Market Concentration: Impact & Risks

Growing Markets, US Dominance

Since the low point of 2008, the value of global bonds and equities has grown to $255 trillion, more than 2.5x their starting value.

In share markets, those 16 years have also seen an expansion of the domination of the US market, to the extent that it now comprises almost 65% of the total value of global share markets. Europe and Japan have seen their combined share fall from 39% to 20%, within which the UK is now just 4% of global stock market value.

Within the developing world, China's star has collapsed in recent years, replaced by the rise of India, which has recently overtaken the UK both in the size of its economy, and the size of its stock market. Other than the obvious issue of that concentration of global stock markets in the United States, there has also been the concentration of returns in the US market in big technology.

While the technology sector is here to stay, is difficult to predict the full economic effects of AI and whether it will be the next industrial revolution, and a sea change in profitability for many companies and industries.

Concentration of Market Returns has been Significant

Over the first six months of 2024, the US stock market produced 75% of total global stock market return.[1] Within that, NVIDIA, was responsible for 59% of the US stock market return, and therefore 50% of total global market return.

Narrow market leadership is not that uncommon, but the level of concentration this year in high quality (but not necessarily cheap) companies, clearly represents a conundrum for investors.

To 'chase' a very narrow segment of companies on the basis of short term performance, or to maintain a more balanced approach on the basis that such periods rarely last, and that investors are ignoring significant investment opportunity in the rest of the US market, and the rest of the world.

Chasing current trends instead of sticking to investment fundamentals can be risky. This was evident in July/August when a weak employment report and unchanged interest rates triggered a sharp correction in "hot" market sectors.

US Interest Rates, Markets, and Recession, or Not?

Whether a US recession happens or not, the direction of travel is for some slowdown in the US, and therefore global, economy.

In itself that shouldn't be feared, provided the slowdown is managed along with a reduction in interest rates, a crucial point for the stock market over the next year.

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[1] As measured by the broadly based Wiltshire 5000 Index.

The Federal Reserve began easing rates in September, and we expect further cuts will take place later this year, the timing of which will likely be impacted by the US presidential election in November (as central banks are loathed to cut rates close to an election, as it is deemed to be too politically sensitive).

This is potentially very important for US, and therefore global, stock market returns over the remainder of the year.

Whither Now?

Market returns are expected to broaden beyond US technology, with other sectors and markets (including infrastructure and fixed income) benefiting from falling interest rates and an improved outlook.

Emerging markets have had a difficult time in recent years, partly because of issues in the Chinese economy. Lower US interest rates should mean a lower US Dollar however, and this has historically been good for emerging market investors.

The rather beaten up and unloved UK market, which is trading on low levels, may also see a revival, (though with the caveat that we have to see what the new Chancellor will announce in the autumn budget at the end of October).

Though most market commentators believe a US recession will be avoided, the global impact of US economic shifts remains a concern, as US market movements are often echoed worldwide - reinforcing the addage, “if America sneezes, the world catches a cold.”

That has never been more relevant than now, given how much the US dominates global markets.

Biography

Chris Sutton | Investment Manager

Chris is an Investment Manager and is responsible for Aubrey's Managed Portfolio Service. He has been with Aubrey since 2014.
Chris was Deputy Regional Director for Rathbone Investment Management in Edinburgh until 2013, having joined the firm in 1997. He was a member of Rathbones national Asset Allocation and Collectives Research Committees and has a significant background in alternative assets. Chris dealt specifically with adviser solutions and has particular experience in managing SIPPs. He joined Aubrey to establish its adviser and MPS services.
Chris is a Chartered Wealth Manager and Chartered FCSI.

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