



September 2024 Quarter in review

more **INVESTED**

GLOBAL EQUITIES BREACH ALL-TIME HIGHS AS RATE CUTS ARRIVE



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Global equities rose to new all-time highs in the third quarter, supported by global monetary easing, which also helped push bond yields lower. The Federal Reserve (Fed) began its easing cycle with a larger-than-expected cut in its key rate in September, and guided for further cuts this year and next, while the European Central Bank (ECB) eased policy further and China announced stimulus measures. Global activity data was somewhat mixed in Q3, but an economic soft landing was still the base case. A volatility event in August was triggered by soft US labour market data, which raised recessionary fears, but subsequent data suggested activity remained robust.

US

Concerns over a potential recession in the US were front and centre at the start of August as economic data showed signs of a slowdown, which led to significant market volatility. The unemployment rate unexpectedly rose to 4.3% in July, which meant that the 'Sahm rule' indicated a recession. The Sahm rule states that, if the three-month moving average of the unemployment rate moves 0.5 percentage points above its 12-month low, then a recession has begun. It is a rule that has coincided with every US recession since 1970. However, subsequent data indicated that a soft landing was still likely. The Fed signalled that it would begin cutting rates at its September meeting, amid falling inflation, which also eased market fears around monetary policy being too tight.

US GDP rose by an annualised 3.0% quarter-on-quarter (q/q) in the second quarter, above market expectations and nearly double the growth rate in Q1 (1.6%). Economic activity was supported by strong household consumption. This continued in Q3 as retail sales unexpectedly rose in August, by 0.1% m/m. ISM services also remained in expansionary territory (above 50) in August, again suggesting economic strength. Meanwhile, headline consumer price inflation decelerated to 2.5% y/y in August, down from 2.9% in July. Core prices rose by 3.2%, the same pace as in July, with falls in core goods inflation offset by rising housing costs.

The Fed's policy meeting in September was a key event, with the central bank starting its easing cycle with a greater-than-expected 50 basis points (bps) rate cuts in the federal funds rate to 4.75-5.00%. In addition, the central bank's updated economic projections showed median expectations among the monetary policy committee were for 50bps of further cuts in 2024 and 100bps of rate reductions in 2025. Overall, this suggested that the Fed was more dovish than expected as it shifted its focus towards limiting growth downside, with its estimates for unemployment rising to 4.4% in 2024 and 2025, compared to 4.2% in August. Both GDP growth and inflation are forecast to be close to 2% this year and next.

Europe

Eurozone Q2 GDP indicated that activity had continued to recover, rising by 0.2% q/q which was above market expectations. This was driven by strength in Spain (0.8% q/q), and in France (0.2%) where growth was supported by the Olympics. Activity in Germany declined by 0.1%, down from a 0.2% rise in Q1 amid falling investment. Subsequent activity data suggested a lacklustre backdrop. The Eurozone composite PMI unexpectedly fell into contractionary territory in September, driven by falls in manufacturing as well as a more significant decline in services.

At the same time, headline inflation continued to fall, with headline consumer prices up by 1.8% y/y in September, down from 2.2% in August, while core prices decelerated from 2.8% to 2.7%. Wage growth was also seen to have moderated, all of which allowed the ECB to continue easing policy. The central bank cut its deposit rate by a further 25bps to 3.5% at its September meeting.

China

Elsewhere, in September, China announced a raft of stimulus measures aimed at supporting the economy and achieving the government's 2024 growth target of 5%. This included a 50bps reduction in the reserve requirement ratio from the central bank, and cuts to lending, deposit and mortgage downpayment rates. In addition, \$114bn of funding is to be made available for companies to buy back stock and for companies like insurers to purchase local equities.

MARKET ROUND-UP

Equities

The backdrop of falling interest rates and a likely soft landing helped support global equities, which moved to new all-time highs, quickly recovering from the August volatility event. In Q3, global equities, as represented by the MSCI All Country World Index (ACWI), rose by 5.0% (2.5% in euro terms).

Emerging market (EM) equities rallied by 6.8% (4.6% in euros) over the quarter. The asset class was supported by stimulus measures from China, with the MSCI China up by 22.4% (18.7% in euros).

Small cap equities rose by 6.8% (5.2% in euros) amid lower bond yields, which could be supportive for small caps given their higher leverage levels and larger share of variable-rate borrowings.

Bonds

The ICE BofA 5+ Year Euro Government bond index returned 5.0% as German bund 10-year yields declined from 2.50% at the end of Q2 to 2.12%, with the magnitude of expected 2024 rate cuts from the ECB increasing.

Corporate bonds were supported by broadly falling yields in Q3. European investment grade (IG) corporate bonds returned 3.3%, supported by income yield and capital gains from declining yields. IG yields fell by 58bps to 3.29% and spreads narrowed marginally, by 1bp to 116bps. Global high yield bonds returned 4.1% in Q3, with yields falling by 70bps to 6.23% and spreads narrowing by 4bps to 246bps.

EM local debt returned 4.8% in Q3 due to income yield and capital gains from falling yields, with yields down by 32bps to 6.62%. EM hard debt returned 5.9% as the asset class also benefitted from a weaker US dollar, which lowers debt repayments in local currency terms, with yields falling by 87bps over the period to 6.61%.

Meanwhile, peripheral Eurozone bond spreads narrowed as more easing from the ECB was expected and political risk fell from the end of Q2 after a government was appointed in France. Italian 10-year spreads over equivalent German bunds fell by 24bps to 133bps, while spreads for Spanish government bonds were down by 11bps to 81bps. French spreads were unchanged from the end of Q2, at 80bps.

CHARTS OF THE QUARTER

Global Equities



Source: ILIM, Bloomberg. Data is accurate as at 30 September 2024.

Bonds – German 10-year yield



Source: ILIM, Bloomberg. Data is accurate as at 30 September 2024.

MARKET SNAPSHOT

Market returns (EUR)



Equity Markets (EUR)	QTD Return (%)	YTD Return (%)	2023 Return (%)
MSCI Ireland	9.4	30.1	20.6
MSCI United Kingdom	3.7	14.2	10.3
MSCI Europe ex UK	2.0	11.7	18.5
MSCI North America	2.0	20.1	22.3
MSCI Japan	1.7	11.6	16.7
MSCI EM (Emerging Markets)	4.6	16.0	6.5
MSCI AC World	2.5	17.9	18.6
10-Year Yields	Yield last month (%)	2023 Yield (%)	2022 Yield (%)
US	3.78	3.88	3.87
Germany	2.12	2.02	2.57
UK	4.00	3.54	3.67
Japan	0.86	0.61	0.42
Ireland	2.47	2.38	3.13
Italy	3.45	3.69	4.70
Greece	3.11	3.06	4.62
Portugal	2.70	2.66	3.59
Spain	2.93	2.99	3.66
FX Rates	End last month	2023 Rates	2022 Rates
U.S. Dollar per Euro	1.11	1.10	1.07
British Pounds per Euro	0.83	0.87	0.89
U.S. Dollar per British Pounds	1.34	1.27	1.21
Commodities (USD)	QTD Return (%)	YTD Return (%)	2023 Return (%)
Oil (Brent)	-16.9	-6.8	-10.3
Gold (Oz)	13.4	27.9	13.1
S&P Goldman Sachs Commodity Index	-5.3	5.2	4.3

Source: ILIM, Bloomberg. Data is accurate as at 1 October 2024.

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THE ILM VIEW – LOOKING AHEAD

With inflation having fallen significantly and central banks now suggesting rates will be cut further in 2024, bond yields are expected to decline over the next 12 months. On a 12-month view, our base case is that German and US 10-year government bond yields fall from current levels of 2.12% and 3.79% to 1.50% and 3.50%, respectively. We believe fixed income offers a strong risk-reward profile at this stage in the cycle, with the potential to offer protection if the economy slows, and is attractive from an income perspective while also providing potential for capital gains via falling yields. We believe that the risks of materially higher bond yields have reduced and, if the economy falters, major central banks will be able to cut rates to support growth. In that scenario, we would expect bonds to outperform to a greater extent.

Global equity valuations are above long-term averages, trading on a 12-month forward price-to-earnings (P/E) multiple of 17.9x against a long-term average of 16.1x. Equities remain expensive against both bonds and cash given the high yields currently available on these assets. Despite this, the outlook on a 12-month view is positive. Central banks have pivoted to looser policy in 2024 as inflation has declined. With growth expected to remain firm with a recession being avoided, earnings are forecast to rebound in 2024, which should be supportive. Over the medium term, the rollout of artificial intelligence (AI) should boost efficiencies and earnings across the whole market and allow equities to 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

OCTOBER

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
				04 October US Non Farm Payrolls (Sep) US Unemployment Rate
		09 DE Balance of Trade US FOMC Minutes	10 US Inflation Rate	11 GB GDP MoM US PPI MoM US Michigan Consumer Sentiment Prel
	15 GB Unemployment Rate DE ZEW Economic Sentiment Index	16 GB Inflation Rate YoY	17 EA ECB Interest Rate Decision and Press Conference JP Balance of Trade US Retail Sales MoM	18 JP Inflation Rate YoY CN GDP Growth Rate YoY GB Retail Sales MoM
			24 DE HCOB Manufacturing PMI Flash (Oct)	25 DE Ifo Business Climate (Oct) US Durable Goods Orders MoM
	29 DE GfK Consumer Confidence US JOLTS Job Openings	30 EA GDP Growth Rate YoY Flash (Q3) US GDP Growth Rate QoQ Adv (Q3) JP Consumer Confidence		31 JP BoJ Interest Rate Decision EA Inflation Rate YoY Flash (Oct) US Core PCE Price Index MoM (Sep) US Personal Spending MoM (Sep)

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