CS INVESTMENT MANAGERS

VIEW FROM THE SQUARE

September 2024

“The time has come for policy to adjust” – Time for portfolio adjustment?

August saw the widely anticipated speech from Federal Reserve (Fed) chair Jay Powell at the Jackson Hole economic conference, which was expected to provide greater clarity on the path of interest rates. The speech generally delivered on this, with comments that ‘the time has come for policy to adjust’ and ‘the direction of travel is clear’ all but confirming that there will be an interest rate cut in the US at the September meeting. It is clear that the Fed is gaining comfort around the inflation element of its dual mandate, while employment, the other side of the coin, is giving a bit more cause for concern.

Indeed, labour market data over recent months (unemployment and job openings) indicate that the US economy is weakening, while consecutive manufacturing sentiment index readings somewhat reinforce this weakening narrative. This has been a key driver of volatility over recent weeks, and we feel comfortable having taken some equity risk off the table in client portfolios through crystalising some profits in the US.

While market consensus continues to believe that a soft landing will play out, we are growing increasingly apprehensive around this outcome, with current US equity valuations leaving little room for error and have been making touches to portfolios as a result.

Within our thematic bucket, we have cut back on energy holdings in light of a weakening economy and hence demand backdrop. Instead, we have a preference for more defensive sectors such as healthcare, consumer staples and utilities. As an example, within healthcare not only is the sector typically resilient, but we are also seeing innovation within the space, with AI likely to be transformational in terms of reducing the R&D cycle.

We have also taken some profits in Japanese equities after moving overweight last year. August’s volatility was a reminder as to the influence of currency movements on the export heavy stock market. In its place, we have opted for a more defensive position in the Yen currency. As Japan looks set to move into a period of tighter monetary policy, while other developed economies move into easing cycles, we anticipate seeing a reversal, which we saw glimpses of in August, in Yen depreciation that we have become accustomed to over the past 5 or so years.

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9 September 2024

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