Wealth Management
Weekly Market Update

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Market Update

A continuation of the risk-on attitude in markets last week saw equity indices broadly climb higher. Globally, all sectors were positive, with the exception of healthcare. US stocks rose +1.8% despite disappointing demand for durable goods and new homes, and UK equities also rose +1.2% despite soaring inflation and disappointing retail sales data. European stocks fell -1.8% as the war in Ukraine is beginning to significantly impact on European economies. Data released last week revealed that business expectations have plummeted, both input and output costs continue to climb and pressures on supply chains show no signs of easing. The bond market also continues to bear the brunt of increased concern over the economic outlook. The UK 10Y gilt yield rose another 20bps, whilst the yield on the US 10Y treasury yield rose 32bps, finishing the week at 2.47%. On the commodities front, oil surged last week, up +10.2%, whilst industrial metals prices rose another +1.3%, which will only serve to exacerbate current inflation trends. The increased economic uncertainty has also been an environment in which gold has prospered, recording a gain of +1.9% last week to finish at $1,944.3/oz.

UK Stocks	US Stocks	EU Stocks	Global Stocks	EM Stocks	Japan Stocks	Gilts	GBP/USD
▲ +1.2%	▲ +1.8%	▼ -1.6%	▲ +1.3%	▲ +0.2%	▲ +1.2%	▼ -1.7%	▲ +0.0%

all returns in GBP to Friday close

Macro News

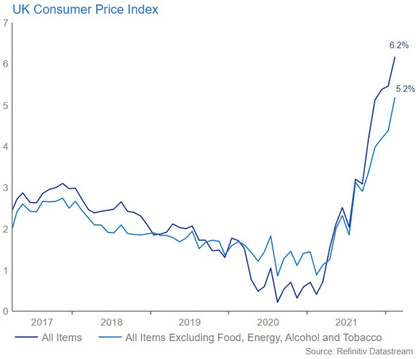
- UK inflation surged to 6.2% year-on-year in February, a 30 year high that beat economist expectations of 5.9%. Core inflation, a measure excluding volatile components such as food and energy, also rose robustly to 5.2% from a previous level of 4.4%. With oil prices soaring, and regulated electricity prices due to increase, these figures are widely expected to increase further over the next few months.
- Durable goods orders in the US fell by 2.2% in February. A large contributor to the fall was a 30% drop in commercial aircraft orders, owing to a large fall in orders reported by Boeing. Defence aircraft orders were a different story, rising by 60% over the month.
- US new home sales dropped by 2% over February as house prices rose due to increasing costs of materials and supply chain issues, and increasing mortgage rates following the Federal Reserve's recent interest rate hike. The fall is the second consecutive monthly decline in new home sales as first time buyers are being squeezed out of the market due to tighter buying conditions.

The Week Ahead

- US Employment data will be in focus next week as the Bureau of Labor Statistics releases its jobs report. In Europe, investors will be watching for the Eurozone inflation rate, which will reveal the effect that the Russian invasion of Ukraine has had on prices.

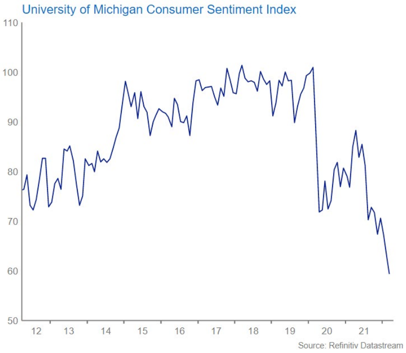
Week in Charts

UK Inflation Surges to 6.2%
UK Consumer Price Index



UK inflation rose to a 30 year high of 6.2% in February, while core inflation rose to 5.2%. The increase was driven by soaring prices for energy, petrol, food and durable goods. Food inflation was 5.1% year-on-year, while clothing rose by 8.9% over February.

Consumer Confidence Plummets
University of Michigan Consumer Sentiment Index



Consumer sentiment in the US has continued to fall as inflation soars, disposable incomes dimmish, and the war in Ukraine continues. This was reflected in the Michigan consumer sentiment index, which fell to a decade low level of 59.4 last week.

View From the Desk

It takes a confluence, rather than individual, risks to cause catastrophe, as any veteran of the Global Financial Crisis will attest. We believe that there's a mounting probability that we are seeing such a confluence of risks now, one that could significantly hurt growth:

- A weak economic backdrop: Economies had barely recovered from the pandemic before the Ukraine war caused prices to spike.
- Inflation in raw materials has become much broader.
- Policy mistakes from central banks who might suffocate growth instead of combatting inflation.
- Policy mistakes from Government Treasuries who may opt for reducing debt instead of fostering growth.
- A possible 'stealth' Chinese slowdown. China spent the last year trying to burst a Real Estate Bubble, both commercial and residential. The US (1996-2006), Spain (1985-2008), Japan (1985-1991) all experienced deep recessions immediately following the bursting of real estate bubbles. To the real estate pressures one must add higher energy costs, a clampdown on tech and other sectors, high municipal debt, wild demand fluctuations and a fresh Covid outbreak.

In this environment, we have to boldly state that we are not sure what the Fed means by suggesting it can "engineer a soft landing". Even without the confluence of so many anti-growth factors, western economies are driven primarily by consumption, which means they are influenced by sentiment.

Instead of keeping hopes up for just slower growth, the world should prepare for the possibility of a bona fide global economic recession. It could be slowed possibly by bank de-regulation or a swift Chinese economic rebound, however we have seen evidence of neither yet.

What does this mean for asset allocators?

First of all, we are raising the possibility of a significant slowdown in global growth, not the certainly. We think the scenario is gaining momentum, but a lot of the above conditions would have to play out on their current trajectory and at the same time for the scenario to materialise.

A global recession is a systemic event, which is bound to affect all assets. Maintaining cash is not a good choice in a high-inflationary environment. Stocks will suffer from slow growth, bonds from inflation and commodities from high volatility and speculation. As in 2008, this is probably a tunnel which all portfolios will have to go through.

The point of asset allocation is the belief that on any given major event, there's high uncertainty. So we can't accurately predict what will outperform and what will not. Marginal differences between portfolios from different vendors are as much the result of randomness as they are of foresight. No one strategy or manager has ever emerged that can outperform in any and all market environments. But by and large, those who remain invested with a diversified portfolio fare much better than those who don't, or those who attempt to time the market (despite all evidence suggesting that this is virtually impossible).

At its core, asset allocation is the belief that, in the face of all difficulties, capitalism adapts in a way to deliver returns. The point is not lost on those who clearly see the possibility of an economic recession, but US equities only marginally below their all-time highs.

David Baker, CIO

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