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Market Commentary and Positioning

'A positive month for risk assets but the pace and scale of interest rate cuts remain a focus for markets.'

Despite mixed inflation signals in recent monthly data, UK, Europe, and US central banks have all held to a common message in recent weeks that this does not derail the expectation of interest rate cuts over the reminder of this year. In the case of the Bank of England, Governor Bailey confirmed last week that interest rate cuts are "in play" at future meetings amid signs that "global shocks are unwinding, and we are not seeing a lot of sticky persistence [in inflation] coming through". It has been a similar story in Europe and the US, with European Central Bank President Lagarde laying the groundwork for bringing rates down, possibly as soon as June, while in the US, the Federal Reserve (Fed)'s 'dot plot' of member forecasts continues to point towards a median of 3 x 25 basis points rate cuts this year.

Given the supportive policy backdrop, risk-appetite has remained constructive. Global equities are up, with valuations edging higher reflecting in part the lower interest rate outlook that is still in prospect. Helpfully, this is not coming at the expense of economic growth hopes – for example, in the US the latest economic growth forecast from the Fed for this year saw an upgrade last week, while in the UK, the economy returned to growth in January. Across developed markets in aggregate, consumer spending is still being supported by residual pandemic savings alongside tight job markets and above-historic average wage rates. This then is the so-called 'goldilocks' scenario, where interest rates curtail inflation without unduly impacting economic growth.

Within equities we retain the barbell investment-style balance between value and growth. Implemented at the start of 2021, the increased amplitude and rate of inflexion between these investment styles over the past three years, compared to the prior decade in our view validates our approach – there will be a time to challenge our equity investment style barbell balance, but that time is not now in our view. Within fixed-income, we maintain a mix between government and corporate fixed-income, being mindful that we are keen for our fixed-income exposures to provide a counterbalance to the equity risk that we have elsewhere. For our sovereign fixed-income exposures, consistent with our constructive economic-outlook view, as inflation moderates and interest rates fall, we would expect shorter-dated bond yields to fall more than longer-dated bond yields (as we have seen take place in the UK government bond market since our last meeting), with the latter supported by a relatively constructive longer-term economic outlook.

Despite the constructive outlook, we remain cognisant that there are tail-risks to our view, the biggest risk that we see currently is if central banks should have to hike unexpectedly due to sticky inflation – as a case in point, we note that oil prices are currently on track for their third monthly gain in a row, and should these prices move higher (and crucially stay high), whether on the back of continued Organization of the Petroleum Exporting Countries+ (OPEC+) producer supply curbs, or as a flipside consequence of resilient industrial and consumer demand, this could present a challenge for the hoped-for 'pull to 2%' inflation targets that central banks are aiming for. While these risks are not at the current time sufficient to impact our asset allocation settings, we will remain vigilant.

Important information

Investors should be aware that the price of your investments and the income from them can go down as well as up and that neither is guaranteed.

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