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Market reflection

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Overview

Following a period of consolidation in April, equity markets made further progress in May, although leadership once again narrowed to the major US technology shares. The adoption of generative artificial intelligence remains the driving force, with chip-designer Nvidia's results providing another boost for its shares, which have doubled this year alone and more than trebled over the last year. Nvidia is now challenging Apple as the world's second largest company by market capitalisation, with the largest, Microsoft, also in its sights. The mood was more uncertain in bond markets. Yields initially fell as the US reported lower-than-expected inflation in April following three consecutive higher-than-expected prints. However, they started to rise again in the face of data pointing to more resilient growth.

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The sell-off gained further momentum following poorly received Treasury bond auctions, a signal that investor appetite for US government debt to fund the persistently high fiscal deficit is not endless – or will at least demand a more generous yield. There could be further tests in the months leading up to November's Presidential election, with neither (current) candidate signalling any intention of reducing the deficit. Stickier inflation and a rebound in growth were apparent elsewhere too, leading to a further repricing of interest rate expectations. Whereas cuts of up to 1.5% in the US, UK and Eurozone during 2024 were priced into futures markets at the start of the year, now it is 0.25% to 0.5% at best. This increases the pressure on more indebted consumers and companies, raising the prospect of a future economic downturn. But were that to develop, it is probable that central banks would once again be inclined to cut interest rates faster, which would, in turn, be supportive of share prices. Markets might well need to consolidate until the outlook becomes clearer.

- The Bloomberg consensus for World GDP growth in 2024 has ticked up again to 3%, up from 2.6% in January, matching the level of 2023. The current expectation for 2025 is a very similar 2.95%. That looks very stable but conceals a very wide range of expectations and an ongoing debate about whether or not the US, in particular, will succumb to a recession owing to the lagged effect of higher interest rates.

- The Bloomberg Global Aggregate Bond Index has lost around 3.9% in dollar terms this year and is -1.3% in the sterling hedged version. The 10-year US Treasury yield has risen from 3.87% to 4.59%, while the 10-year UK Gilt yield has gone from 3.53% to 4.37%. The "last mile" of getting inflation down to central banks' 2% target is proving tough.

- A General Election has been called in the UK and will take place on July 4th. We have consistently been of the opinion that this will be something of a non-event from a financial market perspective. The pound is often the barometer of sentiment towards political developments, and there are certainly no signs of nerves amongst currency traders. The biggest surprise would be if Labour fails to win a Parliamentary majority. This could undermine some of the optimism that has been building around the potential for a period of stability in government, a background that could entice greater investment into the UK.

- President Biden has lost some ground in US polls ahead of the election, with persistent high prices outweighing a stronger economy in voters' minds. It is too early to assess the impact on the campaign of Donald Trump's conviction.

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