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Monthly Market Review

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‘Red October’ causes temporary pullback in markets

Banks pause interest rates

Conflict in the Middle East proves to be a temporary hurdle

Poland roars higher

Markets were volatile in October, caused primarily by the outbreak of conflict and hawkish rhetoric from Central Banks, who suggested that the timing of rate cuts is still uncertain.

The Balanced portfolio benchmark was slightly negative with a return of -1.83%.

The latest event that investors are focused on is the Middle Eastern conflict between Palestine and Israel. Sadly, conflict has persisted within the region for multiple decades and capital markets have equally digested that news across the same period, still managing to grow by multiples despite these circumstances.

From an investment standpoint, the Israeli stock market accounts for only 0.20% of the world’s total, meaning direct impact is minimal and contained. The greater risk is centred on energy markets and the safe passage of Oil & Gas, which is in the interest of many nations further removed from the region. So far, the temporary spike in Oil prices has reversed, which has often proved to be the case when conflict has occurred in the past.

Inflation and interest rates

Bank of England

Bank of England Chief Economist Huw Pill said that recent labour market data showed a weakening of pay growth but was still too high to be consistent with the British central bank's 2% inflation target. Pay is currently growing at 7.70% per year which outstrips Consumer Price inflation of 6.70%.

The bank will undoubtedly continue to watch this level closely for fear of a continuing ‘wage-price spiral,’ meaning that growing wages can themselves be a cause of inflation as consumers continue to spend at higher than expected levels.

“***recent labour market data showed a weakening of pay growth but was still too high to be consistent with the British central bank's 2% inflation target. Pay is currently growing at 7.70% per year which outstrips Consumer Price inflation of 6.70%.***”

More recently, there are growing forecasts predicting that the bank will cut interest rates from as early as May 2024, according to recent data by Morgan Stanley.

It is important to note that forecasts are simply that and even the Bank of England have had their forecasts called into question; so much that there is a parliamentary enquiry into the quality of forecasts on inflation and connected issues.

Understandably, the Bank of England has opted to maintain interest rates at 5.25%, a level last agreed in August of this year.

US Federal Reserve

The US can cheer a fall in inflation to 3.20%, down from 3.70% a month earlier. The Federal Reserve raised rates precisely to combat this issue, with US inflation peaking at 9.10% in 2022. With the avoidance of recession so far, the Federal Reserve can pat themselves on the back for a job well done.

> *There may not be too much further to go to achieve the inflation target of 2.00%*

Whilst Fed Chair, Jerome Powell, cautioned that the campaign to manage interest rates has *"a long way to go,"* recent figures on inflation suggest that there may not be too much further to go to achieve the inflation target of 2.00%.

The bank paused interest rates for last month, opting to take no action other than to review economic data in the coming weeks.

European Central Bank

The Eurozone has pulled back from its 2022 peak of 10%+ inflation, managed by its 'rate hiking cycle'. However, it has not been without cost since EU manufacturing confidence is at the lowest since the Covid crash of 2020 and compatible with 2008.
The EU also paused interest rate rises in October, after 10 consecutive rate rises, as it also preferred to digest data. The ECB repeated its message that rates at current levels would help bring inflation to target if *"maintained for a sufficiently long duration."*

Country/Region	Manufacturing PMI	Services PMI
United States	46.7 ↓	51.8 ↑
United Kingdon	44.8 ↓	49.5 ↓
Eurozone	43.1 ↓	47.8 ↓

Key: Less than 50 = contraction   50 or more = growth

Manufacturing

Manufacturing confidence remains in contraction, with all three regions reporting negative growth for the month.

The Eurozone remains the most challenged as this marked the sixteenth consecutive month that the manufacturing sector has been in contraction territory, and the sharpest in three months. New orders, purchasing activity, and backlogs all contracted significantly and rapidly, leading to a notable decrease in factory production. In fact, October's contraction in new orders was among the largest ever recorded, highlighting significant weaknesses in the Eurozone's manufacturing economy. Furthermore, the survey indicated the fastest reduction in factory employment levels since August 2020. Business confidence also decreased, reaching an 11-month low.

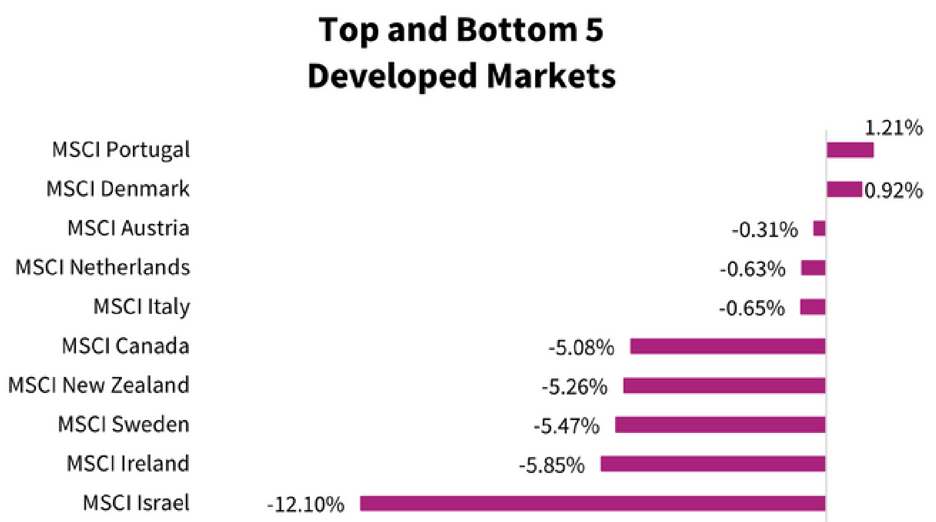
Services

The US led the pack with a move up to 51.8 (50.6 prior). The data indicated a modest expansion in output and the uptick in activity was associated with early signs of recovery in demand conditions, alongside increased capacity, as noted by survey participants. Firms expressed optimism regarding the improvement in demand conditions, with business confidence reaching its highest level in four months. To stimulate new orders, companies resorted to discounting, enabled by a much slower rise in costs. Both input prices and output charges increased at their weakest rates in three years.

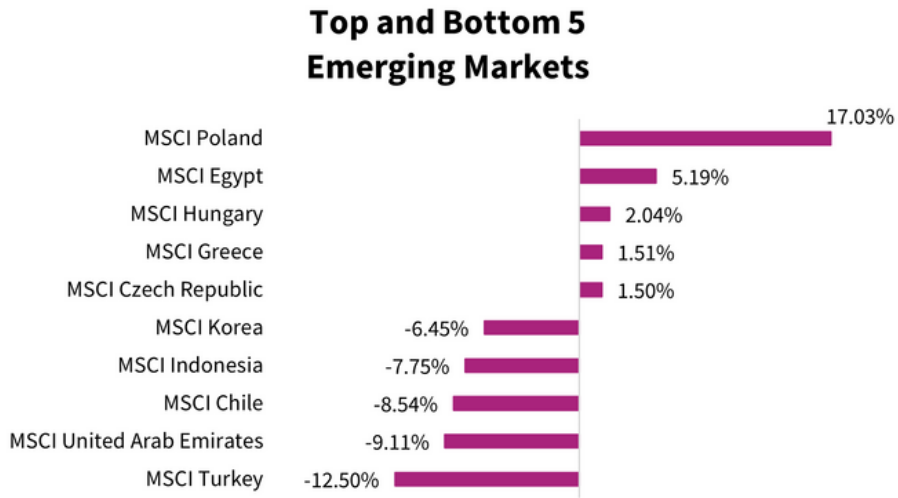
This month marked the third in which UK services contracted, remaining below the important 50 level. Respondents in the survey pointed to factors such as cost of living pressures, high interest rates, and weak consumer confidence as reasons for subdued customer demand.

Market performance

It was slim pickings for Developed Markets this month as only two made a small gain (Portugal and Denmark).
The UK index finished down by 3.61% whilst the US fared slightly better, falling by -1.76%.

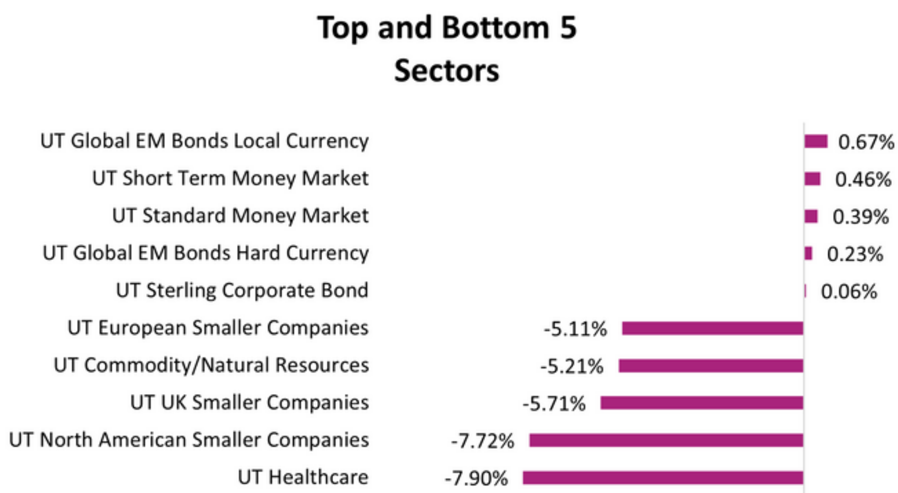


Emerging Markets painted a different picture with a strong rally in Poland, helped by rallies in national grocery store Dino Polska (+22%) and Santander Bank Polska (+16%).
It was a tough month for Turkey, which saw its ETF contract by 12.50%.



Sector performance

Most sectors struggled this month, with only five making a small gain and two being Money Market sectors. India led the group once again, with a performance of 4.47%. Despite conflict in the Middle East and the threat of energy market disruption, the Commodities sector faltered, appearing in the bottom 5 of all sectors.



Source: FE FundInfo, 14/11/23

Summary

Sadly, the world has seen conflict before and markets are known for climbing the ‘wall of worry,’ that is, growing despite challenge and controversy.

The initial spike and reversal in Oil markets has restored some calm, as have better than expected inflation figures reported by the US.

Markets have recovered strongly and quickly from the lows of October and create a compelling case for investors in 2024, particularly with the broadly circulating thesis that interest rates may finally be cut by central banks.

Despite economic challenges, markets function as discounting mechanisms, 'pricing in' forecasts as well as all known data. A recession could be priced into markets already although the depth of which remains to be seen. Rate cuts are likely to see Fixed Income markets rally once they arrive, owing to the strong correlation between rates and capital values. This gives further optimism around what 2024 could bring for investors.

Could it be that Central Bankers have finally engineered a 'soft landing' from high inflation?

Sources:

Economic indicators information from The Institute for Supply Management - Report on business, IHS Markit and Trading Economics

The 'Balanced Portfolio Benchmark' is the UT Mixed Investment 20-60% Shares Sector.

Market and Sector performance data sourced from FE FundInfo, 13/11/23

European Central Bank holds interest rates steady after 10 consecutive hikes by Jenni Reid, CNBC, 26/10/23

Pound rises against dollar as Bank of England expected to cut interest rates by May, By LaToya Harding, Yahoo Finance UK, 13/11/23

BoE's Pill says pay growth is slowing but still too high, by Reuters, 14/11/23

Powell calls Fed policy 'restrictive,' but keeping options open, by Jennifer Schonberger, 09/11/23

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