Wealth Management
Weekly Market Update

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Market Update

Markets returned to positive territory this week, supported in part by progress on the Biden stimulus bill. However, chair of the Federal Reserve Jerome Powell's speech, with a lack of updates to current policy, disappointed investors leading to a sell-off on Thursday afternoon. US equities rose +1.7% in Sterling terms. UK equities rose +2.5%, with UK equity markets benefiting from rising oil prices. Emerging Markets grew +0.9% in Sterling terms, although this was a more moderate +0.1% in local currency terms. Globally the best performing sector was Energy, whilst IT was the worst performing, as the rising yield environment impacted valuations. Japanese equities rose +1.0% The US 10Y yield continued its rise, up 16.1 bps to 1.6%, while the UK 10Y fell 6.4bps to 0.8%. Gold fell -1.1% on the week. Oil rose sharply, up +8.4% on the week to $66.5 following the OPEC meeting where it was decided to hold production at current levels, when a rise in production had been anticipated.

UK Stocks	US Stocks	EU Stocks	Global Stocks	EM Stocks	Japan Stocks	Gilts	GBP/USD
▲ +2.5%	▲ +1.7%	▶ 0.0%	▲ +1.0%	▲ +0.9%	▲ +1.0%	▲ +0.9%	▼ -0.7%

all returns in GBP to Friday close

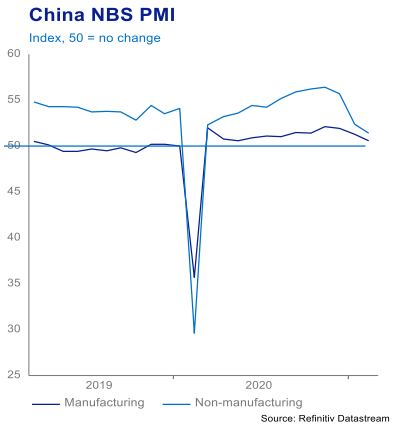
Macro News

- Inflation in the Euro area remained stable in January at 0.9%, while core inflation stood -0.3% lower than the previous month, at 1.1%. In addition, retail sales were very weak during the same month, dropping by -5.9% and -5.1% in the Euro area and EU respectively.
- Rishi Sunak announced the UK's budget. This includes £65bn government spending in the next two years to support employment and the country's recovery, which will be followed by rises in corporate and income taxes of £25bn a year by the middle of the decade. The rise in taxes will serve to pay back the higher debt burden that piled up in response to the pandemic.
- Both Federal Reserve Chair Jay Powell and Governor Lael Brainard issue comments suggesting they don't expect a tightening of rates any time soon.

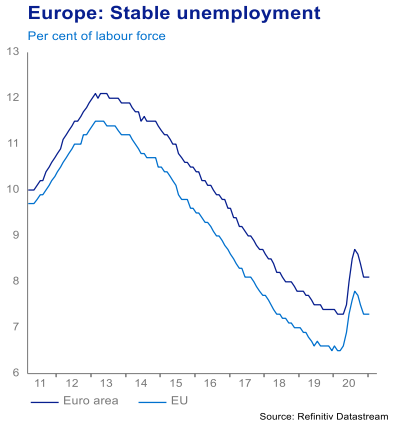
The Week Ahead

- The European Central Bank's (ECB's) monetary policy meeting is expected to take place this week, with officials expected to discuss the recent steep rise in government yields amid rising inflation expectations. The focus remains on whether the Central Bank will increase the firepower of its asset purchasing program or not.

Week in Charts



China's Purchasing Managers' Index (PMI) data came in below expectation for both manufacturing and non-manufacturing sectors. Despite lower index values relative to December, both sectors still exhibited growth figures. In fact, manufacturing PMI stood at 50.9 while services PMI stood at 51.5.



Unemployment remained stable at 8.1% and 7.3% in the Euro area and EU respectively. Part time work subsidy schemes seem to have shielded the labour markets, thus easing the impact of the restrictions in the hospitality sector and non-essential shops.

View From the Desk

Between a very generous post-Brexit and Pandemic budget, the approval of $1.9tn worth of stimulus in the US and a continuously steepening yield curve, last week offered a lot of news. However, in terms of long-term investing, none was as important as Jerome Powell's laconic "patient" response to rising fears of inflation. True to their Pavlovian reflexes, traders were hoping that the recent bout of volatility could mean extra monetary accommodation and were disappointed when the Fed stayed put. Subsequent price action was negative.

While it is true that cost pressures over the past few months have begun to spill over to consumers, and could well be exacerbated by rising oil prices, it is apparent that the Fed is keeping its eye on the ball, which is long rather than short term inflation. Post-stimulus unemployment and growth concerns, vaccine nationalism and the rising possibility of vaccine-resistant Covid-19 strings and belief that supply chains will adjust quickly are on the Fed's side of the fence. Current data and market pressures are on the other.

Where investors couldn't find income, now they are faced with a dilemma. If one stands with central banks - historically there has been little other choice for long term portfolio managers - and believes that this "inflation scare" will go away soon, then one can view the bond market as increasingly providing investors with entry points. However, fixed income is still expensive relative to equities and the risk/reward profile at an index level is still not hugely attractive, especially at the lower end of the credit spectrum. Investors might just yet prefer equity income as companies scramble to return to a regime of good dividend payments and buybacks.

There is still some way to go before asset allocation committees can be overweight bonds again. And when they do, they should be wary of the impact of rising rates to corporations, or indeed countries, with over-burdened balance sheets that need to refinance debt. The business world and nations have used debt to weather the pandemic and every day that goes by brings the inevitable debtor-creditor showdown a tiny step closer. And this, for us, is the heart of the matter. If our analysis suggested that yield curve steepening was reflecting credit fears, we would have said that it is premature, but nevertheless a valid concern. As long as people are speaking only of inflation, then we feel more comfortable staying on the central bank's "patient" side of the fence.

David Baker, CIO

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