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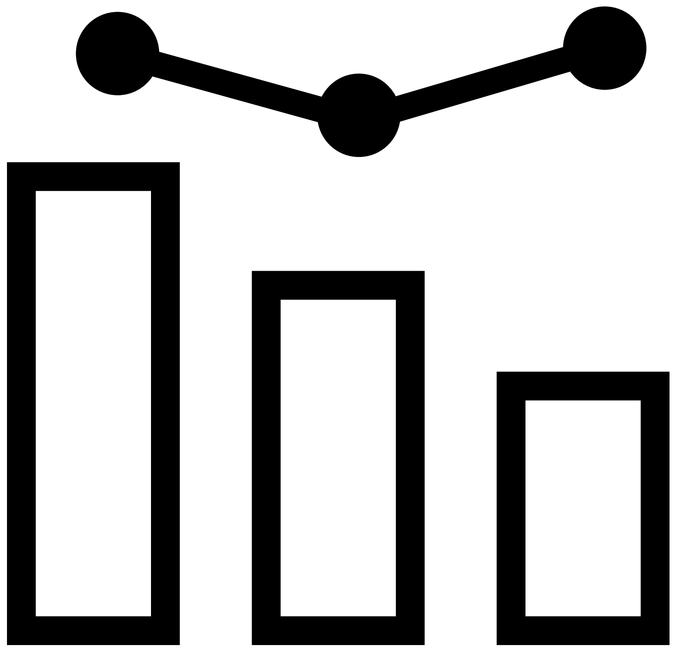


Marketupdate

April 2024

April 2024: Hay fever

The stock markets seem to have their own version of hay fever. Markets were volatile last month, and almost all asset classes had negative returns. In addition to geopolitical turmoil, this was due to disappointing inflation data, which made investors cautious with respect to the timing and scale of upcoming central bank policy rate cuts.

Government bonds fell by 1.4%, partly due to rising interest rates. Investment grade corporate bonds performed slightly better, returning -0.8%, partly because corporate bonds have shorter maturities and are therefore less interest-rate sensitive than government bonds.

Stocks were even worse, especially US stocks, which fell 3% in April. Emerging market equities were by far the best performing asset class last month, rising 1.6% in April (measured in euros). This category has still however underperformed stocks in developed markets over the past 12 months. The underperformance by emerging markets is mainly due to the poor performance of the Chinese stock market, which is still dealing with a struggling real estate sector. US stocks have risen 22% in the past 12 months, while emerging market shares have held steady at 12%.

Despite the April dip, 2024 has so far not been a bad year for stocks. Developed markets stocks are up by almost 8% this year. Listed real estate is doing considerably less well, with a loss of 6%, although it has now become cheaper.

The returns on the various asset classes were as follows:

Return (total return, in euro's)	april	Q2	2024	12 mths
Bloomberg Barclays Eurozone Staatsobligaties	-1,2%	-1,7%	-1,7%	5,3%
Bloomberg Barclays Euro Bedrijfsobligaties	-0,9%	-0,7%	-0,7%	6,6%
Bloomberg Barclays Euro High Yield Bedrijfsobligaties	0,4%	1,1%	1,1%	10,0%
FTSE/EPRA Europe Onroerend Goed	-7,8%	-10,6%	-10,6%	-6,4%
MSCI Europe Aandelen	1,9%	3,5%	3,5%	10,4%
MSCI North America Aandelen	5,0%	8,6%	8,6%	26,5%
MSCI Asia Pacific Aandelen	3,9%	4,1%	4,1%	9,9%
MSCI World Developed Markets Aandelen	4,0%	7,3%	7,3%	20,4%
MSCI Emerging Markets Aande-len	4,6%	1,7%	1,7%	6,5%
EUR/USD	0,1%	-1,8%	-1,8%	2,1%

Source: Bloomberg

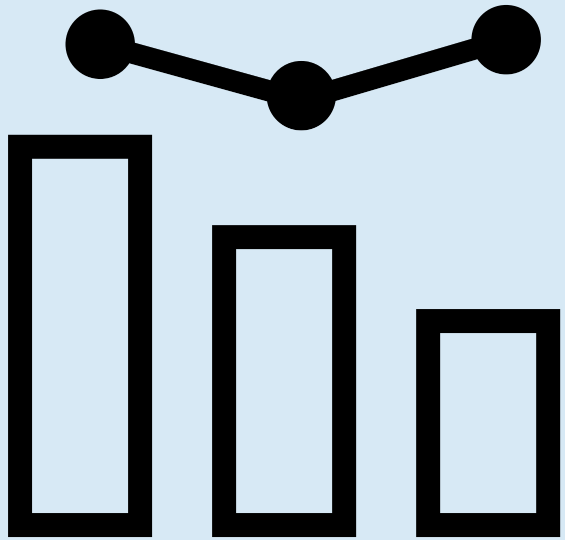
Decent economic growth in the eurozone and China, but disappointing in the US

The eurozone economy grew by 0.4% year-on-year in the first quarter of this year. This was higher than expected (0.2%) by Bloomberg's Consensus Economics. The difference is not great, but what is striking is that expectations were exceeded for several regions. For example, economic growth was higher than expected in Germany, France, Italy and Spain. The German economy grew by 0.2% (quarter-on-quarter) in Q1, partly as industrial production picked up again. Spain actually grew 0.7% in Q1, with this growth also being broadly supported by consumption, investment and trade.

The Chinese economy also grew faster than expected in the past quarter, at a rate of 5.3% year-on-year, aided by government stimulus. So a good start for China to achieve its target of growth of 'around 5%' this year. Unfortunately, the underlying figures are less rosy. Retail sales rose just 3.1% year-on-year in March, while the long-term average for March is 12%. And house prices are still falling. The index of new-build homes in China fell 2.2% year-on-year in March, an acceleration of last month's decline (1.4%). It is thus unlikely that the Chinese economy will grow much more than 5% this year.

The US economy grew less rapidly than expected, at 1.6% (quarter-on-quarter, annualised) in the first quarter of this year. Some of the weaker growth was due to changes in inventories, which does not necessarily indicate weakness in the real economy. What may indicate weakness is that US consumption rose less sharply (2.5%) than in the previous quarter (3.3%). Since the data is seasonally adjusted, the slower growth is not a seasonal effect.

Looking at more recent indicators of economic activity, such as purchasing manager indices (PMIs), it is also worth noting that the US services PMI fell below 50 in April (to 49.4) for the first time since December 2022. This indicates a contraction in the services sector. The US manufacturing PMI also fell below 50 in April (49.2), indicating a contraction in the manufacturing sector.



Will the growth differential between America and the eurozone narrow this year?

One relevant macro theme that will play out in the coming months is whether the economic growth differential between the US and the eurozone will widen or narrow in 2024. As US economic growth has continued to surprise to the upside since 2023 and eurozone growth has continued to surprise to the downside, growth in 2024 is currently forecast at 2.2% for the US and only 0.5% for the eurozone. This is a fairly substantial differential of 1.7%. Expectations for the US economy are therefore relatively high. The opposite applies for the eurozone, where expectations are low.

Meanwhile, recent macro data do seem to indicate some weakness in the US economy. According to recent estimates by the San Francisco Fed, pandemic savings in the US are exhausted. Only $28 billion was left in February 2024 (0.1% of US GDP).

All in all, the US economy seems susceptible to negative (macro-related) surprises and the eurozone seems susceptible to positive surprises, with the risk that the difference in economic growth between the two regions will narrow this year.

Geopolitical risk has increased

A major geopolitical event last month was that Iran fired missiles at Israel, almost all of which were intercepted. For a short period, the financial markets were on edge for a heavy counteroffensive by Israel. This did not materialise, or was at least not that severe, after which the markets recovered fairly quickly.

There is still a chance that similar shocking events will occur more frequently in the months to come. But it appears that their effect on the financial markets will be limited in the long term, according to an analysis by JP Morgan. Such events can however affect oil prices and maritime freight transport in the relatively short term. For example, oil prices increased by 16% between the end of 2023 and April 2024 and the average cost of transporting a standard container increased by 63% in the same period (based on the Drewry World Container Index). With respect to the latter point, it should be said that the effect on inflation does not appear to have been particularly large. According to an IMF analysis, inflation will rise by 0.7% after a year if freight prices double, and in the meantime freight prices are declining again.

Eurozone inflation remains the same

Inflation in the eurozone stood at 2.4% in April, the same as in the previous month. So there was no further decline in inflation last month. But what is known as headline inflation is less interesting than its underlying components. A key component, services inflation, is still high (4%). And interestingly, the energy price component of inflation fell by only 0.6% in April. This declined by 11.5% in November 2023, but the decline became less negative each month thereafter. If this continues, energy could still positively contribute to headline inflation in the eurozone, allowing headline inflation to be higher than markets expect in the short term.

Core inflation in the eurozone fell, from 2.9% in March to 2.7% in April. However, the labour market is still tight. Unemployment is still historically low (6.5% in March) and wage growth is still relatively high. According to the jobs site Indeed, average wage growth in the eurozone was 3.7% in March. Meanwhile, wage growth has been higher than inflation for several months and consumers are finally gaining some purchasing power. The downside is that core inflationary pressures in the eurozone may continue to be elevated.

This applies even more to the US, where unemployment is still at an all-time low, despite a slight increase to 3.9% in April. Wage growth in the US is still quite high, at 4.7% in March according to the median of the Atlanta Fed Wage Growth Tracker. It should be noted that the recent jobs report for non-farm payrolls was significantly weaker (175 thousand jobs added) than the increase of 243 thousand that was expected.

Markets still discounting rate cuts for this year

The financial markets are discounting a total of 3 policy rate cuts by the ECB by the end of this year and 2 policy rate cuts by the Fed (based on prices for overnight index swaps). This is much less than the expectations at the beginning of the year, when the markets were looking for six cuts by the ECB and five by the Fed. The more recent expectations seem to be more realistic. However, there is a feasible scenario in which these expectations are also somewhat optimistic’ especially if core inflation in the US and eurozone remains high for longer, for example because wage growth is declining only marginally.

So far, the stock markets have coped with the change in the discounting of interest rate cuts well. Indeed, the developed equity market index has already risen by almost 8% this year (measured in euros).

The question is whether this will still apply if there are no cuts at all this year. This is not necessarily what we expect, but it is a risk scenario to take into account.

Listed real estate looks relatively cheap, although surrounded by higher risk

Bearing in mind that the upbeat expectations in the financial markets about upcoming rate cuts have now been dampened, and that European listed real estate has continued to decline, this category is starting to look somewhat attractive from a tactical perspective. Stocks have had positive momentum so far, but they are less attractive in terms of valuation (especially US stocks). Furthermore, corporate bonds have performed relatively well compared to government bonds, although they are less attractive from a tactical point of view than listed real estate, for example. Meanwhile, following the further rise in bond yields in April, government bonds appear to be neutrally valued. We are also neutral on cash. There is still a good return available here, but it could become less in the coming months if policy rates are lowered.

The risk scenario here is that policy rates decline less quickly than markets currently expect and/or that geopolitical turmoil flares up further. The expected cuts are, as it were, the antihistamine for the hay fever in the financial markets. The longer it takes for the ‘medicine’ to arrive, the greater the chance that financial markets will continue to sneeze.

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