6-Month Market Review

(as at June 30, 2023)

Investor Focus on AI Fuels Stock Rally

Latest Developments

Investors ignored the scenario of further interest rate hikes, and the growing likelihood of the US economy entering a recession.

Instead, they focused on the potential future benefits from the roll-out of artificial intelligence (AI) systems. The subsequent gains in the mega-cap tech stocks – Apple, Microsoft, Amazon, Nvidia, Alphabet (Google), Meta and Tesla – drove stock markets higher.

These seven stocks, also known as the Magnificent Seven, account for over 50 percent of the Nasdaq's capitalisation and their gains caused it to surge by 32.3% over the last six months.

The Japanese equity market saw similar gains, although for different reasons, with the Nikkei 225 Index up 28.7% since the start of the year.

This is a reaction to the Tokyo Stock Exchange introducing a programme of extensive corporate reform, with the aim of persuading Japanese companies to use their capital more efficiently to prioritise shareholder interests in efforts to boost stock prices.

The MSCI World Index gained 13.9% since the start of the year, and the S&P 500 Index and the Bloomberg European 500 Index rose by 16.9 and 10.8% respectively.

Revised data for US GDP showed that the economy grew at an (annualised) rate of 2% in the first three months of the year, well above the 1.3% rate previously reported.

In June, US price inflation data showed further signs of softening, with the consumer price index rising 0.2% compared to the previous month. Notably, the core rate, which excludes volatile items like food and energy, experienced a slowdown to 4.8%, marking the lowest level since March 2021.

Germany's inflation data showed that the rate of price growth in the eurozone's largest economy rose to 6.8% in June.

In June, the UK's inflation data has indicated a continued slowdown, reaching 7.9% at the time of this report. Of particular concern to the Bank of England (BoE) is the country's core inflation, which has been consistently 2 percentage points higher than that of the eurozone or the US. To address this issue, the BoE has taken investors by surprise by raising interest rates by half a percentage point.

What this Means

The market's interpretation of the inflation data is that the US Federal Reserve (the Fed) is close to being done with rate hikes, and the European Central Bank (the ECB) may soon be finished if core inflation begins trending lower.

Fed chair Powell may not see it quite the same way however, and recently commented that *"Although policy is restrictive, it may not be restrictive enough and it has not been restrictive for long enough"*.

ECB President Christine Lagarde suggested that an ECB rate increase next month was a virtual certainty, though she was less committal on what policymakers would do at their subsequent meeting in September.

The strain of monetary tightening so far is causing the eurozone economy to slow down. Lending growth has collapsed, and headline and core inflation are on course to decline rapidly in coming months.