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Article MARKET COMMENTARY

Market round-up: 15 - 19 July

Tom Watts recaps the week and looks ahead to next week.

Author

Thomas Watts

Investment Analyst

Duration: 5 Mins Date: 19 Jul 2024

This week just ended

With the hot, balmy weather having finally arrived this week, it seems those Dog Days of Summer could well be here. What is not as clear is why such weather is named after our canine friends, with some theories arguing that the summer coincides with the visibility of the star system Sirius, known colloquially as the "Dog Star", whilst others believe quite simply that the celebrations commemorating Saint Roch, the legendary medieval patron saint of dogs happens around the same time.

Whatever the reason behind the beginning of these Dog Days we've been witnessing, it was US small cap stocks that *took the lead* this week. Enjoying a jump of 1% or more for five consecutive days, the small cap index saw its best weekly returns since April 2020, as investors took heart that a rate cut would be on the way soon, broadening their portfolios in anticipation.

With retail sales figures showing that US consumers continue to spend, seemingly unhindered by higher base rates and against a backdrop of falling inflation, investors bet that the almost year-long *paws* in rate movement from the US Federal Reserve could soon come to an end. Helping matters further was a procession of US Federal Reserve officials, who had really put the cat amongst the pigeons in terms of a rate cut in September.

Fed official, Christopher Waller, said at a press conference on Wednesday that the time for a U.S. central bank interest rate cut "is drawing closer," adding "While I don't believe we have reached our final destination, I do believe we are getting closer to the time when a cut in the policy rate is warranted."

Echoing such sentiments was Waller's colleague and vice chair of the rate-setting Committee at the central bank, John Williams, who commented that "I would like to see more data to gain further confidence inflation is moving sustainably towards our 2% goal. We've got a few good months now."

With both speakers hinting at the chance of a rate cut soon, investors have begun to price in a 93% probability we will see the bank act during its next meeting in September.

In contrast, those hoping for a rate cut in the UK next month could well be barking up the wrong tree after stronger than anticipated inflation data was released. Defying forecasts for a slight fall to 1.9%, a reading of 2% prompted markets to begin pricing in a 35% chance of a rate cut, down from 50% at the beginning of the week. Increases in hotel prices during a month when U.S. pop star, Taylor Swift, toured the UK were partly to blame for the stickiness in Services inflation, which came in at 5.7%, way above Bank of England (BoE) forecasts of 5.1%.

From the dog pound to the pound in your pocket, on the news, sterling hit its highest level for nearly two years against the euro and around one year against the dollar, rising above $1.30.

There was more domestic data released during the middle of the week as the Office for National Statistics made public its Average Earnings Index numbers. Even if you've been working like a dog over the last quarter, wages grew at their slowest pace since 2022, at just 5.7% on an annual basis, down from 6% the previous reading. However, such a fall is not likely to lead the BoE into a rate cut just yet, with the reading being close to double the rate that would be consistent with their 2% inflation target.

In what was a fairly *ruff* end to the week for markets, with the backdrop of a world IT outage causing investors to de-risk their portfolios on Friday, luckily the European Central Bank (ECB) had already communicated their message the day beforehand.

Keeping interest rates unchanged as expected on Thursday but stating September's meeting was "wide open" as it downgraded its view of the euro zone's economic prospects and predicted that inflation would keep on falling.

There were a few hints to support investor bets on another reduction in September, however, including ECB President Christine Lagarde's comment that risks to growth were "tilted to the downside", a change to her previous formulation that they were balanced.

Markets are now pricing in almost two ECB rate cuts for the rest of the year, a view no policymaker has openly challenged when speaking to the press for weeks, making a move in September now fully paws-able...

This coming week

With the weather now showing glimpses of how hot the summer can get, the coming week should show economists If the global economy is doing the same.

After a fairly cold opening to the week, Tuesday should act as a nice warmup with European Consumer Confidence figures showing us the heat on the High Street. The data is so well respected due to its's breadth, with a survey of about 2,300 consumers in Eurozone countries asked to rate the relative level of past and future economic conditions as they see them, including their personal financial situation, employment, inflation and the climate for major purchases.

Wednesday will bring with it a mass of Purchasing Manager's Index readings releases. Covering both the Manufacturing and Services sectors for Germany, France, an overall European composite, the UK and US. The readings will give us an invaluable sense of the global economy at a company level as businesses will be asked to rate the relative level of business conditions including employment, production, new orders, prices, supplier deliveries and inventories.

The second half of the week should be dominated by US data releases, starting with quarterly advance GDP figures, the broadest gauge of economic health. Accompanying the data should be US unemployment claims, acting as a good way to judge the strength of the labour market, a key metric for the US Federal Reserve when judging future rate policy.

However, the metric that the Fed reportedly values the most when examining inflation actually comes the following day. The end of the week should be wrapped up with one of the mostly hotly anticipated data releases is made public on Friday, monthly Core PCE Price Index readings. Predicted to make quite the impact on the markets after its release, the data differs from normal inflation readings in that it only measures goods and services targeted towards and consumed by individuals. CPI readings also only covers out-of-pocket expenditures on goods and services purchased. It excludes other expenditures that are not paid for directly, for example, medical care which is usually paid for by insurance in the US. These are, however, included in the PCE.

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