Q1 Economic & Market Update 2024

So how did investment markets fare in the first quarter of 2024?

The first quarter of 2024 has provided a largely benign backdrop for investing. Investors have been increasingly willing to take on risk as confidence has grown that the global economy will avoid a severe downturn and that there will be interest rate cuts in UK, US and Europe by the summer.

2024 started with investors suffering a hangover from the end of year party which had seen a strong rally in equity and bond markets. In the cold light of day, the expectations from the markets of aggressive interest rates were dampened, with inflation ticking upwards and US led global growth remaining robust. This led to a wobble (particularly in bond markets) in January.

However, upgrades in global growth and decent corporate earnings (particularly for AI focused US tech stocks) soon saw a rally in risk assets which continued for much of the quarter. By the end of the quarter, the optimism over a soft landing for the global economy felt like the 'rising tide that lifts all boats' as most risk assets rallied strongly in March and those in the bearish camp seemed to have all but disappeared.

Stockmarkets

It has been the best first quarter in the past five years for global equities, on increased hopes of a soft landing for the global economy. The MSCI World index produced a return of 10.1%. It was also the biggest quarterly outperformance of equities over bonds since 2020, illustrating investors' increasing appetite for risk.

Japan was once again hard to beat with the benchmark generating a return of 17.1% and hitting a new high after 34 years! The rally in Japanese equities feels like it has legs with corporate governance improvements and earnings continuing to drive the market upwards, helped by a weak Yen boosting exporters.

The growth potential of Artificial Intelligence has continued to drive technology stocks higher. The 'magnificent seven' US tech behemoths remained in demand and pushed the S&P 500 to new highs & a return of 10.4%. The rally broadened out in March as investors took advantage of value in cheaper markets, with cyclical areas such as oil and mining stocks and smaller companies returning to favour.

Despite concerns over economic growth in the Eurozone, the MSCI Europe Ex UK Index produced a healthy 9.5% return. But the UK stockmarket proved lacklustre with a lack of growth stocks being the main reason, although a return to favour for energy and mining stocks saw the CBOE UK All Share post 3.9% in Q1. China continued to drag down Asian and emerging markets in the early weeks of 2024, but towards the end of the quarter there were signs that the targeted stimulus measures are beginning to take effect. Despite this the MSCI China index fell back 1.7% and Chinese equities remain at 20+ year lows against broader global equities. The broader MSCI Emerging markets index posted a return of 4.5% during the quarter with India continuing to benefit from strong growth, with MSCI India up by 6.1%.

Bond markets

2023 had ended on a high for most investment areas, with bond markets particularly strong on the belief that interest rates would be reduced aggressively. At the beginning of the year six US interest rate cuts were priced into bond markets, which always seemed optimistic as the Federal Reserve rhetoric continued to focus on the threat of inflation. The Fed was quick to reinforce this point early in the year, which saw a sharp sell-off. Bond markets did stabilise by the end of the quarter, but most areas posted quarterly negative returns. The FTSE Global Government Bond index fell back by 0.9% and the Bloomberg Global Aggregate bond index by 2.6%.

However, resilient economic growth & appetite risk was positive for high yield bonds and the Bloomberg Global High yield bond index was up 2.1% in Q1.

Property

The interest rate sensitivity of real estate resulted in downward pressure for the sector in the first few weeks of the year, as hopes of steep rate cuts diminished. However, by the end of the quarter there were signs of bulls looking through the property malaise to focus on impending rate cuts. The MSCI AW Real Estate sector, a proxy for global property stocks, finished flat on the quarter.

Infrastructure

followed a similar trend, selling off in January before showing a recovery to wipe out much of the losses later in the quarter. The MSCI ACWI Infrastructure finished the quarter down by 1.3%, though UK listed infrastructure trusts largely remained out of favour.

Commodities

There was a broad rally in commodity prices towards the end of the first quarter on the improving prospects for economic growth. Oil and industrial metals were particularly helped by positive signals from China towards the end of the quarter that their economy is finally showing signs of coming out of the doldrums. The price of (brent crude) oil increased by 17.7% to end March at $87 a barrel, with OPEC holding back new supply further pushing up the price.

The price of gold has also seen a strong rally in the past few weeks, with demand fuelled by ongoing geopolitical uncertainty and Central banks hinting that interest rates cuts are on the way, despite stickier US inflation. The price of an ounce of gold finished the quarter at an all-time high of $2,238, an increase of 8.2%, and the shiny stuff is proving a good diversifier in portfolios.

Currencies

It has been a quiet quarter in terms of currency fluctuations with the Euro, pound and US dollar all trading in a narrow range. The dollar is up by 1.1% versus the pound, with the euro 1.2% weaker versus Sterling than the start of the year. The key move has been in the Yen, which continues to weaken, falling more than 5% versus Sterling. Despite the Bank of Japan finally abandoning negative rates, the Japanese base rate remains at zero. Bitcoin feels like a good barometer of the appetite for risk and the price rose 61% in dollar terms in the first three months of 2024!

Q1 Fund Review

Once again, investors riding the technology wave were rewarded. The IA Technology & Technology sector posted 11.1% in Q1 as AI fuelled corporate earnings saw big tech continue to get bigger (Nvidia added $1 trillion to its market cap in the quarter, which equates to 20% of the total gain for global stockmarkets!). IA North America was a key beneficiary (up 10.7%) and the strong performance of mega cap tech stocks would have boosted US and global passive funds. Japan funds were unsurprisingly near the top of performance tables, the IA Japan sector was up by 9.4%, but exceptional stockmarket returns diluted for Sterling investors by the weakness of the Yen.

The Financial and Financial innovation sector was also one of the strongest, up by 9.2%. Higher rates have been positive for the sector. European banks for example are trading at multi year highs, benefiting from the increased margin between what they receive in loans and pay on deposits.

It was bond funds that dominated the worst performers. The highly interest rate sensitive index linked gilts propped up the performance tables, falling by 2.7%, with European and global Government bond sectors also in the bottom five fund sectors. Infrastructure was also a laggard and clean energy was one of the worst areas, with several funds in this area suffering double digit losses.

For investment trust investors it was US, Japanese and global equity trusts that topped the table, whilst property and renewable energy were the sectors that were hit the hardest.

Looking ahead

Are investors getting too complacent? The widely quoted Bank of America's Global Fund Manager Survey is showing that fund managers are at their most bullish for two years, with around two-thirds of respondents expecting a soft landing, and nearly a quarter see no downturn at all. The Vix index, which measures US equity market volatility (often dubbed the fear index) is trading at very low levels. It would therefore be no surprise to see increased levels of volatility in the short-term.

But if announcements of Q1 corporate earnings (particularly the US Technology leaders) remain supportive then the risk rally could have further to run, whilst the quarter ended with investors looking at opportunities in cheaper areas of equity markets.

All eyes will remain on Central banks and whether they make their first move to cut rates in the second quarter. Consensus is now that there will be three US interest rate cuts this year, which seems realistic, and at current yields bonds offer value for income seeking investors and those looking for insurance against a slowdown in economic activity. Interest rate sensitive areas such as property infrastructure also look well placed to continue recent recovery.