

Portfolio and Market Review

3rd Quarter 2024

Important Regulatory Information

Past performance is no guarantee of future return. The value of investments and the income from them can go down as well as up. You may get back less than you invest. Transaction costs, taxes and inflation reduce investment returns.

Economic Outlook and Market Commentary

What a year 2024 has been so far. Gold medals are still shining from the Olympic and Paralympic Games this summer, football (almost) came home for England's men's squad and Andy Murray hung up his racket on the professional circuit.

Yet August may have brought the most unexpected event of the year (or even the decade): Noel and Liam Gallagher have agreed to reunite for a worldwide tour. With these historic moments now in the rearview mirror, the world awaits with bated breath to see what the final quarter of 2024 has in store.

Labour's victory: A landslide, but not a smooth ride

Since our last commentary, the UK has witnessed an historic election, with voters decisively choosing Keir Starmer to end the 14-year Conservative leadership.

While this may have been a landslide victory, Starmer hasn't been able to rest on his laurels in his first few months as Prime Minister. The win appears to be less about pro-Labour enthusiasm and more about an anti-Conservative sentiment, with Labour emerging as the natural alternative. Since the election in July, the approval ratings for top Labour politicians have sharply declined, with Starmer dropping 45 points since the last poll on July 19th.¹



Source: Opinium (2024)

With the self-proclaimed “painful” Autumn Budget just around the corner, many are speculating which taxes Chancellor Reeves might target. Labour has pledged not to raise the headline rates of income tax, NICs or VAT (and we all know that what politicians say is scripture). However,

¹ Guardian, 2024.

other taxes appear to be in play. Whilst we must reiterate that any potential changes are purely speculation, a few heavily rumoured possibilities have emerged.

Firstly, Inheritance Tax (IHT) could be in the crosshairs - an easy win for Labour, as only 30,000 households pay this tax each year.² Yet, with increasing house prices across the country and frozen nil rate bands, this is likely to push more families into this bracket with each coming year. Capital Gains Tax (CGT) is another likely target, although the approach remains unclear, as there are several potential ways this could be implemented. Whilst Starmer has ruled out the implementation of CGT on primary residence sales, Labour could attack either the already diminished allowance or simply raise the rates.

Finally, Reeves may look to tax investment wrappers with both pensions and ISAs on the firing line. There's speculation that ISA benefits may be capped at a maximum of £100,000 and that pensions may become subject to IHT upon death. None of these rumours have been confirmed by the party yet, and we'll likely have no clarity until the famous red briefcase makes its way to Parliament. One thing is certain: this budget is set to ruffle some feathers.

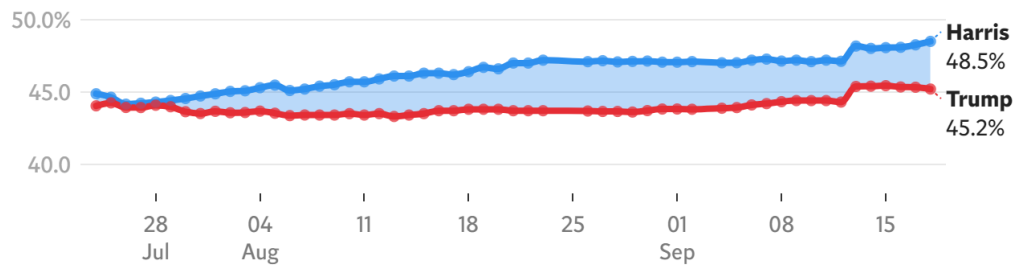
US election: Harris v Trump

With the thunderous presence of the US elections still lingering in the distance, tensions are steadily rising across the Atlantic. Since our last review, the presidential race has packed in more surprises than anticipated, and it's almost certain there are more bombshells to come as November 5th approaches.

To kick off events in July, Biden withdrew from the race with Harris stepping in as the Democrat's nominee for the White House. While this development alone would normally be enough excitement, it was only the beginning of this year's rollercoaster in the world's most-watched political drama.

This summer saw two assassination attempts thwarted against former President Donald Trump during his campaign trail—an alarming, though not unheard-of, reality in US politics. While public assassination attempts are extremely rare, they aren't unprecedented. Bookies in the States, including the well-known platform 'PredictIt', bumped up the odds of a Trump victory after the first failed attempt. However, with Harris now leading the Democratic charge, she's proving to be a formidable opponent, and the latest polls show her pulling ahead of Trump.

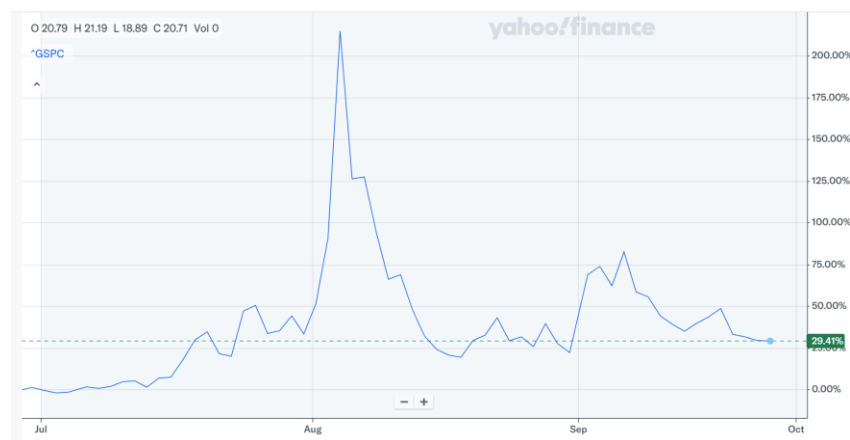
² Morningstar, 2024.



Source: The Independent (2024)

Uncertainty triggers market volatility

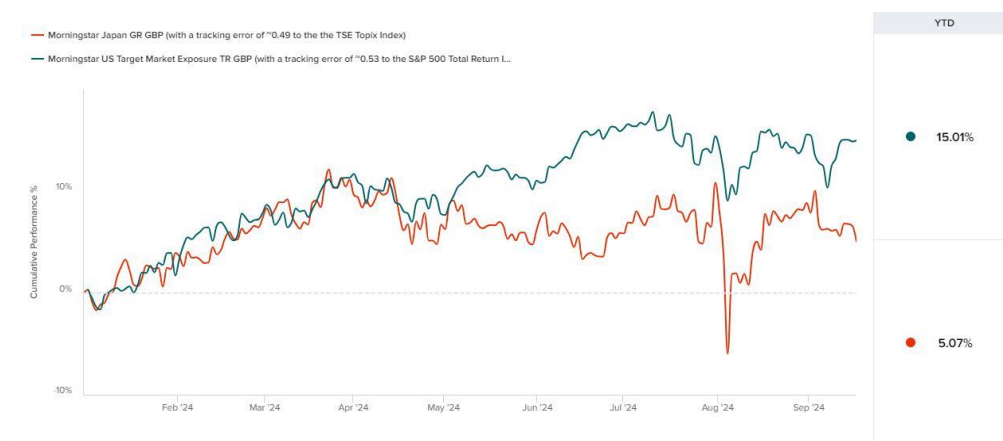
So, what impact has this eventful summer had on the markets? As we moved into early August, the VIX index—often called Wall Street’s ‘Fear Gauge’ and a key measure of market volatility—spiked, sparking global concern.



Source: Yahoo! Finance (2024)

Only partly sparked by the US, in the form of a slightly underwhelming jobs data report, the main catalyst was the Japanese and Asian markets. In July, the Bank of Japan raised its interest rates to the highest level since 2008, prompting monetary policy responses from the government and in turn reducing the value of the yen against the dollar. Without going too deep into specifics, this impacted a large number of financial market participants who had been profiting from ‘carry trades’—a strategy where investors borrow cheap money in one currency (in this case, the yen) to invest in riskier assets elsewhere.

The combination of Japan's rate hike, the weakening yen, and the US jobs report created a 'perfect storm' that sent international markets tumbling. However, fears of a US recession were short-lived, with markets quickly recovering and hitting an all-time high on 18th September in the US.



Source: Timeline (2024)

Whilst it may be a case of preaching to the converted, the excitement of this quarter only strengthens the old adage: it's time in the market, not timing the market, that's the key to successful investing. It also serves as a reminder that the year is far from over, and there may still be more surprises in store before 2025 begins.

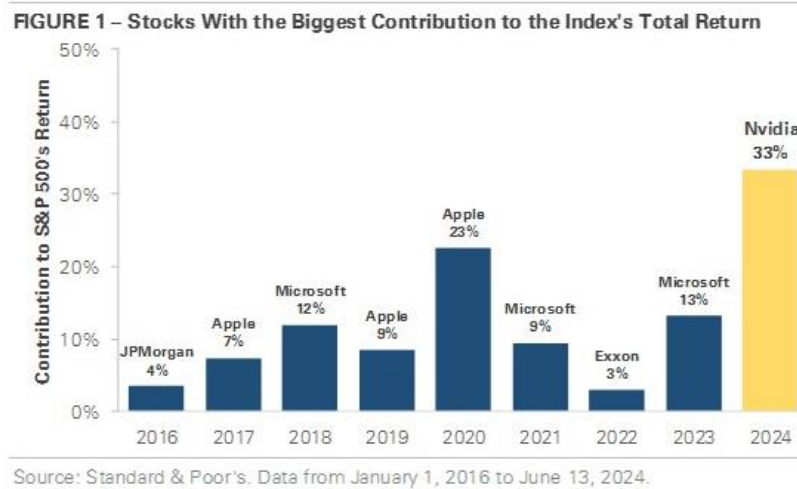
Artificial intelligence: Is the bubble going to burst?

A day hardly seems to go by without AI making headlines or being discussed in boardrooms. Whether it's ChatGPT helping write an email or a real 'wearable' companion to help tackle loneliness, AI has truly become part of modern life.

While some of this may seem like an episode of 'Black Mirror', it's clear AI is here to stay. With the hype surrounding the sector reaching a fever pitch, it evokes eerie flashbacks to the 'dot-com' bubble of 2000. This begs the question: is the excitement around AI warranted, or should investors take a step back and assess whether this could be a bubble waiting to burst?

Over the past few years, technology has driven the performance of the S&P 500, with the "Magnificent 7" leading the charge. None more so than Nvidia, the company that manufactures

the computer chips used to power AI. As of June 2024, Nvidia is the largest contributor to the S&P 500's return, accounting for 33%.



Source: Barker Boyer, Standard & Poor's data (2024)

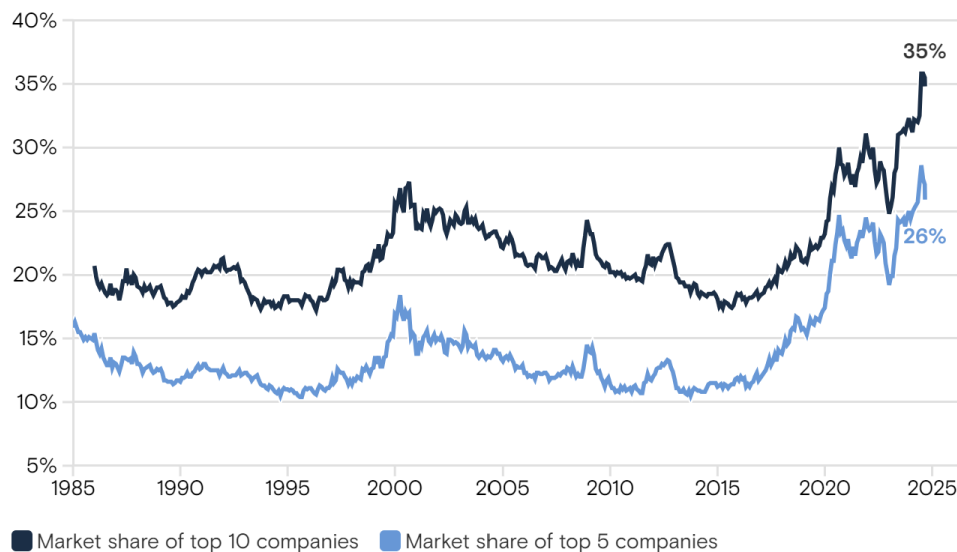
In early September the stock's share price tumbled by 9.5% when the company's quarterly forecast failed to meet the lofty expectations of investors. This left investors questioning whether the current AI boom is similar to the dot-com bubble. At present, there are arguments both for and against this being a 'bubble' and the reality is, no one can say either way with certainty. Only time will tell what the future holds for investors and the markets regarding AI.

As you might expect, AI is incredibly capital-intensive in the early phases and requires far more start-up capital than other sectors to become a viable business. In the low-interest rate environment of recent years, this has been a fantastic backdrop to support the early stages of many AI companies.

In 2022, there were 60,000 patents approved for AI-related products, an increase from roughly 8,000 just four years earlier³. This influx of early capital funding has helped many companies achieve profitability earlier in their lifespan due to the accessibility of cheap debt. This situation contrasts significantly with the 2000 dot-com bubble, when many companies had yet to prove their viability. While we are not in the same low-interest rate environment of the Covid era, rates are still historically low, and companies that capitalised on these conditions have reaped the rewards in the form of early profitability.

³ Goldman Sachs, 2024.

AI is booming, as seen by the staggering number of patents being filed. However, there is a dark cloud overhead in the form of high concentration among the largest players in the AI field. This concentration risk is a real concern for investors, with the top 10% of companies in the sector controlling roughly 35% of the market share.



Source: Datastream, Compustat, Goldman Sachs Research (2024)

These few companies face not only sector risks but also company-specific risks, particularly when considering Nvidia and its recent volatility. As investors have heard numerous times before, the important lesson of this story is indeed diversification.

Some of the top players in the sector, including household names like Google, Amazon and Meta are perfect examples of why this concern may be mitigated in some ways. Unlike during the dot-com bubble, where companies relied on a single revenue stream, these are established and largely profitable companies. The majority of their revenue comes from avenues such as cloud computing and ad generation rather than solely AI. The diversification within these companies should reassure investors that should AI suddenly turn out to be a bubble, their other revenue streams might help mitigate the significant losses experienced in 2000.

Readers should be warned, that we may see a familiar narrative play out in the markets over the next few years. Often, there is not an industry-wide collapse when the proverbial penny finally drops; rather, there can be sharp declines in an industry as valuations finally catch up with realistic prices and returns. Nvidia's recent share volatility was not due to a lack of profits, but rather to unrealistic expectations set by markets. As a result, the drop was moderate, and the company continues to be one of the largest drivers of return in the markets. During such times, it is important to take a step back from the short-term noise and consider the bigger picture.

As AI becomes more widely adopted across sectors, there will be a widespread positive impact on company valuations. Therefore, even if investors are not directly invested in the AI sector, they will still benefit indirectly from these pivotal advancements within their portfolios.

At a recent conference at Goldman Sachs, an analyst admitted that their equity analysis team had been using AI for ten years to assess the vocal inclinations of board members delivering

information, helping to ascertain how truthful they may be. The gradual widespread adoption of this advanced technology has not happened overnight, although it may seem that way due to media coverage.

Diversifying away from solely AI stocks will still provide investors with gains and exposure to AI, as all sectors continue to adopt advancements that help strengthen balance sheets by addressing cost inefficiencies. Given the uncertainty surrounding the sector, it may be wise to adhere to the old adage of not putting all your eggs in one basket; diversification across all sectors is likely to be key to navigating the AI wave.

Asset Class Returns Q3 2024

In Q3 2024, global financial markets saw mixed performance across asset classes, shaped by central bank policies, inflation concerns, and geopolitical tensions. While equities experienced heightened volatility, fixed income gained traction due to interest rate cuts. Despite concerns about inflation and geopolitical issues, stocks have shown resilience.

Asset Class Returns



Source: Timeline (2024)⁴

⁴ Proxies. Asia ex-Japanese Equities: Asia ex-Japanese Equities: Morningstar Asia Pacific ex-Japan Large-Mid Cap GR GBP; Developed Market Equities: Developed Market Equities: Morningstar Developed Markets Target Market Exposure GR GBP; Emerging Market Equities: Emerging Market Equities: Morningstar Emerging Markets Target Market Exposure GR GBP; Europe ex-UK Equities: Europe ex-UK Equities: Vanguard Emerging Markets Stock Index Acc GBP in GB; Global Bonds: Global Bonds: Vanguard Global Bond Index Hedged Acc GBP in GB; Global Corporate Bonds (hedged £): Vanguard Global Bond Index Hedged Acc GBP in GB; Global Equities: Global Equities: Morningstar Global Markets GR GBP; Global Growth Equities: Global Growth Equities: Morningstar Global Growth Target Market Exposure GR GBP; Global Property: Global Property: Morningstar Global Real Estate GR GBP; Global Value Equities: Global Value Equities: Morningstar Global Value Target Market Exposure GR GBP; Japanese Bonds: Japanese Bonds: Morningstar Japan Treasury Bond TR GBP Hedged; Japanese Equities: Japanese Equities: Morningstar Japan GR GBP; Overseas Government Bonds: Overseas Government Bonds: iShares Overseas Government Bond Index (UK) D Acc in GB; UK Equities: UK Equities: Morningstar UK GR GBP; UK Government Bonds: Vanguard UK Government Bond Index Acc GBP in GB; US Equities: US Equities: Morningstar US Target Market Exposure TR GBP. Performance periods: 3rd Quarter: 30/06/2024 -- 30/09/2024, Year: 30/09/2023 - 30/09/2024; 3 Year: 30/09/2021 - 30/09/2024, 5 Year: 30/09/2019 - 30/09/2024; Year to Date: 31/12/2023 - 30/09/2024.

Global equity

We're living in what feels like the "Equity Era". In the third quarter of 2024, global equity markets experienced heightened volatility, but unlike Q2, this volatility was largely driven by macroeconomic uncertainties.

Nvidia, the global superstar of 2023, briefly became the largest company on earth, propelling U.S. equity markets with its innovation-driven rise. Despite a narrow group of tech stocks dominating the market last year, the first half of 2024 saw broader participation, particularly from Asia. Yet, as big tech firms see their influence wane, hidden gems in pharmaceuticals, housing, and "quality at a reasonable price" stocks are emerging, offering fresh opportunities for cautious optimism. The future remains uncertain, but for now, the equity show must go on.

In Europe, performance fluctuated. The market witnessed instability early in the quarter, largely due to mixed inflation data and concerns about future interest rate cuts. However, by September, optimism around the European Central Bank's rate reductions pushed indices like the FTSE 100 and MSCI Europe higher. Valuations remained elevated in developed markets, with investors questioning how sustainable growth is, especially in sectors like technology.

In emerging markets, Chinese stocks remained under pressure, facing headwinds from both domestic and geopolitical issues. Indian equities, on the other hand, continued to show resilience, with the NIFTY 50 outperforming other emerging markets.

Fixed income

The fixed income market experienced notable shifts in the third quarter as central banks began implementing significant rate cuts across the board. At the beginning of August, the Bank of England made its first rate cut since March 2020, reducing the benchmark rate from 5.25% to 5%. This move was a welcome sign indicating that inflation is more manageable than this time last year.

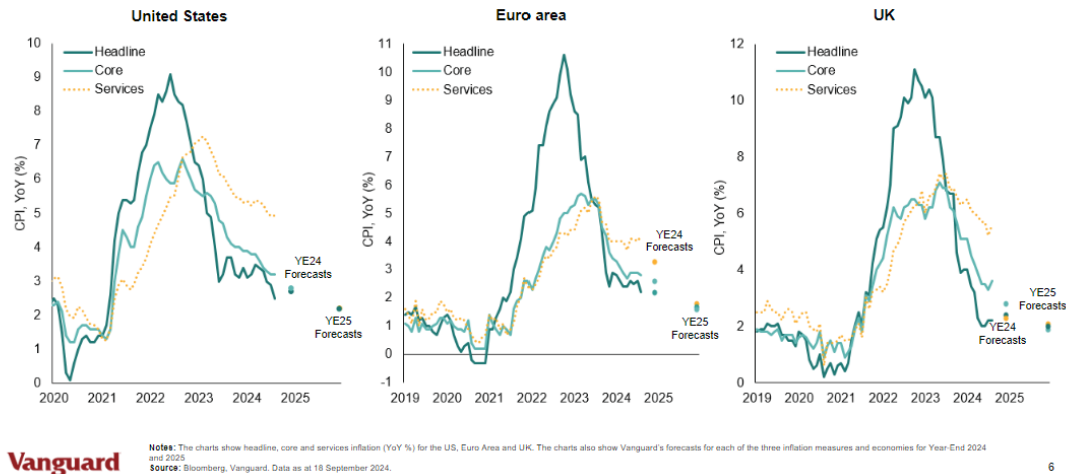
Inflation sat at around 2.2% in late August⁵, and the BoE projects this will rise to 2.75% by the end of the year before returning to its 2% target in 2025. The chart below highlights the trajectory of inflation across various regions over the past few years, as well as predictions for where inflation may fall in 2025.

The rate cut provided a boost to UK government bonds, contributing to a rally in the fixed income market, particularly in longer-dated bonds.

⁵ Office for National Statistics, 2024.

Inflation trending towards 2% by mid-2025

Headline / core / services CPI across the US and Europe and the UK



Source: Vanguard (2024)

In a major move, the US Federal Reserve slashed its benchmark interest rate by a full half percentage point, bringing it down to a range of 4.75% to 5%. This marks the Fed's first cut since the pandemic era and signals the start of a new easing cycle, as the central bank aims to get ahead of any potential weakening in the U.S. economy and labour market. The last time the Fed implemented a rate cut of this magnitude was during the onset of the COVID-19 crisis in 2020. Much like in the UK, predictions suggest that the US will hit the 2% inflation mark by the end of 2025.

Despite indications that global interest rates may have peaked, bonds are still struggling to capture investors' enthusiasm. However, with the Fed's decisive rate cut and more reductions on the horizon, fixed income might finally be gearing up for its comeback. After a strong period of outperforming shorter-duration bonds, these cuts enhance the performance potential for mid- to long-maturity bonds as well.

United Kingdom

In the UK, the stage has been set for a dramatic political and economic shift. A landslide Labour victory in July, ending 14 years of Tory leadership, has renewed optimism in UK markets.

Domestically focused mid- and small-caps, long underperformers, could be in for a revival as investors warm up to the newfound political stability.

With Labour's promises of closer ties to the EU and a pro-business stance, there's cautious optimism surrounding the UK's FTSE 250 and smaller companies. However, given Labour's

historical tendency to raise corporate taxes and introduce regulations that could stifle entrepreneurship, the outlook remains uncertain. While some investors may be eyeing a return to the British equity stage, the impact of policy changes on business growth could temper expectations.

In Q3 2024, UK equities maintained steady performance, with both the FTSE 100 and FTSE All-Share Index rising modestly. Despite ongoing global volatility, these indices gained approximately 2.5% during the quarter, driven by resilient corporate earnings and easing inflationary pressures. However, the Bank of England's cautious stance on interest rates still weighed on sentiment. While improving macroeconomic conditions have helped buoy markets, including gradually declining inflation, investor confidence remains fragile, reflected by continued outflows from UK equity funds.

Final Thoughts

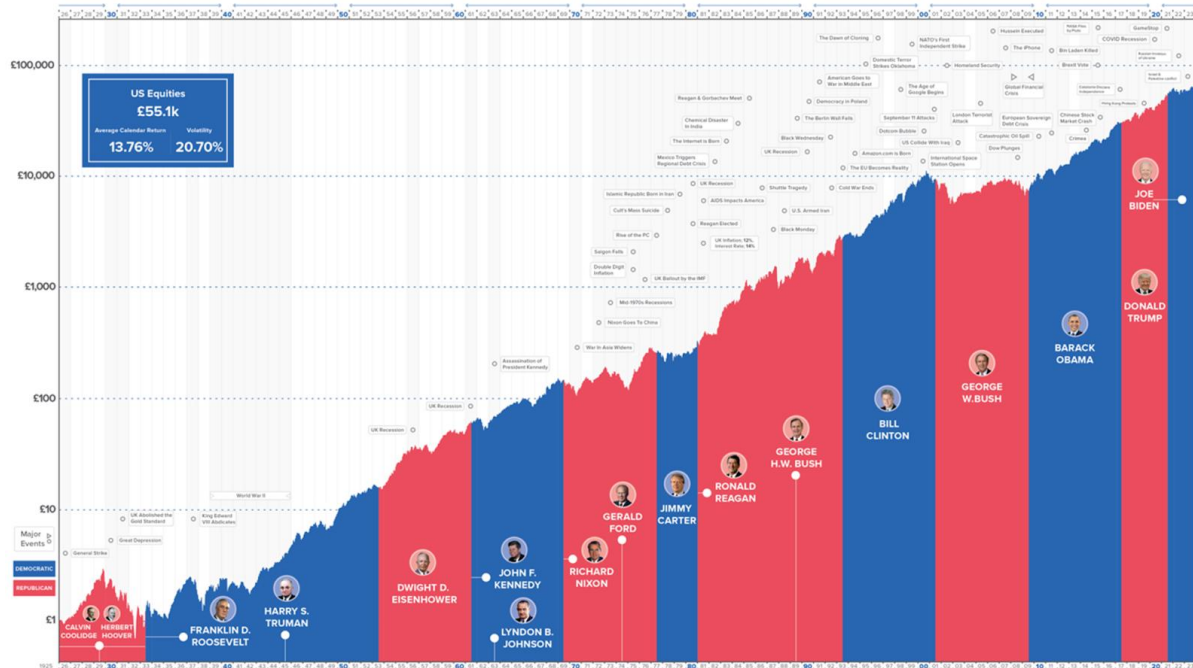
As 2024 approaches its conclusion, it has been quite a year so far. With interest rate cuts happening across the board, fixed income finally looks set to gain some breathing room over the coming months. While this has been a promising start, we hope to see positive returns in this asset class continue into next year.

Although it may be premature to say, inflation appears to be much more under control than at this time last year, helping to ease some of the burden on household incomes.

Despite these positive developments in the market, volatility plagued global markets this quarter, creating general unrest about potential recessions and equity downturns. However, tensions seem to have settled for now, and markets have ended the quarter relatively flat—somewhat of a relief compared to expectations in August. With the US election still on the horizon, investors shouldn't sit on their laurels just yet, as volatility often accompanies the excitement of polling day.

While still underperforming, emerging markets are likely to benefit from the recent Fed interest rate cut. The availability of cheaper debt to finance companies should hopefully reflect in more positive valuations over the next year or so.

With a year full of elections—including the fallout from the new Labour government and the continued excitement of the US presidential race—there is likely to be some short-term volatility for the remainder of this year. However, a familiar reminder for readers is that the markets are indifferent to political outcomes, so it's important to keep focusing on the longer term.



Source: Timeline (2024)

Advisers understand the importance of viewing investments over the longer term, so we won't preach too much to the proverbial choir. Our portfolios take a long-term view, disregarding the short-term noise that can disrupt markets. With three months still remaining this year, there's plenty more to come before 2025 arrives.

How can we help?

By using Belmayne, investors can trust that their hard-earned money is being invested in strategies designed to maintain resilience under all market conditions. This gives you the best chance of achieving your long-term investment objectives.

Contact us:

If you would like to discuss the contents of this report in more detail, please don't hesitate to contact the Belmayne team on (01246) 298181 or email enquiries@belmayne-ifa.com