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# A Month in the Markets

**SEPTEMBER 2023**

In this latest edition our Multi Asset Solutions Team look at the challenges investment markets faced in August. Shares experienced their biggest drop in eight months[1] and developed nation bonds delivered negative returns[2] in August on worries that interest rates will stay higher for longer.[3]

## Market Overview

A late comeback towards the end of the month wasn't enough to avoid losses, given that the mood soured during the first half of the month. Investors were concerned that a strong US economy[4], UK wage growth[5] and consumer inflation expectations above the European Central Bank's (ECB) target may stall progress in the fight against rising prices.[6]

Rising energy costs and a flagging Chinese economy added to the gloom.[7]

Given that bond prices and yields move in opposite directions, a drop in bond prices pushed 10-year UK government  bonds yields to a 15-year high[9] in August. In the US, 10-year government bond yields[10] climbed to their highest level since 2007[11] before falling back. Yields on bonds of companies based in developed countries also rose despite staging declines in the last week of August.[12]

Gains in stock markets in the last few days marked the end of a rocky August as fears of inflation shocks[13] and interest rate rises weakened slightly.[14]

### Baffled by bonds?

It may be worth taking some time to learn the basics to help you better understand how they work. Visit our Basics on Bonds page for more information.

## UK and Europe

The Bank of England (BoE) raised interest rates to a 15-year high at the beginning of the month and warned businesses and households that rates will remain elevated for at least the next two years. The central bank also forecast that the economy will grow less than 1% over the next three years, although it won't shrink.[15]

A survey of business leaders painted a bleaker picture, showing that Britain's economy might be heading for a recession, defined as two successive quarters of negative growth. Business activity in August shrank by the biggest margin since January 2021, when there was a COVID-19 lockdown.[16]

The FTSE 100, which consists of the largest companies listed on the London Stock Exchange, and the FTSE 250, which comprises mid-sized firms, both recorded their worst month since May.[17]

In Europe, data released at the end of the month showed that Eurozone inflation remained steady in August. Core inflation, which excludes energy and food prices, fell. That prompted some traders to bet that the European Central Bank (ECB) will pause its interest-rate hiking cycle in September rather than increase rates once again.[18]

A survey of business leaders showed Eurozone business output reached its lowest point in August since November 2020, as the region's downturn spread from manufacturing to the services sector, which includes industries such as banking, education and nursing. Hiring reached a standstill as companies stopped expanding due to poor demand and prospects.[19]

## US

Data released on the last day of the month showed that the Federal Reserve's (Fed) favoured way of measuring inflation met economists' estimates. This makes it more likely that the US central bank won't alter interest rates at their next meeting. The same report also revealed that people spent more money in July, indicating that the US economy is growing steadily.[20]

The jobs market is showing signs of slowing, which will also help the fight against inflation. Businesses posted fewer open positions in July, while the number of Americans quitting their jobs for better-paying work fell sharply, according to data released in August.[21]

At an annual meeting in Jackson Hole, Wyoming, from 24-26 August[22], Fed Chair Jerome Powell said, while progress has been made in bringing US inflation down, it is still above where policymakers feel comfortable.[23]

## Asia Pacific

China risks missing its government's annual growth target of 5% as the world's second-largest economy struggles to deal with plunging property prices, weak consumer spending, falling demand for loans, and a shrinking manufacturing sector.[24]

While authorities have accelerated efforts to reverse the slump in China's real estate market, which threatens the nation's financial system and global financial markets, responses have been mixed with regard to their effectiveness.[25]

Chinese shares slid the most since February.[26] In contrast, yields on local bonds dropped[27], driving prices higher. Insurers are buying more Chinese bonds, and household deposits are growing quickly. Uncertainty about China's economy is causing local investors to buy bonds as a safer option than investments like shares.[28]

Japan's benchmark shares index, the Nikkei 225[29], had its biggest monthly decline since December, as concerns about higher interest rates and China affected the export-driven economy.[30]

The index reached a 33-year high earlier this year, in part helped by a push from the Tokyo Stock Exchange to get companies to disclose plans to improve how they handle their capital, boost their valuations, and, as a result, their dividends.[31]

In the third week of August, yields on 10-year Japanese government bonds reached their highest level since January 2014. This increase took place after foreign investors sold their bonds in response to a weaker yen, which would raise the cost of imports. Despite typically controlling bond yields, the government chose not to intervene and prevent yields from rising. Foreign investors also sold shares.[32]

## Outlook

The market is still reacting strongly to changes in inflation expectations and how central banks might respond. As a result, we continue to treat shares with caution and bonds with greater optimism.

Our outlook on bonds remains positive because we believe interest rates are approaching their peak. This is expected to decrease the likelihood of bonds falling in value, given that yields are elevated and less likely to rise further.

We are positive on highly-rated high-yield bonds, which both contributed to the performance of some portfolios in August.

We expect interest rates to remain higher for longer, and holding highly-rated high-yield corporate bonds in the UK, US, and Europe is also less volatile than shares.

We anticipate that global economic growth will be slow and that inflation will continue to decline gradually. Sluggish growth in China should also dampen global demand.

We expect to remain underweight shares relative to the benchmark.

All data as at 31 August 2023.

[1] S&P Global BMI, 31 August 2023
[2] S&P Global Developed Sovereign Bond Index, 31 August 2023
[3] Associated Press, 31 August 2023
[4] Associated Press, 30 August 2023
[5] The Guardian, 15 August 2023
[6] Bloomberg, 8 August 2023
[7] Reuters, 21 August 2023
[8] CNBC, UK 10-year Gilt, 31 August 2023
[9] Bloomberg, 17 August 2023
[10] CNBC, US 10-year Treasury, 31 August 2023
[11] Reuters, 23 August 2023
[12] S&P Global Developed Corporate Bond Index, 31 August 2023
[13] Reuters, 31 August 2023
[14] Reuters, 31 August 2023
[15] The Guardian, 3 August 2023
[16] Reuters, 23 August 2023
[17] Reuters, 31 August 2023
[18] Bloomberg, 31 August 2023
[19] HCOB Flash Eurozone PMI, 23 August 2023
[20] Associated Press, 31 August 2023
[21] Associated Press, 29 August 2023
[22] Federal Reserve Bank of Kansas City
[23] CNBC, 25 August 2023
[24] Reuters, 31 August 2023
[25] Bloomberg, 31 August 2023
[26] S&P China BMI, 31 August 2023
[27] S&P China Bond Index, 31 August 2023
[28] Bloomberg, 24 August 2023
[29] Google Finance, 31 August 2023
[30] Livemint, 18 August 2023
[31] Reuters, 31 August 2023
[32] Reuters, 31 August 2023