



Labour and smaller companies on the podium

We can safely say that July has been anything but a quiet month with elections, an assassination attempt, and the opening of the Olympics, to name but a few. Against all that, the latest inflation numbers and interest rate decisions look rather small fry, although notably on August 1st UK interest rates were cut. The month also saw some market rotation out of the US technology related giants and into smaller companies, and the UK stock market at last appearing to find some appeal with investors.

The month opened with election results in both the UK and France, though there wasn't much surprising in the former, as Labour dismantled the sitting Conservative government to claim a landslide victory. Since then, an apparent £22bn fiscal blackhole means that tax hikes are likely on their way - more on this below. Following the domination of France's far-right National Rally in the European Parliamentary elections, a loose left-wing coalition won the most seats in the second round of the French legislative elections. However, a new prime minister has yet to be announced and there is little confidence that this coalition can function effectively.

US politics has also been in the spotlight, with a failed assassination on Donald Trump that seemingly galvanised his support base, followed by President Biden bowing to the inevitable and dropping out of the presidential race. Biden's likely successor, Kamala Harris, has reenergised the democratic bid and the race is definitely back on.

Outside of politics, UK interest rates were cut by 0.25% on August 1st, reflecting the improved inflationary backdrop. In the US, inflation fell for a third straight month and also led to hopes of rate cuts. The nation's smaller sized companies, which are more exposed to interest rates, responded accordingly and rose strongly. This, combined with concerns about future profits for the big players in Artificial Intelligence, led to a general rotation from large companies into small. In fact, July saw the largest ever single-day outperformance of US smaller companies over the tech heavy Nasdaq.

This general theme played throughout markets, and smaller sized companies in the UK also outperformed their larger sized peers. It was also pleasingly a decent month for the UK market more generally. Long maligned for its lack of technology exposure, this proved to be a tailwind in July as technology related firms struggled. Furthermore, a more settled political backdrop (unlike across both the pond and the Channel) and a return to (albeit meagre) economic growth has apparently stirred the embers of support for the UK's market.

Bond markets also responded to the prospects of lower interest rates, as July saw some fairly benign inflation numbers, and prices rose over the month. Yields remain far higher today than they have for years. The yield on the UK 10-year gilt is c.4%, a level not seen since 2009/2010.

Bottom Line

Market expectations for a lower interest rate environment remain high. Given the delayed economic impact of higher rates, the hope is we arrive there soon. Whilst there is no sign of a US recession yet, some cracks are starting to appear. Not least with the US consumer and rising levels of debt in arrears. For now, remaining well diversified and not overly exposed to one theme appears to us, as ever, to be the most sensible way to navigate choppy market conditions.

Month by numbers

Change in various markets over the month:

Asset	Change Value
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Equities

UK	↑	2.91%
Europe	↑	1.07%
US	↑	1.09%
Emerging Markets	↓	-1.33%
Japan	↓	-3.81%

Bonds / Rates

* Absolute change (%)

UK Base Rates	—	0.00%	5.25
Fed Funds Rate	—	0.00%	5.5
UK 10-Year Yield	↓	-0.21%	3.97
US 10-Year Yield	↓	-0.33%	4.04

Currencies

GBP / USD	↑	0.94%	1.28
GBP / EUR	↑	0.42%	1.18
DXY (USD Index)	↓	-1.20%	104.15

Commodities

Gold	↑	3.78%	2478.6
Oil (Brent)	↓	-5.79%	81.36

Noteworthy

Dexcom	↓	-39.80%
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Q&A

What's on your mind?

Will there be tax hikes in the UK?

The short answer is yes, although the new Chancellor of the Exchequer, Rachel Reeves, has repeated her commitment not to raise the rates of income tax, National Insurance, VAT and corporation tax. Therefore, the most likely candidates left for an uplift are inheritance tax, capital gains tax or pension reform. The government has already announced it will add VAT to private school fees at the standard rate of 20% to fund 6,500 new teachers in England. All this follows a rather damning salvo from our new Chancellor to her predecessor, Jeremy Hunt, claiming the Conservatives left a £22bn unfunded blackhole in the nation's finances. We shall have to wait and see exactly which taxes are on the up, but please speak to your financial adviser if you have specific tax related questions.

The prologue, or the final act? An update on U.S. earnings season

Global investors waited pensively for second quarter earnings this year as, more than ever, they would lay bare the resiliency of company profits. Earnings reports in July would likely provide a stark insight into the real economy, and the impact high interest rates are having. Reporting kicked off with US financials opening proceedings – with numbers that beat expectations, producing a sigh of relief from the market. Now, after three weeks of earnings, the figures look promising, as profits growth seem reasonable. However, other metrics do not look as rosy, for example only 43% of companies have beaten revenue expectations, the lowest reading in five years. This may certainly point to the fact that higher interest rates, are indeed, starting to have an impact.

An update on the U.S. election campaigns

With Vice President Kamala Harris likely superseding President Biden as the Democrat presidential nominee, this now looks to be a much more even contest. The Republican presidential nominee, Donald Trump, is campaigning on themes such as economic nationalism, stricter immigration controls, and general criticism of the Biden administration. Despite facing multiple legal challenges, including indictments related to his actions surrounding the 2020 election, Trump remains popular among his base and continues to poll well, especially amongst Republicans. For the Democrats, Harris' campaign efforts focus on defending the current administration's record and addressing issues surrounding reproductive rights and social justice, aiming to energise the Democratic base for the upcoming election. With stark contrasts in vision and policy, the campaigns are shaping up to be pivotal in defining the future direction of the United States.

For more information, please contact your adviser.

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