Cantor Fitzgerald

Cantor Fitzgerald Strategy & Outlook

MARKET UPDATE

July

Global equities began the third quarter with a gain of 2.8%, bringing the year-to-date gain to +14.9%. July's gains were led by energy (+5.6%), financials (+4.2%) and materials (+4.6%), with defensive sectors such as consumer staples (+1.1%), utilities (+0.9) and healthcare (+0.6%) underperforming, as the market moves into total acceptance of the economic soft-landing scenario, having gone full circle from total belief in impending recession. Indeed, just 12 months into the fastest interest-rate hiking cycle in history, neither western stock markets nor economies are thus far showing the weakness that was expected. Inflation in the US has fallen for 11 straight months and the labour market, and the economy in general, remains strong. The EU and UK haven't been as successful in clamping down on inflation, but the signs are that it has at least peaked.

Monetary policy acting with a lag is an insufficient explanation for the strength of global markets and economies. Macro prudential regulations brought in after the global financial crisis worked in providing economic stability but have made the job of central banks harder. Measures ranging from the capital standards at European banks to the loan-to-value requirements of domestic mortgages holders have resulted in less cyclical exposure to rate rises. In addition, many years of almost zero interest rates has seen the proportion of homeowners on fixed-rate mortgages increase dramatically, limiting or at least further delaying the impact of rate rises on the economy in aggregate. Furthermore, housing in the west has a significant supply / demand imbalance - traditionally the most interest rate sensitive sector, yet despite mortgage rates going from 2pc to 7pc US housing activity is actually picking up again.

Post-Covid savings have cushioned the cost-of-living crisis and kept spending high, and recent data in the EU has indicated that the benefit to savers of rising interest rates has so far been greater than the hit to mortgage holders.

Inflation has fallen significantly from the levels of last year, particularly in the US. But the easy drop in inflation is behind us. Central banks are left with economies with full employment and inflation still at least double their mandate. It becomes more difficult for inflation to continue its downward trend, as it is now being driven by the service sector.

Thus, markets may eventually have to accept the clear and consistent message form central banks – rates will remain at high levels for an extended period of time. When you factor in that equities are as expensive, relative to bonds, as they have been this century – and they've already rallied 20pc to 40pc off their lows – the risk-free yield looks particularly attractive.

This is sowing the seeds for a less positive backdrop into the second half of the year.

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Want to talk to us about investments?

T: +353 1 670 2500 | **e:** CFAMEinfo@cantor.com | **www.cantorfitzgerald.ie** | Cantor Fitzgerald House, 23 St Stephen's Green, Dublin 2.

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MARKET UPDATE

Higher-for-longer interest rates bring back into play the threats surrounding global commercial real estate and banking deposit flight, as well as increasing the chances of a policy error – as central bankers, emboldened by their success thus far, risk over tightening to comprehensively tame inflation.

This could manifest itself as a sudden slowing in global growth as the culmination of high rates hit home, or as another market crisis (akin to the LDI UK pension crisis or the Silicon Valley bank failure) as misunderstood leverage comes to the fore. Other global issues abound. The Bank of Japan is about to embark on its own policy normalisation and China's reopening of their economy has brought their property crisis back onto the radar.

Luckily for investors, they can earn a solid return on cash whilst waiting to find out how conflicting and contrasting forces play out over the next few months, and the positioning of our funds reflects this, being at the lower end of the range for growth assets, defensive assets invested in safe assets with a yield of 3.5%.

WARNING: Past performance is not a reliable guide to future performance.

WARNING: The value of your investment may go down as well as up.

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