London
&Capital

AUGUST 2023
MONTHLY COMMENTARY

Global equity markets sank over the month of August amid growing concerns over China's worsening economic data and renewed weakness in its real estate sector. This sentiment was reflected in falling bond prices and rising sovereign yields. Developed markets outperformed emerging markets. The US dollar strengthened against all major currencies as it benefitted from strong domestic growth rivalling a weaker global backdrop. Energy prices rose amid ongoing production cuts from Saudi Arabia and other Opec+ (Organization of the Petroleum Exporting Countries) producers.

US

In the US, investors continued to speculate over the Federal Reserve's next actions and whether the current interest rate tightening cycle ended with the rate rise in July. Therefore, market movements continued to be driven by inflation and economic data released during the month. Retail sales improved in July coming in higher than expectations, likely driven by a strong discount Prime Day. Whereas, purchasing managers' index (PMI) data, which provides insights into business activity, for manufacturing and services showed a softening in economic activity.

The unemployment rate rose from 3.5% in July to 3.8% where most projections had held expectations of an unchanged reading. This showed a slight cooling in the labour market but employment in the US remains resilient. And finally, headline inflation ticked up to 3.2% from July's 3%. The data released spurred market participants to increase the probability of a 'soft landing' scenario and no future rate hikes despite comments from Powell at the annual Jackson Hole symposium that kept potential future rate hikes firmly on the table.

August saw Fitch Ratings, a main credit rating agency in the US, downgrade the US government's credit rating from AAA to AA+, citing an erosion of governance and the growing debt burden as key motives for the decision. A decision which, despite plenty news covering, had little impact on 10-year yields. Later in the month, however, the US Treasury announced further, higher-than-expected, borrowing intentions over the coming months which led to a rise in 10-year yields and a fall in 2-year yields, shrinking the steepness of the currently inverted US yield curve. Energy stocks were the most resilient over the month, as prices lifted on the back of tighter oil supply.

EUROZONE

In Europe, stocks fell in August as market participant concerns over the economic picture in Europe grew. The purchasing managers' index (PMI) composite, which provides insight into business activity, fell further to 47 in August (a 33 month low, and well below the 50 level which signals economic contraction). Furthermore, bank stocks underperformed after the Italian government announced a tax on banks' "excess" profits.

Headline inflation remained stable and ‘core’ inflation, which strips out food and energy, eased slightly to 5.3% from 5.5% in July. While improving, inflation nevertheless remains well above the European Central Bank (ECB)’s target.

Investors continued to debate the European Central Bank’s next move over future interest rates given the weakening economic backdrop amid stubbornly high inflation readings. The ECB’s next meeting is on the 14th of September.

UK

The pessimism spilled over into the UK with equities also falling over August. Headline inflation moderated in line with expectations to 6.8%. But investors were troubled by other data from the Office for National Statistics (ONS) that revealed annualised private sector wage growth picked up to 7.9% in the three months to June. Ultimately, the high inflation figures led the Bank of England to raise rates from 5% to 5.25% and warned that interest rates would need to remain restrictive.

Despite the tight monetary policy, the UK economy surprised to the upside during the second quarter of 2023, as GDP (Gross Domestic Product) rose by 0.2% quarter on quarter versus expectations of 0%. Although better than its Eurozone counterparts, the first reading of the composite purchasing managers’ index, which shows business activity, fell below the notable 50 level in August. This represents a dip into contraction from expansion.

Housing prices fell, which negatively affected sentiment in domestically focused areas of real estate and consumer discretionary sectors. Energy stocks rose on the back of the higher oil prices.

Given the possible economic headwinds approaching, we believe that our high-quality equity and fixed income strategies remain a core part of portfolios. The equity strategy thesis of compounding high quality stocks is now more attractively valued and should remain resilient as the possibility remains real that bad economic news may be treated as bad market news, as growth wilts more than the expected soft landing would suggest.