MORNINGSTAR®

Economic & Market Round-up

Summary: the positivity that markets started the year with was short-lived as the tide very much turned in February. Broadly speaking, both bond and equity markets fell on the expectation that central banks may rise rates higher, or at least not be inclined to cut them any time soon, due to inflation remaining high and economies proving more resilient (reduced likelihood of a recession).

- For equity, developed markets outperformed emerging markets, with Chinese equities pulling the emerging market index lower on the back of heightened geopolitical risk. Nevertheless, the reopening of the Chinese economy should prove beneficial, and the market remains way off its 2021 peak. There were positive moves during the month from the UK and European equity markets, with the FTSE 100 reaching a new record high. The market gains were on the back of better economic news, the UK escaped a second quarter of negative economic growth in Q4 2022 (thereby avoiding a technical recession), and dollar strength was beneficial for companies with US earnings (buys more ££'s when converting back).
- Most bond markets posted a negative return with global government bonds falling 3.5%. High yield fell to a lesser extent than government and investment grade credit (company-issued debt). Yields moved higher on the broad expectation that interest rate may need to remain higher for longer to tackle inflation. Year-to-date, most markets remain in positive territory, or at least flat given the positive moves in January, although the UK government bond market slipped into negative territory following a particularly poor February, with year-to-date return now at -0.8%.

Recession reaction: the reduced likelihood of a recession sounds like good news, especially for equity markets, but as has been the case in the past few months, markets are attempting to price in the actions of central banks. While stocks don't like recessions, seemingly they like the prospect of higher interest rates even less. For stocks, higher interest rates mean that future earnings get discounted at a higher rate (revenues are worth less in the future), thereby diminishing the value of the company, as well as other issues like borrowing becoming more expensive. For fixed income, higher interest rates (or the expectation of, or even the changed scenario from what was previously priced in), causes yields to rise (investors demand more) and prices fall (due to the inverse relationship between price and yield).

Interest rates: given the amount of rate rises from central banks, it can be hard to keep up to date, therefore here's a rundown from three of the main central banks following the expected interest rates rises in February: 1) the US central bank raised rates to 4.75% (upper banding); 2) the European central bank raised rates to 3.0%; and 3) the UK central bank raised rates to 4.0%. Market expectations of future interest rate increases has risen given comments from central banks around inflation, which although falling, remains too high (central banks tend to target an inflation rate of 2%). Nevertheless, the UK central bank sought to reassure markets by stating that it should not be presumed further interest rate rises will be require. All we know for sure is that central banks will react to data, and markets will also aim to price in what is the likely expectation, which can cause volatility in the short term given the unknown.

Performance

The Morningstar Multi–Asset Funds performed well against the broader peer groups overall in February, in what was a disappointing month for markets, with only small pockets producing a positive return. The MA40 fund ranked 44th percentile in the IA Mixed 20-60% Shares peer group and MA60 and MA80 ranked 41st and 18th percentile in the IA Mixed 40-85% Shares peer group. One-year numbers continue to compare favorably against the peer group at 43rd, 19th and 6th percentile for the MA40, MA60 and MA80 respectively against the relevant peer group as detailed. Since inception (30/11/2020) the funds have returned -0.03%, 8.79% and 17.02% (MA40, MA60 and MA80).

In what was a disappointing month for markets, the Morningstar Managed Portfolios proved resilient in the Moderate through to Adventurous risk profiles across Active, Governed and ESG ranges, which outperformed the relevant ARC benchmark, while the Passive range outperformed across the Moderately Cautious through to Adventurous risk profiles. Medium to Longer term performance (3, 5 and 7 years, where applicable) remains strong across the range, with all but the majority of the lowest risk profiles outperforming.

Outlook

Investors have been put through a rough ride over the past few years, with increased volatility and few places to hide. Cautious investors have had an especially bumpy ride, with many still scarred from the bond market decline last year. Although the outlook may seem uncertain, and possibly a little gloomy, it's important to look forward, as markets do, and not let the recent volatility overtake clients' long-term investment objectives. We believe that the Morningstar portfolios and funds are well placed to navigate the many possible outcomes that we could face, and ultimately help clients achieve their financial goals.

For more of our insight, we have recently released our 2023 Outlook, which highlights the most important issues facing investors, provides insights from our research, and addresses some topics relevant to client decision making as we enter 2023.

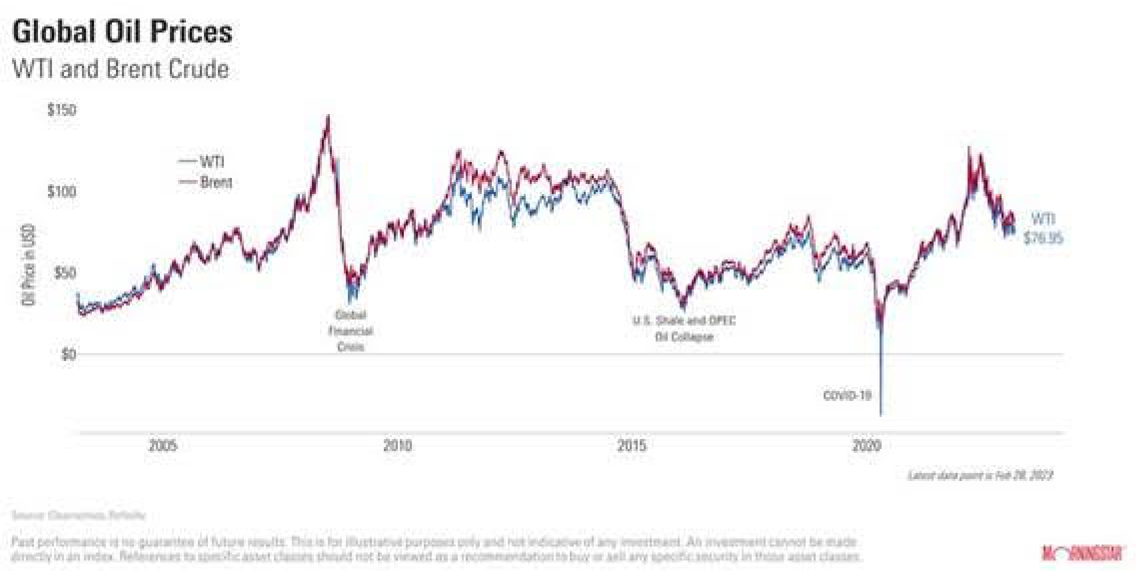
Credit Suisse

Dan Kemp reacts to the sale of Credit Suisse, and surmises that the end of the bank as we know it has been a long time coming.

Credit Suisse reaction

Chart of the month

Wholesale energy prices have fallen considerably from their peaks, including both oil and gas prices. Not only will this be helpful to households (although not right away), but it is also beneficial for economies given the cost of energy will be a lesser drag on company revenues, particularly those within manufacturing sectors. Gas prices have fallen 85% from their peak in August last year when it was feared that the ceased exports from Russian could cause huge disruption. The fall in energy prices has been helped by a milder winter in Europe, sufficient storage facilities and use of alternatives.



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