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Market Pulse

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STOCK MARKETS RALLY TO ALL-TIME HIGHS

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Numerous global stock markets rallied to new all-time highs in February, buoyed by the expectation of interest rate cuts later in 2024, strong labour markets, a better-than-expected earnings reporting season and the potential for increased profits from the application of artificial intelligence (AI). Global activity data was mixed, with US data generally remaining strong, although there were some indications of slowing household consumption and reaccelerating inflation. Activity in Europe remained subdued, although sentiment surveys mainly showed continued improvement. Major central banks pushed against the notion of rate cuts in Q1, suggesting that monetary easing for the US Federal Reserve (Fed) and the European Central Bank (ECB) would start around mid-year or even later. Bond markets fell in response to the somewhat hawkish central bank commentary. Meanwhile, commodities continued to rise amid ongoing Middle East tensions.

Macro

Global activity data was mixed in February, with US data generally remaining strong, although there were some indications of slowing household consumption and reaccelerating inflation. European activity data remained subdued, although sentiment surveys mainly continued to improve.

February purchasing managers' indices (PMIs) were broadly suggestive of a recovery in manufacturing output, with rises in the US and the UK – the composite indices in both regions remained in expansionary territory (above 50). However, the Eurozone was mixed, with a fall in Germany and increases in the rest of the region. The Eurozone's composite PMI rose by more than expected; while it remained in contractionary territory, there were strong improvements in the employment and new orders subcomponents.

Meanwhile, central banks continued to push against the notion of rate cuts in Q1, suggesting that monetary easing for the Fed and the ECB would start around mid-year or even later.

US

US inflationary pressures in January accelerated by more than consensus expectations, with headline consumer prices up by 3.1% year-on-year (y/y) and core prices by 3.9%. This was driven by a rise in the housing subcomponent (4.6% y/y) while core services (5.4% y/y) also showed continued signs of pricing strength amid robust demand. The rise in inflation likely partly reflected annual start-of-year price changes.

Labour market data continued to be robust. Non-farm payrolls showed that 353k jobs were added in January, nearly double consensus expectations of 185k. Unemployment remained low at 3.7%, and average hourly earnings rose by more than expected (4.5% y/y). Job openings were up by 1.1% month-on-month (m/m) in December, with the ratio of job openings to unemployed also rising slightly, suggesting continued strong labour demand.

However, there were signs of slowing household consumption, with January retail sales down by 0.8% m/m. The control group, which is used to calculate GDP, was down by 0.4% and previous months' data were revised down. Although cold weather likely contributed to the weakness in January, areas like non-store retail sales (-0.8%) were indicative of weaker demand at the start of 2024. The deterioration in credit conditions also continued in Q4, albeit at a slower pace than Q3, with the Senior Loan Officer Opinion Survey showing tighter lending standards and weaker loan demand.

Meanwhile, the Fed's January meeting minutes reflected a somewhat cautious tone among the Federal Open Market Committee, with most members concerned about moving "too quickly to ease the stance of policy". This suggested that rate cuts may come later in 2024 than previously expected.

Europe

Eurozone data also showed weakness in household consumption. Retail sales fell by 1.1% m/m in December. The fall was broad-based across countries, with declines in Germany (-1.6%), France (-1.0%) and Spain (-1.4%). Consumption may have been weighed down by the treatment of spending on vouchers during the holiday period and still-weak consumer confidence relative to history. German industrial production fell by 1.6% m/m in December (with a 3.4% fall in the construction sector a key drag amid poor weather) and manufacturing production was down by 1.4%. Overall, the weaker economic backdrop led the European Commission to downgrade its 2024 GDP growth forecast for the region from 1.2% y/y to 0.8%.

Meanwhile, February headline consumer prices decelerated to 2.6% y/y, from 2.8% in January, and core inflation also slowed to 3.1%, from 3.3%. However, the ECB's January meeting minutes were hawkish, with the Governing Council expressing the need to "stay the course" and avoid cutting too early as this "could entail high reputational costs". Governing Council Member Holzmann, who is considered a hawkish member, suggested in an interview in February that it was unlikely the ECB would cut before the Fed, stating, "I don't see circumstances which bring us to cut before."

MARKET ROUND-UP

Equities

Numerous global stock markets rallied to new all-time highs in February, with the MSCI All Country World index up by 4.7% (4.7% in euros) over the month. The MSCI USA rallied by 5.4% (5.8% in euros), while European ex-UK equities were up by 2.8% (2.4% in euros).

Equities were buoyed by likely rate cuts later in 2024, still-strong labour markets and the potential for increased profits from the application of AI. In terms of the latter, Nvidia's Q4 earnings were a key market focus, and the company posted another blockbuster set of figures. Revenue rose by 265% y/y in Q4 to $22.1bn, compared to market expectations of $20.4bn. CEO Jensen Huang stated: "Accelerated computing and generative AI have hit the tipping point... Demand is surging worldwide across companies, industries and nations." Nvidia is now the third largest US company by market cap, moving above Amazon and Google and only behind Apple and Microsoft.

Japanese equities also rose to new historical highs for the first time since December 1989 amid support from improving corporate governance, economic normalisation, loose monetary policy relative to other major central banks and strong exports. The MSCI Japan was up by 5.5% (3.4% in euros) in February.

Small-cap equities rallied by 3.9% (3.8% in euros), more than recovering losses from January. However, the asset class underperformed large caps as higher rates acted as a headwind.

Emerging-market (EM) equities outperformed developed markets, rallying by 5.1% (5.2% in euros). The asset class was supported by a rally in Chinese equities (8.6%) as the authorities sought to stem stock market losses and introduced measures to prevent excessive selling, while also cutting lending rates.

Bonds

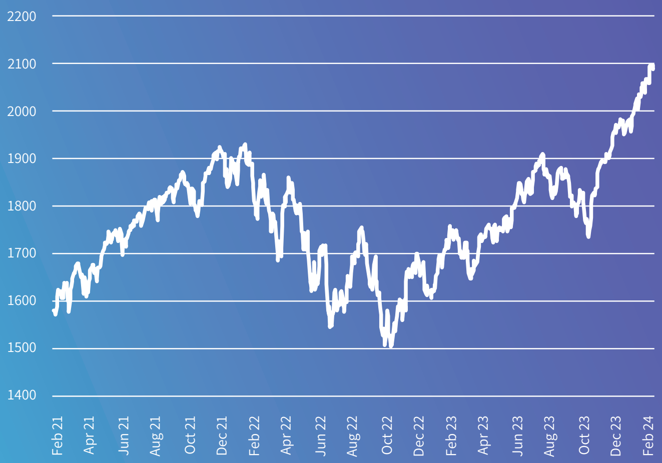
Global bond markets fell in February, hampered by rising yields as the timing of rate cuts for 2024 was pushed out and the magnitude of expected cuts was reduced. The ICE BofA 5+ Year Euro Government bond index was down by 1.4% over the month.

European investment-grade (IG) corporate bonds fell by 0.9% as yields rose by 29 basis points (bps) to 3.94%, with the spread narrowing by 9bps to 120bps. Global high-yield bonds eked out a 0.1% gain as the income yield offset the modest capital loss, with yields up by 7bps to 7.03%. High-yield spreads narrowed by 31bps to 271bps over the month.

EM local debt fell by 0.3% in February, with yields up by 6bps to 6.21%. EM hard debt returned 0.6%, with elevated yields offsetting a small capital loss as yields rose by 1bp to 7.62%.

CHARTS OF THE MONTH

Global Equities



Source: ILIM, Bloomberg. Data is accurate as at 29 February 2024.

Bonds – German 10-year yield

Source: ILIM, Bloomberg. Data is accurate as at 29 February 2024.

MARKET SNAPSHOT

Market returns (EUR)

Equity Markets (EUR)	MTD Return (%)	YTD Return (%)	2023 Return (%)
MSCI Ireland	4.2	11.5	20.6
MSCI United Kingdom	0.4	0.7	10.3
MSCI Europe ex UK	2.4	4.4	18.5
MSCI North America	5.6	8.9	22.3
MSCI Japan	3.4	10.0	16.7
MSCI EM (Emerging Markets)	5.2	2.0	6.5
MSCI AC World	4.7	7.1	18.6

10-Year Yields	Yield last month (%)	2023 Yield (%)	2022 Yield (%)
US	4.25	3.88	3.87
Germany	2.41	2.02	2.57
UK	4.12	3.54	3.67
Japan	0.71	0.61	0.42
Ireland	2.82	2.38	3.13
Italy	3.84	3.69	4.70
Greece	3.46	3.06	4.62
Portugal	3.12	2.66	3.59
Spain	3.29	2.99	3.66

FX Rates	End last month	2023 Rates	2022 Rates
U.S. Dollar per Euro	1.08	1.10	1.07
British Pounds per Euro	0.86	0.87	0.89
U.S. Dollar per British Pounds	1.26	1.27	1.21

Commodities (USD)	MTD Return (%)	YTD Return (%)	2023 Return (%)
Oil (Brent)	2.3	8.5	-10.3
Gold (Oz)	-0.2	-0.8	13.1
S&P Goldman Sachs Commodity Index	0.9	5.4	4.3

Source: ILIM, Bloomberg. Data is accurate as at 1 March 2024.

THE ILIM VIEW – LOOKING AHEAD

Sovereign bond yields rose through most of 2023 on the back of a slower-than-expected moderation in inflation. However, yields have fallen since the peak in October 2023 as concerns around inflation have abated, with German 10-year yields below their levels from 12 months ago and US 10-year yields only slightly higher. With inflation having clearly peaked and central banks now suggesting rates will be cut in 2024, bond yields are expected to decline over the next 12 months.

On a 12-month view, our base case is that German and US 10-year government bond yields fall from current levels of 2.41% and 4.25% to 1.75% and 3.50% respectively. We believe fixed income offers a strong risk-reward profile at this stage in the cycle, with the potential to offer protection if the economy slows; the asset class is attractive from an income perspective, while also providing potential for capital gains via falling yields. We believe that the risks of materially higher bond yields have reduced and, if the economy falters, major central banks will be able to cut rates to support growth. In that scenario, we would expect bonds to outperform to a greater extent.

Global equities were resilient in 2023 as recession fears receded and a peak in central bank policy rates was likely reached. While global earnings are forecast to have fallen by 0.3% in 2023, they have held up better than feared at the start of the year as sales surprised to the upside in the better economic backdrop, and the margin squeeze for corporates has been less than anticipated. Earnings are expected to grow by 10.2% in 2024.

Global equities valuations are trading above long-term averages, and they remain expensive against both bonds and cash given the high yields currently available on these assets. Despite equities appearing expensive on a relative valuation basis, however, the outlook on a 12-month view is positive. Central banks are likely to pivot towards looser policy in 2024 as inflation continues to fall. An increasing probability of a soft landing with a rebound in earnings in 2024 should provide support. An upward bias to growth forecasts is also supportive. Over the medium term, the rollout of AI should boost efficiencies and earnings across the whole market and allow equities to trade at higher valuation levels. The ongoing green-related capex cycle could also boost earnings over the medium term. Any short-term volatility in markets is likely to be offset by the above factors, resulting in positive returns on a 12-month timeframe.

THE MONTH AHEAD

MARCH

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
		6 Fed Chair Powell Testimony	7 ECB Interest Rate Decision	8 US Inflation Rate YoY GB Unemployment Rate
	12 US Inflation Rate YoY GB Unemployment Rate	13 GB GDP MoM	14 US PPI MoM US Retail Sales MoM	15 US Michigan Consumer Sentiment Prel
18 CN Industrial Production YoY CN Retail Sales YoY	19 BoJ Interest Rate Decision	20 Fed Interest Rate Decision GB Inflation Rate YoY	21 BoE interest Rate Decision DE HCOB Manufacturing PMI Flash	22 JP Inflation Rate YoY GB Retail Sales MoM DE Ifo Business Climate
	26 US Durable Goods Orders MoM		28 GDP Growth Rate QoQ Final	29 US Core PCE Price Index MoM

Source: tradingeconomics.com

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The author cannot make a personal recommendation for any person and you should seek personal investment advice as to the suitability of any investment decision or strategy to your own needs and circumstances. Any comments on specific stocks are intended as an objective, independent view in relation to that stock generally, and not in relation to its suitability to any specific person.

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Figures referenced herein have been sourced from ILIM and Bloomberg. Forecast figures have been prepared by ILIM based on reasonable assumptions, internal data and data sourced from Bloomberg.

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