

momentum
global investment management

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Global Matters | Monthly Market Review

October 2023

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Professional Portfolio International

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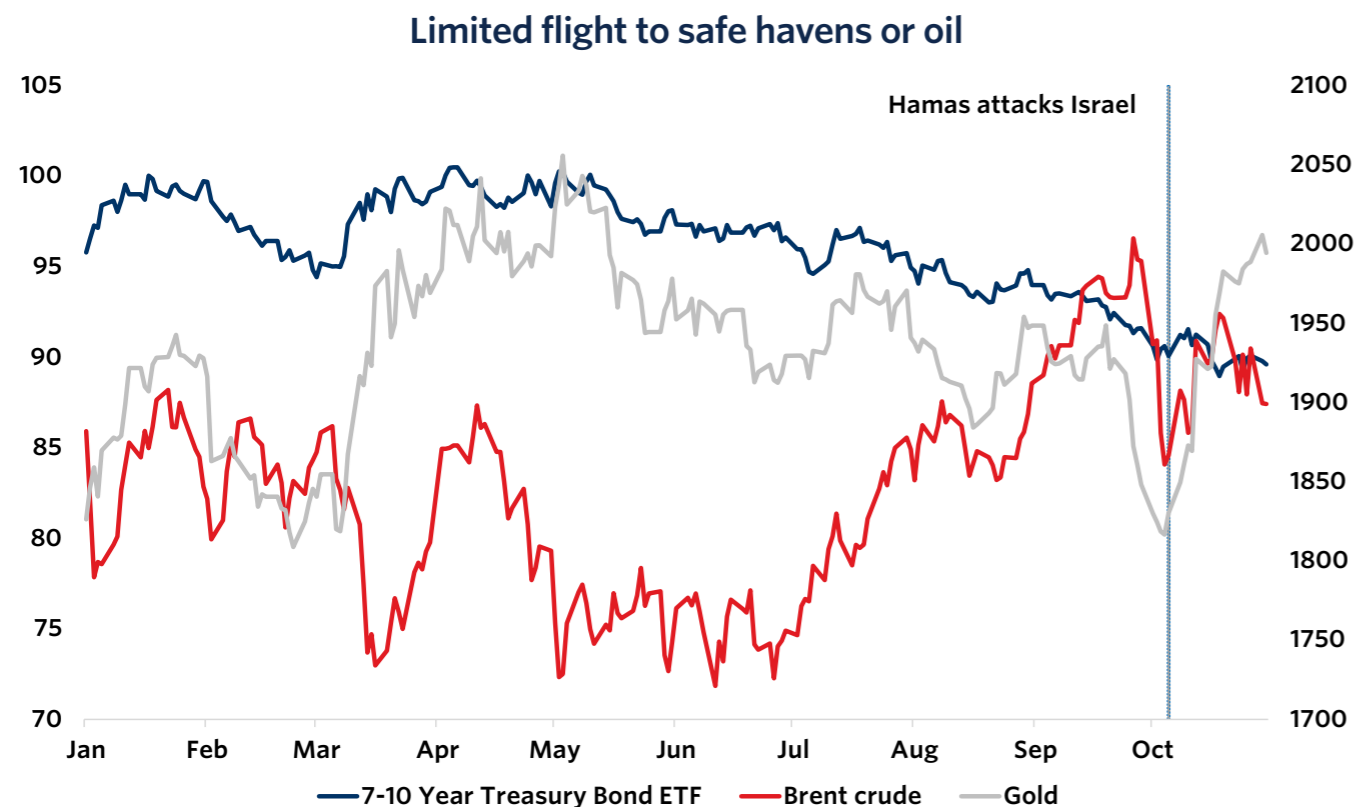


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Global market review & outlook

The worst atrocity inflicted on Jewish civilians since the Holocaust and the ensuing war between Israel and Hamas overshadowed all else in October. From the perspective of financial markets, the key question was the extent to which the conflict would spill over into a wider conflagration, drawing in Iran and its Axis of Resistance, with broader implications globally and raising the risk of Middle East oil supply disruption.

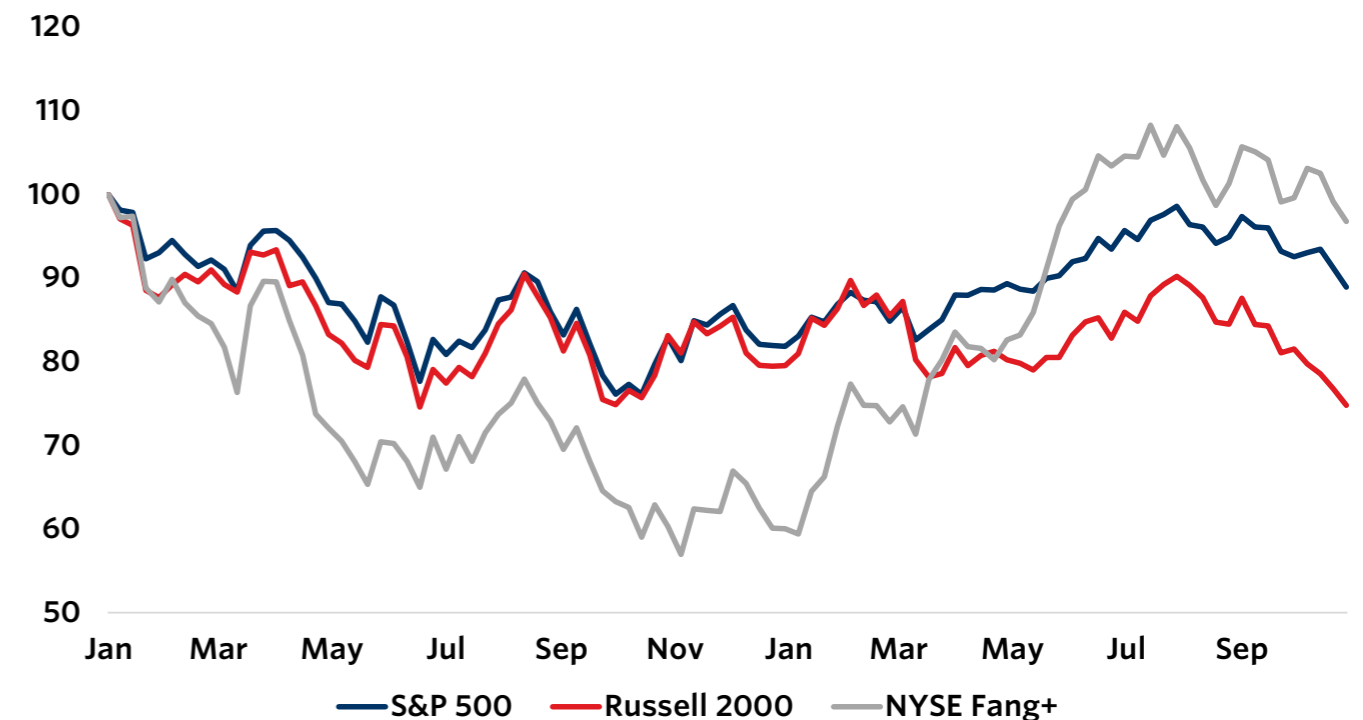
However, there was limited evidence of a flight to safe havens in the aftermath of the attack. Initially bond and equity markets fell while gold rose, up by 10% to reach \$2,006, close to its all-time high, but as it became increasingly evident that the aggressive rhetoric of the anti-Israel axis was not reflected in action, markets began to take a more measured view of the risks. By month end bonds and equities were recovering, while gold gave back some of its gains. The US dollar saw little movement over the month. The oil price, which had fallen by 13% in the week before the attack on evidence of ample supply and weak Chinese economic data, initially rose by 10% but lost most of the gain, leaving it down by 8% over the month, and little changed so far this year.



Source: Bloomberg Finance L.P., Momentum Global Investment Management as at 31 October 2023

Equities weakened, but not dramatically, the S&P 500 and MSCI World index both down by close to 6% from their peaks early in the month, taking them into correction territory, down 10%, from the highs for this year at the end of July, before rallying towards month end. Over the month, global equities returned -2.9%, with all regions falling, while emerging markets returned -3.9%, weighed down by continuing weakness in China, -4.3%, and falls in Latin America, -4.8%, giving up some of its gains earlier in the year. The US megacap tech stocks which led markets so powerfully in the first half of the year had a volatile month; the NYSE FANG+ index suffered a 9% drop in 2 weeks during October, but has moved broadly in line with the S&P 500 index since the end of June. Small cap stocks continue to face headwinds; they are most exposed to higher interest rates and challenging economic conditions, and are well into a bear market. The Russell 2000 index of small cap US stocks has fallen by 17% since the end of July, and is down by 32% from its peak in November 2021, with similar moves in other small cap indices globally.

US equities weaken – small cap underperform sharply



Source: Bloomberg Finance L.P., Momentum Global Investment Management as at 31 October 2023

Arguably the most significant moves in the month were again in bond markets, with yields rising across the maturity spectrum but especially sharply at longer tenors. From 4.6% at the end of September, the yield on the US 10Y Treasury rose to 5% in mid-month, its highest since June 2007 and a level reached only for brief periods this century. From the low for this year of 3.3% soon after the mini-banking crisis in March, the yield had risen by 160bps by the end of October. The yield on 2Y bonds moved very little over the month, meaning that the yield curve continued its steepening, with the 2Y-10Y curve inverted by only 15bps at month end compared with over 100bps as recently as July. Most of the rise in yields again came through higher real yields, up by 30bps to 2.5% on 10Y Treasuries.

These huge shifts in nominal and real yields have tightened financial conditions materially, a fact acknowledged by the Fed when it decided to hold the Fed Funds rate steady at the latest FOMC meeting. The economy has remained remarkably strong, with GDP growth at an annualised 4.9% quarter-on-quarter in Q3, personal consumption still buoyant and the labour market resilient. Although there have been some tentative signs of a softening in the labour market and wage growth has fallen to 5.3% from a peak of 7.1% in June, core inflation rates remain too high (4.1% for CPI and 3.7% for PCE) and the Fed expects 'the process of getting inflation sustainably down to 2 percent has a long way to go'. A further rise in rates cannot be ruled out, but more likely is that rates have reached a peak and then will be kept at high and restrictive levels well into 2024. The Fed's QT programme will continue at a rate of \$95bn per month, further tightening financial conditions, something the Fed sees as vital in reducing inflation sustainably to the 2% target.

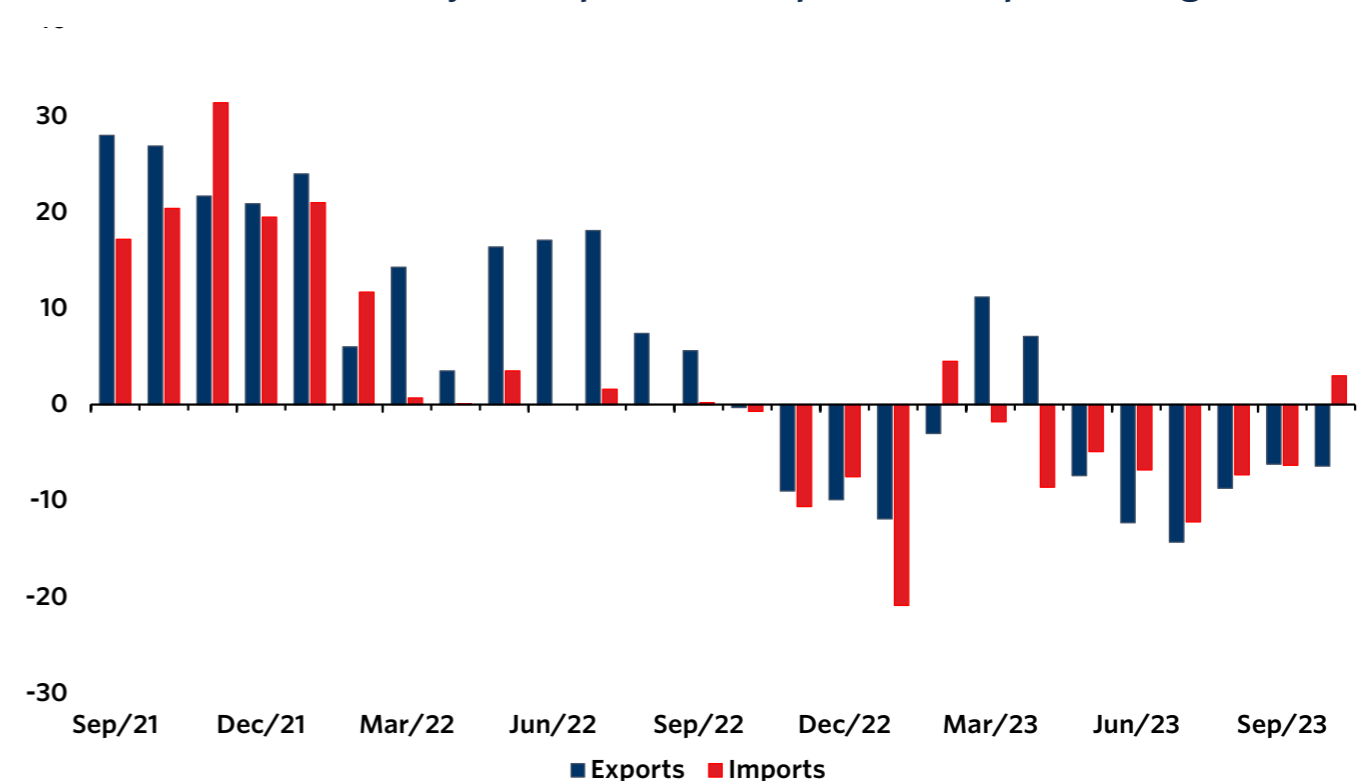
In Europe and the UK, economic conditions are much clearer than in the US, with economic data pointing unambiguously to weakness. EU GDP shrunk by 0.1% in Q3, the key German economy has been in recessionary conditions for 18 months, and forward indicators point to continuing weakness. The UK has surprised by avoiding recession so far, but a sharp slowdown seems inevitable given the tight monetary and fiscal policies in place, weakness in the housing market and increasing evidence of a softer labour market. In the EU and UK, money supply has been shrinking and bank lending standards tightening, and it was no surprise when the European Central Bank and Bank of England kept policy rates steady, at 4.0% and 5.25% respectively. While cuts in rates are not yet on the agenda given the persistence of inflation, especially in the UK, it is now probable that we have seen the peak of the rate cycle in the EU and UK.

The Bank of Japan (BoJ) remains out on a limb, the only major central bank to have kept policy ultra-loose, with interest rates still negative. However, with inflation at 3% or higher through 2023 and the economy resilient, the BoJ appears increasingly optimistic about the rate holding at its 2% target, and made a second adjustment to its yield curve control policy (YCC) in October by redefining the 1% yield cap as an upper bound, thereby allowing the yield to rise above 1%. While modest in size and impact, the change is a further step towards policy normalisation, and an end to negative interest rates and YCC is in sight. The yen reacted to the shift by weakening further, down by 1.5% versus the dollar in October and by 14% YTD, taking it to a 33-year low. At these levels it is substantially undervalued, but the timing of any change in direction remains largely in the hands of policy makers.

China reported unexpectedly strong growth in GDP in Q3, +4.9%, boosted by strong consumption spending, but key parts of its economy, property and trade, remain under a cloud. The property development industry continues to struggle with excessive debt, house prices are falling and investment is down by 9.1% in the first 9 months of 2023. Both exports and imports have been weak this year, reflecting subdued global growth, the impact of US sanctions and the shift of production by international companies away from China.

The authorities have responded by gradually loosening monetary policy, and, in a surprise move in October which reflects the concern that growth targets are under pressure, approved the issue of an additional 1tn yuan (\$137bn) of government debt to spend on various infrastructure projects, increasing the fiscal deficit to 3.8% from 3% set in March. Details remain sketchy, and the move has had little impact on investors' negative perception of China, with the equity market languishing at levels not far above the lows of the past 15 years.

China's economy under pressure - exports and imports falling



Source: Bloomberg Finance L.P. , Momentum Global Investment Management as at 31 October 2023

"In Europe and the UK, economic conditions are much clearer than in the US, with economic data pointing unambiguously to weakness"

The challenges and uncertainties ahead have been compounded by events in Israel and Gaza. Initial fears about escalation of the conflict have diminished, and there is a broad view reflected in markets that the conflict will be contained. There is no doubt that Hamas has no friends in the West, and few in the Arab world, but if civilian casualties in Gaza continue to mount matters could change. On the balance of probabilities, it is likely that a diplomatic solution will be negotiated and a wider conflict avoided, but the path to that end is likely to be bumpy.

At the same time, monetary policy is at its tightest in decades. The Fed has moved to a more balanced policy outlook and although the door to additional tightening is not closed, we are at or very close to the peak in rates. It is likely that monetary conditions are now sufficiently tight in the US, as well as the EU and UK, to contain inflation, but not without a prolonged period of restrictive policy. In an era of heightened geopolitical risks, there is considerable uncertainty about the macro-economic variables impacting policy, and hence on the timing of rate cuts, and the risk of policy error is rising.

This calls for continuing caution in equity markets in the short term, a caution amplified by the big valuation shift in the past few weeks in favour of bonds, especially those with longer maturity. Nominal and real yields of US Treasury bonds are at or very close to their highest levels in 15 years, and are firmly in attractive valuation territory. As well as offering high yields, they would be the biggest beneficiaries of a sharp slowdown or recession, and offer the ultimate safe haven should geopolitical events escalate further.

“In an era of heightened geopolitical risks, there is considerable uncertainty about the macro-economic variables impacting policy, and hence on the timing of rate cuts, and the risk of policy error is rising”



Market performance - Global (local returns) as at 31 October 2023

Asset Class / Region	Index	Ccy	1 month	3 months	YTD	12 months
Developed Markets Equities						
United States	S&P 500 NR	USD	-2.1%	-8.4%	10.2%	9.6%
United Kingdom	MSCI UK NR	GBP	-3.7%	-3.4%	1.9%	6.6%
Continental Europe	MSCI Europe ex UK NR	EUR	-3.4%	-8.1%	5.4%	9.1%
Japan	Topix TR	JPY	-3.0%	-2.1%	21.9%	19.8%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	-4.1%	-12.4%	-4.5%	11.8%
Global	MSCI World NR	USD	-2.9%	-9.3%	7.9%	10.5%
Emerging Markets Equities						
Emerging Europe	MSCI EM Europe NR	USD	1.5%	-6.0%	16.7%	44.3%
Emerging Asia	MSCI EM Asia NR	USD	-4.0%	-12.2%	-3.0%	14.2%
Emerging Latin America	MSCI EM Latin America NR	USD	-4.8%	-13.7%	7.5%	3.7%
China	MSCI EM China NR	USD	-3.8%	-11.4%	-4.9%	13.0%
BRICs	MSCI BRIC NR	USD	-4.3%	-15.2%	-11.2%	21.1%
Global emerging markets	MSCI Emerging Markets NR	USD	-3.9%	-12.2%	-2.1%	10.8%
Bonds						
US Treasuries	JP Morgan United States Government Bond TR	USD	-1.2%	-3.8%	-2.7%	-0.6%
US Treasuries (inflation protected)	BBgBarc US Government Inflation Linked TR	USD	-0.8%	-3.6%	-1.7%	-0.8%
US Corporate (investment grade)	BBgBarc US Corporate Investment Grade TR	USD	-1.9%	-5.2%	-1.9%	2.8%
US High Yield	BBgBarc US High Yield 2% Issuer Cap TR	USD	-1.2%	-2.1%	4.6%	6.2%
UK Gilts	JP Morgan UK Government Bond TR	GBP	-0.4%	-1.9%	-4.7%	-6.1%
UK Corporate (investment grade)	ICE BofAML Sterling Non-Gilt TR	GBP	-0.1%	0.1%	1.1%	2.7%
Euro Government Bonds	ICE BofAML Euro Government TR	EUR	0.4%	-1.9%	0.0%	-2.0%
Euro Corporate (investment grade)	BBgBarc Euro Aggregate Corporate TR	EUR	0.4%	-0.3%	2.9%	4.0%
Euro High Yield	BBgBarc European HY 3% Constrained TR	EUR	-0.3%	0.3%	6.0%	9.0%
Japanese Government	JP Morgan Japan Government Bond TR	JPY	-1.7%	-3.2%	-2.2%	-4.0%
Australian Government	JP Morgan Australia GBI TR	AUD	-1.9%	-3.1%	-1.4%	-2.5%
Global Government Bonds	JP Morgan Global GBI	USD	-1.3%	-5.6%	-4.7%	-0.5%
Global Bonds	ICE BofAML Global Broad Market	USD	-1.3%	-5.6%	-3.7%	1.1%
Global Convertible Bonds	ICE BofAML Global Convertibles	USD	-3.6%	-8.8%	0.8%	2.9%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	-1.5%	-6.6%	-1.7%	6.4%

Asset Class / Region	Index	Ccy	1 month	3 months	YTD	12 months
Property						
US Property Securities	MSCI US REIT NR	USD	-4.4%	-13.8%	-7.2%	-7.1%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	-5.8%	-12.6%	-7.8%	-7.9%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	-4.6%	-11.3%	-14.0%	1.9%
Global Property Securities	S&P Global Property USD TR	USD	-4.8%	-12.9%	-8.2%	-3.2%
Currencies						
Euro		USD	0.0%	-3.8%	-1.2%	7.0%
UK Pound Sterling		USD	-0.4%	-5.3%	0.6%	6.0%
Japanese Yen		USD	-1.5%	-6.2%	-13.6%	-1.9%
Australian Dollar		USD	-1.5%	-5.7%	-7.0%	-1.0%
South African Rand		USD	1.5%	-4.3%	-8.6%	-1.6%
Commodities & Alternatives						
Commodities	RICI TR	USD	-1.9%	-0.9%	-0.6%	0.9%
Agricultural Commodities	RICI Agriculture TR	USD	0.0%	-3.4%	0.8%	2.8%
Oil	Brent Crude Oil	USD	-8.3%	2.2%	1.7%	-7.8%
Gold	Gold Spot	USD	7.3%	1.0%	8.8%	21.4%
Hedge funds	Bloomberg All Hedge Fund Index	USD	tbc	tbc	tbc	tbc
Interest Rates						
						Current Rate
United States						5.50%
United Kingdom						5.25%
Eurozone						4.50%
Japan						-0.10%
Australia						4.10%
South Africa						8.25%

Source: Bloomberg Finance L.P., Momentum Global Investment Management. Past performance is not indicative of future returns.

Market performance - UK (all returns GBP) as at 31 October 2023

Asset Class / Region	Index	Local Ccy	1 month	3 months	YTD	12 months
Equities						
UK - All Cap	MSCI UK NR	GBP	-3.7%	-3.4%	1.9%	6.6%
UK - Large Cap	MSCI UK Large Cap NR	GBP	-3.4%	-2.0%	0.6%	6.2%
UK - Mid Cap	MSCI UK Mid Cap NR	GBP	-5.0%	-10.2%	2.4%	8.0%
UK - Small Cap	MSCI Small Cap NR	GBP	-6.8%	-10.1%	-5.6%	-0.2%
United States	S&P 500 NR	USD	-1.7%	-3.0%	9.8%	3.5%
Continental Europe	MSCI Europe ex UK NR	EUR	-3.0%	-6.6%	3.7%	10.1%
Japan	Topix TR	JPY	-3.9%	-2.8%	5.0%	11.0%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	-3.6%	-7.2%	-4.9%	5.5%
Global developed markets	MSCI World NR	USD	-2.4%	-4.0%	7.4%	4.3%
Global emerging markets	MSCI Emerging Markets NR	USD	-3.4%	-7.0%	-2.5%	4.6%
Bonds						
Gilts - All	ICE BofAML UK Gilt TR	GBP	-0.4%	-2.0%	-5.0%	-6.4%
Gilts - Under 5 years	ICE BofAML UK Gilt TR 0-5 years	GBP	0.4%	1.7%	1.5%	1.8%
Gilts - 5 to 15 years	ICE BofAML UK Gilt TR 5-15 years	GBP	-0.2%	-0.3%	-2.4%	-2.5%
Gilts - Over 15 years	ICE BofAML UK Gilt TR 15+ years	GBP	-1.3%	-6.8%	-12.3%	-16.0%
Index Linked Gilts - All	ICE BofAML UK Gilt Inflation-Linked TR	GBP	-1.5%	-6.2%	-9.3%	-10.7%
Index Linked Gilts - 5 to 15 years	ICE BofAML UK Gilt Inflation-Linked TR 5-15 years	GBP	-1.0%	-1.6%	-0.1%	0.4%
Index Linked Gilts - Over 15 years	ICE BofAML UK Gilt Inflation-Linked TR 15+ years	GBP	-2.3%	-11.1%	-17.7%	-20.8%
UK Corporate (investment grade)	ICE BofAML Sterling Non-Gilt TR	GBP	-0.1%	0.1%	1.1%	2.7%
US Treasuries	JP Morgan US Government Bond TR	USD	-0.6%	2.0%	-3.5%	-5.7%
US Corporate (investment grade)	BBgBarc US Corporate Investment Grade TR	USD	-1.3%	0.5%	-2.7%	-2.5%
US High Yield	BBgBarc US High Yield 2% Issuer Cap TR	USD	-1.2%	-2.1%	4.6%	6.2%
Euro Government Bonds	ICE BofAML Euro Government TR	EUR	0.4%	-1.9%	0.0%	-2.0%
Euro Corporate (investment grade)	BBgBarc Euro Aggregate Corporate TR	EUR	0.4%	-0.3%	2.9%	4.0%
Euro High Yield	BBgBarc European High Yield 3% Constrained TR	EUR	-0.3%	0.3%	6.0%	9.0%
Global Government Bonds	JP Morgan Global GBI	GBP	-0.8%	-0.1%	-5.1%	-6.1%
Global Bonds	ICE BofAML Global Broad Market	GBP	-1.3%	-5.6%	-3.7%	1.1%
Global Convertible Bonds	ICE BofAML Global Convertibles	GBP	-3.6%	-8.8%	0.8%	2.9%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	GBP	-1.0%	-1.1%	-2.1%	0.4%

Asset Class / Region	Index	Local Ccy	1 month	3 months	YTD	12 months
Property						
Global Property Securities	S&P Global Property TR	GBP	-4.3%	-7.8%	-8.6%	-8.7%
Currencies						
Euro		GBP	0.4%	1.6%	-1.7%	1.0%
US Dollar		GBP	0.4%	5.6%	-0.6%	-5.6%
Japanese Yen		GBP	-1.1%	-0.9%	-14.0%	-7.5%
Commodities & Alternatives						
Commodities	Rogers International Commodity (RICI) TR	GBP	-1.4%	4.9%	-1.0%	-4.8%
Agricultural Commodities	Rogers International Commodity (RICI) Agriculture TR	GBP	0.4%	2.2%	0.4%	-2.9%
Oil	Brent Crude Oil	GBP	-7.9%	8.1%	1.3%	-13.0%
Gold	Gold Spot	GBP	7.8%	6.9%	8.3%	14.6%
Interest Rates						
						Current Rate
United Kingdom						5.25%

Source: Bloomberg Finance L.P. , Momentum Global Investment Management. Past performance is not indicative of future returns.

Asset allocation views

Our Overall View

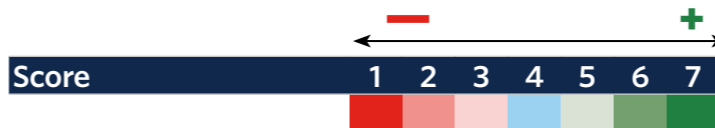
Score	Change	1	2	3	4	5	6	7
MAIN ASSET CLASSES	▲/▼/—	1	2	3	4	5	6	7
Equities	—							
Fixed Income	—							
Alternatives	—							
Cash	—							

Score	Change	1	2	3	4	5	6	7
EQUITIES	▲/▼/—	1	2	3	4	5	6	7
Developed Equities	—							
UK Equities	—							
European Equities	—							
US Equities	—							
Japanese Equities	▼							
Emerging Market Equities	—							

Score	Change	1	2	3	4	5	6	7
FIXED INCOME	▲/▼/—	1	2	3	4	5	6	7
Government	▲							
Index-Linked	—							
Investment Grade Corporate	—							
High Yield Corporate	—							
Emerging Market Debt	▼							
Convertible Bonds	—							

Score	Change	1	2	3	4	5	6	7
SPECIALIST ASSETS/ALTERNATIVES	▲/▼/—	1	2	3	4	5	6	7
Commodities	—							
Property	—							
Infrastructure	—							
Liquid Alternatives	—							
Private Equity	—							
Specialist Financial	—							

Score	Change	1	2	3	4	5	6	7
CURRENCIES vs. USD	▲/▼/—	1	2	3	4	5	6	7
GBP	—							
EUR	—							
JPY	—							
Gold	—							



The lack of depth in this year's market rally is a cause for concern with fears of a recession still high and lead indicators suggesting slower growth ahead. Our fixed income view remains broadly neutral overall, but in light of the recent sharp moves higher in treasury yields, we upgrade our government view. Although the threat of a recession requires an element of caution with certain fixed income assets, good opportunities can be found in selective rates and credit markets. Alternative assets remain a good diversifier of returns, especially favourable should market volatility increase. Cash is an attractive lure today but won't preserve real wealth long term.

We temper our positive view on Japanese equities, taking some profit after the strong year to date performance. Last year's aggressive rate hikes continue to show signs of pushing developed economies towards recession and there is a risk of complacency taking hold in risk markets. US equities in particular have shown a worrying lack of breadth in this year's rally, but the opportunity set for active managers is appealing. European equities look reasonably attractive, but the most compelling markets remain the UK and Japan which trade at a discount to global peers and offer healthy dividends.

After their rapid move higher over the summer months, treasury yields have reached levels we think offer value today, and we upgrade our government view. Despite offering alluring all in yields, we think the spreads offered today on investment grade and riskier high yield corporate bonds do not compensate investors adequately for the underlying fundamental credit risk. The possibility of a recession and rising default rates suggest that an element of caution is necessary. We continue to prefer shorter duration bonds in both developed and emerging markets. Improving real yields and weak growth expectations have recently improved the appeal of inflation linked bonds.

Commodity prices are likely to be challenged against a slowdown in global growth. With expectations of a more turbulent period ahead in markets, alternatives continue to offer diversification benefits at attractive valuations after a period of poor investor sentiment. Discounts in NAVs in private equity continue to appear overly pessimistic while secular trends in infrastructure and specialist financials have boosted our outlook for both asset classes. Our liquid alternatives continue to offer attractive diversification benefits especially during periods of market uncertainty.

Against long term valuation metrics, Sterling and Yen continue to remain cheap relative to the Dollar. The Bank of Japan's ongoing policy of yield curve control policy holds the Yen back, for now. Recession expectations in the US and inflation in Europe could mean divergent rate expectations in support of the Euro, but the Fed's higher for longer narrative keeps the common currency in check for now. Gold's status as a haven asset means it remains a useful diversifier, although somewhat expensive versus real rates today.

"Our liquid alternatives continue to offer attractive diversification benefits especially during periods of market uncertainty"



The asset allocation views are updated at the end of each quarter unless otherwise stated.

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