Cantor Fitzgerald

Cantor Fitzgerald Strategy & Outlook

MARKET UPDATE

August

Global equities finished the month down just 1.3%, a 4% rally in the final week of the month, along with a 1.4% rally in the US dollar against the euro flattering what was a poor month for asset returns. Except for energy (+2.2%) and healthcare (+0.5%) all sectors were down on the month.

The highlight of the month from a market-worthy news-flow perspective was the speech by Fed chair Jay Powell at the annual Jackson Hole event in Wyoming, where he continued with the narrative that the Fed can be cautious in its approach, but each meeting is live, they might need to hike again, but any idea that they are going to quickly reverse course and start cutting rates isn't even on their radar yet. The speech had dovish and hawkish tones.

On dovish side, he gave no clear commitment to delivering on the dots, arguing that while more hikes could be warranted, the Fed is fully data dependent so it could simply pause. He was balanced about the risk of further tightening vs the risk of doing too little, and highlighted uncertainty about lags meaning there could be significant further drag from the hikes that have already happened.

But these are repeated dovish points. On the hawkish side, apart from repeating the need for softening labour market and below trend growth to bring inflation down in a sustainable way, he talked "uncertainty about the precise level of monetary restraint", which is a reference to the debate about whether the neutral rate has increased, and more importantly, highlighted the risk of re-acceleration, something which is likely front and centre for Fed officials given the resilience of the economic data.

Indeed, the Atlanta Fed GDP Now Model is implying a rapid acceleration towards a 6% annualised pace of growth in the current quarter. But there are some mixed messages on the US economy: the ISM data has been very weak, but the new orders to inventories ratio within that survey is pointing to an acceleration from here, and the Atlanta Fed model suggests the same. However, bank lending data, short term delinquency rates, the large expansion of credit card debt, the cost of that debt, the resumption of student debt repayments, along with a significant drawdown of pandemic era savings suggest the consumer could be facing significant headwinds for the remainder of the year. Elsewhere, economic data in Europe and China continues to be weak.

Ultimately, equities markets look priced for a very rosy scenario, one of soft landings, declining inflation, and double-digit earnings growth, which in turn allows central banks to first pause, then rapidly reduce rates at some point next year. This leaves the US equity risk premium at a 20-year low compared to the highest risk-free alternative in 15 years. Where inflation goes from here looks like a coin toss to us – energy prices, very low unemployment rates, a rise in union power, wage demands and base effects could see it reaccelerate, whereas longer lags in monetary policy transmission, an economic slowdown, potential fiscal tightening, and China weakness could see it continue to fall. It is clear that the easy wins in terms of bringing inflation down are behind us, yet core inflation is still running at 4.7% in the US and 5.5% in the euro area. Small wonder central banks are keen to beat the higher-for-longer drum.

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The above leaves the bar to adding risk quite high. Away from AI and tech, there are other interesting areas of the market such as the high cash yield available on European banks and the high free cash flow yields available on energy companies. In addition, the returns available on cash are attractive, particularly whilst waiting to find out how conflicting and contrasting forces play out over the next few months. 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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