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Market Pulse

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MARKETS LOWER AMID RISING TREASURY YIELDS

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US Treasury yields continued to rise over October, even amid increased geopolitical uncertainty, and global bond indices were mixed. Global stock markets were also weaker, dragged down by rising bond yields and somewhat lacklustre third-quarter earnings. Strong US economic activity contrasted with mixed data in the Eurozone. Meanwhile, the Middle East conflict raised concerns over geopolitical tensions in the region and the potential for disruption to oil supplies.

US economy

Third-quarter US GDP expanded strongly, rising quarter-on-quarter (q/q) by an annualised rate of 4.9% against consensus expectations of 4.5%, and up from 2.1% in Q2. This was the fastest growth rate since Q4 2021 and was supported by an 8.4% rise in private domestic investment, as well as strong gains in consumer (4.0%) and government spending (4.6%).

US labour-market data were indicative of a market in rude health too. August job openings rose by 0.8 million to 9.6 million, compared to an expected unchanged reading. September non-farm payrolls showed that 336K jobs were added, nearly double consensus expectations of 170K. Average hourly earnings rose by 4.2% year-on-year (y/y), down from 4.3% in August. This backdrop has likely supported the US consumer, with September retail sales rising by 0.7% month-on-month (m/m). However, sentiment among small businesses has continued to decline. The US NFIB small business optimism index fell by half a point to 90.8 in September.

US consumer prices rose by 3.7% y/y at the headline level and 4.1% (core) in September. The former was above expectations, driven by rising energy prices. However, the core figure was in line with projections and continued its downward trend of the past 12 months, reaching its lowest since September 2021.

US policy

Minutes from September's Federal Reserve (Fed) meeting and comments from Fed governors in October indicated that the central bank remains data dependent. It could now continue to hold rates at their current level amid tighter financial conditions following the rise in real interest rates (nominal rate minus inflation) in recent months. The five- and 10-year US Treasury real yields rose to 2.47% and 2.51%, respectively, in October, the highest levels since 2008. However, Fed Chair Powell reiterated a somewhat hawkish stance in a speech during the month, stating: "We've certainly got a resilient economy on our hands. It may just be that rates have not been high enough for long enough."

US fiscal concerns also remained, even after a shutdown at the end of September was avoided. Republican House Speaker McCarthy was ousted in October, raising uncertainty around negotiations over the budget, with Republican Representative Mike Johnson voted in as the replacement towards the end of the month. Negotiations to avoid another potential government shutdown in mid-November are expected to be fraught.

Europe

Eurozone data was mixed, with September retail sales down by 1.2% m/m and below market expectations. German manufacturing production also rose by less than expected (0.5% m/m) in August after a 1.5% fall in July. However, other data were suggestive of healthy demand. German factory orders were up by 3.9% m/m in August, more than double the projected rate of 1.5%. Orders for June through August rose by 4.9% from those in the previous three months (March to May). Moreover, German business sentiment showed a marked improvement as the October ZEW expectations index rose to -1.1 from -11.4 in September. The report stated: "The heightened economic expectations are accompanied by the anticipation that inflation rates will decrease further".

Consumer prices for the region fell to 2.9% y/y in October, the lowest since July 2021, amid falls in energy and food price inflation. Core prices fell to 4.2% y/y, from 4.5% in September.

Minutes from the European Central Bank (ECB) September meeting – which resulted in a surprise 25 basis points (bps) hike in the deposit rate to 4.0% – showed that the Governing Council was focused on getting inflation down to its 2% target and was willing to keep rates 'higher for longer' to achieve this. As expected, the ECB left its deposit rate unchanged at the October meeting and President Lagarde stated that "rates will be set at sufficiently restrictive levels for as long as necessary".

China

Third-quarter GDP in China rose by 4.9% y/y, above consensus expectations of 4.5%. Retail sales expanded by 5.5% y/y, industrial production by 4.5% and fixed asset investment by 3.1%. In October, China's government approved the issuance of CNY 1 trillion (€129bn) of government bonds aimed at providing infrastructure projects for areas hit by disasters. This is projected to raise the 2023 budget deficit from 3.0% of GDP to 3.8% and is likely to support activity over the next 12 months. Consensus expectations are for 5.1% y/y GDP growth in 2023 and 4.5% in 2024.

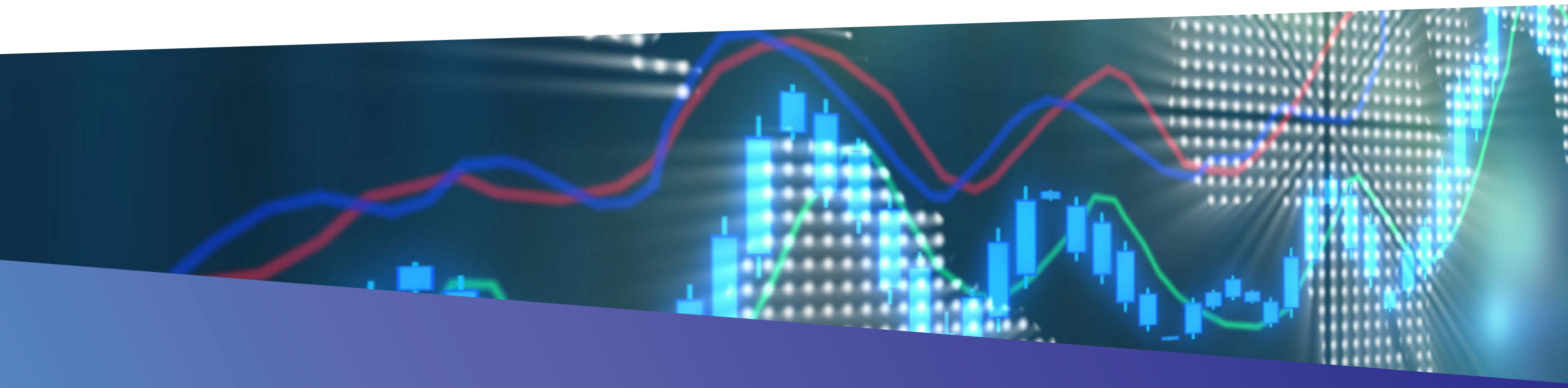
MARKET ROUND-UP

Equities

Global stock markets were weaker in October, dragged lower by rising nominal and real interest rates and somewhat lacklustre third-quarter earnings. The MSCI All Country World index fell by 2.7% (-2.8% in euros) over the month. The MSCI USA was down by 2.3% (-2.1% in euros), while European ex-UK equities fell by 3.3% (-3.4% in euros) amid a weak economic outlook.

Bonds

Bond markets were mixed in October, with yields rising as central-bank rhetoric continued to emphasise higher policy rates for longer. High yields meant that bonds benefited from carry and some indices managed to eke out a gain for the month. The ICE BofA 5+ Year Euro Government bond index was up by 0.2% over the month, with German 10-year yields falling by 3bps, to 2.81%, on the continued weak economic backdrop and falling inflation.



CHARTS OF THE MONTH

Global Equities

Source: ILIM, Bloomberg. Data is accurate as at 31 October 2023.

Bonds – German 10-year yield

Source: ILIM, Bloomberg. Data is accurate as at 31 October 2023.

MARKET SNAPSHOT

Market returns (EUR)

Equity Markets (EUR)	MTD Return (%)	YTD Return (%)	2022 Return (%)
MSCI Ireland	-6.2	11.1	-21.1
MSCI United Kingdom	-4.0	3.3	1.4
MSCI Europe ex UK	-3.4	6.3	-11.9
MSCI North America	-2.3	11.4	-13.8
MSCI Japan	-4.3	7.6	-10.8
MSCI EM (Emerging Markets)	-3.7	-0.8	-14.5
MSCI AC World	-2.8	8.2	-12.6
10-Year Yields	**Yield Last Month (%)**	**2022 Yield (%)**	**2021 Yield (%)**
US	4.93	3.87	1.51
Germany	2.81	2.57	-0.18
UK	4.51	3.67	0.97
Japan	0.95	0.42	0.07
Ireland	3.24	3.13	0.24
Italy	4.72	4.70	1.17
Greece	4.18	4.62	1.34
Portugal	3.53	3.59	0.47
Spain	3.88	3.66	0.57
FX Rates	**End last month**	**2022 Rates**	**2021 Rates**
U.S. Dollar per Euro	1.06	1.07	1.14
British Pounds per Euro	0.87	0.89	0.84
U.S. Dollar per British Pounds	1.21	1.21	1.35
Commodities (USD)	**MTD Return (%)**	**YTD Return (%)**	**2022 Return (%)**
Oil (Brent)	-8.3	1.7	10.5
Gold (Oz)	7.3	8.8	-0.3
S&P Goldman Sachs Commodity Index	-4.2	2.8	26.0

Source: ILIM, Bloomberg. Data is accurate as at 31 October 2023.

THE ILIM VIEW – LOOKING AHEAD

Sovereign bond yields are broadly higher this year on the back of a slower-than-expected pace of moderation in inflation, resilient economic activity and an upward reset for the level and timing of peak policy rates. With inflation having clearly peaked and central banks now suggesting that the end of the tightening cycle is very close, bond yields are expected to decline over the next 12 months.

On a 12-month view, our base case is that German 10-year government bond yields fall from 2.81% at end-October to around 2.00%, and that the equivalent for the US falls from 4.93% to somewhere in the region of 4.00%. We believe fixed income offers a strong risk-reward profile at this stage in the cycle and is attractive from a wealth preservation perspective. The current relatively high levels of bond yields and central banks' commitments to bring inflation down mean bonds should remain attractive on a multi-year basis with high single-digit returns possible over the next 12 months in riskier segments of fixed income.

Global equities have proved resilient in 2023 as recession fears have receded and a peak in central bank policy rates has come into view. While global earnings are forecast to be only modestly higher this year – by approximately 0.6% – they have held up better than feared at the start of the year as sales have surprised to the upside and the margin squeeze for corporates has been less than anticipated. Earnings are expected to grow by over 11% in 2024.

Global equity valuations are below long-term averages, trading on a 12-month forward price-to-earnings (P/E) multiple of 15.1x against a long-term average of 16.0x. However, equities remain expensive against both bonds and cash given the high yields currently available on these assets.

Despite equities appearing fully valued on a relative valuation basis, they are now trading attractively on an absolute basis, and 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 both growth and earnings in 2024 should also provide support. Over the medium term, the rollout of AI should boost efficiencies and earnings across the whole market and allow equities 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 time frame.

THE MONTH AHEAD

NOVEMBER

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
				3 US Non Farm Payrolls US Unemployment Rate
				10 GB GDP Growth Rate YoY Prel
	14 US Inflation Rate YoY GB Unemployment Rate	15 GB Inflation Rate YoY US PPI MoM US Retail Sales MoM		17 GB Retail Sales MoM
		22 US Durable Goods Orders		24 JP Inflation Rate YoY
	28 DE GfK Consumer Confidence	29 DE Inflation Rate YoY Prel US GDP Growth Rate QoQ 2nd Est (Q3)	30 EA Inflation Rate YoY Flash	

Source: tradingeconomics.com

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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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