Monthly Review and Outlook

September 2022

Review

Global equities were broadly lower in September and bond prices fell sharply as inflation remained high.

US shares declined sharply, with all industry sectors lower. The US Federal Reserve (Fed) raised the federal funds rate by 0.75 percentage points to 3.25 per cent.

Emerging markets equities fell, due to expectations of further US rate rises and of declining global economic growth.

Company shares

UK equities (shares) fell in September. Some areas of the market, which contain businesses that can typically maintain good profitability in challenging economic climates, performed less weakly. These include companies selling essential consumer goods. Overall, UK companies involved in energy and raw materials benefited from the weakness of the pound against the US dollar. Small and medium-sized UK companies generally performed more weakly than large UK companies. US equities declined sharply in the month, with all industry sectors of the stock market falling. The Fed made its third consecutive 0.75 percentage point increase, which pushed borrowing costs to highs last seen in 2008. This followed the Fed's preferred measure of annual inflation (Core PCE inflation) rising again, in August, from 4.7 per cent to 4.9 per cent. Shares in technology and real estate companies had some of the most significant falls while healthcare companies generally held up relatively well. Eurozone shares were also weak, with declines in all sectors. Communication services and real estate were among the weakest eurozone sectors. The European Central Bank raised interest rates by 0.75 percentage points in the month. This helped companies in the financials sector, which can benefit from higher interest rates. Asian equities (excluding Japan) fell due to investor concerns over rising inflation and fears of a global slowdown. The sharpest declines were seen in South Korea, the Philippines and Taiwan. Emerging markets equities fell sharply, due to rising US rates, US dollar strength and declining global economic growth expectations. Growth-sensitive north Asian markets were hard hit, with South Korea performing particularly poorly.

Bonds

Bond prices continued to fall, meaning that bond yields rose. The yield on US government bonds with a ten-year expiry date rose from 3.19 per cent to 3.83 per cent, while the yield on US government bonds with a two-year expiry date rose from 3.48 per cent to 4.23 per cent. The German ten-year government bond yield increased from 1.54 per cent to 2.11 per cent, with Italy's up from 3.89 per cent to 4.51 per cent, after a high of 4.74 per cent in late September. The UK ten-year yield increased from 2.80 per cent to 4.15 per cent and the two-year rose from 2.89 per cent to 3.92 per cent. The month ended with sell-offs in bonds from both companies and governments. There was also a downturn in emerging markets bonds and higher risk bonds.

Commodities

The S&P GSCI Index fell in September, driven lower by weaker prices for energy and industrial metals. Energy was the worst-performing component of the index in the month. Within the industrial metals component, zinc and aluminium prices saw sharp declines in the month. In agriculture, higher prices for wheat, corn and sugar helped to offset a sharp fall in the price of cotton.

Outlook

We believe that market expectations of US interest rate rises have become more realistic, consequently we have moved to a neutral stance on government bonds. In our view a recession in the US and Europe is very likely in 2023, due to the need for central banks to raise interest rates to quell inflation. Against this backdrop, we remain cautious on equities as we expect further weakness in earnings from companies. We have a neutral stance on bonds from companies as we believe these are less exposed to recession risk than equities. We have re-established a positive stance on commodities, following a fall in commodity prices during the summer.

Asset overview

Our general view of assets in the coming months is summarised as follows:

Equities	● (red)	We remain cautious on equities, as we expect further weakness in earnings from companies.
Government bonds	● (amber)	We have moved to a neutral stance, as we believe valuations and market expectations of interest rate rises are now more realistic.
Corporate bonds	● (amber)	Our neutral stance reflects the fact that bonds from companies are more sheltered from recession risk than company shares.
Commodities	● (green)	We have upgraded to a positive stance, due to supply constraints in the energy and agriculture markets.

	Legend
● (green)	Positive outlook
● (red)	Negative outlook
● (amber)	Neutral outlook

Source: Schroders, 11 October 2022

Important information

Forecasts of future performance are not a reliable guide to actual results, neither is past performance a reliable indicator of future results. The value of investments and the income from them can fall as well as rise and are not guaranteed, and the investor might not get back their initial investment.