

Economic & Market Round-up

A respite short-lived: despite some light relief for investors in July, August was a similar story to the rest of the year with both bonds and equities falling in many regions as central banks continued to grapple with inflation. Developed market equities underperformed Emerging markets with Europe being the hardest hit, down 4.7% (EUR), driven by heightened uncertainty and the ongoing energy crisis. The US gave up some of the positivity of last month, down 3.9% (USD), given the central bank comments on continued interest rates rises to fight inflation. More positively, Japan, Asia ex Japan and Emerging market equities were all up over the month, with EM Latin America performing best, up 2.2%. Emerging market debt also held up relatively well, down just 1.2%, in line with European High Yield. UK government bonds did not fare well, down over 8%, compared to the US at -2.5%. Given the weakness in Sterling, equity and bond markets fared relatively well in GBP terms except for the UK and Europe – good news for those overseas investments (unhedged).

Fighting inflation: the intentions from central banks are clear: tackle the soaring price increases despite the risk of an economic slowdown. The tactic being used by central banks to dampen inflation is to increase interest rates, thereby making borrowings more expensive and saving more attractive (all else being equal). This generally causes bond yields to rise (prices fall), given the expectation of higher interest rates and equities struggle through fear of recession and increased borrowing costs. The idea is that demand will be squashed, leading to a reversal of the current supply-demand imbalance and, hey-presto, the price of goods and services fall, bringing inflation back down. However, energy prices, particularly gas, remain elevated given the continued disruption, attributed to the invasion of Ukraine, impacting many areas across various supply chains, including food. Nevertheless, core inflation (excluding food and energy) remains elevated across many regions, and even though US inflation looks to have peaked, reducing from 9.1% in June to 8.5% in July, it remains high enough for the US central bank to justify a possible further rate increase of 0.75% in September.

Finding opportunities: Germany & China: Two of our active positions are Germany & China. China has struggled to recover from Covid as it continues to mandate as zero-covid tolerance policy, thereby imposing lockdowns as cases emerge. This is causing sluggish output from factories, amongst other disruption, thereby impacting supply chains around the world. In addition, China has been hit by record heat waves, causing drought, thereby causing further economic issues. China have recently announced increased support for the economy, as well as reducing increase rates, contrary to many other economies. Germany have of course had issues with the uncertainty over it's gas supply, as well as having a high reliance on global supply chains, thereby impacting equity performance. Specifically, German companies were negatively impacted by China's growth and supply chain disruptions (continued lockdowns in China impact global trade, with German being a beneficiary of globalisation). We continue to have high conviction in these areas given the relatively depressed valuations and the potential of each to benefit from the recovery-trade to come.

Performance

The Morningstar Multi-Asset Funds have performed relatively well this year (to end August), with the MA40 fund ranking 26th percentile in the IA Mixed 20-60% Shares peer group and MA60 and MA80 ranking 9th and 5th percentile in the IA Mixed 40-85% Shares peer group. Over the past 12 months the funds rank in the 26th, 9th and 4th percentile (MA40, MA60 and MA80). Since inception (30/11/2020) the funds have returned 0.10%, 7.65% and 14.45% (MA40, MA60 and MA80).

The Morningstar Managed Portfolios had a good month with all risk profiles outperforming the relevant ARC benchmark except for ESG Cautious and Moderately Adventurous. Our Income (including Governed) and Real Return portfolios have outperformed the relevant ARC benchmark year-to-date, as well as Moderately Cautious through to Adventurous portfolios within the Governed and Passive ranges, and Moderate to Adventurous in our Active range. Across 3 years, all portfolios have outperformed the relevant ARC benchmark except for the lowest risk profile in each range. Over 5 years, our Income range and all portfolios across our other ranges have outperformed the relevant ARC benchmark except for the lowest risk profile in each range that have a track record (all except for ESG). All portfolios that have a 7-year track record have outperformed their ARC PCI (Income, Real Return, Active and Passive).

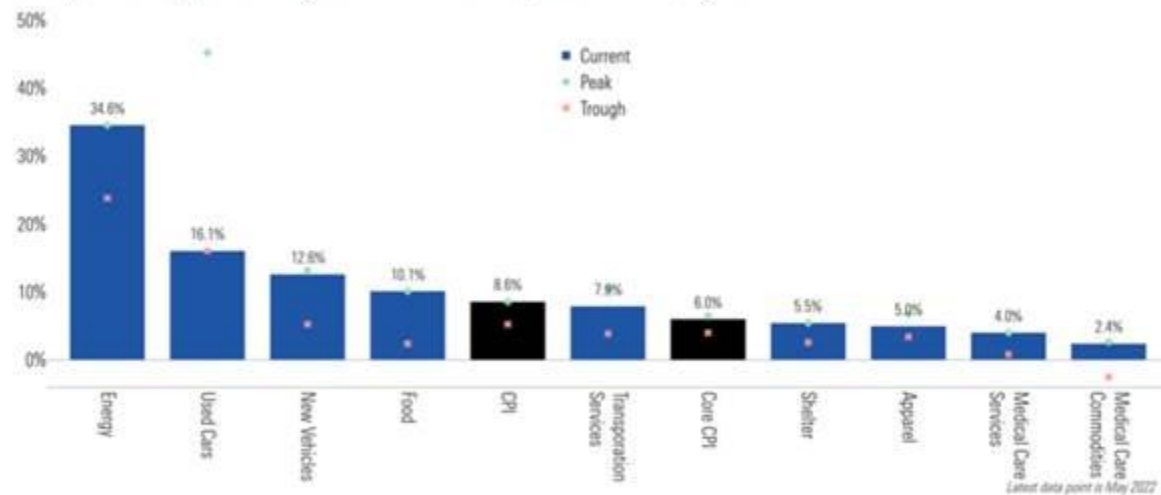
Outlook

Markets hate uncertainty, a factor very prevalent so far in 2022. Last month, investors were optimistic that given the risk of an economic slowdown, central banks would scale back the expected interest rate rises and may even cut rates next year. During August, central banks made it very clear that fighting inflation was still very much a priority. Combined with the ongoing geo-political risks (the Ukraine invasion and tensions between China and the west), as well as markets trying to decipher central banks' next moves, uncertainty is heightened, thereby causing huge amounts of volatility. The important thing to remember is that we invest based on long-term, research-driven analysis, and trying to time the market is unlikely to yield good results. In this environment diversification is your friend, and we balance our best ideas from a valuation perspective with the current temperature of the market, enabling the portfolios to perform well across the different scenarios we face, and ultimately helping clients achieve their financial goals.

Chart of the month

Consumer Price Index Components

Current year-over-year changes and 12-month peaks and troughs



Source: Economics, U.S. Bureau of Labor Statistics

US core CPI remains elevated despite food and energy pushing up overall CPI. With central banks tending to target inflation of 2% per annum, it remains high enough to justify another rate increase. Markets are pricing in a high chance of another 0.75% rate increase from the US central bank in September (next meeting 20-21 September).

CPD Webinar

The next webinar will take place on Wednesday 21st September – **“Portfolios that find value in all investing conditions”**. If you have not received an invite for the webinar, please get in touch.