

REVIEW – EQUITIES & BONDS

Markets were more volatile in the first quarter as US inflation data remained persistently ahead of forecast, although the rate of increase slowed. Markets were positive, but therefore forced to readjust to the prospect of interest rates remaining higher for longer and bonds gave up much of their gains from the fourth quarter last year. Quarterly results from the large US technology companies were strong, none more so than computer processor designer Nvidia, which surprised markets with very strong revenue growth expectations based on companies' investment in Artificial Intelligence (AI) capability. Attacks on shipping by rebel forces in the Middle East led to supply chain interruptions and a sharply rising oil price. The Chinese central bank loosened monetary policy in response to continued weakness in the property sector, while the government embarked on a programme of state sponsored equity buying. Gold rose to all-time highs due to continued geopolitical uncertainty.

Markets became more sanguine in the second quarter. More encouraging inflation data and slowing GDP growth gave rise once again to hopes of interest rate cuts from the US Federal Reserve. Indeed, other central banks including the European Central Bank cut rates. The rate of inflation in major economies continued to fall, including UK inflation eventually falling back to the Bank of England's 2% target. Investor excitement surrounding AI led to continued strength in the US mega-cap technology companies

which led global equity indices higher. Elections were called in the UK and unexpectedly in France, which led to volatility in European bond and equity markets. The six-month period saw further corporate activity in the UK, with bids for International Distribution Services, D S Smith, Spirent and Virgin Money, all underlining perceived value in the UK market.

OUTLOOK

Global equities have enjoyed a strong six months, driven by gains in the world's largest companies. Against this background of such strong gains by a limited range of companies, a number of good quality funds have struggled to beat or keep up with indices over the period. In our view, if a fund has achieved good performance in absolute terms with less exposure to these companies, then they have still made a valuable contribution through diversification. There are also some concerns about over-valuation of these mega-cap US companies. While the price to earnings ratio is only one relatively simplistic metric, these companies are certainly expensive on this basis. These companies are leaders in their markets with unique attributes and it is therefore assumed that they will continue to grow strongly and justify their high valuations. However, they have benefited from strong momentum and it seems premature to declare who the "winners" are so early in an immature cycle. We would certainly not suggest having no exposure to them, but it makes sense in our view to ensure there is also exposure to other companies which have not so far benefitted from the same strong share price gains

Key Indicators

Equity Market Indices (Income Withdrawn, Local Currency)	30/06/2024	31/12/23	% change six months	30/06/23	% change one year
UK – FTSE 100	8164.12	7733.24	+ 5.6	7531.53	+ 8.4
UK – FTSE ALL Share	4451.92	4232.01	+ 5.2	4096.26	+ 8.7
UK – FTSE Mid 250	20286.03	19689.63	+ 3.0	18416.76	+ 10.1
UK FT Small Cap	6727.92	6425.03	+ 4.7	6094.23	+ 10.4
USA – Dow Jones	39118.86	37689.54	+ 3.8	34407.6	+ 13.7
USA – S&P 500	5460.48	4769.83	+ 14.5	4450.38	+ 22.7
USA – Nasdaq	17732.60	15011.35	+ 18.1	13787.92	+ 28.6
Japan – Nikkei 225	39583.08	33464.17	+ 18.3	33189.04	+ 19.3
Europe – FT Europe ex UK	278.11	258.25	+ 7.7	250.47	+ 11.0
Asia – FT Asia Pacific ex Japan (£)	706.57	655.63	+ 7.8	634.43	+ 11.4
Emerging – FT Emerging (£)	652.84	605.94	+ 7.7	586.89	+ 11.2
Global – FT AW World (£)	618.84	557.63	+ 11.0	524.77	+ 17.9
Currencies					
£ / \$	1.2646	1.2732	- 0.7	1.2708	+ 0.2
£ / Euro	1.1813	1.1534	+ 2.4	1.1640	- 0.9
£ / Yen	203.47	179.52	+ 11.8	183.64	- 2.2

Sources: FE Analytics and Refinitiv, returns shown in local currency unless otherwise stated, income withdrawn.

It is important to remember that the value of investments and the income from them can fall as well as rise.

Past performance is not necessarily a guide to future performance. Investors may not get back the amount invested.

despite good operational performances.

The excitement surrounding AI has been considerable and it is already finding its way into our everyday lives. You may have noticed Copilot AI in the latest Microsoft Windows update, and ChatGPT is increasingly used in academia and corporate life (although your author promises this commentary was written with no AI assistance). Apple are set to include AI in the next generation of iPhones to be launched later this year. We are excited by the benefits AI might bring in terms of increased productivity; it is not only the AI technology companies that will benefit, but others who can use it to save costs and improve processes which will feed through to better profitability and outcomes for customers.

As a result, the wider technology sector continues to look interesting; for example, AI systems development is very power-hungry so companies will need to upgrade hardware. Electricity demand will continue to increase, requiring additional power generation and transmission capacity, presenting opportunities for related sectors. Aside from this, we anticipate continued innovation from around the world in areas such as batteries, medical devices, financial services and transport.

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Investors have also remained preoccupied with central bank interest rates. At the beginning of the year markets were expecting as many as six rate cuts by the US Federal Reserve, but it now seems likely that we will see one, or perhaps two, rate cuts toward the end of the year. Inflation data has proved ‘sticky’; inevitably, as high price levels from previous years drop out of calculations this will make year on year falls less dramatic, but also it appears that different parts of economies are experiencing different inflation rates. While manufacturing and retail conditions are more difficult and leading to price cuts, services inflation including for example prices of flights, restaurants and hotels is relatively buoyant. Wages have also continued to grow at a rate inconsistent with inflation falling back to target, although this is a lagging indicator with the labour market attempting to catch up with higher costs. With economic growth remaining robust, the US Federal Reserve has chosen to leave rates unchanged, waiting for more evidence that inflationary pressures are not building again.

This has made for relatively muted conditions for Fixed Income. However, as yields are relatively high, we feel that bonds offer attractive returns with investors ‘paid to wait’ until the point where capital values should start to increase as central bank rates fall. We have already seen a rate cut from the European Central Bank, Canada and others, so it is reasonable to expect that we have seen the top of the rate cycle.

While economic growth in the US and company earnings have remained very supportive, there are some signs, for example consumer spending, some employment indicators, and rising credit card debt and defaults, that suggest the US economy is beginning to slow. While this is to be expected given the restrictive interest rates intended to see off inflation, investors are now watching closely to see whether the US Fed are behind the curve in reducing rates. Other large economies such as China have some unique challenges to deal with, while the manufacturing sectors in European economies are also slowing. It therefore seems appropriate to expect more supportive monetary policies including rate cuts.

Politics is set to remain an interesting theme for the year with half of the world’s population going to the polls in 2024. European governments are looking less stable after the French elections, and with an uneasy coalition leading Germany. After many years of leadership changes, UK politics looks settled for the time being which could, in our view, increase the attractiveness of UK assets which remain at an unwarranted discount. A key event later in the year is the US Presidential election and investors are assessing the increasing likelihood of a second Trump presidency and what this might bring. We envisage a continuation of his more capricious style of international relations which is likely to bring about volatility, and an economic agenda centred around domestic growth that should be good for US shares, but probably exacerbate inflationary pressures.

After a strong performance by equities and with some uncertainty ahead, it seems prudent to expect a period of consolidation while investors look for areas of the market that have performed less strongly. In our view a diversified portfolio of growth-oriented and more defensive holdings offers investors good prospects in the period ahead.

Key Indicators

Equity Market Indices (£ Total Return)	% change six months	% change 2023	% change 2022	% change 2021	% change 2020	% change 2019	% change 2018
UK – FTSE All Share	+ 7.43	+ 7.92	+ 0.34	+ 18.32	– 9.82	+ 19.17	– 9.47
UK – FTSE 100	+ 7.88	+ 7.93	+ 4.70	+ 18.44	– 11.55	+ 17.32	– 8.73
UK – FT Mid 250	+ 4.82	+ 8.03	– 17.39	+ 16.90	– 4.55	+ 28.88	– 13.25
UK – FT Small Cap	+ 6.66	+ 6.73	– 13.56	+ 23.04	+ 7.15	+ 18.82	– 9.52
USA – Dow Jones IA	+ 5.37	+ 8.92	+ 4.22	+ 21.39	+ 5.61	+ 19.63	+ 1.83
USA – S&P 500	+ 16.02	+ 18.58	– 8.25	+ 29.34	+ 14.12	+ 25.65	+ 0.96
USA – Nasdaq	+ 19.57	+ 36.48	– 24.04	+ 23.30	+ 40.44	+ 31.42	+ 1.83
EU – FTSE Europe ex UK	+ 6.42	+ 14.77	– 10.08	+ 16.81	+ 7.11	+ 20.19	– 9.83
Japan – Nikkei 225	+ 4.54	+ 12.42	– 10.59	– 5.15	+ 18.00	+ 15.83	– 4.34
Asia – FT AW Asia Pac ex Japan	+ 9.05	+ 1.97	– 6.21	– 0.34	+ 19.11	+ 14.16	– 8.76
Emerging – FT AW Emerging	+ 9.16	+ 2.51	– 6.84	+ 0.68	+ 11.57	+ 15.48	– 7.96
Global – FT AW World	+ 11.96	+ 15.12	– 7.75	+ 19.49	+ 12.43	+ 21.64	– 3.95

Unit Trust Sectors (Retail, £ Total Return)

Mixed Inv 0%-35% Shares	+ 2.18	+ 5.99	– 10.21	+ 2.95	+ 3.67	+ 8.45	– 3.28
Mixed Inv 20%-60% Shares	+ 3.70	+ 6.55	– 9.52	+ 7.12	+ 2.90	+ 11.64	– 5.15
Mixed Inv 40%-85% Shares	+ 5.97	+ 7.96	– 9.45	+ 10.95	+ 5.49	+ 15.64	– 6.22
Flexible Investment	+ 6.02	+ 7.29	– 9.19	+ 11.48	+ 6.63	+ 14.81	– 6.13
UK All Companies	+ 6.48	+ 7.07	– 9.05	+ 17.09	– 6.15	+ 21.64	– 10.98
UK Equity Income	+ 7.14	+ 6.71	– 2.26	+ 17.80	– 11.25	+ 19.63	– 10.77
UK Smaller Companies	+ 8.75	+ 0.29	– 24.97	+ 23.02	+ 5.76	+ 24.86	– 11.76
Asia Pacific ex Japan	+ 8.53	– 0.15	– 6.59	+ 1.58	+ 19.25	+ 15.28	– 8.75
Europe Excluding UK	+ 5.53	+ 12.69	– 9.36	+ 15.32	+ 10.51	+ 19.93	– 12.62
Global Emerging Markets	+ 6.99	+ 4.25	– 12.16	– 0.26	+ 14.77	+ 16.59	– 11.19
Japan	+ 4.98	+ 9.88	– 7.27	+ 2.28	+ 12.60	+ 16.79	– 11.77
North America	+ 13.05	+ 17.57	– 11.19	+ 25.70	+ 15.75	+ 24.44	– 1.74
Global Equity Income	+ 6.93	+ 9.99	– 2.40	+ 18.36	+ 3.81	+ 19.55	– 6.47
Global	+ 8.89	+ 12.17	– 11.83	+ 16.70	+ 14.70	+ 21.54	– 6.04
Technology & Telecoms	+ 20.26	+ 39.88	– 29.80	+ 16.01	+ 42.38	+ 29.31	+ 2.80
Property	– 3.19	+ 6.39	– 17.74	+ 21.66	– 5.70	+ 18.48	– 3.33
Targeted Absolute Return	+ 3.95	+ 3.89	– 2.43	+ 3.26	+ 2.49	+ 4.56	– 2.91
Sterling Corporate Bond	+ 0.61	+ 9.41	– 16.17	– 2.02	+ 7.33	+ 8.64	– 2.34
Sterling High Yield	+ 3.28	+ 11.15	– 11.16	+ 3.39	+ 4.45	+ 11.08	– 3.82
Sterling Strategic Bond	+ 1.20	+ 7.72	– 12.03	+ 0.20	+ 6.69	+ 8.50	– 2.52
Money Market	+ 2.53	+ 4.56	+ 1.16	– 0.12	+ 0.44	– 0.36	+ 0.36
UK Gilts	– 2.22	+ 3.59	– 24.02	– 5.02	+ 8.24	+ 6.37	+ 0.13
UK Index-Linked Gilts	– 4.18	+ 0.56	– 32.45	+ 3.87	+ 10.49	+ 5.42	– 0.66
Global Bonds	– 0.13	+ 3.82	– 9.08	– 1.47	+ 5.13	+ 5.16	– 0.53
Global Emerging Market Bond	+ 1.12	+ 7.89	– 10.27	– 2.60	+ 3.40	+ 10.55	– 2.70

Sources: FE Analytics, returns in Sterling unless otherwise stated, net income reinvested.

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