Allianz Global Investors

06/2024

Market Snapshot

Equity Snapshot

United States

US equities rallied, with the S&P 500 Index and Nasdaq Composite Index hitting fresh highs driven by further strong gains from technology stocks. It was another strong month for growth stocks which outperformed value ones by the largest margin in over a year, while large companies also outstripped small-cap stocks.

US economic news was mixed. On one hand, the US economy added 272,000 jobs in May, the most in five months. Additionally, the flash estimate of the S&P Global US composite purchasing managers' index reached 54.6 in June, the highest level in more than two years, helped by accelerating activity in both manufacturing and services. On the other hand, higher interest rates did appear to be weighing on consumer spending. The University of Michigan consumer sentiment index dipped to 68.2 in June, the lowest level since November 2023, and retail sales rose just 0.1% in May.

Headline inflation slowed to a three-month low of 3.3% in May but remained higher than the Federal Reserve's (Fed) target, while the core PCE Index, the Fed's preferred measure of inflation eased to 2.6% in May, marking the lowest level since March 2021. The US central bank kept rates on hold at 5.25%-5.5%. Policymakers signaled that US interest rates would likely remain higher for longer. While the dot plot of Fed projections shows that rates are likely to be cut once towards the end of the year, members of the Federal Open Market Committee appear divided as to whether there is scope for a cut this year at all.

Europe

Euro-zone equities fell modestly over June as sentiment was undermined by an unexpected stagnation in euro-zone economic activity and rising political uncertainty. French president Emmanuel Macron unexpectedly called a snap parliamentary election: a victory for the far-right could threaten the integrity of the EU and lead to a sharp increase in government spending, further increasing France's already large budget deficit. As a result, French stocks declined sharply to a five-month low, underperforming the broader region.

The HCOB euro-zone composite purchasing managers' index (PMI) slumped to 50.8 in June from a one-year high of 52.2 in May. The weaker-than-expected reading was mainly down to a slump in manufacturing activity which contracted at the fastest pace in six months. Headline euro-zone inflation quickened to 2.6% in May, up from 2.4% in the previous two months, although early inflation indicators for France and Spain indicated that inflation may have slowed again in June. As widely expected, the European Central Bank cut rates by 25 basis points in June, its first reduction in five years, but signaled that movements thereafter would be data dependent.

Asia

Equity markets in Asia were mixed over June. Mainland Chinese indices slumped to a four-month low, and Hong Kong shares also weakened as investors appear underwhelmed with official measures to stimulate the economy and restore confidence in the real estate sector. On the other hand, Taiwanese equities were boosted by strong returns from semiconductor stocks, which benefitted from robust demand from generative artificial intelligence (AI). South Korean equities also advanced strongly. Elsewhere, Indian equities also closed the month with notable gains, overcoming a sharp sell-off at the start of the month when Prime Minister Narendra Modi's Bharatiya Janata Party (BJP) unexpectedly failed to achieve outright parliamentary majority. ASEAN markets delivered mixed returns as Indonesia rallied the most, followed by the Philippines and Singapore. In contrast, Malaysian stocks closed the month flat while Thailand equities retreated.

Bond

Global bonds rose in June, boosted by a slowdown in US inflation. 10-year benchmark government bond yields in the US and Germany declined respectively. France was a notable exception, with yields rising slightly amid fears that a victory for the far-right in the country's snap elections may lead to a sharp increase in government spending.

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Outlook

Economic data from the US showed a mixed picture in June. Jobs growth increased by the fastest pace in five months and the Purchasing Mangers' Index (PMI) reached its highest level for two years, with accelerating activity in both services and manufacturing. There are however tentative signs that higher interest rates are having an impact on consumer spending, with retail sales flat for the month and various consumer sentiment indices showing a slowdown. Inflation is easing towards the Federal Reserves' target rate for the first time in two and a half years, but the last mile is often the hardest. The expectation is that the Fed will remain data dependent and will want to see continued improvements before any potential rate cut towards the end of the year. The recent loss of momentum in the US growth numbers strengthens the case for a 'soft landing' of the US economy, a scenario where growth slows and inflation comes down without risking a recession.

Tentative signs of recovery have boosted the outlook for the euro zone economy after a period of stagnating growth. Lower interest rates should provide a further boost: the ECB cut by 25bps in June, with the possibility of further cuts before the year ends. Inflation pressures are also easing in the UK and there is a strong possibility that the Bank of England will follow the ECB in reducing rates at their next meeting. However, we do not expect a sudden downward spiral of rates, with policy makers cutting at different speeds and waiting to see the potential economic impact of their decisions before committing further.

Political uncertainty could also have a bigger impact on markets in the coming months. The announcement of a snap parliamentary election in France came as a big surprise, with voting taking place in early July, weeks before the Paris Olympics. President Macron made the dramatic announcement after a big victory for the right-wing National Rally in France's EU elections. It was also confirmed that the UK would elect a new ruling party on July 4th, earlier than many predicted. November's US elections could mean the re-election of Donald Trump whose policies may have far-reaching consequences, including on tariffs where fault lines within Europe are already evident. The ongoing war in the Ukraine and conflict in the Middle East still have potential to impact the markets, especially commodities if there is an escalation or indeed if a diplomatic solution is found.

As we enter the Q2 reporting season, it will be interesting to see if the recent improvement in earnings growth within the cyclical areas of the market can be maintained. Valuations have also become more extended and there are lofty expectations for some of the higher momentum stocks that are currently driving the market. A slight miss or even results that are merely 'solid' could see disproportion share price reactions. We believe that over time, the stable earnings of the portfolio companies ensure that they will grow faster than the average company. Although this process is not linear and there will be market fluctuations, we believe that we will be rewarded over time. The fundamentals of the companies that the portfolio is invested in generally remain strong and now interest rates expectations have been re-priced by the market, we are hopeful that earnings and profitability will once again be the focus.