## Market Review July 2024

Although most equity indices changed relatively little in July, the month was nonetheless quite eventful. After a strong start that saw the S&P 500 and Nasdaq 100 hit all-time highs, a sector rotation began. Investors took profits on growth companies, particularly in the technology sector, and repositioned themselves on the 'unloved' ones, namely *"value companies"* and small and mid caps. As a result, the Russell 2000 index soared by more than 10% to become July's best performer relative to its peers. The Nasdaq 100 gave up 1.6% over the month, while the Dow Jones Industrial, which includes more mature and defensive companies, gained 4.4%. It is interesting to note on the chart below that the sector rotation was initiated at the same time as a powerful rebound in the Japanese yen (JPY) following another massive intervention in the foreign exchange market by the Japanese Central Bank (BoJ). The BoJ is said to have injected more than $22 billion in two days (after having injected more than $60 billion in the spring) to support its currency. Thanks to very low interest rates for more than thirty years and good visibility on the central bank's monetary policy, the JPY is a popular currency for leveraged investors. For many years, hedge funds have therefore borrowed JPY at low cost in order to invest in US dollars (or other currencies) in high-potential growth companies. When the BoJ decides to defend its currency, this triggers "*carry trade*" unwindings, which weigh on risk asset prices around the world. The rebound of the Japanese currency (+7.2% over the month) logically weighed on the Nikkei 225 (-1.2%) as well as on the main European indices, which also lost between 1% and 2%.



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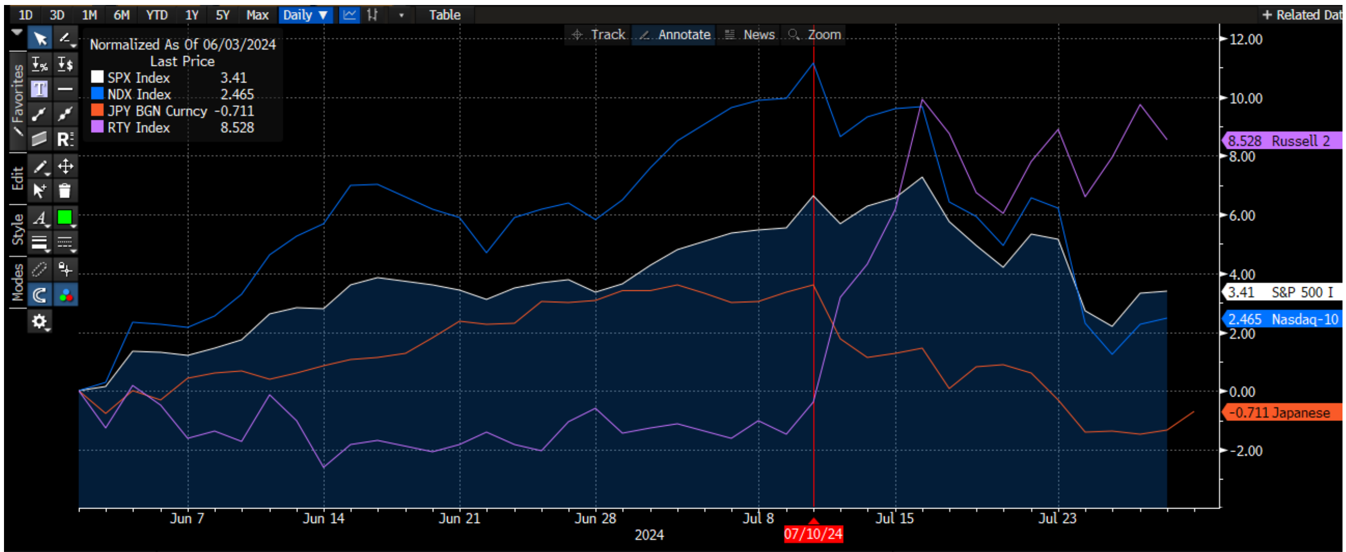
## Performance since the beginning of June 2024




Source: Bloomberg, Weisshorn

The rebound in *small and mid caps* can also be explained by expectations of interest rate cuts in the United States. As we have discussed in recent months, periods of monetary tightening tend to penalise SMEs more severely, as they struggle to find banks or investors willing to finance their capital expenditure. When they borrow, they therefore have to pay a premium of varying size compared with government rates. When government rates rise, this has a double negative effect for these companies. On the other hand, in periods of monetary easing, as is already the case in Europe and most other parts of the world (the FED is also likely to initiate a rate-cutting cycle soon), the financing prospects for small caps brighten and investors tend to return to this segment. In our view, it is too early to declare victory for this theme, but we believe that the worst is probably behind us and plan to increase this allocation in our portfolios in the near future. The FTSE 100 index, which includes the UK's leading stocks, gained 1.4% amid a changing political climate. Following Rishi Sunak's decision to call an early general election, the likelihood of the Conservatives losing power in parliament was high, and there were no surprises. The Labour Party, led by its strongman Keir Stramer, won the election and opened the doors of 10 Downing Street to him. Although the British economy is in relatively good shape and inflation has returned to target, the period of 'hyperinflation' that the country endured and the various political setbacks and scandals of the Boris Johnson era have driven the Conservative party from power after fourteen years. Keir Stramer will focus his mandate on economic recovery and intends to warm up relations between Great Britain and the European Union. He seems determined to embark on sensitive reforms such as nationalising the railways and tackling immigration. This could trigger a new dynamic in a country still digesting the consequences of Brexit.

## Market performances as of end of July 2024

| End of July | MSCI World | S&P 500 | EuroStoxx | CAC | Spain | Switzerland | MSCI EM | CSI 300 |
|---|---|---|---|---|---|---|---|---|
| | | | Equities in Local Currencies | | | | | |
| Perf 1 Month | 1.70% | 1.13% | -0.43% | 0.70% | 1.11% | 2.70% | -0.14% | -0.57% |
| Perf 3 Month | 8.06% | 9.66% | -0.98% | -5.68% | 1.94% | 9.38% | 3.71% | -4.50% |
| Perf YTD | 12.70% | 15.78% | 7.77% | -0.15% | 9.53% | 10.59% | 5.96% | 0.32% |

| End of July | WTI Oil | Brent Oil | Gold | Copper | USD | JPY | GBP | CHF |
|---|---|---|---|---|---|---|---|---|
| | | Commodities | | | | Currencies vs EUR | | |
| Perf 1 Month | -4.45% | -6.58% | 5.19% | -3.90% | -1.04% | 6.18% | 0.63% | 1.28% |
| Perf 3 Month | -4.91% | -8.13% | 7.06% | -7.67% | -1.48% | 3.61% | 1.39% | 3.16% |
| Perf YTD | 8.74% | 4.78% | 18.64% | 7.78% | 1.96% | -4.09% | 2.95% | -2.29% |

| End of July | Global Aggregate | US Aggregate | Euro Aggregate | US 10 Year Treasury | German 10 Year Bund | Global Credit | Global High Yield | Emerging Sovereign $ |
|---|---|---|---|---|---|---|---|---|
| | | | Bloomberg Indices Bonds Total returns | | | | | |
| Perf 1 Month | 2.76% | 2.34% | 2.04% | 2.90% | 2.98% | 2.38% | 1.96% | 1.85% |
| Perf 3 Month | 4.26% | 5.06% | 2.43% | 6.08% | 4.09% | 4.53% | 3.89% | 4.26% |
| Perf YTD | -0.49% | 1.61% | 0.80% | 1.27% | -2.33% | 1.29% | 5.20% | 4.11% |

Source: Bloomberg 31/07/24

Bond yields tended to fall across the curve on both sides of the Atlantic. Short rates fell more sharply than long rates, causing the curves to steepen slightly. On the US side, the 10-year yield fell by 36 basis points to 4.03%, while the 2-year yield contracted by 50 basis points. The same was true of the German 2-year yield, which fell back to 2.53%, the same level as in February 2024. It is interesting to note that although the spread between the US 2-year and 10-year yields is still negative, the spread between the 2-year and 30-year yields has moved back into positive territory (+4 basis points).

This contraction in yields took place in an economic environment of mixed fortunes. While a number of leading indicators (such as the PMIs) suggest that the slowdown is well under way, the first estimate of US GDP growth for the second quarter came in well above expectations at 2.8%, compared with the expected 2%. It should be noted, however, that household consumption has tended to slow and that inventory base effects have inflated this figure somewhat. It should also be remembered that GDP growth tends to be a lagging indicator (unless we take into account the Atlanta Fed's estimate (GDPNOW), which stands at 2.5% and includes leading indicators in its calculation).

While gold performed rather well (+2.8%) and even had the luxury of trading at its all-time high ($2483 per ounce) during the month, other commodities were under pressure. China's current economic woes are not the only reason for this poor performance. Indeed, while the financial community is impatient to see the Chinese economy pick up again, the economic statistics published recently do not point in the right direction. The central bank (PBoC) has once again cut interest rates, but as we said at the end of last year, these homeopathic measures are not enough to provoke the electroshock needed to get the country back on track for sustained growth. The Chinese equity market, which began a strong and promising rebound in February this year, seems to be fading and giving the impression of a false start.



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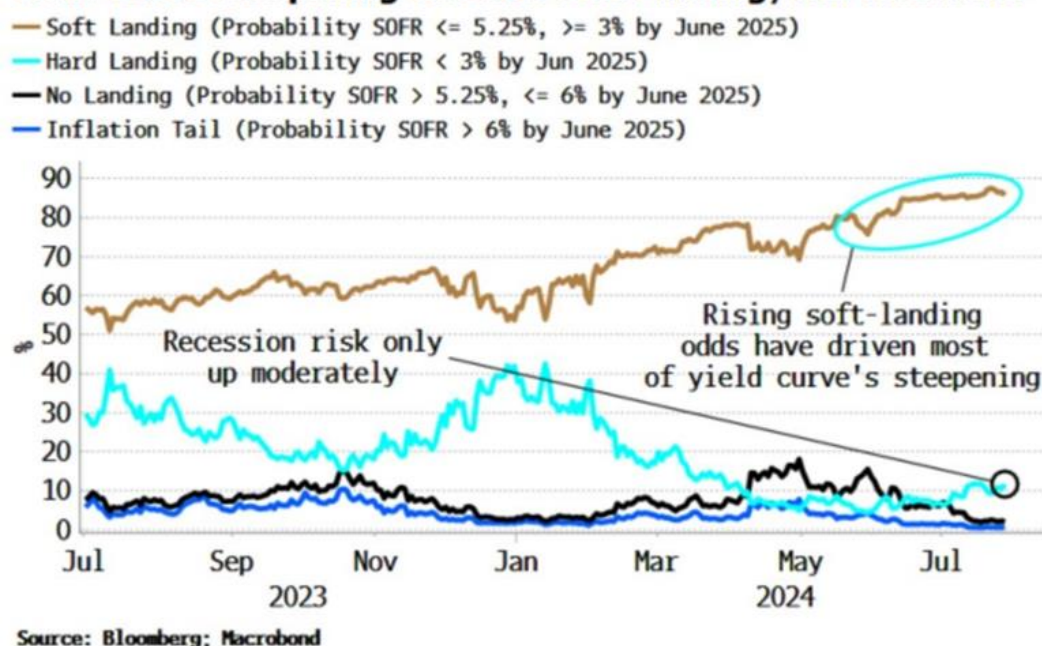
The performance of digital assets was mixed last month. Ethereum, down 2.5%, did not really benefit (for the time being) from the green light given by the SEC, which now authorises the issue of ETFs on this asset. As for Bitcoin (up 7.5%), it seems to have been invited to take part in the US presidential campaign in spite of itself. Candidate Trump, who was totally against the use of digital currency until 2023, seems to have realised that there were votes to be won in the crypto community. In recent speeches as part of his presidential campaign, Mr Trump has made numerous positive references to Bitcoin. He even gave a speech at the Bitcoin conference in Nashville where he hinted that he was in favour of the US becoming a strategic Bitcoin reserve and the country becoming the crypto capital of the world. On the Democratic side, the stance is more skeptical at the moment. As we have mentioned several times in recent years, investors are going to have to come to terms with the democratisation of digital assets, which are becoming more and more a part of people's daily lives, and this can only accelerate if the candidates in the US presidential election make this a campaign issue.




The British central bank (BoE) has "finally" joined the club of central banks that are easing their monetary policy. Following a very close vote (5 votes for a cut against 4 for the status quo), the committee decided to make its first cut since 2020, reducing its key rate to 5% (-25 basis points). Although the decision was not unanimous, it seems relatively logical given the country's economic performance in recent months. British inflation has returned to the 2% target, while the job market is gradually easing. The same is true of the Canadian Central Bank (BoC), which cut rates by 25 basis points for the second time in a row. At the very end of the month, all eyes were on the Fed, which was meeting for its turn.



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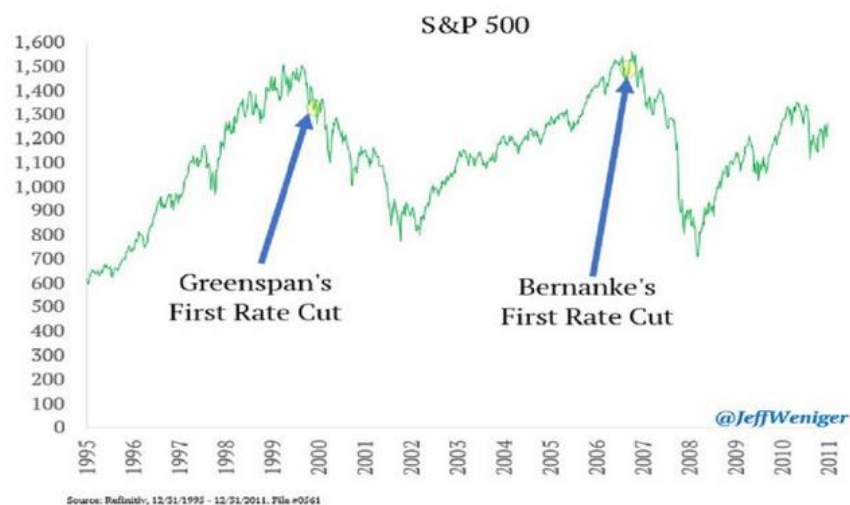
While the consensus was not expecting any rate movements at this meeting, the financial community was hoping to obtain tangible information on the evolution of US monetary policy and the timing of the (probable) future rate cut by the institution. Mr Powell was not as clear as the consensus might have hoped. While he confirmed that economic activity was slowing and that the labour market was showing signs of a gradual easing, he hinted that the Bank would continue to monitor statistical developments ("*data dependency*") before making any decisions. The consensus, which was betting on an initial fall in September, has been somewhat disappointed and will therefore have to wait for the annual meeting of the major monetary authorities in Jackson Hole at the end of August to hope for a clearer picture. As we said earlier, the Japanese Central Bank (BoJ) is sounding a completely different note, having decided to raise rates by 15 basis points to 0.25%, which has accentuated the unwinding of *carry trades* despite the fact that the Japanese economy is slowing down.




It's been an eventful few weeks on the political front. We mentioned above the change of Prime Minister in the UK, France is sailing blind without a government (at least until the end of the Olympic Games) and the German government's popularity rating is at an all-time low. History was made in the United States with the attempted assassination of Mr Trump. Strange as it may seem, a gunman managed to stand on a rooftop 150 metres from the former US president at a campaign rally in Pennsylvania and shoot him during his speech. As you have all read, several bullets were fired; one hit the presidential candidate's right ear and the attack left one member of the audience dead. The event forced the head of the US *Secret Service* (responsible, among other things, for protecting the presidential candidates) to resign and boosted Mr Trump's popularity in the polls. This popularity quickly fell when, a few days after the attack, President Biden announced his withdrawal from the race for re-election and endorsed his current Vice-President Kamala Harris. The latter quickly received the support of the party heavyweights like the Clintons and Obamas. Barring a huge surprise at the Democratic convention between 19 and 22 August, which will decide the party's official candidate, Ms Harris is expected to challenge Mr Trump in November.
As you can see, this election campaign is likely to be full of surprises. We can already say that it will go down in the annals of history.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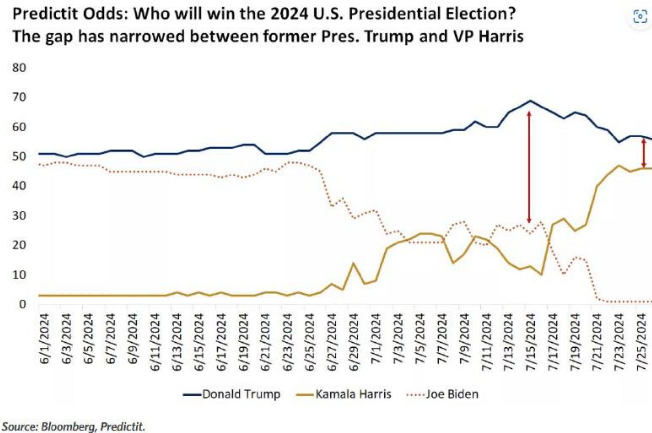


The most skeptical investors regularly point to the fact that equity markets are trading at high valuations. Admittedly, the S&P 500 is currently trading at a PER (Price-Earning Ratio) of 21x, whereas the historical median over the last twenty years has been around 17x. On the basis of this ratio, the US market is indeed not 'cheap'. A little closer analysis reveals that it is a handful of companies that inflate this ratio at index level. These are technology giants such as Alphabet, Microsoft and Nvidia. If we exclude the 10 "most expensive" companies, the S&P500's P/E stands at 17x. Across the Atlantic, the Stoxx Europe 600 index is also trading close to its historical average, which leads us to conclude that despite the recent rise in equity markets, the valuation of the entire stock market is not indecent. This is all the more true given that the vast majority of the companies making up these indices are delivering quarter after quarter of excellent results and an encouraging outlook. In our previous letter, we mentioned that investors severely punished companies that disappointed on the *guidance front, which* is logical when the guidance *is* perfect. The fact remains that, in the vast majority of cases, companies deliver what investors expect of them, or even better. To date, around half the companies in the S&P500 have published their results for the 2nd quarter, and it should be noted that around 79% have reported above expectations. Even if temporary corrections cannot be avoided, we remain confident in the equity markets as long as the quality of the results remain strong, which is typically an indicator of a bull market.



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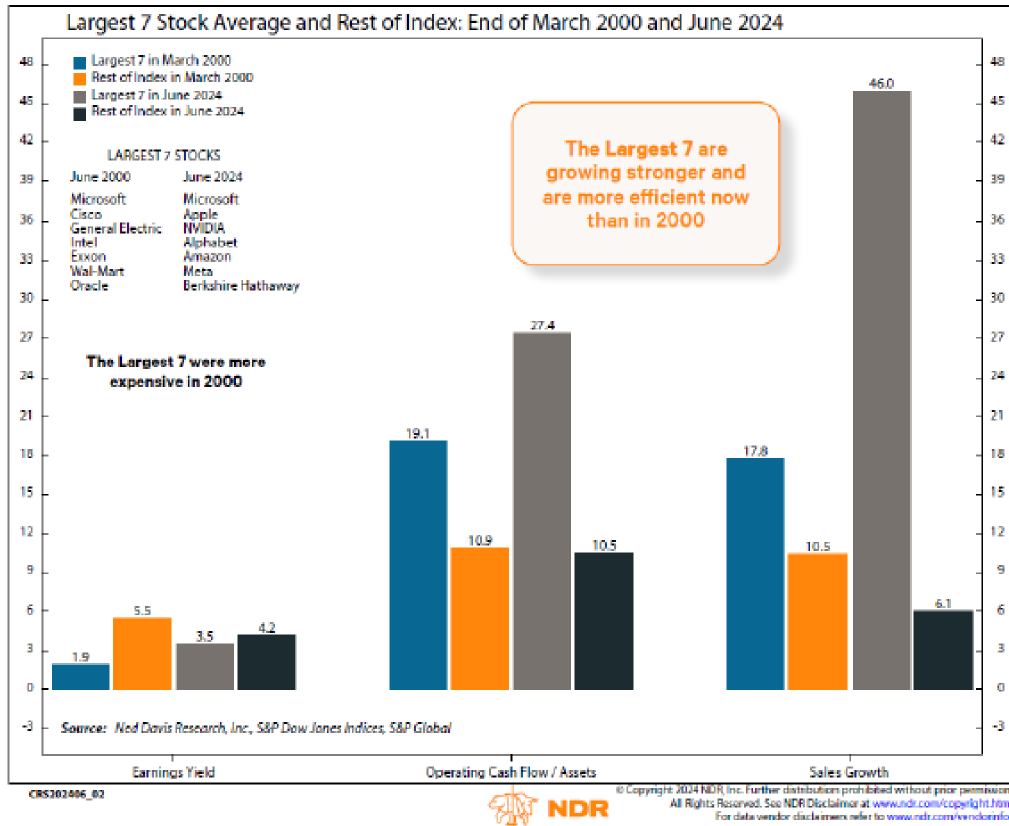
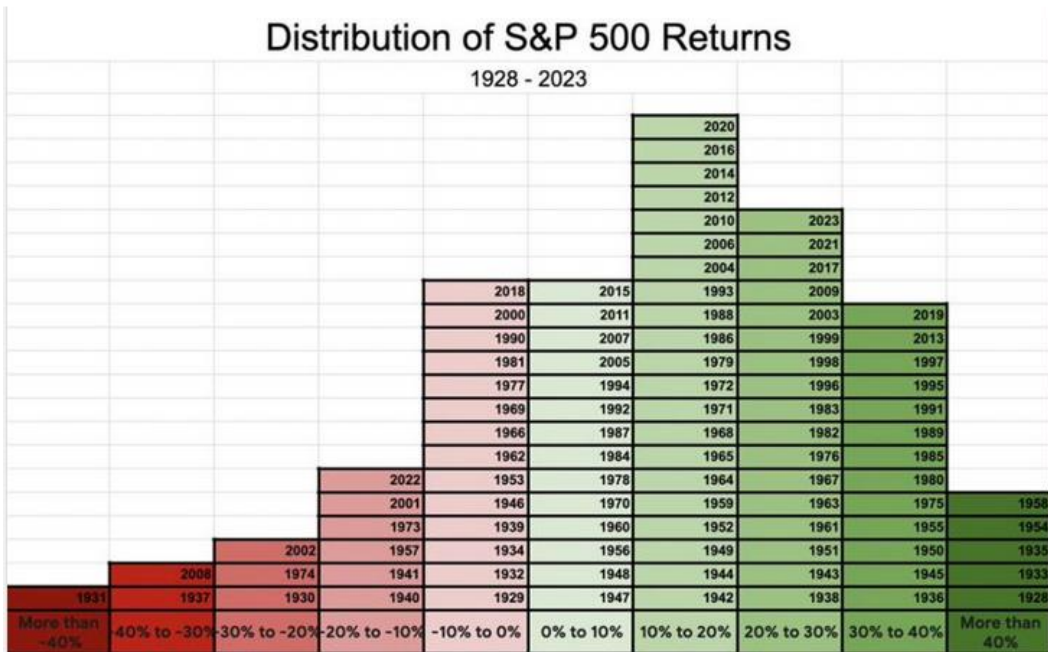
Today's Largest 7 are cheaper and of higher quality vs. 2000




The geopolitical situation in the Middle East remains tense. As we have said on several occasions, we need to keep an eye on this and factor it into our scenarios, without building our portfolios for the worst-case scenario. Inflation is still heading towards target and the economy is (finally) slowing down in most parts of the world. We can therefore deduce that the efforts of central banks are beginning to bear fruit. Companies remain resilient in terms of both balance sheet quality and profit margins. The new deal could come with the unwinding of the *carry trades* we explained above. These could bring considerable volatility to the markets over the next few weeks. Investors will therefore need to keep a close eye on developments in the BoJ's monetary policy, which will, more than ever, have an impact on Western assets. We would tend to take advantage of any downward exaggeration to buy quality companies at good prices.

We wish you a great August and a wonderful holiday for those of you who are lucky enough to take one.

Bonus graphics :

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