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NUGENIS NEWS



Financial planning for a *brighter* wealth

Investment Commentary

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Market overview

March concluded an excellent first quarter of the year for equity markets with the MSCI World Index up a further 3.4% in sterling terms. Markets remain encouraged by economic data pointing to a resilient economic backdrop, particularly in the US where estimates and forecasts continue to be revised upwards. The closely observed Purchasing Managers' Indices ('PMIs') in the US remain in expansionary territory, implying improving economic conditions and market demand.

'Growth' stocks have led the way so far this year however March saw some broadening out in terms of market leadership and this was reflected in some better relative performance from 'value' stocks and sectors as well as from markets such as the UK and continental Europe. The Japanese market continues to perform strongly as investors increasingly see value opportunities as the health of the economy and corporate sector continue to improve. March saw the long-awaited end to the Bank of Japan's negative interest rate policy with a modest tick up in rates now expected in the summer.

Resilient economic data and cautious rhetoric from central banks continues to cause some volatility in fixed income markets. March, however, saw some positive returns across both sovereign and corporate bonds against a mixed inflation backdrop. Wage pressure, which has remained stubbornly high over the past couple of years, continues to alleviate – surveys in the UK for example suggest that companies have scaled back the outlook for pay rises to less than 5%. On the other hand, there have been some relatively sharp increases recently in both input costs and output prices in the US.

The European Central Bank has flagged a possible interest rate cut in June, dependent on wage growth continuing to moderate and the expectation for the number of rate cuts in the US this year has now fallen to three (from six at the beginning of the year), also beginning in the summer.

Strategy Positioning

Global stockmarkets have been buoyed again by the near certainty of interest rate cuts coming for many key economies before the middle of this year. We remain positive on the outlook and feel well placed to participate in further market momentum as monetary policy and inflation conditions become more favourable for risk assets.

The US and Asia, now including Japan, remain our favoured regions for stockmarket exposure – these markets offer the best combination of plentiful and superior growth opportunities (notably the USA), attractive valuations and access to longer-term beneficiaries of domestic demand (emerging Asia) and structural recovery potential (Japan). Exposure to European markets, including the UK, is also merited based on cheap valuations and future recovery potential.

Within fixed income our shifts made during 2023 and early 2024 to increase exposure to – and lengthen the maturity profile of – fixed interest investments are beginning to pay off as reductions in inflation and more certainty over interest rate cuts come into view.

Exposure to alternative investments has been reduced in the past year to fund increased allocations to bond markets, but they have not lost their fundamental appeal.



When Will Interest Rates Come Down?

In the intricate world of finance, interest rates are like the tides of the economy, ebbing and flowing with the currents of fiscal policy, inflation, and market sentiment. The recent trajectory of interest rates has been a topic of significant interest and speculation, particularly in light of the Bank of England's proactive stance against inflation. With interest rates at a 16-year high and inflation showing signs of moderation, the focus has shifted to when rates might start to come down.

At present, the prevailing sentiment among economists and analysts is one of cautious optimism coupled with a hint of trepidation. The global economy, though in recovery mode from the tumultuous events of recent years, still bears the scars of the pandemic-induced downturn. Central banks, including the Bank of England, have adopted accommodative monetary policies to stimulate growth, keeping interest rates at historic lows. However, the spectre of inflation looms large, fuelled by supply chain disruptions, pent-up demand, and rising commodity prices.

Bank of England's Stance

The Bank of England (BoE), like its counterparts across the globe, faces the delicate task of balancing the need to support economic recovery with the imperative of curbing inflationary pressures. The prevailing consensus suggests that while interest rates are unlikely to remain at rock-bottom levels indefinitely, any significant upward adjustments in the near term are improbable. The central bank is expected to proceed with caution, exercising prudence to avoid derailing the fragile economic recovery.

Over the past couple of years, the BoE has raised interest rates multiple times to combat rising inflation. However, in recent months they have opted to keep rates on hold at 5.25%. BoE Governor Andrew Bailey has hinted at the possibility of rate cuts before inflation reaches their Government imposed target of 2%, emphasising the importance of forward-looking action.

Analysts' Predictions

While all believe rate cuts are likely, market analysts are divided on the timing of when they may start.

Capital Economics has suggested a rate cut in June, anticipating a faster decline in inflation than expected, however S&P Global Ratings anticipate the first rate cut in August, citing the need for more moderation in wages and prices. AXA Investment Managers is currently leaning towards June as well but acknowledge the possibility of August, and Mizuho Bank sees June as possible but considers August more likely.

Critique and Caution

While the debate on rate cuts continues some economists, like Carsten Jung from the IPPR, have criticised the BoE's tight monetary policy, suggesting it may hinder future growth, something echoed by Suren Thiru from ICAEW who warned of the potential economic toll of past rate hikes and urges the Bank to consider rate cuts more promptly.

Most analysts anticipate that the BoE may embark on a gradual path of monetary tightening over the next 9 to 12 months, cautiously nudging interest rates upward in response to inflationary signals and improving economic indicators. However, the pace and magnitude of these adjustments are likely to be tempered by concerns over the sustainability of the recovery and the potential impact on highly indebted households and businesses.

Several factors are poised to influence the trajectory of interest rates in the coming months. Chief among these is the evolution of inflationary pressures, which will be closely monitored by policymakers and market participants alike. A sustained surge in inflation could prompt the central bank to adopt a more hawkish stance, accelerating the pace of rate hikes to rein in price growth and safeguard the purchasing power of the currency.

Furthermore, the path of interest rates will be intricately intertwined with developments on the global stage, including geopolitical tensions, trade dynamics, and the trajectory of the COVID-19 pandemic. Any unexpected twists or turns in these arenas could have profound implications for monetary policy decisions, introducing an element of uncertainty into the forecast for interest rates.

For consumers, the prospect of rising interest rates carries both challenges and opportunities. Borrowers may face increased costs on variable-rate loans, such as mortgages and credit cards, prompting some to consider locking in fixed-rate arrangements to shield themselves from future rate hikes. Savers, on the other hand, stand to benefit from higher returns on savings and investment products, albeit with the caveat that the pace of rate increases may not keep pace with inflation.

In conclusion, the forecast for general interest rates over the next 9 to 12 months reflects a delicate balancing act between the imperatives of supporting economic recovery and addressing inflationary pressures. While the prospect of gradual monetary tightening looms on the horizon, uncertainty abounds, underscoring the importance of vigilance and adaptability in navigating the ever-changing landscape of global finance. As the proverbial tide of interest rates continues to ebb and flow, stakeholders would be wise to stay attuned to the currents of economic data and policy developments that shape our financial future.

Sources

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