DART CAPITAL

Market Commentary

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Following a negative first half of the year, equity markets have enjoyed a more positive start to the third quarter, bolstered by corporate earnings reports which have remained broadly resilient, and, perhaps most importantly, growing signs that the US Federal Reserve will possibly slow their pace of interest rate hikes in response to the slowing of the US economy.

US

In a much-anticipated move, July's meeting saw the Federal Reserve raise their base rate (known as the Federal Funds rate) by 75 basis points to a range of 2.25%-2.5%. Whilst the size of the interest rate hike was largely expected, there were some newsworthy comments from the Chairman of the Federal Reserve, Jerome Powell, in the press conference following the meeting. In particular, Powell indicated that whilst further rate increases are likely, the Committee are starting to see a slowing of the economy which they believe will be required in order to eventually bring inflation back to their 2% target in due course.

Furthermore, he went onto note that – instead of using forward guidance as they have been recently - the size and number of future interest rate increases over coming months will be now be data dependent. This shift to data dependent decision making indicates that the Federal Reserve may well be inclined to take a more cautious approach to further interest rate hikes, given how weak forward-looking indicators for the US economy have been over recent weeks with particular slowing across the labour market, housing market and business investment. Whilst the above comments certainly do not rule out the Federal Reserve pushing interest rates significantly higher than current levels and we have positioned portfolios to reflect this risk, it may signal the start of a more conducive environment for equity and bond market returns.

Expectations for the largest technology companies were generally lowered prior to their earnings announcements, which helped most of these stocks beat analyst expectations, albeit with profit growth levels which were far below their levels from the pandemic boom. Microsoft continued to enjoy strong growth in its cloud computing division, although growth elsewhere within the business was slower. Apple is seeing slowing smartphone demand, although the growing number of connected devices within the Apple ecosystem helped them deliver strong growth within their services division, which includes iCloud and Apple Music, and profits which were 2% higher than the same quarter last year. Technology stocks as a group rebounded over the month, with the recent addition to Risk Strategy 3 and above portfolios - Polar Capital Technology Trust - gaining 15% in sterling terms. The S&P 500 gained 9.1% in US Dollar terms over the month.

UK

Having raised the base rate by 25 basis points in their last meeting in June, the Bank of England's Monetary Policy Committee (MPC) are expected to announce a larger increase of 50 basis points in their meeting on the 4th August, a decision which would bring the base rate up to 1.75%. In his comments over the month, the Governor of the Bank of England also noted that the MPC will look to reduce the Bank's holdings of Gilts by £50-100bn over the next year once the Quantitative Tightening programme starts in September, and we believe this may place some upward pressure on long-dated Gilt yields. Inflation continued to move higher over the quarter with the most recent reading for CPI standing at 9.4% in the 12 months to the end of June, with the peak expected to be in October when the second hike in the energy price cap is introduced. Data from the labour market has remained relatively strong, although this is expected to weaken somewhat as weaker business confidence feeds into hiring plans. Gilt yields moved down significantly over the month in sympathy with US Treasuries, with the yield on the 10-year Gilt declining 39 basis points to end the month at 1.85%.

The start of corporate earnings season has been generally positive for many of the biggest stocks in the UK market, with heavyweight consumer staples companies, led by Unilever and Reckitt Benkiser, beating analyst expectations on the back of significant price rises of their goods which helped offset rising costs. Elsewhere, banks have generally benefitted from the higher level of interest rates, with the likes of Natwest delivering particularly strong results. Within healthcare, GlaxoSmithKline (GSK) spun out its consumer goods division which produces brands such as Panadol and Sensodyne, with the newly separated business, Haleon, joining the FTSE 100, whilst the remaining part of GSK will focus on pharmaceuticals. MSCI UK All-Cap ended the month up 4.1% in capital return terms.

Eurozone

Whilst figures released over the month showed that Eurozone GDP growth surprised to the upside over the second quarter on the back of a bounce-back in tourism, expectations for growth across the EU continue to be lowered, as higher energy prices and the prospect of stretched energy supply impact consumer and business plans. Given surging inflation across the currency bloc, with CPI increasing to 8.6% year-on-year in June, the European Central Bank (ECB) have brought forward plans to raise interest rates, and in their meeting this month they announced a 50 basis points increase in the base rate, which brought the main refinancing rate up to 0%. MSCI Europe ex-UK ended the month up 6.9% in local currency terms.

China

China narrowly avoided negative year-on-year growth over the second quarter, according to official government data released over the month, although growth did slow markedly on the back of localised lockdowns and weakness in the property market. There are indications that the government will gradually move away from their "Zero COVID" policy later this year given the clear negative impact it is having on the economy, although no official announcement is expected until October's party congress where President Xi is expected to be ratified for his third term. However, in the meantime the government have introduced a number of stimulus measures, including working with property development companies which are experiencing financial difficulties in order to ensure that property developments are completed. Further fines for the largest technology companies dampened investor spirits over the month, with Chinese equities ending the month down slightly. MSCI China H ended the month down 9% in local currency terms.