ALBERT E SHARP

INVESTMENT MANAGEMENT & STOCKBROKING

Market Commentary

March 2023

Published: 13/04/2023

Monthly returns and summary

Index	Portfolio Benchmark Risk Level	31/03/2023	1 Month	3 Months	1 Year	3 Years	5 Years
ARC Cautious	Low Risk	194.28	+0.6%	+1.7%	-3.8%	+9.2%	+8.5%
ARC Balanced	Medium Risk	237.50	+0.2%	+2.2%	-4.4%	+17.2%	+14.1%
ARC Steady Growth	Medium High Risk	282.28	-0.1%	+2.5%	-4.7%	+23.9%	+19.9%
ARC Equity Risk	High Risk	328.35	-0.4%	+2.6%	-5.0%	+30.7%	+25.2%

Source: ARC. NB: Price returns only, excluding dividends. Figures based on ARC estimates.

Index	Region / Asset Class	31/03/2023	1 Month	3 Months	1 Year	3 Years	5 Years
UK 100	UK	7631.74	-3.1%	2.4%	1.5%	34.6%	4.8%
UK All Share	UK	4157.88	-3.4%	2.0%	-0.7%	33.8%	4.5%
Dow Jones Ind Avg	US	33274.15	1.9%	0.4%	-4.0%	51.8%	28.3%
S&P 500 Index	US	4109.31	3.5%	7.0%	-9.3%	59.0%	45.0%
Nikkei 225	Japan	28041.48	2.2%	7.5%	0.8%	48.2%	32.2%
MSCI Europe Ex UK	Europe	182.81	0.5%	9.5%	2.1%	45.4%	26.8%
MSCI Asia Ex Japan	Asia	644.53	3.3%	4.1%	-11.0%	15.0%	-2.9%
MSCI Emg Mkts (£)	Emg Mkts	610.45	0.9%	1.1%	-4.9%	25.7%	8.7%
MSCI World Index (£)	Global	2791.44	2.8%	7.3%	-8.6%	50.7%	32.4%
UK Conventional	Gilts	3079.84	2.9%	2.0%	-16.3%	-24.9%	-17.5%
UK Index-linked	Gilts	4172.43	6.2%	4.3%	-26.7%	-21.2%	-19.5%
FTSE All-Share Real Estate Investment Trust Index	Property	1986.96	-8.6%	-2.3%	-33.8%	-7.9%	-25.0%
WTI Crude ($/Barrel)	Oil	75.67	-1.8%	-5.7%	-24.5%	269.5%	25.8%
Gold Spot $/Oz	Commodities	1969.28	7.8%	8.0%	1.6%	24.9%	52.4%
£1 = US$	Currencies	1.2337	2.6%	2.1%	-6.1%	-0.7%	-5.4%
£1 = €	Currencies	1.1374	0.0%	0.7%	-4.2%	1.1%	-2.1%
£1 = Yen	Currencies	163.82	0.1%	3.4%	2.5%	22.6%	13.4%

Source: Bloomberg. NB: Price returns only, excluding dividends

Index	Region / Asset Class	31/03/2023	1 Month	3 Months	1 Year	3 Years	5 Years
FTSE All-Share Investment Companies Index	Diversified	11,353.63	-3.4%	-2.1%	-12.4%	25.6%	11.0%
Latest Weighted Average Discount	-16.4%						
Previous Month Weighted Average Discount	-14.4%						
Average Discount Since January 2020	-6.3%						

Source: Bloomberg, Refinitiv. NB: Price returns only, excluding dividends

General Comments

Had this commentary been written a few weeks ago the above numbers would have looked very different. Now, if one was to only look at the figures, they might assume it was an uneventful month. European equities (The Euro Stoxx 50) are trading at 52-week highs, not something that would make sense a couple of weeks ago when there were (arguably exaggerated) allegations of a banking crisis in Switzerland.

Ultimately, March was a positive month for most asset classes. Equities had a good month as did bonds. European and Japanese equities are now showing strong year-to-date returns, while the tech-heavy US Nasdaq index is up nearly 16% in 2023. The FTSE 100 weighed on the UK market this month, following a tough comparator of an all time high the previous month and some concerns over various banks and financials, which represent a large weight in the UK index.

In commodities, cyclicals such as oil and copper initially traded weaker during the month before recovering most of those losses, while gold continued its recent strong run with additional popularity among investors. Meanwhile, sterling made further gains against the US dollar.

UK Commentary

The Bank of England went off-piste this month when they uncharacteristically released a prediction that wasn't entirely filled with doom-mongering. They said they expect that the UK is no longer entering an immediate recession, in line with what the OBR predicted a few days earlier. The bank expects both global and UK growth to be stronger than previously expected, with the UK's economy expanding rather than contracting in coming months.

Simultaneously, they increased rates for an 11th time in a row, this time by a smaller amount of 0.25%. This takes the UK base rate to 4.25%, with predictions now implying that we are near the top of this hiking cycle and that rates are unlikely to go too much higher from here.

In political news, Sunak defeated Tory rebels (which included 3 recent prime ministers) to get his "Windsor Framework" Northern Ireland deal through parliament, meaning we finally have some sort of arrangement with the EU on how to handle this contentious issue post-Brexit. We hope this is a sign of smoother relations moving forwards for all parties.

As mentioned below, the government and treasury were forced to act quickly to find a suitor for the UK branch of Silicon Valley Bank (SVB). HSBC stepped up and all was sorted over the weekend before markets could reopen.

North America Commentary

The headlines from North America in March were centred around banks. SVB seemed to have started worries with what looks like an old-fashioned bank run. This is a bank with a very concentrated client base and indeed plenty of mark-to-market losses from lending to similar clients. It has concentration risk built into its business model and suffered as a result.

This seems to have triggered worries around various regional and smaller banks. However, the Federal Reserve acted swiftly and encouraged major banks to support their smaller peers. Deposits were believed to have been guaranteed (although there was some ambiguity here for legal reasons) and, crucially, collateral was allowed to be placed with the central bank at par value, which helped greatly given the amount of paper losses showing on bank balance sheets as a result of rapid interest rate rises.

The Federal Reserve also increased interest rates by 0.25%, taking their key rate range to 4.75-5.0%, the highest level since September 2007. Notably, chair Powell said that tightening credit conditions could be equivalent to, or even greater than, an interest rate hike. This implies there may not be many further rate rises to come and that the above pockets of stress in the banking system could have the very effect that interest rate rises were intended to have.

Elsewhere, pharmaceutical giant Pfizer made one of the largest pharma deals in history by agreeing to pay £43bn in cash for biotech firm Seagen.

Europe Commentary

Europe saw a mixed bag in terms of inflation data releases. For example, Spain and France recorded sharply falling inflation while Germany notably exceeded predictions with a 'hot' reading. Overall, Eurozone inflation cooled to 6.9% in March, down from 8.5% previously and below the 7.1% expected by economists in a Bloomberg poll. However, core inflation (which excludes volatile items such as food and energy) continued it's upward move to 5.7%, a fresh all time high. This is perhaps a sign of the degree to which inflation can become embedded with wage increases and how it rarely moves in a straight line.

Elsewhere, The Swiss authorities moved quickly to arrange a 'shotgun wedding' between Credit Suisse and UBS, which saw the former taken over by the latter. The writing has been on the wall for Credit Suisse for a very long time and it came as no surprise to many. There was some controversy as some bondholders felt rules were re-written to prioritise shareholders. Ultimately though, the authorities acted quickly and efficiently to protect depositors.

Both the European and Swiss central banks rose interest rates 0.5% despite the Credit Suisse issue. It was interesting that the ECB said that further rate setting decisions would be based upon data coming out rather than guiding what their next move would be, as had been the custom previously.

Asia Pacific Commentary

China announced a large political reshuffle which is seen by many as a consolidation of power by President Xi. They also announced a 5% GDP growth target for 2023, the lowest target for more than three decades.

In other Chinese news, there are reports that behemoth conglomerate Alibaba may split into 6 distinct businesses in an attempt to unlock shareholder value. The market reacted positively to the news, adding roughly 10% to the share price in the following days.

In Japan, outgoing central bank governor Kuroda had his final meeting and declared his decade of ultra-loose monetary policy a success, leaving his successor Kazuo Ueda to implement any possible change of direction. This comes as their 'core-core' consumer price index showed inflation had reached a 41-year high, albeit at just 3.5%.

Emerging Market Commentary

The Credit Suisse debacle even reached Saudi Arabia, as Saudi National Bank (SNB) bought a 9.9% stake in the Swiss company last year. SNB chair Ammar Alkhudairy was also forced to resign having given a questionable TV interview regarding Credit Suisse in which he stated they wouldn't be buying any more shares, which certainly didn't help the issue.

Elsewhere, India's growth slowed for a second consecutive quarter for October-December, to 4.4%. However, inflation in the country fell in February to 6.4%

Lastly, it is worth highlighting that The International Criminal Court finally issued an arrest warrant for Russian president Vladimir Putin over the kidnapping of Ukrainian children.

Chart of the month – Investment Company Discounts

This chart from the AIC highlights how discounts to net asset values are significantly wider on average than three years ago at the end of March 2020, merely a few days after the UK's first COVID lockdown was announced.

This is a quite remarkable and historically unusual level of irrationality. We can, on average, buy £1 of investment company shares for 88p. We believe this is an extremely compelling entry point and will look immensely good value when we look back in a few years' time.

Investment Profile – North American Income Trust (NAIT)

Fran Radano of Scottish fund management company abrdn has managed this value-focussed strategy for over a decade and has generated a roughly 10% total return per annum over that period, as well as offering a high degree of resilience in tougher times thanks to their disciplined approach.

When we last spoke to Fran in November, he called his approach "growth at a Scottish price", although he admits he stole the phrase from a colleague. The rigorous approach to valuation results in a portfolio which is far cheaper than the index on average and pays a much higher dividend yield, around 3.6% currently. This is also a dividend which has now risen for 11 consecutive years, making NAIT an upcoming dividend hero according to the AIC.

They achieve this by focussing on US-listed large cap companies such as soft drinks giant Coca-Cola, healthcare conglomerate CVS Health and life insurer MetLife. While these are enormous companies, the likes of Apple, Alphabet and Amazon which dominate US stock indices make them look somewhat small in comparison. The differentiation from many typical indices that NAIT brings offers an element of diversification to portfolios and some excellent alternative sources of returns.

Investment Team's thoughts

If one looks at the above three-year performance numbers they might be surprised. This is an unusual period to choose given the effects of the UK's initial COVID lockdown, but it does raise the issue that prior periods of panic have seen irrational behaviour in the markets. Those who kept their composure and were buyers during March 2020, or at least not sellers, would have done remarkably well. Those who got caught up in panic will certainly have regretted it.

This is an age-old tale and one that we could apply to days within this month. The point is that alarmist headlines have always been a factor and those who have seen the wood through the trees have always done better than those who pay too much attention to reactionary statements.

As we are going through one of the most aggressive monetary tightening cycles ever seen it is important to keep in mind that it would be abnormal if various pockets of the market did not struggle to adjust to this new environment. Companies (banks in recent weeks) with esoteric risks or that have been poorly managed in recent years will likely struggle.

However, we think this is normal. In fact, it is exactly this type of environment which emphasises why we are so focussed on investing in good businesses with high quality management teams. It would be fair to say that SVB and Credit Suisse would not have fallen into these categories.

Volatile markets do not "excite" us, we would prefer smooth and rational progress forwards. They do, however, give us exciting opportunities to purchase assets at valuations which we believe will look like excellent value in coming years. This is what we are focussed on, as we have been in the past and as we will be in the future. We continue to strive to be the rational actors who ultimately prosper over the longer term.