possibly higher inflation and interest rates. Many companies will benefit in the meantime from government largesse, whether it is well targeted or otherwise, so short term pessimism seems exaggerated whilst longer term concerns are valid. Some quoted companies stand to benefit more from increased public spending than they will lose in increased NICs.

In the US, neither Presidential candidate saw much virtue in fiscal rectitude and the electorate favoured President Trump's agenda of lower taxes, higher spending and a burgeoning Federal deficit. President Trump would argue that higher growth will permit the US Treasury to bring the deficit under control, with lower taxes. The difficulty is that the US political establishment has seemingly lost its appetite to worry about Federal deficits. They have been cheaply financed by the rest of the world and the US economic juggernaut powers on. Will there ever be a day of reckoning, with financial markets refusing to absorb ever larger issuance of US Treasury Bills? Not in sight presently it would seem.

US corporations stand to benefit handsomely from increased federal spending and from a President actively seeking a Chair of the Federal Reserve who will regard lower interest rates as a priority. The strength of Corporate America is likely to continue and shareholders stand to benefit from it. There will be increasing danger of boom turning to bust – but that will be some time away and investors stand to profit from Mr Trump's policies, hence the rise in US share prices and the US dollar. We will be increasing portfolio exposures to US equities as earnings growth seems likely to remain strong, alongside decent share price performance.

Europe is an economic zone in difficulty as the EU's most important nation fiscally and economically suffers economic stagnation and political impasse. The German economy is unapologetically focussed on all forms of manufacturing, but is particularly strong in high value manufacturing, including engineering and scientific prowess. Past success has led to demands from workers for increased wages – at a time when energy prices have risen significantly, with access to cheap Russian gas severed by sanctions. Against this challenging economic background, the political class is in crisis with a moribund coalition government having collapsed and fresh elections in February 2025. German leadership is absent from the eurozone presently and France's President Macron cannot fill the vacuum because the French elections have left France without an elected government.

The existence of the ECB and the stable leadership of Christine Lagarde have been critical to maintaining EU monetary credibility. There has been notable success in controlling inflation and the EU unemployment rate remains low. The eurozone economy is growing sluggishly and inflationary pressures still lurk, so the ECB's policies are inevitably cautious. Some EU economies, most notably Spain's and to some extent Italy's, are performing well, whilst French government expenditure continues to ensure a reasonable level of growth in France. Donald Trump's potential tariffs/trade regime could hit Europe's exporters hard, which is an additional concern.

The Asia Pacific region has received a boost resulting from Chinese government stimulus measures, a stronger dollar ensuring exports remain competitive and additional re-shoring of US/European investment from China to the wider region. We continue to hold high quality, well diversified Asia Pacific equity funds.

It remains likely that interest rates in the developed economies, with the exception of Japan, will continue to fall. Presently, only the pace and scale of such falls are questioned. Lower interest rates make the fixed income from bonds increasingly attractive with relatively high level of yields available currently. Against this background, bonds appear to be returning to their traditional role of balancing equity market risks effectively.

If you have any queries please do not hesitate to contact your Cartlidge Morland consultant.

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