Allianz Global Investors

03/2024

Market Snapshot

Equity Snapshot

United States

US equities advanced over March, with the S&P 500 Index and Nasdaq Composite Index setting fresh all-time highs as investors looked ahead to lower borrowing costs in 2024. For once, value stocks outperformed growth-oriented companies as the advance broadened out from the technology sector. The S&P Global US composite purchasing managers' index came in at 52.2 in March, only slightly below February's eight-month high of 52.5. While services activity eased to a three-month low of 51.7, manufacturing activity rose to a 21-month high of 52.5. Job growth was also stronger than expected, with 275,000 added in February, although January's data was revised down to a gain of 229,000 from an initial estimate of 353,000. Headline inflation proved stickier than forecast, ticking up slightly to 3.2% in February due to higher-than-expected energy costs.

The Federal Reserve (Fed) kept rates on hold as expected at its March meeting. It also maintained its guidance for three interest rate cuts in 2024 although policymakers see less than one reduction in 2025. Despite the modest uptick in inflation in February, Fed chair Jay Powell signalled that policymakers are "not far" from having the confidence to start cutting rates.

Europe

European equities rose solidly over March, touching fresh highs, boosted by growing optimism that the European Central Bank (ECB) would cut rates in June. At sector level, real estate, energy, materials and financials were among the best performers, with the strong returns of the latter boosting returns in the bank-heavy markets of Spain and Italy. In contrast, information technology and consumer staples were the weakest sectors.

There were early signs of improvement in the euro-zone economy. The HCOB eurozone composite purchasing managers' index (PMI) rose to a nine-month high of 49.9 in March: the services PMI suggested a return to growth with March's reading of 51.1 the highest since June 2023, although activity in the manufacturing sector fell to a three-month low of 45.7. Euro-zone headline inflation eased to an annual rate of 2.6% in February, while core inflation slowed to 3.1%, the lowest level since March 2022. The ECB indicated that it would be June at the earliest before rates were cut and that the extent to which borrowing costs were reduced would be data dependent.

Asia

Equity markets in Asia advanced over March. Sentiment was lifted by signs of a pick-up in growth in China and Europe, as well as the ongoing resilience of the US economy. China equities were relatively stable in March, consolidating the pre- and post-Chinese New Year rally. Both onshore and offshore markets have recovered from previous weakness to deliver relatively flat returns year to date. Elsewhere, stocks surged in Taiwan and South Korea as semiconductor companies benefited from the AI wave. ASEAN markets also advanced, with Singapore gaining the most and the Philippines being broadly flat, lagging the general region.

Bond

Global bonds gained as central banks appeared to be less concerned about the possibility of a resurgence in inflation than many had feared. The largest downward movement in yields was seen in Europe, particularly in the UK after inflation fell more than expected. Elsewhere, the yield on the 10-year German Bund fell 10 bps to 2.3% while the 10-year US Treasury yield declined 5 bps to 4.2%. Japan was the exception with bond yields rising slightly after the Bank of Japan finally ended its below-zero interest rate policy.

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Outlook

The first quarter of 2024 has seen a continuation of strong returns from global equity markets, with many country or regional indices reaching record highs towards the end of the period, before retreating slightly. The end of 2023 saw markets soar as central banks signaled that interest had likely peaked, releasing some of the valuation pressure on higher quality, structurally growing companies, which formed the forefront of the subsequent rally. Since the turn of the year there has been a broader base of positive returns across sectors with lower multiple value stocks also showing momentum, especially towards the end of the quarter.

Market expectations of the first Federal Reserve (Fed) interest rate cut and the speed of descent for 2024 have tempered since the end of 2023 (at one point the consensus estimate was for 7 cuts in 2024). The US economy has remained far stronger than many anticipated with solid growth and Purchasing Managers Indices (PMIs) above 50, (suggesting expansion) in both services and manufacturing. Coupled with resilient jobs growth there is little urgency for action and with inflation stickier than hoped, they can afford to be cautious.

Alongside the robust growth in the US, there are tentative signs that sentiment may be shifting within the Eurozone and the UK, as PMIs climbed to the highest levels since mid- 2023. As revised economic data showed that some economies entered a technical recession at the tail end of last year, positive momentum is very welcome. Inflation data in the Eurozone and the UK has continued to ease, opening the door for potential rate cuts, perhaps even in advance of the Federal Reserve.

The Chinese real estate sector remains an area of concern with developer Evergrande issued with a liquidation order by a Hong Kong judge and fellow developer Country Garden hit with a wind-up petition from a creditor. A number of policies that aim to provide growth stimulus for the economy, primarily through infrastructure projects, were announced at the National People's Congress but it remains to be seen if this is enough to sustain an ambitious 5% growth target.

The geopolitical landscape remains uncertain, with ongoing conflicts in the Ukraine and the Middle East. Attacks in the Red Sea have also caused disruption to shipping, but it seems that the swift action taken has mitigated the impact for the time being. 2024 is also a big year for elections as 40% of the World's population vote for new leaders, including the US and UK. A variety of fiscal stimulus could be used or promised in an attempt to sway voters.

The recent earnings season has been generally healthy with the portfolio companies mainly on the right side of earnings numbers. FY 2023 earnings numbers for the MSCI AC World have been flat but distorted by the extraordinary growth trajectory of the "Magnificent 7" (Apple, Amazon, Alphabet, Meta, Microsoft, Nvidia and Tesla). Estimates for 2024 and where available 2025, show a slightly wider base of positive earnings. We are also hearing a more positive tone in company management meetings, where optimism is high for the second half of 2024 and beyond. Higher, but not yet prohibitive valuations, mean that earnings visibility will be key in the coming months. The recent results from Nvidia, Meta and Amazon and the following positive share price reaction show that there is still capacity to surprise on the upside. Apple however dropped after their earning release, as otherwise positive numbers were overshadowed by declining iPhone sales in China, highlighting the fact that at these heightened valuations, a small misstep can have a disproportionate impact on share prices. We are confident that the structural growth, low debt levels and high earnings visibility of our companies means the portfolio is well positioned but will be mindful of valuations and adjust position sizes where we feel appropriate.