Private Client Partners
Family Office Services
Banque Bonhôte & Cie AG

Market review
August 2024

A shot across the bow

Looking back at August, one might conclude that it was a perfectly normal, positive month for investors. Yet the month started with significant dislocations, without a black swan being sighted. In addition to somewhat weaker US economic data, the Japanese central bank raised its key interest rate by 0.15%. This was enough to create panic in a nervous market environment.

The yen rallied, triggering margin calls on the carry trades of various speculators. In a carry trade, investors borrow money in Japan at low interest rates and then invest it in higher-yielding assets around the world and sometimes in other currencies. Due to the now rising yen and margin calls, speculators immediately closed out their positions and dumped their stocks and bonds on the market. What happened next will likely be seen more often in the future when there are massive market movements. As with a snowball effect, momentum strategies, fast and partly AI-supported electronic trading and passive ETFs created effects that, for example, caused the Japanese stock market to crash by over 19% in a short period of time.

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The same market participants then caused the Japanese market to rise again by 11.5%. Similar price movements could be observed worldwide. The fundamental picture has not changed significantly. Investors' nervousness was reflected in the volatility. Within a very short period of time, the volatility index rose to its third-highest level ever measured.

By the end of August, however, the markets had largely normalised again and returned to the old index levels. New data from the US economy contributed to this, suggesting that no immediate downturn in the US economy is to be expected. However, what remained of the interim market correction were the higher expectations of the central banks with regard to interest rate cuts.

In his speech in Jackson Hole, Fed President Jerome Powell emphasised that he is aware of the cooling of the labour market, but wants to avoid a too sharp a slowdown. It is therefore clear to everyone that there will be a rate cut of at least 0.25% at the Fed's September meeting. We see support for this in the general enthusiasm over the decline in US inflation to 2.9% and therefore the expectation of a new era of rate cuts until 2026.

We see a general enthusiasm over the decline in US inflation.

What is being ignored is the risk of a renewed flare-up of inflation next year, because both the left-wing economic populism of Harris and the nationalist anti-economics of Trump will be equally fiscally expansionary. Although fiscal-monetary tensions in the US are at an all-time high, the fiscal consolidation that is urgently needed to finally regain control over inflation will hardly take place. The future US administration would actually have to take decisive action to tackle the budget deficit, the culprit behind the persistent inflation above the target range of 2%. No matter who wins the elections in November, this is not on the cards, even with the best will in the world.

Similarly, interest rate cuts are expected in Europe, as inflation is finally low enough. The weak economic performance, especially in Germany and France, is also fuelling expectations of further interest rate cuts to avert a possible recession in Europe.

The change in sentiment on the markets towards the end of the month was primarily due to the perception of the data compared with the beginning of August. It was less the data itself, which, although mixed, is not as negative as it has been interpreted in some quarters.

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Stock Markets

After the sharp price falls and the associated extreme volatility had calmed down, stock markets recovered across the board. Despite interim double-digit percentage losses, almost all markets closed higher than at the end of July. The exception is Japan, where the price falls were most extreme.

In terms of sectors, it is striking that utilities and pharmaceutical stocks performed particularly well. Consumer staples stocks also posted good gains, which is hardly surprising given that the US consumer remains very willing to spend.

Interest rates

Interest rates changed only slightly in August, as much of the anticipation surrounding interest rate cuts has already been priced in since July. Yields on US bonds came under some pressure as there was increased speculation that there could be a 0.50 % interest rate cut.

We do not share this view, as this could mean that the US economy is in a worse state than generally assumed. Current figures suggest an orderly slowdown in the US economy. And the much-cited recession is still not on the horizon.

Currencies and commodities

The USD is showing weakness due to the expected interest rate cuts and lost over 3% against the CHF and over 2% against the EUR. The strength of the CHF also results from the fact that the ‘safe haven’ was suddenly en-vouge again.

Gold continues to benefit from strong investor interest and is still rising. Crude oil lost over 4% in August, but has since recovered from the lows. Industrial metals and other commodities improved somewhat compared to last month and prices rose. Bitcoin lost almost 9% due to heavy selling.

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