LGT Vestra Monthly Market Commentary in association with PIA Wealth Management

September / October 2018

Equity markets marched higher into the end of September, only to reverse quite sharply in October as rising interest rates and trade concerns weighed on markets.

The US Federal Reserve (Fed) raised rates for a third time this year by 0.25%, with another one priced in for December which would take interest rates to 2.5%. Unemployment hit a 49-year low and there are signs that wages will continue to pick up. Fiscal stimulus, combined with an already strong economy, is fuelling economic growth. The Fed is now reducing its balance sheet at a pace of $50bn a month paired with a high deficit. This has weighed on bond markets, but yields have now risen to such an extent that we are starting to see some value in long-dated US Treasuries.

After the announcement of a new NAFTA agreement with Mexico, the US reached a consensus with Canada, replacing the existing one by the US Mexico Canada Agreement (USMCA). Negotiations with China continued, President Trump increased tariffs once more and China retaliated, with no let-up expected anytime soon.

Uncertainty around Brexit negotiations continues in the face of the forthcoming deadline, which has been reflected in declining consumer confidence. Having increased interest rates in August, the Bank of England put monetary policy on hold last month until more clarity is seen. Brexit aside, the UK has maintained its momentum with the labour market still tight, weekly earnings picking up and inflation coming through.

On mainland Europe, the focus has been on the contentious Italian budget negotiations. Italian sovereign bonds have come under pressure as Italy's finance minister proposed a deficit of 2.4% of GDP. EU officials warned that this may constitute a breach of Eurozone spending rules. Thus far, no party appears to be backing down, however concerns surrounding Italian debt sustainability have weighed on Eurozone assets.

A weaker yen against the dollar supported the Japanese equity in the last two weeks of September, but the equity market has since moderated in line with other developed markets. Despite the US withdrawal, Japan is sticking with the Trans-Pacific Partnership and even suggested the UK could join it, endorsing the UK's stance that there are more opportunities outside the EU after Brexit.
Looking to emerging markets, the Indian rupee fell to record lows after its central bank kept interest rates unchanged when a hike was expected. Additionally, they revised the wording to "calibrated tightening" from "neutral" and lowered the inflation outlook from 4.8% to a range of 3.9-4.5% for the second half of 2019. Turkey raised its interest rates by 6.25% to 24% in September and Argentinian rates continued to climb upward to a staggering 72%. Brazilian equities surged after Jair Bolsonaro, the right-wing candidate, won the first round of elections, bucking the trend seen in most other equity markets at the start of October.