A Month in the Markets

By Stefano Amato

November 2021

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Month of October

Market Review

Global stock markets performed well in October as they bounced back from the previous month's turbulence. Several recurring themes continued to influence returns, including a slowdown of economic growth, supply chain disruptions, high demand and rising prices, and the prospect of increasing interest rates.

Among the major stock markets, the top performers were the US, Europe and China. Their performance was closely followed by the UK, Asia Pacific excluding Japan and the emerging markets. October was more challenging for bond markets, as yields on government bonds – which move in the opposite direction of prices – increased.

UK and Europe

The UK and Europe experienced differing fortunes in October. The UK saw accelerated activity among private sector businesses and buoyant consumer spending, with companies in the services sector being the main drivers of this growth[1]. This was balanced out by the manufacturing sector experiencing slower growth due to continuing supply chain disruptions, staffing issues and higher prices for materials[2]. Inflation continued to cause concern in October, with staff shortages pushing up wages and the rising cost of goods lifting consumer prices[3].

It was a different story in Europe, where supply chain bottlenecks and ongoing concerns about COVID-19 infections took their toll on business activity[4]. Much like other parts of the world, inflation continued to rear its head in Europe as businesses passed on the rising cost of goods and materials to customers. This led to headline inflation in the eurozone reaching 4.1% in October[5], a 13-year high. Much of this is believed to come from surging energy prices caused by higher demand as the region emerges from COVID-19 restrictions and a global energy supply shortage.

Despite this, the European Central Bank (ECB) decided not to raise interest rates during its October meeting[6]. The ECB pushed back on suggestions that rates will rise in early 2022 by suggesting that inflation will be "moderately" above its target of 2% for a "transitory period".

US

Business activity accelerated in the US in the past month with the services sector – which includes restaurants and leisure companies – benefiting most[7]. That said, it was not all smooth sailing.

Firstly, it was clear that the pandemic continued to take its toll on the economy. Gross domestic product (GDP) – a measure of the health of an economy – grew by an annual rate of just 2% in the three months to the end of September[8], compared with 6.7% in the previous three months.

PLEASE REMEMBER THAT ALL INVESTMENTS CARRY VARYING DEGREES OF RISK TO YOUR MONEY. THE VALUE OF INVESTMENTS AND ANY INCOME FROM THEM CAN GO DOWN AS WELL AS UP AND YOU MAY GET BACK LESS THAN THE FULL AMOUNT YOU INVESTED. PAST PERFORMANCE IS NOT A RELIABLE INDICATOR OF FUTURE RESULTS.

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Similarly, strong demand for goods and services, staff shortages and supply chain bottlenecks pushed prices upward. As with many other regions of the world, this impacted the consumer price inflation for September which came in at 5.4%[9] - the highest since 2008.

Asia Pacific

China's economy continued to weaken in October due to power shortages and systemic problems in its property sector[10]. Despite being one of the stronger recovery stories from the past year, China faced major challenges with economic growth falling short of expectations and Evergrande - a major real estate company - coming close to collapse. Economic growth for the three months to the end of September measured 4.9%, falling short of the 5.2% that was expected.[11]

Meanwhile, Japan's economy was impacted by supply chain issues that constrained its export-heavy manufacturing sector, prompting major automotive manufacturers to cut back production plans[12]. The uncertain backdrop of the ongoing pandemic disrupted supply chains. Computer chip shortages exacerbated the situation, resulting in the Bank of Japan (BoJ) lowering its expectations for economic growth in the current fiscal year[13].

Outlook

Despite the ongoing pandemic and concerns about higher inflation, we continue to have a broadly positive outlook for stock markets.

While potential interest rate hikes in the US and UK will likely act as a minor challenge for shares, we believe there is still room for growth given that company earnings are the main driver of stock market returns. Conversely, this is a challenging environment for bonds. In our experience, expectations of higher interest rates tend to cause bond prices to fall as investors demand higher yields.

Overall, our outlook is broadly similar to last month. We prefer shares over bonds in this environment, but are aware of several risks to our current view. Most prominent among these is the potential for a resurgence of COVID-19 infections that causes further economic disruption. But, in our view there are other potential risks, including a general slowdown of economic growth around the world, a broader spill-over of the economic and real estate market problems in China, as well as sudden interest rate hikes from major central banks.

Portfolio Activity

Across the majority of portfolios, we maintained our position towards taking risk through investing in shares. In terms of regional preferences, we see attractive risk-return trade offs within Europe, US and Japanese markets. We continue to prefer shares relative to bonds because we feel current high prices and low yields still do not offer many compelling investment opportunities.

While we did not make major portfolio changes over the month, we are reassessing the opportunities in the emerging economies of Asia. Although problems in China continue, we are beginning to see reduced geopolitical risk as tentative steps are being taken to resolve problems in the real estate market.

1 https://www.markiteconomics.com/Public/Home/PressRelease/6c4111f9b7054ecba6a8e85eedb9ebf7

2 https://www.markiteconomics.com/Public/Home/PressRelease/6c4111f9b7054ecba6a8e85eedb9ebf7

3 https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/september2021

4 https://www.markiteconomics.com/Public/Home/PressRelease/318d8368fea74e588e80760a5eb9c21f

5 https://www.cnbc.com/2021/10/29/euro-zone-inflation-rises-to-4point1percent-for-october-hitting-a-new-13-year-high.html

6 https://tradingeconomics.com/euro-area/interest-rate

7 https://www.markiteconomics.com/Public/Home/PressRelease/291a6f7539534735b69350b6e4e0f921

8 https://www.bbc.co.uk/news/business-59081177

9 https://www.cbc.ca/news/business/us-inflation-1.6208981

10 https://www.reuters.com/world/china/china-q3-gdp-growth-hits-1-year-low-raising-heat-policymakers-2021-10-17/

11 https://www.cnbc.com/2021/10/18/asia-markets-china-economy-currencies-oil.html

12 https://www.marketwatch.com/story/boj-lowers-outlook-for-japan-growth-inflation-271635390471

13 https://tradingeconomics.com/japan/interest-rate

Note: The Portfolio Investments and Atlas Portfolios are Multi-asset, globally diversified portfolios. Although the portfolios may share similar underlying investments in terms of asset and fund selection, they will differ in terms of the way the funds are managed and the proposition in which they are held. Please refer to the Key Investor Information Document (KIID) for details on the objectives of the individual funds. If you have any questions relating to specific differences of the Portfolio Investments or Atlas Portfolios fund ranges, please contact your Private Banker.

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