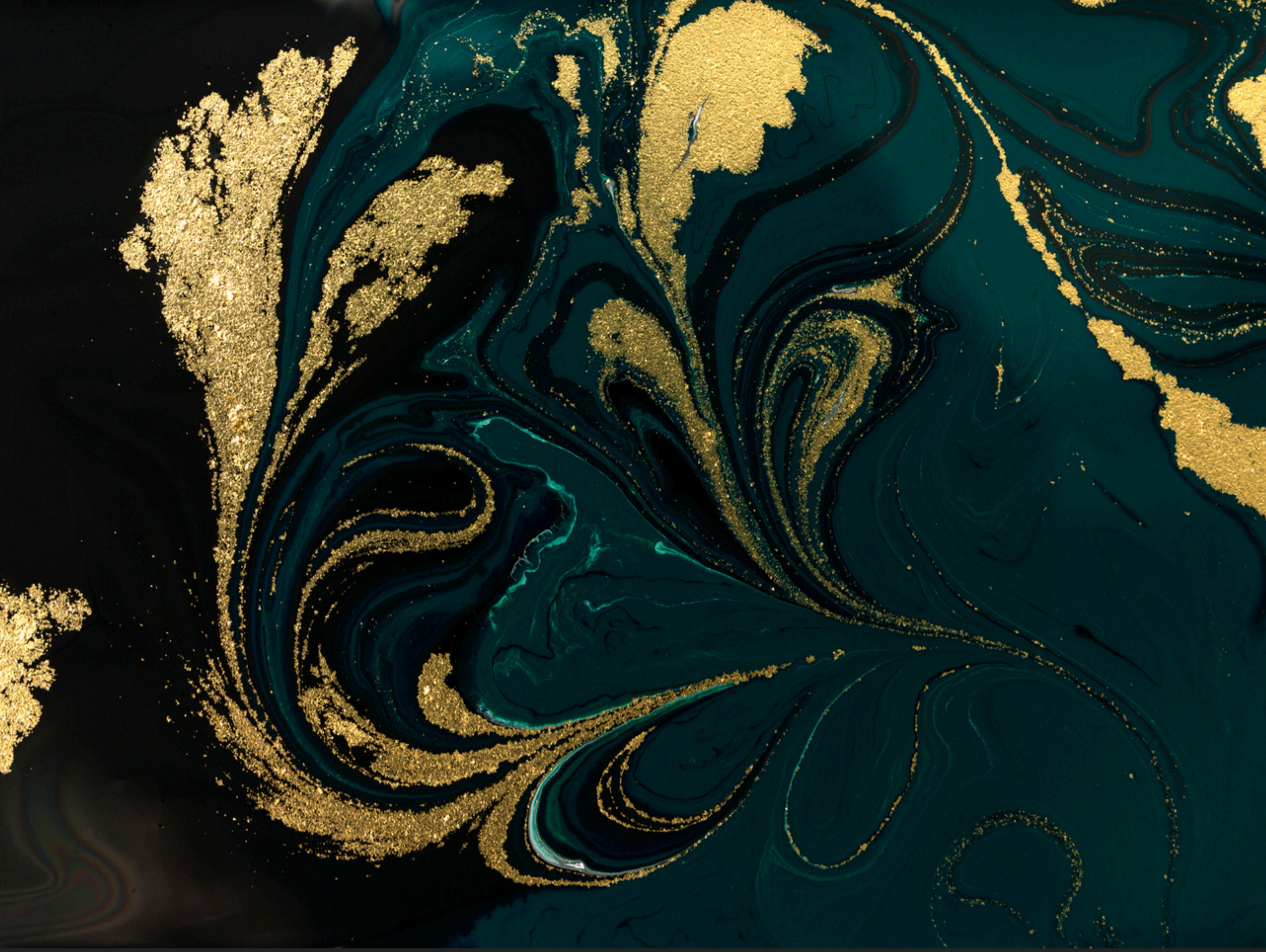

Turns, Shifts and Cuts

Unio Global Macro Committee Outlook

August 2024

Turns, Shifts and Cuts

Sports, politics and geopolitics often bring impressive reversals of fortune – the recent re-energising of the Democratic party by the change in its candidate for the president of the United States is a good example. In markets and economics, we also see such reversals of fortune or 'regime shifts'.

One such tectonic shift is the change in behaviour of central banks from a tightening bias to a loosening one. Some of the key central banks – the Bank of England, Royal Bank of Canada and the Swiss National Bank have cut rates. At last week's Jackson Hole central banking symposium in Wyoming, the Chair of the Federal Reserve Jerome Powell signalled that the Fed was ready to start cutting rates. Bond yields dropped and Powell's remarks set off a sharp drop in the dollar.

It seems that a new 'regime' is in place for interest rates. Our view is that, at least as far as the United States is concerned, the forthcoming Fed meeting will usher in a series of rate cuts, though perhaps not a rate cutting cycle (which would be more aggressive).

In Europe, we also expect the European Central Bank to continue cutting rates, and this has the potential to kickstart lending.

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Often turns in interest rates are also accompanied by shifts in the performance of inter-related asset classes, or investment styles.

One example is the relative performance of small and (very) large companies, which as we have noted in prior months has been at a multi-decade low recently (large caps have been outperforming small caps).

In that light, we devoted the recent Global Macro Council meeting to an analysis of the performance of investment styles at turning points in the economy.

Success factors

Various stocks, categorised by attributes such as earnings, debt levels, and market presence, exhibit different behaviours across different macroeconomic phases.

In the context of these macroeconomic drivers, we believe it is beneficial to sort stocks into different buckets of ‘style’ according to these attributes. For example, 'quality' companies typically have stable revenue streams and established success factors. On the other hand, ‘high-risk’ or 'high beta' companies may have little or no earnings and have risky business models but tend to perform well when investor risk appetite is high.

In the current market environment, characterised by declining interest rates, slowing growth, and geopolitical uncertainties, our sense is that companies that display quality and value factors, particularly in Europe, are likely to perform well.

These companies often have strong balance sheets and generate consistent cash flows, making them attractive to investors seeking stability. Additionally, sectors such as healthcare, consumer staples, and utilities, known for their defensive qualities, are also likely to draw increased interest.

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