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## MARKET VIEWS – JULY 2023

*"With a good perspective on history, we can have a better understanding of the past and present, and thus a clear vision of the future." — Carlos Slim Helu*



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## **At a glance**

The quote from Carlos Helu reflects where we are today. It is very easy to lose perspective when everything seems so negative. Looking back through history, the markets recovered from the 2008 financial crisis, the dotcom bust and even the great depression.

In this part of the report we want to share some charts which we hope will put things into perspective.

The key take outs from this update are:

### Europe, UK, and Europe

1. The US has paused interest rate rises but they have indicated this might not be the end.
2. The EU and UK look set to continue to rise rates further.
3. In the short term everything is pointing to a recession across the US, EU, and UK before the end of the year.
4. Markets tend to recover once we enter a recession.
5. Long term the outlook seems to favour Europe over the US.

### Emerging Markets and Asia

1. The last decade has been a lost decade for investors.
2. The next decade could see some emerging markets and Asian economies outperform the US and UK.
3. Signs of recovery in China.
4. India moving forward to a global powerhouse.
5. Japan moving from “Japan Passing” to “Japan Rising”.

There are five charts we would like to share in this section (some of these will appear again in the report).

### Counter trend rallies

Counter trend rallies are commonplace, and confusing during periods such as we are currently in. This is where we see a recovery in markets and then markets fall further:

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**Largest Historical Recessionary Counter Trend Rallies**

Recession Start	Recession End	Largest Counter Trend Rally
Dec. 1969	Nov. 1970	6%
Nov. 1973	Mar. 1975	10%
Aug. 1973	Oct. 1973	11%
Jan. 1980	July 1980	4%
Jul. 1981	Nov. 1982	12%
Jul. 1990	Mar. 1991	6%
Mar. 2001	Nov. 2001	19%
Dec. 2007	June 2009	24%
Feb. 2020	Apr. 2020	9%
<b>Average:</b>		<b>11%</b>
<b>Current:</b>		<b>17%</b>

**S&P 500 Counter Trend Rallies: 2007-2009**



## Markets do recover

Market lows tend to hit during a recession. If we are heading towards a recession before the end of this year we can expect to see that recovery come through towards the end of 2023 and early 2024.

Recession Start	Recession End	Length (Months)	Market Low During Recession?	Distance from Recession Start (Months)	Distance from Recession End (Months)
Nov. 1948	Oct. 1949	11	Yes	6	-5
July 1953	May 1954	10	Yes	1	-9
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July 1990	March 1991	8	Yes	2	-6
March 2001	Nov. 2001	8	No	18	10
Dec. 2007	June 2009	18	Yes	14	-4
Feb. 2020	April 2020	2	Yes	1	-1
<b>Average:</b>		<b>10.3</b>		<b>6.6</b>	<b>-3.8</b>

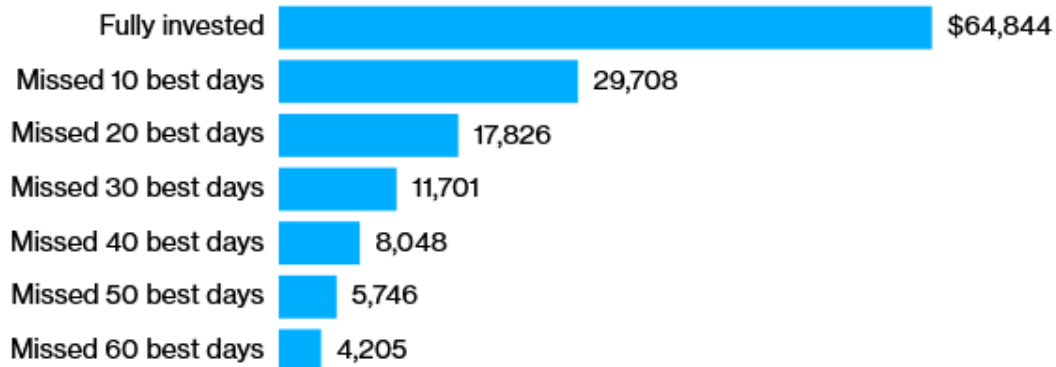
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### Navigating the market

All the evidence shows that selling out and trying to time the market doesn't work.

## **Investors Pay Steep Price for Missing Best Days of Rally**

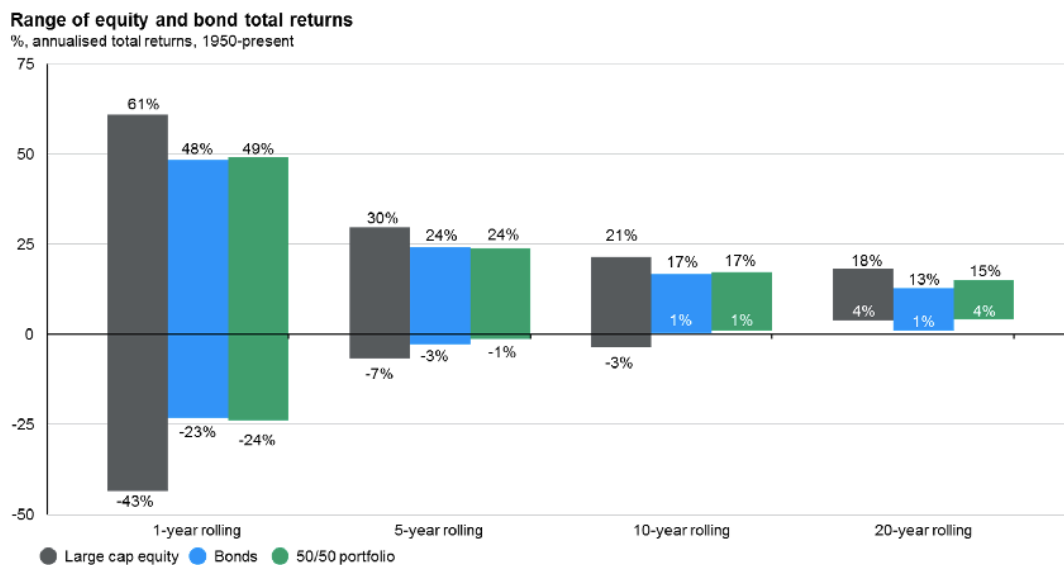
Performance of \$10,000 invested in S&P 500 in 20 years to end of 2022



Source: JPMorgan Asset Management

### Asset returns

There are two charts we would like to share. The first shows the range of equity and bond total returns from 1950 to present. This shows how the longer an asset is held the more likely it is to deliver a positive return.

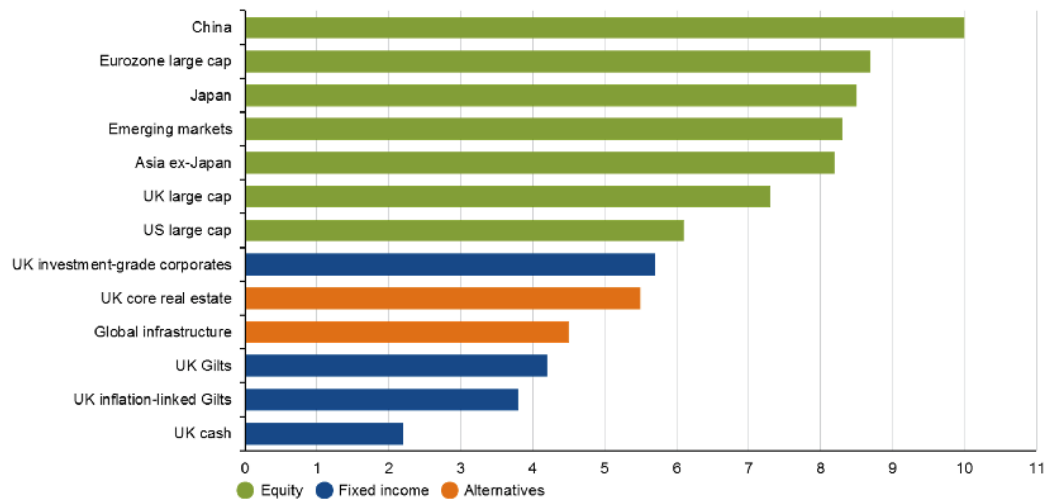


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To end, with we want to share what the long-term capital market assumptions are for long term returns.

**2023 Long-Term Capital Market Assumptions** expected returns in coming 10-15 years

% , annualised return in GBP



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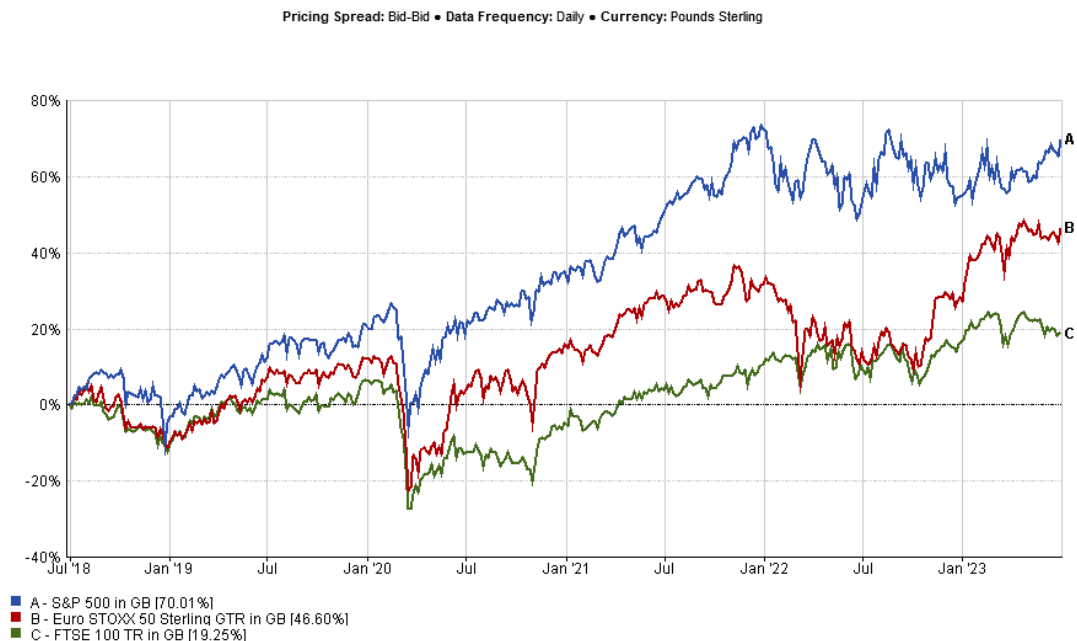
## US, Europe, and UK

In this section we will consider the US, Europe, and the UK.

The key take outs are:

1. The US has paused interest rate rises but they have indicated this might not be the end.
2. The EU and UK look set to continue to rise rates further.
3. In the short term everything is pointing to a recession across the US, EU and UK before the end of the year.
4. Markets tend to recover once we enter a recession.
5. Long term the outlook seems to favour Europe over the US.

### Five-year market returns



29/06/2018 - 30/06/2023 Data from FE fundinfo 2023

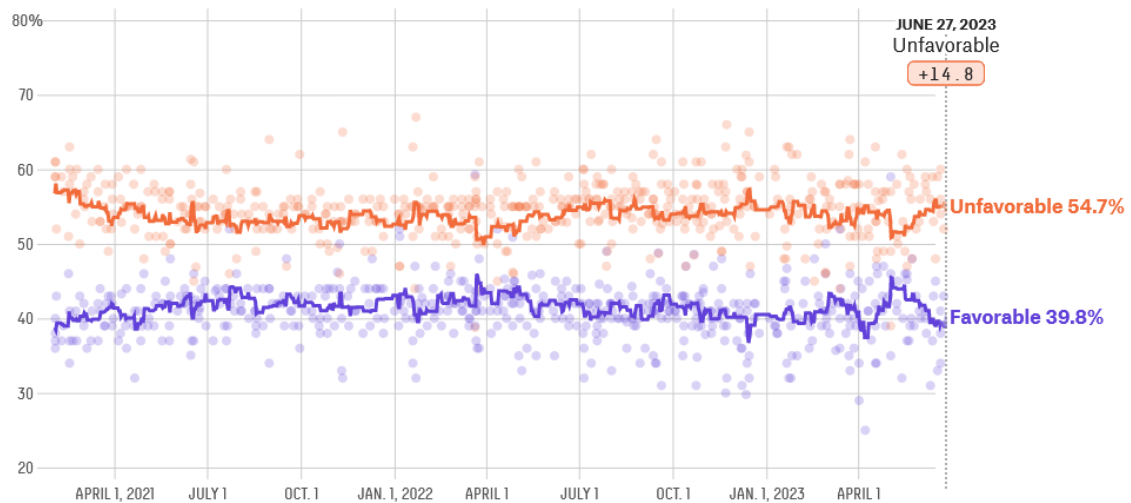
### US

Trump remains uppermost in our minds. Could he really become the President next year? Apparently even if he goes to prison, he could still become President. We can see a spike upwards in favourability, but this has come back. What this really shows is the unpredictability that we all face coming into next year.

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## Do Americans have a favorable or unfavorable opinion of Donald Trump?

An updating average, accounting for each poll's quality, recency, sample size and partisan lean.

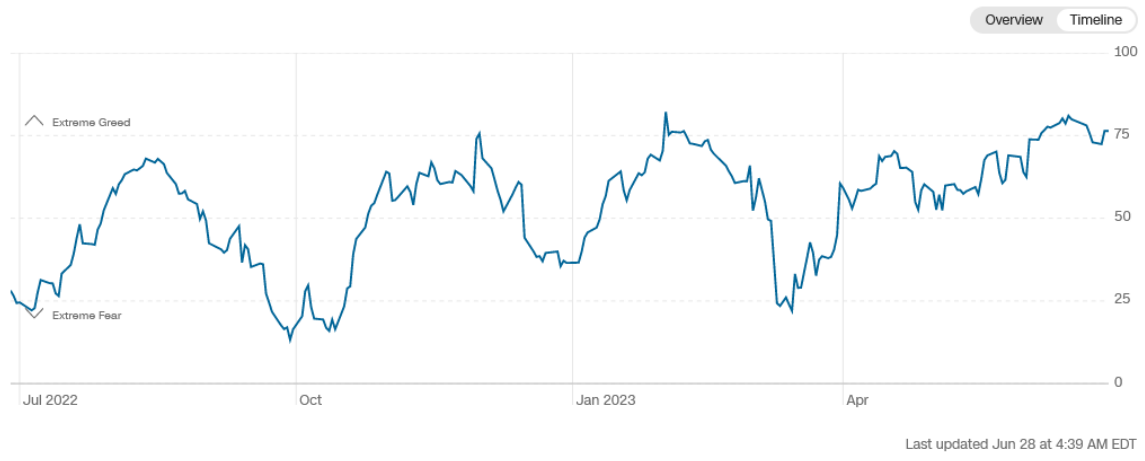


The first half of the year has been challenging, with the big questions around whether interest rates go higher and when inflation comes down. Despite this the S&P 500 has seen an unsteady climb from October 2022.

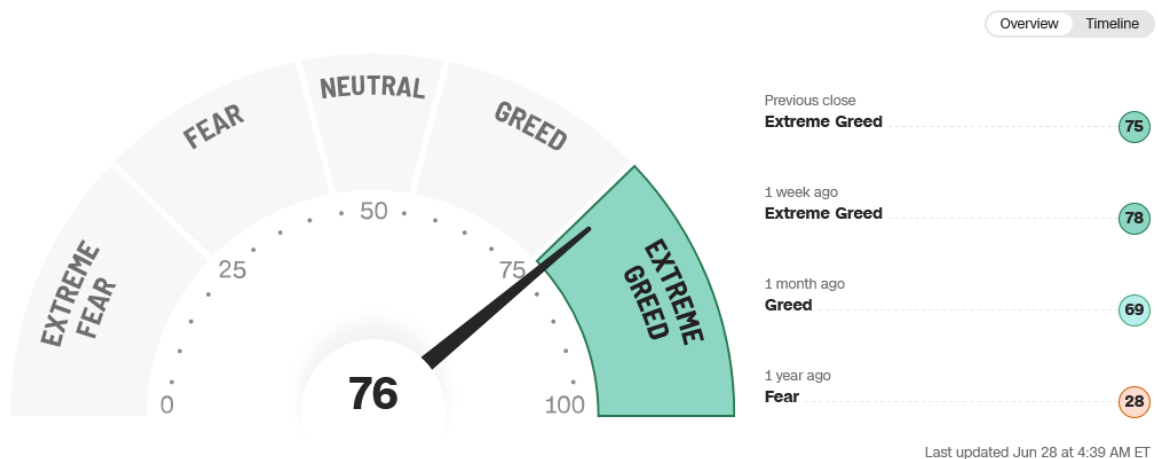


We follow the CNN Fear and Greed Index which could almost match the S&P 500.

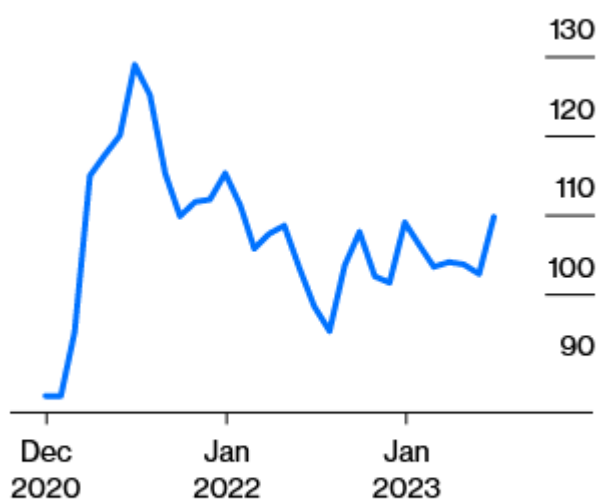
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What this shows is that markets have moved from fear 12 months ago to extreme greed.



### Consumer confidence



Source: The Conference Board

So where do we stand?

Let us start with the US. There has been much talk about a recession and it is expected that the US will drop into a recession by the end of the year. Cracks are appearing in the economy but labour markets remain tight and inflation remains elevated. Also, recent data indicated an uplift in consumer confidence.

The US does seem to be the first economy to pause interest rate rises. The markets initially thought this would be an end to rate rises. However Janet Yellen indicated that potentially more could come.

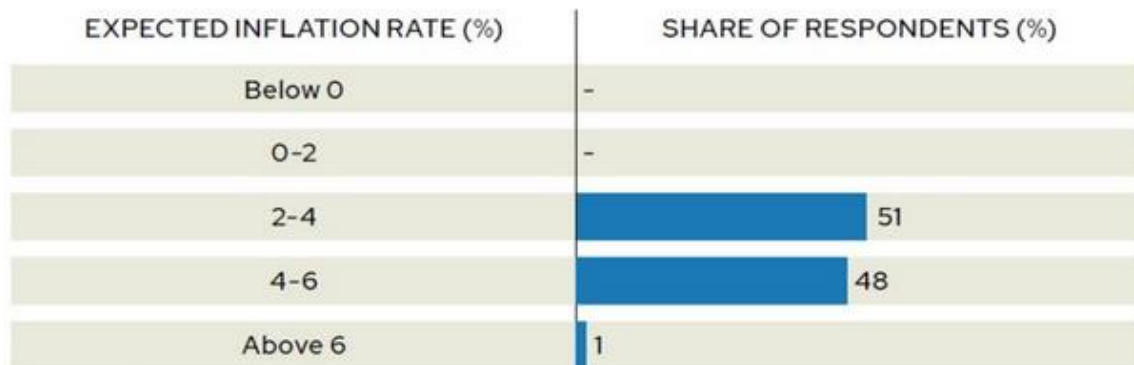


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There is much debate on where inflation ends up.

The chart below is interesting:

What do you expect that the rate of inflation in most major economies will be over the next 12-24 months?



Source: OMFIF GPI survey 2023

If we look at the US recession risk indicators, everything is pointing to a recession:

	Current	2020	2007-2009	2001	1990-1991	1981-1982	1980	1973-1975	1969-1970
Consumer	Housing Permits	✗	↑	✗	●	✗	✗	✗	✗
	Job Sentiment	✗	●	✗	✗	✗	●	●	●
	Jobless Claims	●	↑	●	✗	✗	✗	↑	✗
	Retail Sales	✗	↑	✗	✗	✗	✗	●	✗
	Wage Growth	✗	✗	✗	✗	✗	✗	✗	✗
Business Activity	Commodities	✗	↑	✗	✗	✗	●	●	●
	ISM New Orders	✗	●	✗	✗	✗	✗	✗	✗
	Profit Margins	✗	✗	✗	✗	✗	✗	●	✗
	Truck Shipments	●	↑	●	✗	✗	✗	n/a	n/a
Financial	Credit Spreads	✗	↑	✗	✗	✗	✗	↑	●
	Money Supply	✗	↑	✗	✗	✗	✗	✗	✗
	Yield Curve	✗	✗	✗	✗	✗	✗	✗	✗
Overall Signal		✗	●	✗	✗	✗	✗	●	✗
↑ Expansion      ● Caution      ✗ Recession									

In terms of markets, it is important to reflect that the market low tends to occur during the recession.

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Recession Start	Recession End	Length (Months)	Market Low During Recession?	Distance from Recession Start (Months)	Distance from Recession End (Months)
Nov. 1948	Oct. 1949	11	Yes	6	-5
July 1953	May 1954	10	Yes	1	-9
Aug. 1957	April 1958	8	Yes	2	-6
April 1960	Feb. 1961	10	Yes	6	-4
Dec. 1969	Nov. 1970	11	Yes	5	-6
Nov. 1973	March 1975	16	Yes	10	-6
Jan. 1980	July 1980	6	Yes	2	-4
July 1981	Nov. 1982	16	Yes	12	-4
July 1990	March 1991	8	Yes	2	-6
March 2001	Nov. 2001	8	No	18	10
Dec. 2007	June 2009	18	Yes	14	-4
Feb. 2020	April 2020	2	Yes	1	-1
Average:		10.3		6.6	-3.8

Therefore, it is fair to say that we can expect more volatility as we come closer to a recession. However, once we get to that point then we should start to see a more sustained recovery in asset values.

### Europe

Longer term the outlook for Europe remains positive. There are three key areas for Europe:

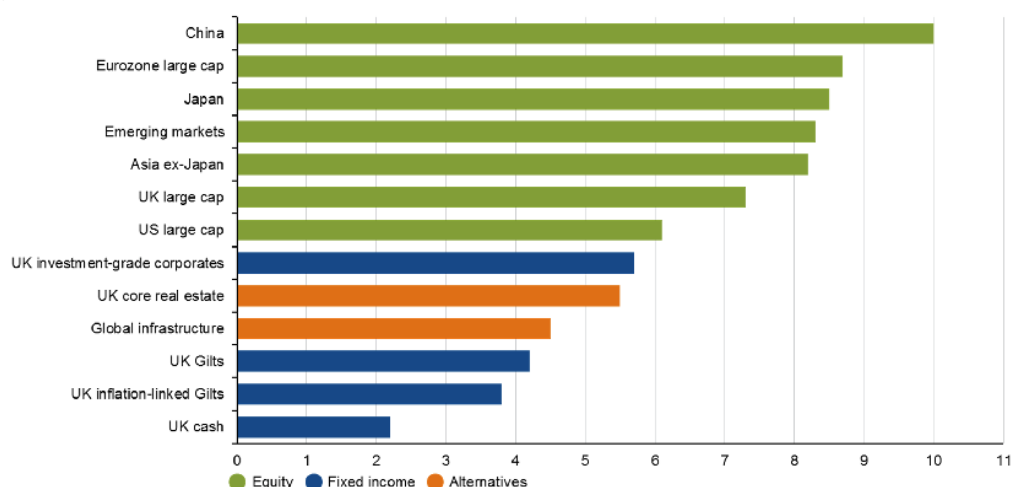
1. Energy Innovation
2. Energy Efficiency
3. Renewed need for renewables

Europe is at the forefront of the energy revolution and this makes it an interesting long term investment proposition.

If we look at long term asset return expectations, Europe is ahead of the US and the UK in expected returns.

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**2023 Long-Term Capital Market Assumptions** expected returns in coming 10-15 years  
%, annualised return in GBP



The other area of interest with Europe is the link with China. As the US tries to smooth relationships with China there is a real danger that there is a split between Europe and the US on how they interact. In the Washington Post there was a fascinating article. It discussed how China is the world's leading exporter of automobiles, and how two out of three of every EV is made in China.

Nio cars are designed in Munich and have research centres in San Jose, Oxford, Beijing, and Shanghai. Where Europe supports the US over Russia, there is less commitment around China. It cannot afford to follow the US protectionism policy. Trade with the rest of the world, including China, is vital, which for the US is not the case.

Helle Thorning-Schmidt, former Prime Minister of Denmark, concurred “Europe cannot divorce itself from China.” She explained, “That would be the end of globalization. That is why we want to de-risk, not decouple.”

So, looking forward the integration with China and Asia is vital to the growth in Europe and this could cause a split with the US.

In the short term, interest rates look certain to continue to go up. Expectations are that rates could peak at 4.0%. They have also indicated that they will not reduce rates quickly:

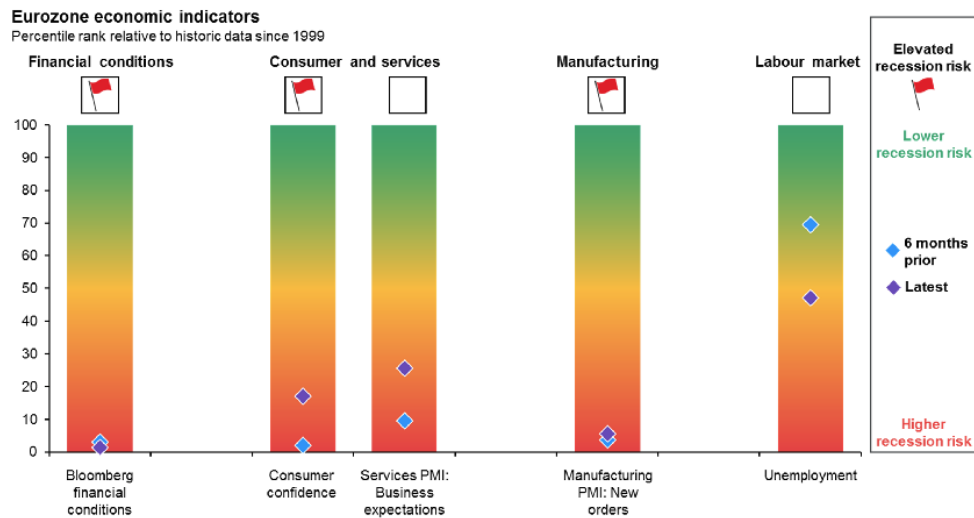
“We need to communicate clearly that we will stay ‘at those levels for as long as necessary,’” Lagarde said. “This will ensure that hiking rates do not elicit expectations of a too-rapid policy reversal and will allow the full impact of our past actions to materialize.”

If we consider the Eurozone economic monitor, this is signalling an elevated recession risk.

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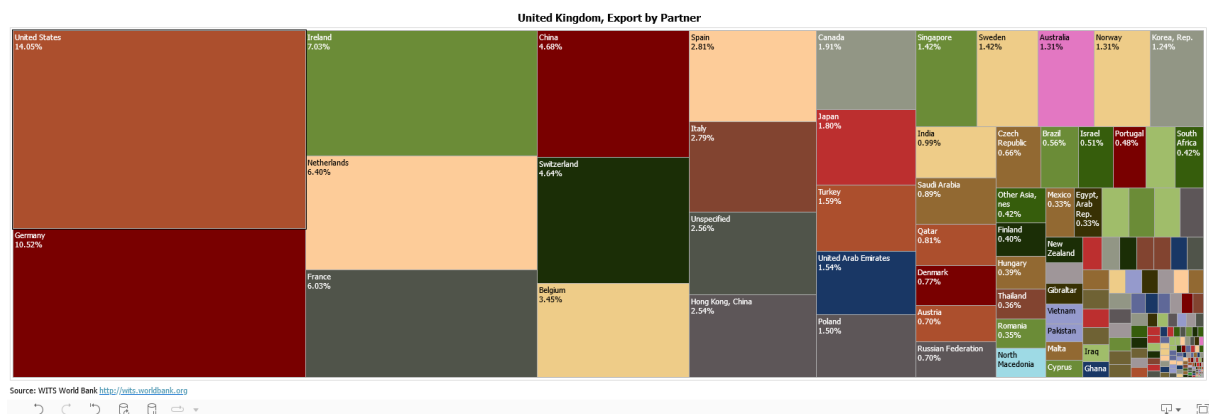
## Eurozone Economic Monitor

Actions ▾



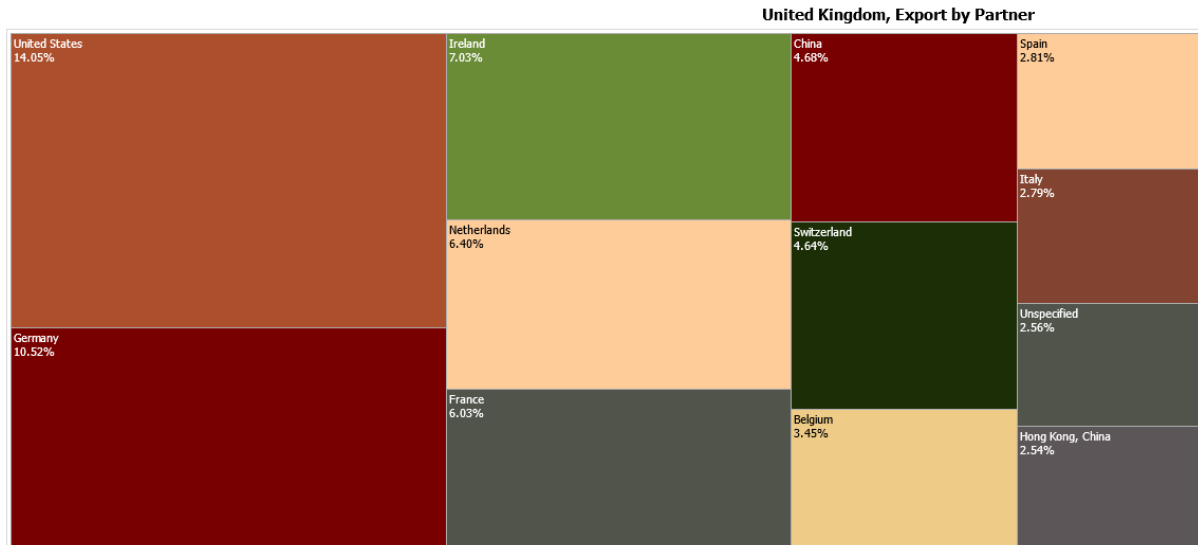
## UK

Turning now to the UK. Just looking at the headlines there seems to be much to worry about in the short term. Whatever our views of Brexit, the chart below shows our reliance on Europe as a trading partner, and how creating barriers to trade will cause short term problems.



The US is around 14.05%. Germany, Ireland, Netherlands, France, Switzerland, Belgium, Spain and Italy make up 43.67%.

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Source: WITS World Bank <http://wits.worldbank.org>

Some of the recent headlines include:

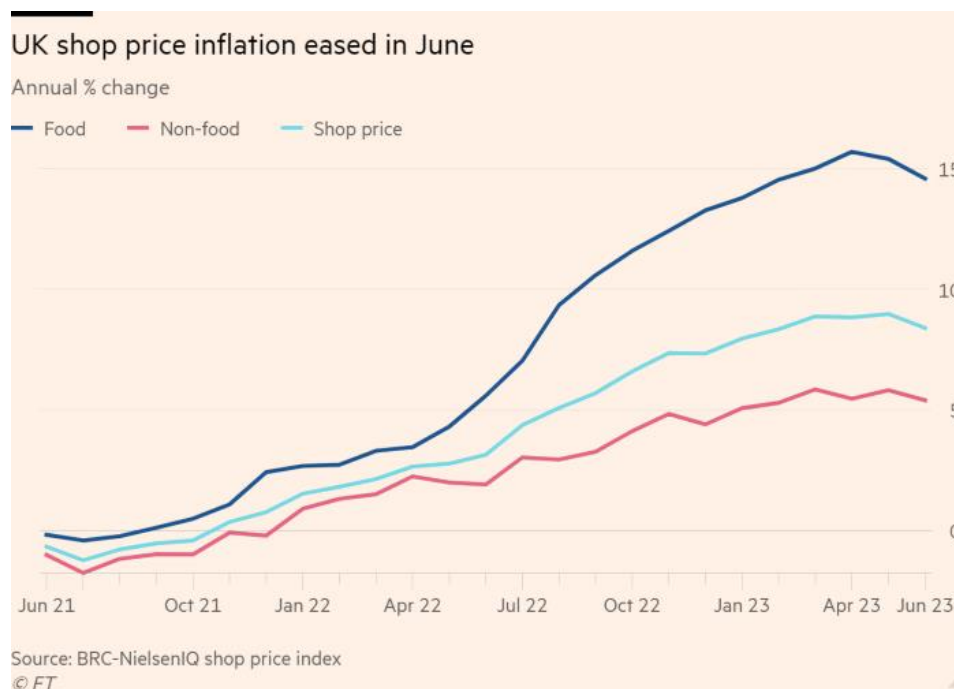
“UK manufacturers warn Brexit is undermining their place in EU supply chains.”

“The last Brexit deal? Gibraltar fears a hard border with Spain.”

“UK progress on climate change worryingly slow, advisers warn.”

“Price discounts jump as rising mortgage costs ‘spook’ UK house buyers.”

Inflation and interest rates are the short-term worry for the UK. There are some signs that inflation might be easing when we look at the shop index:



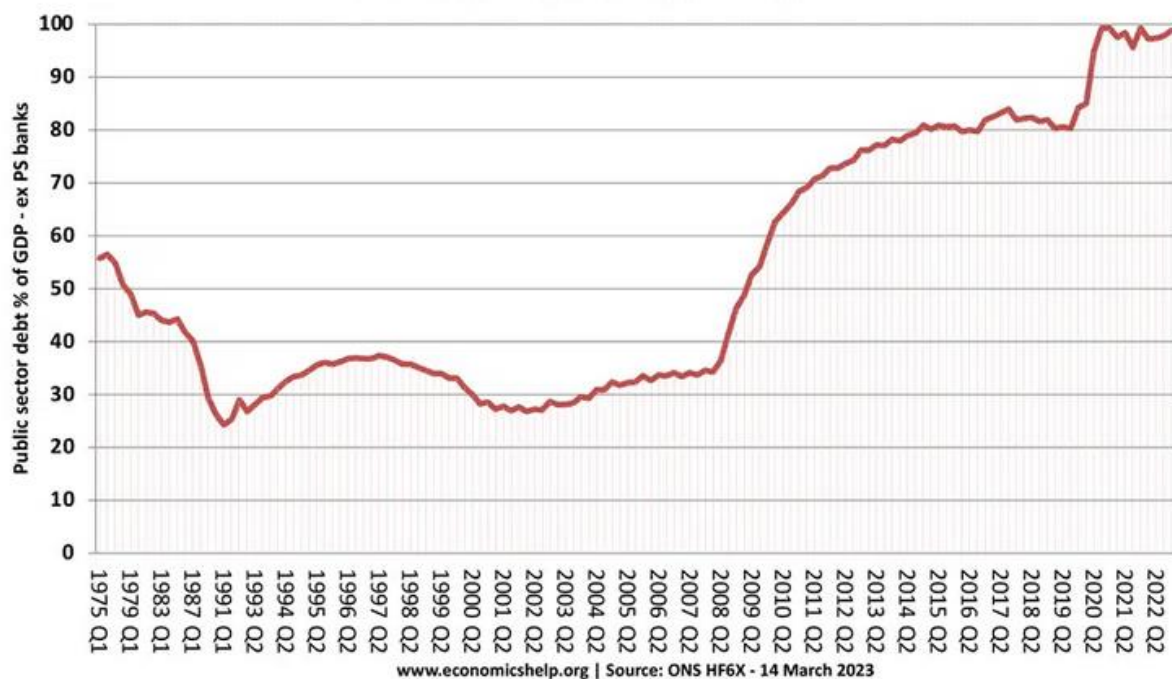
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But interest rates are likely to keep rising to curb inflation, pushing the UK into a recession. Almost all economists agree that the UK will enter a recession before the end of the year. Interestingly, consumer confidence remains strong in the UK.



The UK faces many challenges; inflation, higher interest rates and rising national debt.

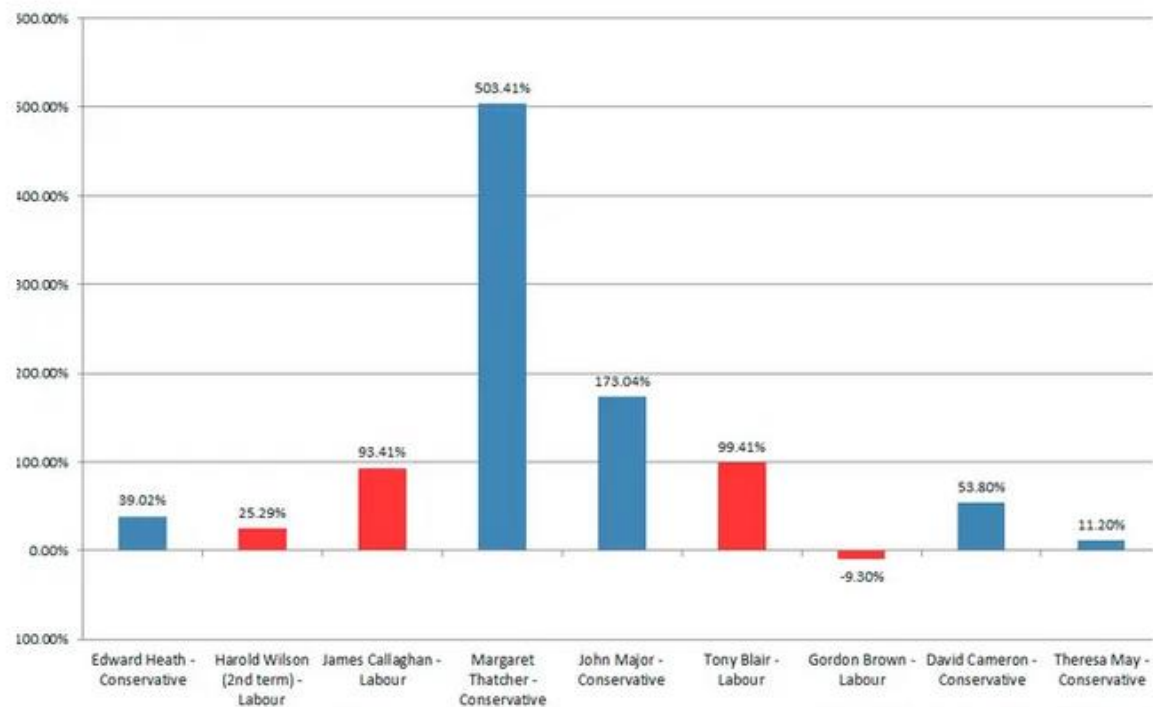
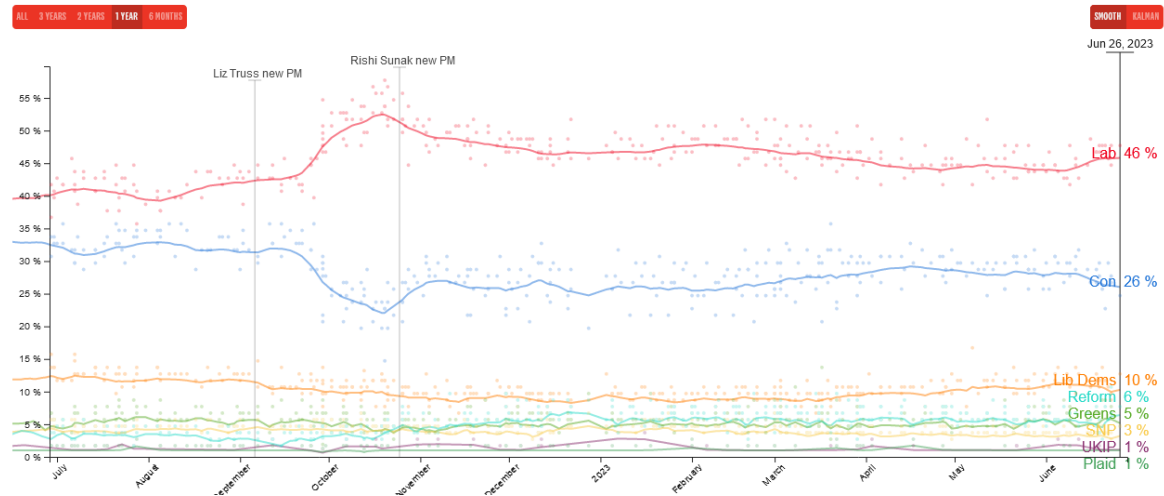
### UK National Debt % GDP



To end, next year is likely to be an election year, with everything seeming to point towards a Labour victory. Whether this changes things will be something to see.

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## National parliament voting intention



### Summary

As we head towards likely recessions across the US, Europe and UK, and we what seems like a gloomy outlook, there are three charts we go back to. The first is that history shows that markets recover once we go into a recession. We often have counter trend rallies. This is normal so any sharp rise in markets does not necessarily signal a change in market sentiment.

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**Largest Historical Recessionary Counter Trend Rallies**

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Feb. 2020	Apr. 2020	9%
<b>Average:</b>		<b>11%</b>
<b>Current:</b>		<b>17%</b>

**S&P 500 Counter Trend Rallies: 2007-2009**



The second chart shows that on average the market low is 6.6 months into a recession. In 1980 and 1990 this was 2 months. We believe that all the main economies will go into a recession this year, then we could start to see that recovery towards the end of the year and into 2024.

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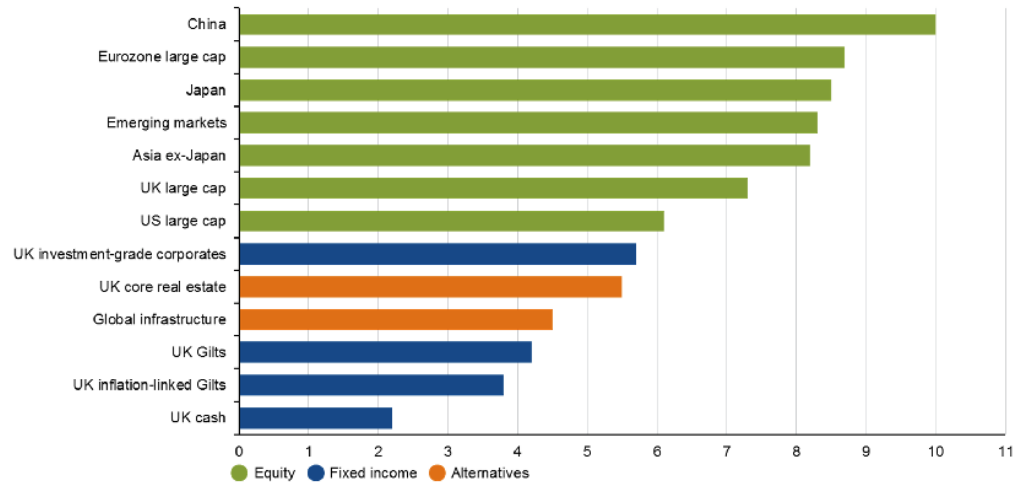
And the final chart shows potential asset class future returns, which are healthy looking over a longer period.



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**2023 Long-Term Capital Market Assumptions** expected returns in coming 10-15 years

%, annualised return in GBP



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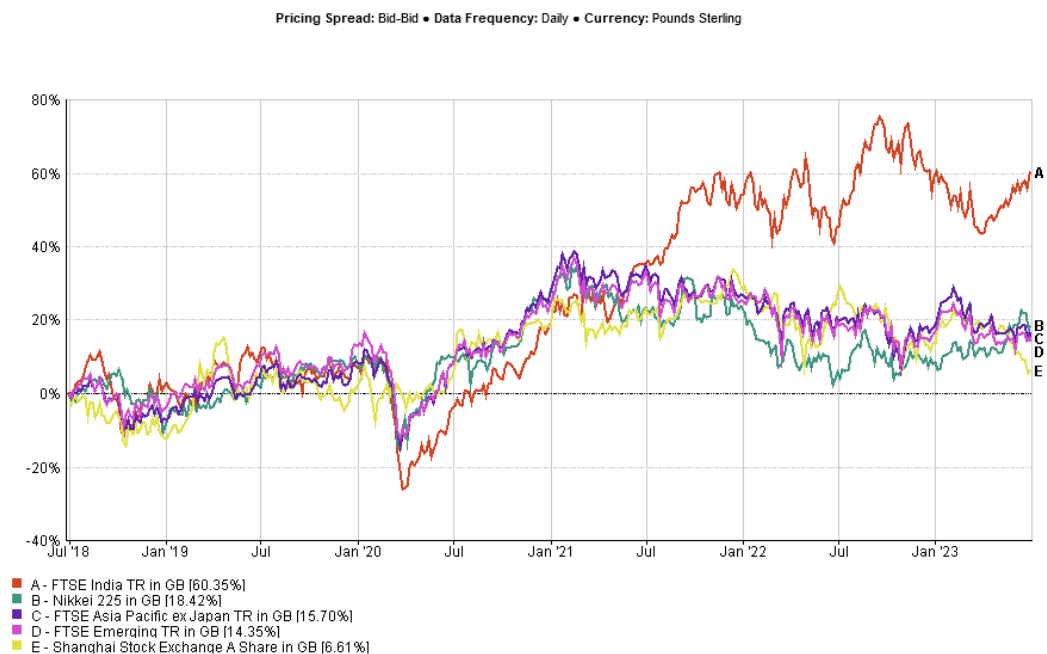
## Emerging Markets, and Asia

In this section we will consider Emerging markets and Asia.

The key take outs are:

1. The last decade has been a lost decade for investors.
2. The next decade could see some emerging markets and Asian economies outperform the US and UK.
3. Signs of recovery in China.
4. India moving forward to a global powerhouse.
5. Japan moving from “Japan Passing” to “Japan Rising”.

### Five-year market returns

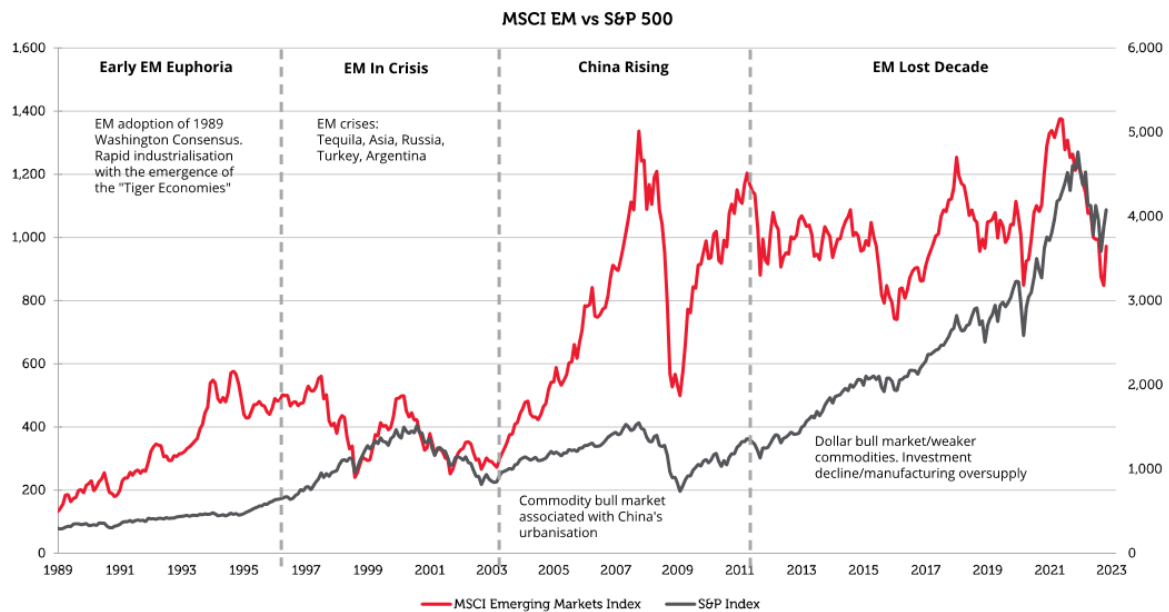


29/06/2018 - 30/06/2023 Data from FEfundinfo2023

### Overview

The last decade is probably best described as a lost decade for investors, as is shown by the chart below.

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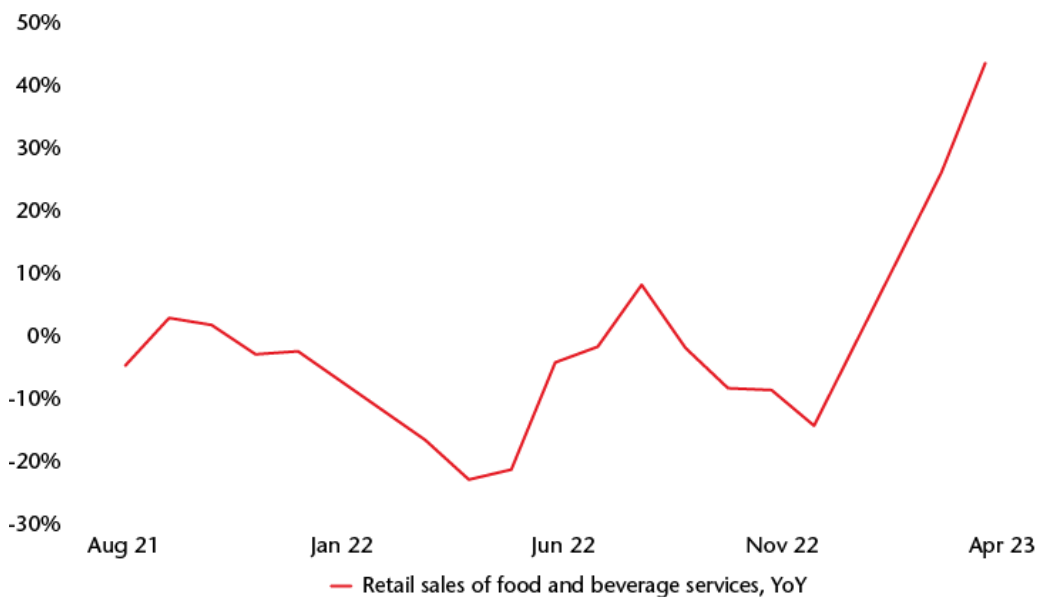
In this update we will look at China, India, and Japan.

## China

The fascinating thing with China is the fear of a public revolt. Everything is targeted to making things better. We saw the climb down over the zero COVID policy. It seems that China, like the rest of the world, is learning to live with COVID.

There are signs that there is an early gradual consumer-led recovery. Sales of food and beverages are seeing a strong recovery.

**Figure 1: SALES OF RESTAURANTS AND BARS FULLY RECOVERED**



Source: CEIC

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Retail sales are expanding and property sales recovering.

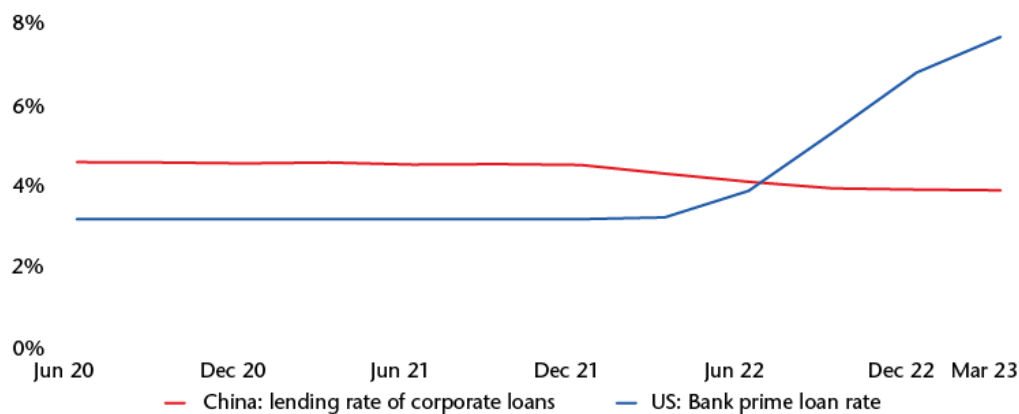
In terms of the economy, consumers have the means to spend. There has been a 3.8% year on year rise in real income. Consumer spending and confidence is supported by the 59% rise in family bank balances from the start of 2020.

Like economies such as the UK and US, Chinese households saved rather than spent during the lockdown. The net increase in household bank accounts is equal to \$6.9 trillion which is greater than the GDP of Japan in 2022. This is equal to 118% of China's 2019 retail sales.

It is also important to note that 95% of the mainland equities are held by domestic investors so any consumer spending rebound will likely benefit equities.

China's central bank is likely to continue easing while much of the world is tightening.

**Figure 6. CHINA LIKELY TO CONTINUE EASING WHILE FED KEEPS TIGHTENING**



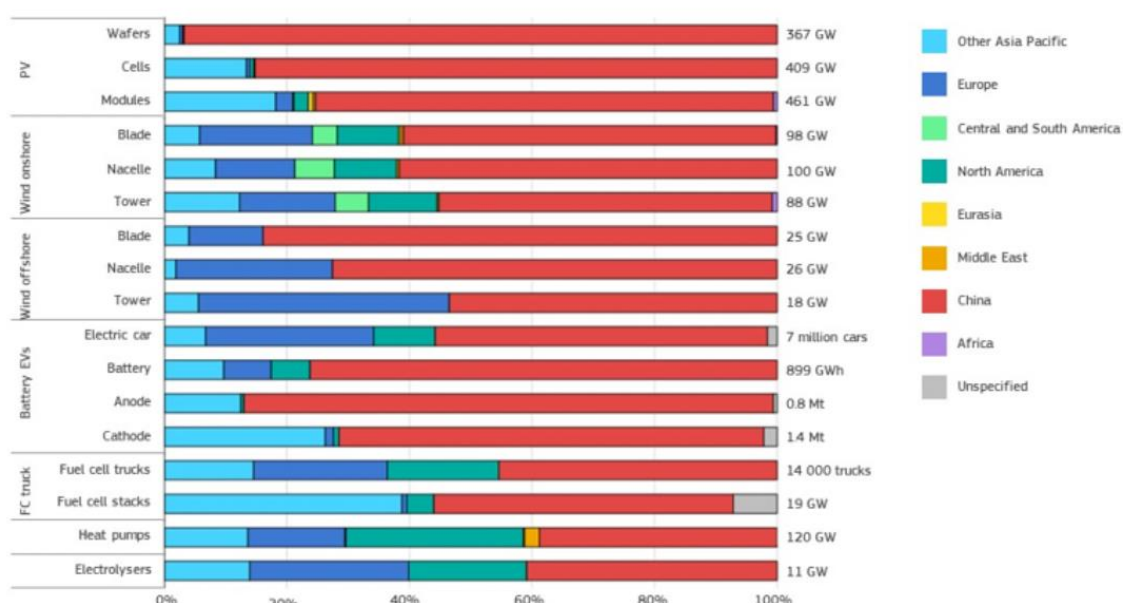
Sources: CEIC, Federal Reserve Bank of St. Louis

Other statistics which I find interesting are:

1. Per capita income rose 148-fold between 1980 and 2022, compared to a five-fold increase in the US, and seven-fold increase in the UK.
2. During the last ten years, real per capita income rose at an average annual pace of 6.2%, compared to 1.4% in the US and 1% in the UK.

In terms of the energy revolution, China is dominant across supply chains and materials.

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There are tensions with the US but the reality, as we have indicated, is that the world needs China and China needs the world. All the signs are for a slow but sustained recovery.

## India

India has a young population; it is the world's second largest population and people are getting richer and consuming in ways that have not been seen before. India like other countries has set bold targets to transition to renewable sources of energy.

Modi recently visited the US to strengthen the defence and manufacturing relationship. Discussions covered joint production of jet engines, long range artillery and military vehicles. The US has also increased investment in semiconductor and chip manufacturing in India, to reduce dependence on Chinese manufacturing.

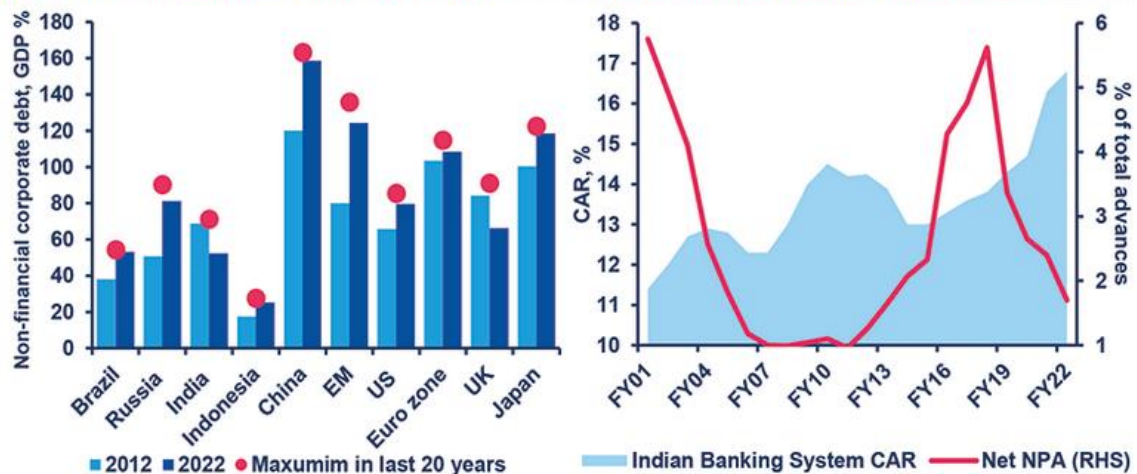
The long-term story for India focuses on its demographics, urbanisation, digitalising, rising middle class and rising ability to spend. Unlike many Western economies, the average age remains below 30, providing both labour and controlling labour costs.

Indian corporates have deleveraged and banks have cleaner balance sheets.

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**Figure 1: Indian corporates have deleveraged...**

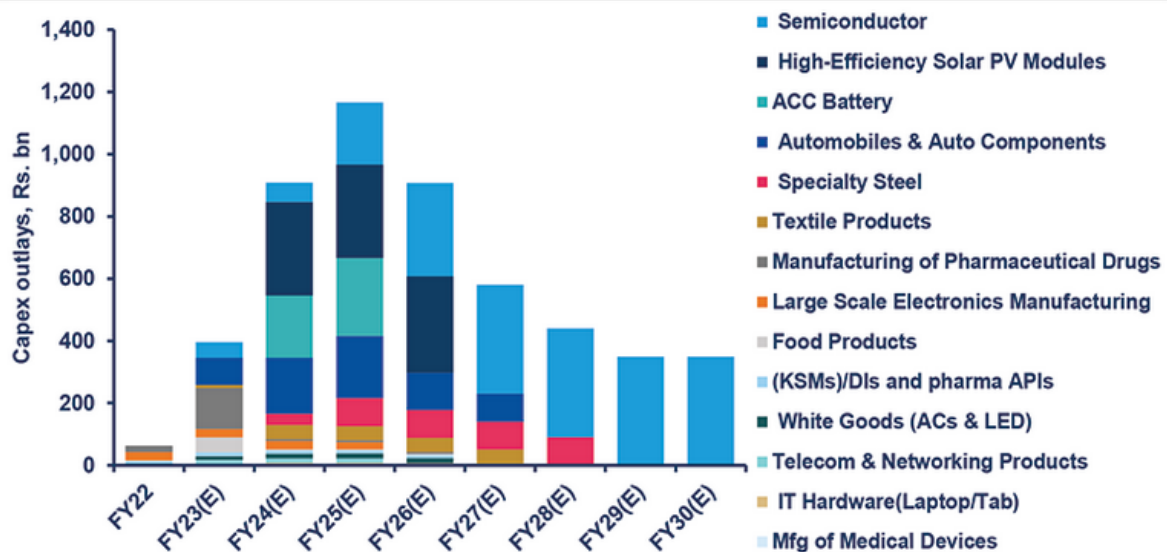
**...and banks have cleaner balance sheets**



Source: Amundi Institute on Bloomberg data as of 30 March 2023.

The government has selected certain industries to boost manufacturing. Fundamentally this is about taking some of the supply chains from China and encouraging investment across areas such as semiconductors and renewable energy.

**Figure 3: PLI-linked capex to pick up from 2023 onwards**



Source: Amundi Institute on PLI documents from Indian government website as of 30 March 2023.

The chart shows the trade as a share of GDP for India in 2020.

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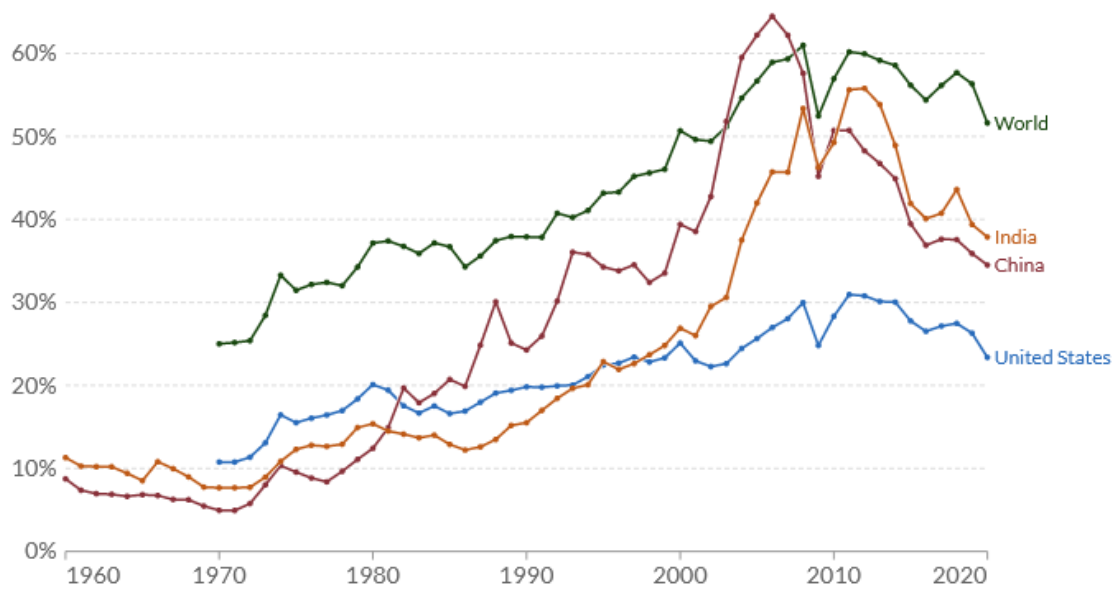
## Trade as share of GDP, 1960 to 2020

Shown is the 'trade openness index' – the sum of exports and imports of goods and services, divided by the gross domestic product.

Our World  
in Data

+ Add country or region

All together ▼



Source: World Bank and OECD

OurWorldInData.org/trade-and-globalization • CC BY

1960 2020

CHART

MAP

TABLE

SOURCES

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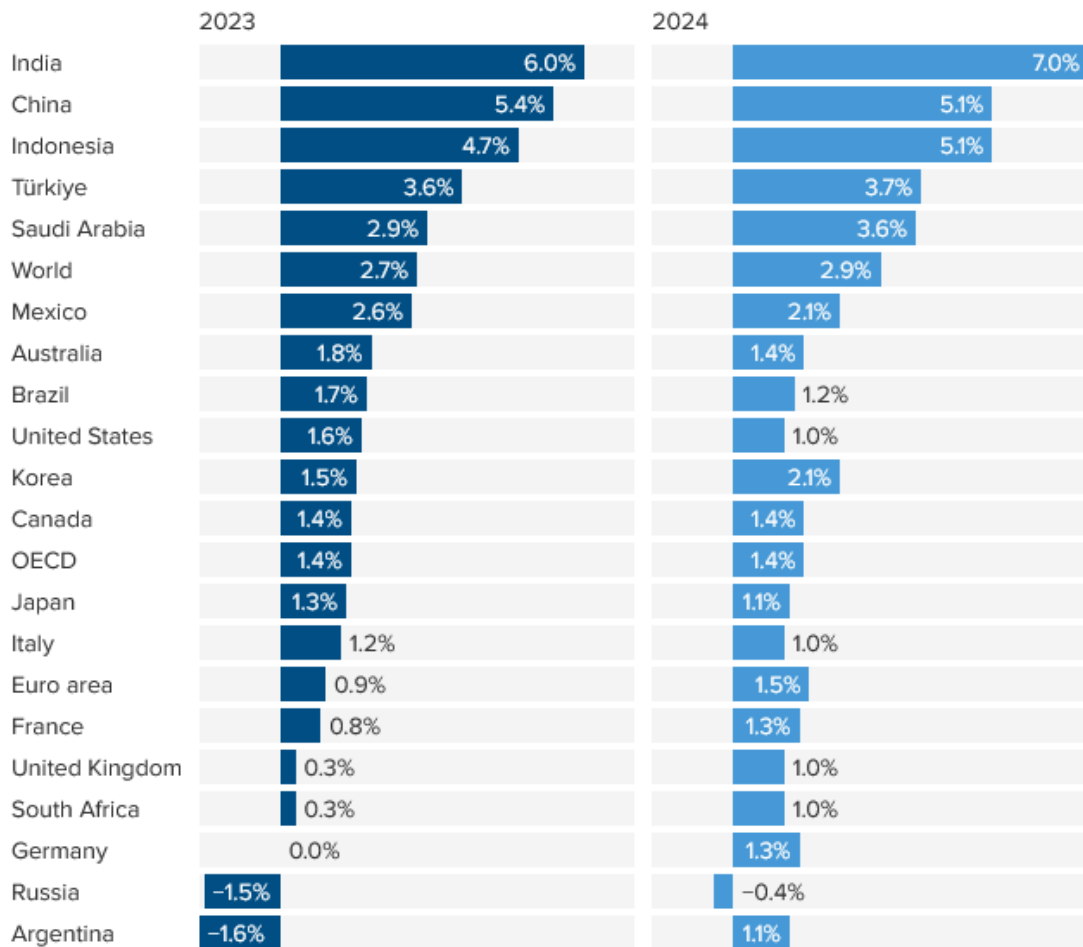
Share

The chart below shows GDP projections:

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## GDP growth projections

%, year-on-year



Source: [OECD Economic Outlook, June 2023](#)



In summary, India has considerable positives and could become a core exposure in the future.

### Japan

For decades Japan seemed to be going nowhere. As their dominance slipped, so China's grew. However, things are changing.

As decoupling from China gathers pace, so Japan is proving a leading alternative for investments due to its strategic location, its economy and financial resources.

Semiconductor giants such as TSMC and IBM are starting to set up production facilities in Japan. Other companies, from drones to digital companies, are looking to gradually take market share from Chinese companies.

Acquisitions of Chinese companies declined by 76% since 2021, whilst investment in Japanese businesses reach \$13.3 billion.

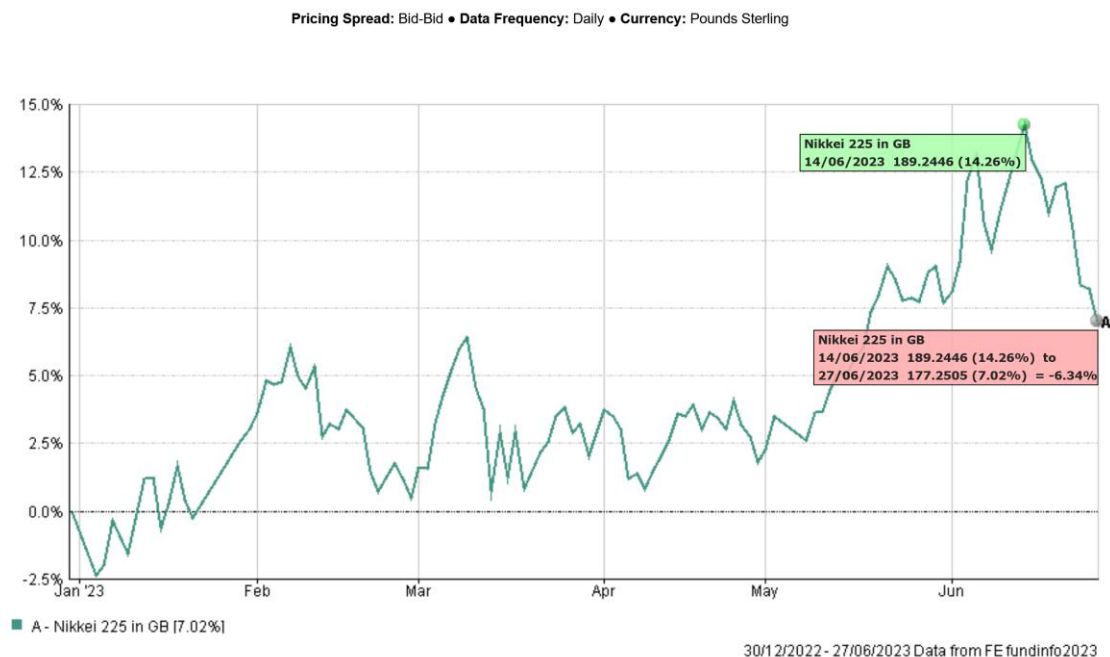


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Much of the change was driven by the late Prime Minister Abe, not only internally but also in strengthening ties in Southeast Asia.

After decades of near zero inflation, wages and core inflation are starting to rise. Wage rises are expected to rise by 2.85%, the steepest increase in many years. Companies are more dynamic, removing lifetime employment and seniority-based systems is leading to greater innovation.

Also, all of this has seen a sharp rise in asset prices this year, although this has dropped back slightly.



In summary, Japan is changing and benefiting from close ties, particularly to Southeast Asia, and the policies driven by Abe. It now seems to be moving forward under Kishida.

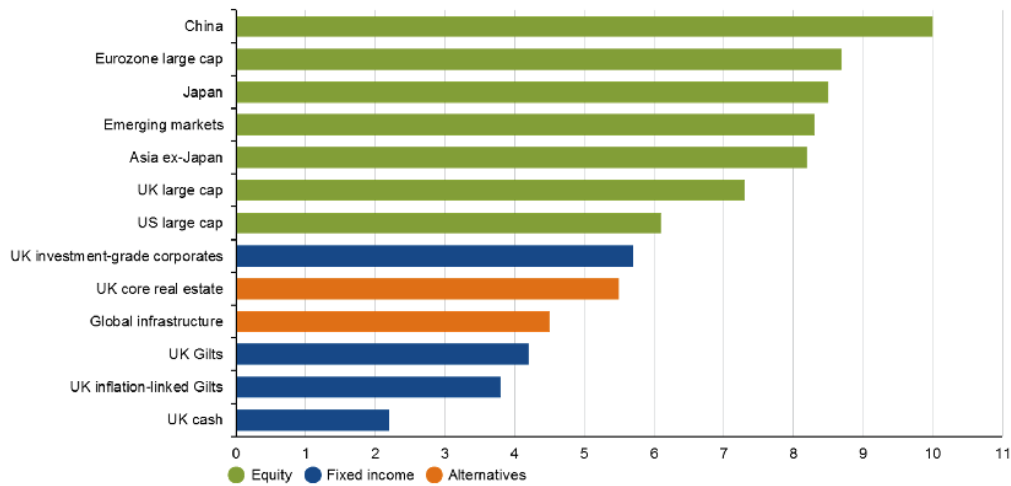
### Summary

Where developed economies seem stuck with inflation and interest rates, emerging market and Asia economies such as China, India and Japan are moving forward at different paces.

It has been a lost decade for emerging markets but that might be changing. Although the chart below doesn't show India, it does show Japan and China and how they could provide the strongest returns over the coming decade.

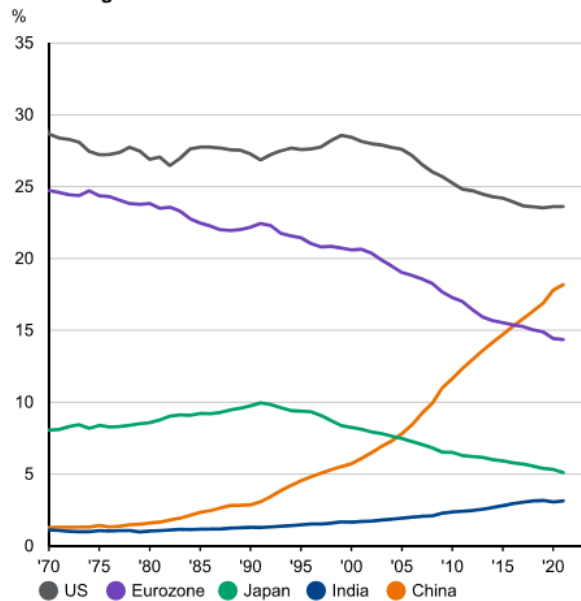
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**2023 Long-Term Capital Market Assumptions** expected returns in coming 10-15 years  
%, annualised return in GBP

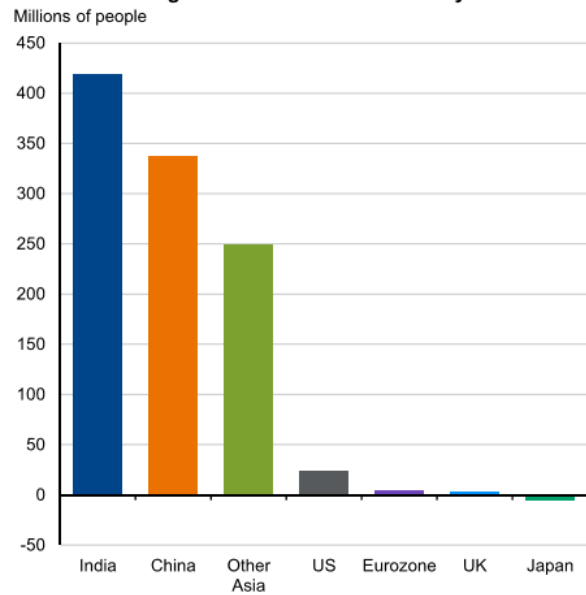


The charts below show the share of global growth and how for India and China this is expanding. It also shows the estimated change in consumer class by 2030.

**Share of global real GDP**



**Estimated change in the “consumer class” by 2030**

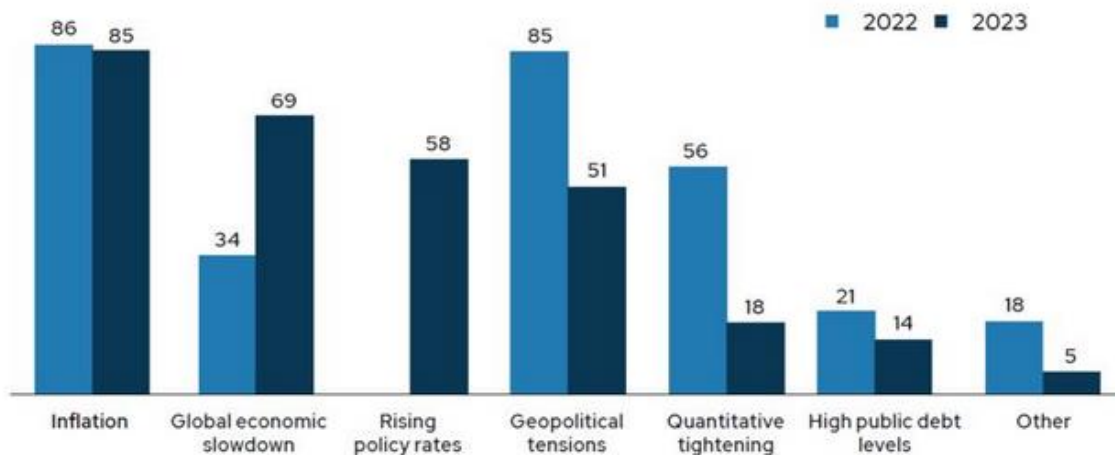


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## Big picture summary

The last 18-months have been difficult to navigate. The chart below shows what people are worried about.

What are the most important economic challenges affecting your investment approach over the next 12-24 months? Share of respondents, %



Source: OMFIF GPI survey 2022-23

\*Note: Rising policy rates not included in 2022

If we are taking a handful of points from this update, they are:

1. It seems in developed countries a recession is coming.
2. A recession is not bad for markets and could at last provide a recovery towards the end of 2023 / beginning of 2024.
3. Emerging markets have been a lost decade, but China is slowly coming back, and watch for the emergence of India.
4. Japan seems to be moving into a new era and benefiting from the move away from China.
5. China, Europe, and Japan could provide strong returns over the next decade vs the US and UK.

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*General disclaimer: The data has been sourced from external sources (the charts for example are from FE) and although we have looked to ensure this is as accurate as possible, we are not responsible for data they supply.*

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*Please also note past performance is no guide to future performance and investments can fall as well as rise.*

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