FlyingColours

Portfolio & Market Update

October 2024

Introduction

The global markets were jittery throughout October, due to speculation over interest rate cuts and their impact on economic growth and inflation.

Uncertainty was heightened by the US presidential election, which proved difficult to predict for pollsters. The VIX index, tracking implied volatility in the US equity market, reached its second-highest level since March last year.

In the UK, inflation fell to its lowest level in over three years, while the Chancellor's Budget introduced significant tax rises. Market responses were fairly negative, with the FTSE 100 index falling and gilt yields rising.

Overall, October was a volatile month for markets, with equities moving more slowly after a strong rally earlier in the year. Growth risks remain a primary concern for investors.

Markets

With all the uncertainty described above, multi-asset portfolios had a challenging month. In GBP (Sterling) terms, the US markets performed positively, while other regions struggled to generate positive returns.

Fixed income markets generated negative returns on the back of the UK budget and the potential increase of debt in the UK. This resulted in a shaper rise in yields toward the end of the month.

US

The US market had a positive month in GBP terms, but only due to currency movements. The September Consumer Price Index (CPI) report showed a 0.2% month-over-month and a 2.4% year-over-year increase. This equated to the slowest annual rise since early 2021.

However, core inflation remained high at 3.3%, driven by medical care, auto insurance and airline fares. Following the Federal Reserve's 0.5% interest rate cut in September, the persistent core inflation underscores the challenge for US policymakers to balance a solid labour market with price stability.

Interest rate cuts are anticipated in November and possibly December, but the strong labour market and resilient inflation have reduced the likelihood of a further 0.5% cut. Election uncertainty and cooling rate cut expectations pushed the 2-year and 10-year Treasury yields above 4.0%, leading to a -2.4% return for US Treasuries in October.

The unemployment rate held steady at 4.1%, with the labour force participation rate slightly down to 62.6%. The S&P Global US Composite Purchasing Manager's Index (PMI) edged up to 54.1 in October, indicating steady growth in business activity, driven by the services sector, while manufacturing output continued to decline. Employment saw slight reductions across both sectors, and output price inflation dropped to its lowest level in 53 months.

UK

The UK market wrapped up the month on a sour note, with the FTSE 100 dipping by 1.45%.

Inflation took a surprising tumble to 1.7%, its lowest in more than three years. In an historic moment, Chancellor Rachel Reeves unveiled Labour's first Budget since 2010, outlining plans to increase taxes by £40 billion starting next year.

The Budget was accompanied by OBR's forecasts, predicting a modest 1.1% growth for the UK in real GDP terms this year, followed by a hopeful rise to 2.0% next year, then a gentle ease to 1.8% in 2026, before levelling off around 1.5%.

After the budget, the market responded with jittery vibes, sending the FTSE 100 index down by 1.33% over two days, and pushing the 10-

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year gilt yield to its highest level in almost a year. Signs of a cooling economy are evident, as the PMI number slows, yet remains in the expansion zone. On a brighter note, the housing market has picked up steam, hinting at pockets of resilience within the uncertain economic landscape.

Europe

October was a rough ride for European equity markets, which dipped by 2.05% for the month.

Inflation grabbed the headlines, climbing to 2.0% year-over-year, largely thanks to energy costs. In a surprising twist, the European central Bank (ECB) decided to slash rates by 0.25% to 3.25%, blaming sluggish economic momentum.

The HCOB Purchasing Managers' Index Eurozone Composite PMI held its breath at 50, signalling a standstill in private business activities.

Despite an unexpected rise in Q3 GDP growth, a thought-provoking report spearheaded by Mario Draghi called for Europe to step up its game. It emphasised the urgent need for more investment and innovation, shining a light on Europe's shortage of dynamic startups and the burden of restrictive regulations holding them back.

Japan

In Japan, October saw the TOPIX index dip by 0.13% when measured in GBP terms, largely due to the Yen's slide against the British Pound.

This comes amid a hawkish stance from the Bank of Japan (BoJ) and political tremors following the ruling coalition's election setback. On the brighter side, Tokyo's core inflation ticked up to 1.8% year-over-year, buoyed by encouraging wage growth. While the BoJ kept interest rates steady, their hawkish rhetoric spooked investors, triggering a sell-off in Japanese government bonds.

Asia & Emerging Markets

China's recent support measures have renewed focus on its equity market. In October, policymakers introduced initiatives allowing local governments to use special bonds to purchase land from troubled developers and planned a debt ceiling hike, signaling Beijing's commitment to managing the real estate bubble and boosting consumption.

While the impact is yet to be fully assessed, looser monetary and fiscal policy could lead to improved growth in 2025. Despite this, Emerging and Asian markets returned slight losses of 0.31% and 0.62% respectively, due to a stronger dollar.

Indian stocks fell sharply in October on weak corporate results. The National People's Congress may provide more clarity on stimulus measures. China's GDP growth for Q3 was 4.6%, below the 5% target, highlighting the need for increased consumption.

Fixed Income

Global bonds reversed in October, erasing 2024 gains, due to three main factors: the resilience of economic output, especially in the US, suggesting a slower pace of rate cuts; concerns about inflation not returning to central banks' 2% target soon, influenced by potential US tariffs and UK spending plans; and worries about government debt levels and future supply.

The rise in breakeven rates reflects these inflation concerns. The political climate continues to favour more spending or lower taxes over fiscal consolidation. Fixed income markets are expected to remain volatile until the path for rate cuts becomes clearer, with the US presidential election adding to the uncertainty and contributing to higher bond yields.

Outlook

The forecast for the upcoming months indicates ongoing market volatility. The result of the US

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election has the potential to be a disruptive factor for the markets in the near term. On a positive note, we recognise that inflation is currently on a downward trend.

Our perspective suggests that while there is a possibility of a global economic slowdown, a recession is unlikely in the near future. Central banks will continue to face the challenge of balancing inflation and economic growth.

At Flying Colours, we are committed to continuously monitoring the economic outlook and market signals to ensure our portfolios remain aligned with the best interests of our clients.

Our investment strategies are long-term focused, managing risks over the extended horizon rather than reacting to short-term trends that could be detrimental to our investors. Our goal is to achieve well-managed risk-adjusted returns, consistent with our investment philosophy.

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