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MARKET MATTERS

STRONG JOBS DATA LIKELY TO SLOW PACE OF RATE CUTS

Market overview:
Western markets were weighed down for much of the week by the increasing tension in the Middle East before stunning jobs numbers in the US jolted shares higher and sent bonds sharply lower. Out in Asia, despite mainland Chinese markets being shut for Golden Week, the rally continued in Chinese shares listed in peripheral markets such as HK and the US. Oil rose as the market braced for the possibility that Israel's retaliation against Iran for its recent missile barrage will include strikes on the country's oil infrastructure. Gold got caught between the pull higher as a hedge against geopolitical uncertainty and the downward pressure of rising yields. Bonds suffered one of their worst weeks of the year as the job numbers finally put recessionary fears to bed in the US.

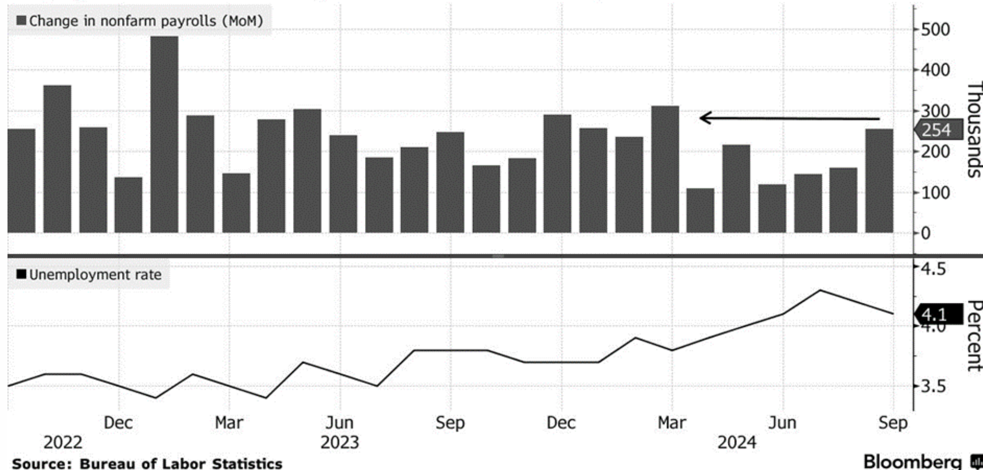
US: Job Numbers finally confirm the underlying strength of the US Economy
US job growth in September exceeded all expectations, with the economy adding 254,000 jobs—the highest in six months. According to the Bureau of Labour Statistics, the unemployment rate dropped unexpectedly to 4.1%, and wage growth accelerated by 4% year-on-year. July and August payrolls were also revised a combined 72,000 higher, taking the three-month average monthly payroll gains to 186,000. That's above the pre-pandemic average. The household measure of employment rose by an even larger 430,000 in September.

These strong labour market figures have lowered the likelihood of the Federal Reserve making another significant interest rate cut in November. Earlier reports this week also pointed to robust worker demand and low layoffs, alleviating concerns about a weakening labour market. The data showed a decrease in the number of people working part-time for economic reasons, and those who recently lost jobs could find new employment.

Equity Indices	1 wk %
MSCI China TR	11.72
MSCI AC Asia ex Japan TR	2.00
MSCI Emerging Markets TR	1.01
S&P 500 TR in US	0.22
FTSE 100 TR in GB	-0.48
Russell 2000 TR in US	-0.54
FTSE 250 TR in GB	-1.60
MSCI Europe ex UK TR	-2.00
Nikkei 225 in JP	-3.00
MSCI India TR	-4.33

Bonds/Currency/Commod	27.09.2024	04.10.2024
Bond: UK 10 Year Yield	3.974	4.141
Bond: US 10 Year Yield	3.751	3.969
Currency : GBP/USD	1.3373	1.3116
Currency : USD/YEN	142.19	148.71
OIL: WTI $	68.64	74.45
Gold $	2680.80	2673.20

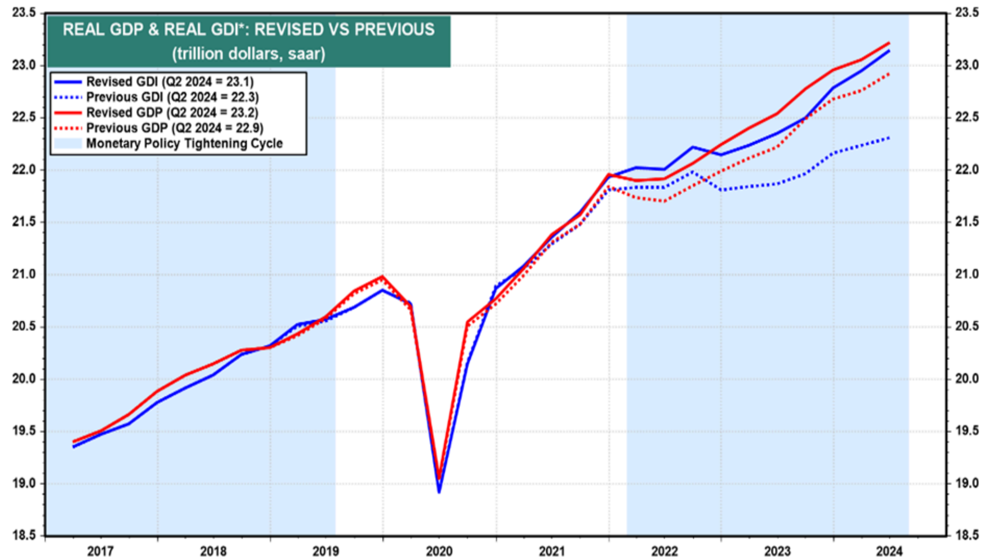
Source - Bloomberg



The resilient US economy has again disrupted predictions from Wall Street pessimists who have warned of a recession all year. Since June, there has been an ongoing debate between stock and bond market bulls about whether the Federal Reserve's restrictive policies would trigger a downturn. Still, this report showed the most significant jump in US hiring in six months, finally putting the debate to bed. The US economy is in good shape, period. Small-cap stocks led the rally on Friday, as the strong labour market reinforced optimism in domestic investment and consumer spending. Meanwhile, a long-dated Treasury exchange-traded fund, having previously risen with equities and corporate bonds, saw its worst week since April.

It isn't just the job numbers that underline the economic strength; if anything, it has taken the longest to show up in that dataset. At the end of last month, the Bureau of Economic Analysis (BEA) released substantial upward revisions to key economic indicators like real GDP, real Gross Domestic Income (GDI), personal income, and personal savings. The data showed that real GDP had increased every quarter but one since the pandemic recession in early 2020. Despite the aggressive monetary tightening from March 2022 to August 2024, the economy did not slip into recession. There has been no need for any landing, either soft or hard.

Source - LSEG Database and Yardeni Research, and Bureau of Economic Statistics

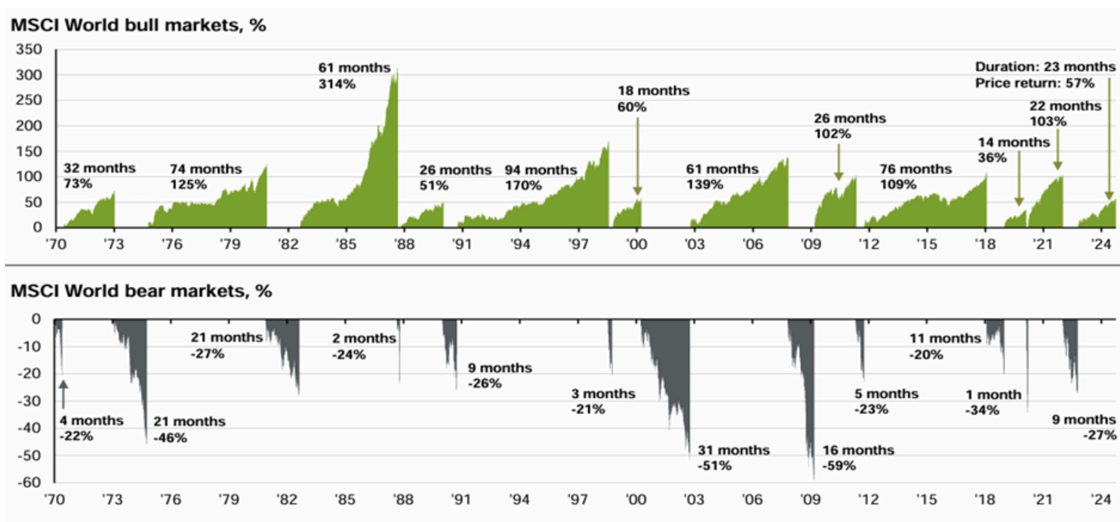


For regular readers of this missive, you will know that I have been arguing for quite some time that the US economy was in better shape than most investors had appreciated and that, if anything, it was the bond market, not equities, that looked overvalued. Last week's move has gone a long way to rectifying that imbalance, and I think US longer-dated treasuries will find support, probably in a range of 4 – 4.5% for the US 10-year Treasury.

With equities, this bull market has further to run. I had thought that we were likely to tread water given the uncertainties in the Middle East and the looming presidential election and that new highs were likely to occur in a traditional Santa Rally. I am not so sure now. The next earnings season is about to start, and the omens look good for Corporate America to exceed expectations yet again, albeit primarily due to analysts' earnings forecasts having been downgraded aggressively. There is an increasing chance of a melt-up in risk assets, which could provide short-term euphoria and enhance the opportunity of something going wrong.

For now, I would be happiest with a Fed that only cuts another 0.25%, a market that treads sideways and lets strong earnings bring valuations back into more comfortable territory. That will increase the sustainability of this bull market, which is still in its infancy by historical standards, as the following chart from JP Morgan highlights.

Source - JP Morgan

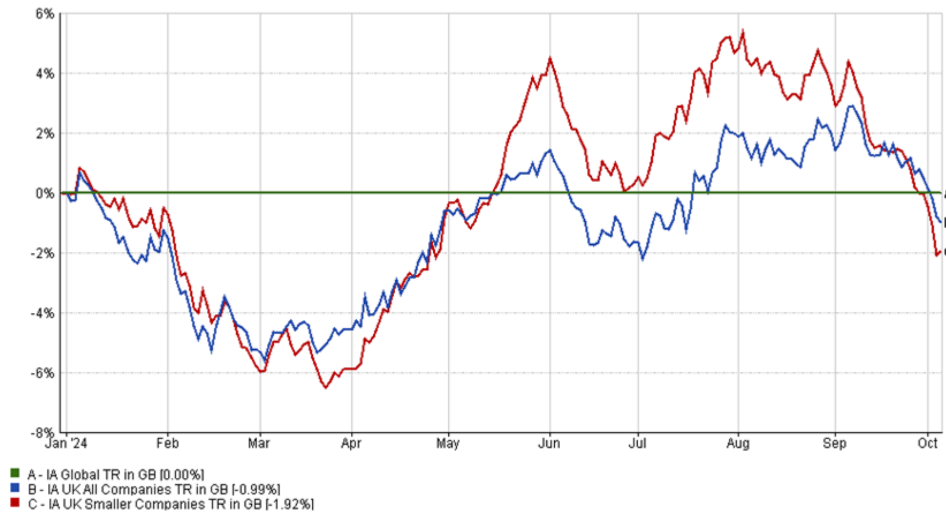


UK Budget Worries Weigh on Stocks

Sometime around the middle of summer, investors' moods in UK equities soured. Up until then, our domestic market had been outperforming Global equities, and there was a building sense of optimism around economic growth, rate cuts, political stability, and falling inflation, which was starting to lure in investors and corporate buyers attracted by the cheap valuations.

Even Bank of America's monthly survey of global fund managers showed their views on UK equities gently ticking up this year. And then the mood music changed. Inflation perhaps a little warmer and growth a little slower than expected, but the actual downward shift seems to have originated from "on high". Labour spin was so keen to tell us what a mess the Conservatives had left the country in that it now appears that might be damaging morale.

Source - FE Fundinfo 2024

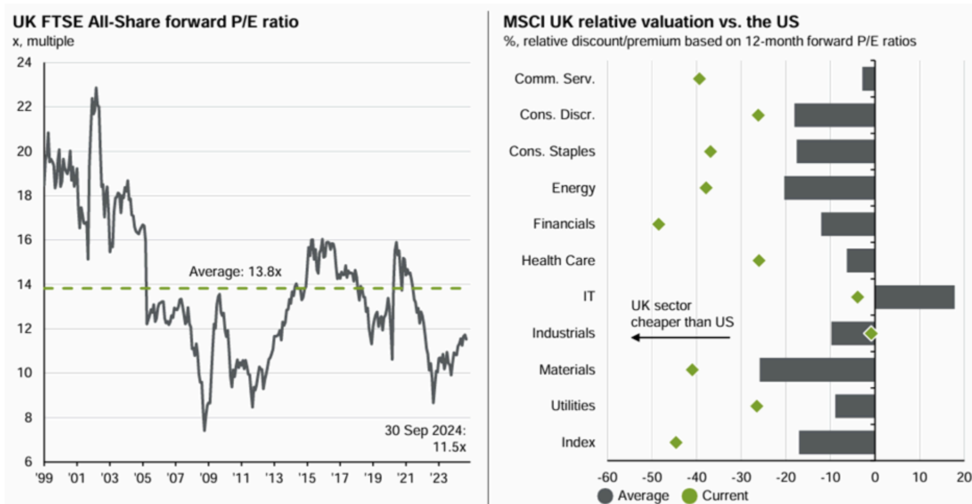


The latest data from global funds network Calastone reveals that September was another month money fled UK equity funds. Not only that, but the outflows were more extensive than they have been in the last few months, coming in at £666 million. Edward Glyn, head of global markets at Calastone, seems to agree with my take and that 'the new government's rather pessimistic commentary about the UK economy appears to have put a stop the nascent revival in interest in domestic equities that we first detected in trading data in July'.

Without question, despite some economic improvements, the government's downbeat tone has unsettled voters and businesses alike. This uncertainty, particularly regarding the upcoming Budget, has led to drops in consumer confidence and investment delays, as people fear financial hardship without precise details on policy plans.

There are bright spots in this otherwise stormy outlook. First, the government has realized that its constant drumbeat of doom is doing more harm than good. It's one thing when a few ultra-wealthy individuals talk about leaving, but it's a whole different challenge when your base starts worrying about a return to 'austerity.' That's much harder to brush off. Also, since this situation is driven by uncertainty rather than actual economic decline, we should be able to ride out the storm. As long as the upcoming Budget's roar is worse than its bite, most analysts believe we should see things pick up once October is behind us. A glance at the chart below shows the value on offer from UK Equities, particularly versus the US.

Source - JP Morgan

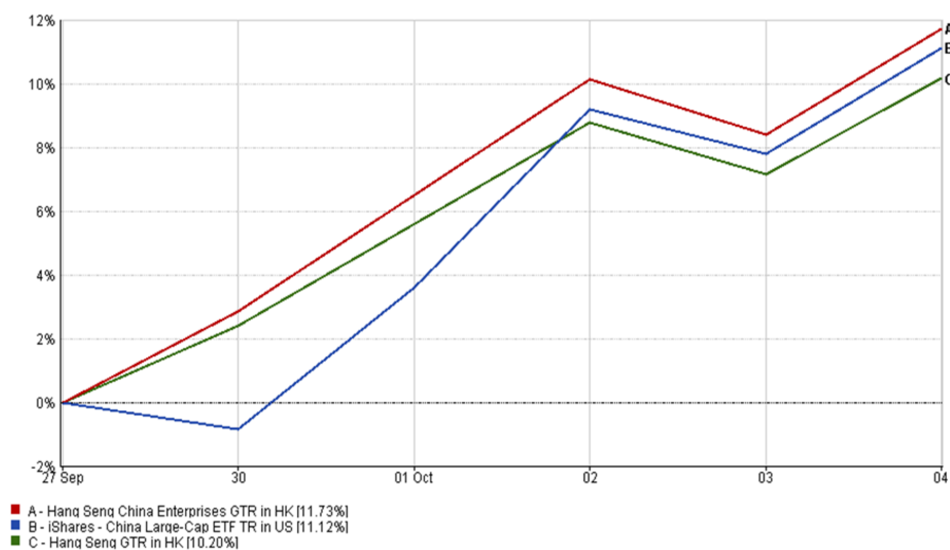


There are reasons to be cheerful, and I would welcome a Government focused on some positives instead, such as news last week that in September, the UK's construction sector grew at its fastest pace in two-and-a-half years, according to a survey by S&P Global, with the headline PMI rising sharply to a stunning 57.2 from 53.6 in August. This surge, the highest since April 2022, was driven by factors such as lower interest rates, domestic economic stability, and robust infrastructure development. The sector experienced increased client confidence and a post-election rebound in sales inquiries, particularly in housebuilding and civil engineering, which saw the fastest expansion in over three years, fuelled by infrastructure projects related to energy security and renewables. A quick caveat emptor that despite optimism across the industry, inflation remains a concern, with rising costs attributed to increased demand for raw materials and wage hikes being passed on by suppliers.

Golden Week in China

Despite the main domestic China stock markets being shut for Golden Week last week, the rally seems to have continued as ETFs that contain China shares listed in other Asian and US markets have continued to rise and the Hong Kong listed stocks have maintained their upward move. The holiday season typically sees a surge in Chinese travellers, making it a key indicator of consumer spending in the world's second-biggest economy.

Source - FE Fund Info



This has taken on extra significance this year, with economists and traders looking to see if President Xi Jinping's latest stimulus blitz can reinvigorate the country's consumers. Indeed, it would seem that the recent moves by authorities put the people in a good mood, as early reports on this year's holiday indicate that domestic travel and spending have surged significantly compared to previous years. The Chinese government expects nearly 2 billion domestic trips this year, marking a 19% increase from pre-pandemic levels in 2019. This recovery is also reflected in outbound travel, which is nearing 85% of 2019, driven by a notable rise in long-haul trips to destinations such as Europe, the Middle East, and Australia. Spending per capita has also been strong, with average trip expenditures surpassing pre-pandemic levels. There is a lot of pressure on the mainland markets to follow through when they reopen on Monday 7th. We shall soon find out...

This Week

Key things to watch include the release of the minutes from the last Fed meeting and getting both CPI and PPI inflation data from the US. In the UK, we have preliminary GDP data as well as industrial production data, which is also released for Europe. Japan provides its latest economic updates, and we should get more detail on Golden Week with official figures released. The earnings season for US corporates kicks off next week with the big banks on Friday.

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