CIO believes investors should not lose sight of fundamental factors that would drive markets in a more sustained way while the election outcome remains uncertain. (UBS)

Focus on preparing portfolios for a lower-rate environment

16 July 2024, 2:17 pm CEST, written by UBS Editorial Team

US politics has dominated headlines in recent days. Following the attempted assassination of former US President Donald Trump over the weekend, he emerged in good spirits during the first night of the Republican National Convention in Milwaukee on Monday, alongside his choice for running mate announced earlier in the day, Ohio Senator JD Vance.

More headlines around the presidential campaigns can be expected in the coming weeks and months, as well as a pickup in market volatility. But we think investors should not lose sight of fundamental factors that would drive markets in a more sustained way while the election outcome remains uncertain.

The Federal Reserve is inching closer to the first interest rate cut since the pandemic. Fed Chair Jerome Powell said on Monday that recent inflation prints "add somewhat to confidence" that the pace of price increases is returning to the central bank's target sustainably. "We've had three better readings, and if you average them, that's a pretty good place," he said at an event at the Economic Club of Washington. Powell's comments followed the encouraging consumer price index data for June, which registered the first monthly decline since December 2022 and was the latest in a series of soft economic data that have increased the probability of a Fed rate cut in September. With both inflation and the labor market cooling, we expect the Fed to use the FOMC meeting at the end of this month to signal that it is prepared to begin policy easing.

Corporate earnings should prove durable amid increasing AI investment. We think the second-quarter reporting season should confirm a broadening out in earnings growth. For the S&P 500, we expect earnings to grow 10–12% year over year, the fastest pace since the first quarter of 2022. While the bulk of this is likely driven by big tech companies amid robust demand for artificial intelligence, trends are generally favorable across the S&P 500. We expect S&P 500 companies excluding the Magnificent 7 to post the first quarter of positive earnings per share (EPS) growth since 2022.

So while developments in US politics may contribute to market swings in the lead-up to the election, we think investors should focus on preparing their portfolios for a lower-rate environment amid technological advances. In our view, this means deploying excess cash to quality fixed income and ensuring sufficient exposure to quality growth stocks. We also think that a well-diversified portfolio including allocations to alternatives and gold can help investors navigate near-term uncertainty while maintaining focus on achieving long-term financial goals.

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Original report - **Political news masks fundamental market drivers, 16 July 2024.**