ALBERT E SHARP

INVESTMENT MANAGEMENT & STOCKBROKING

Market Commentary

September 2022

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Monthly returns and summary

Index	Portfolio Benchmark Risk Level	31/08/2022	1 Month	3 Months	1 Year	3 Years	5 Years
ARC Cautious	Low Risk	191.68	-2.5%	-2.8%	-6.9%	+1.7%	+5.4%
ARC Balanced	Medium Risk	234.55	-2.2%	-2.5%	-7.6%	+5.0%	+10.8%
ARC Steady Growth	Medium High Risk	278.69	-1.8%	-2.1%	-8.2%	+7.9%	+15.9%
ARC Equity Risk	High Risk	323.58	-1.7%	-2.1%	-9.4%	+11.0%	+20.3%

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

Index	Region / Asset Class	31/08/2022	1 Month	3 Months	1 Year	3 Years	5 Years
UK 100	UK	6924.19	-4.9%	-3.4%	-2.3%	-6.5%	-6.1%
UK All Share	UK	3773.54	-5.8%	-4.2%	-7.0%	-7.1%	-6.8%
Dow Jones Ind Avg	US	29225.61	-7.3%	-5.0%	-13.6%	8.6%	30.4%
S&P 500 Index	US	3640.47	-8.0%	-3.8%	-15.5%	22.3%	44.5%
Nikkei 225	Japan	25937.21	-7.7%	-1.7%	-11.9%	19.2%	27.4%
MSCI Europe Ex UK	Europe	149.86	-7.5%	-5.3%	-17.6%	-1.4%	0.5%
MSCI Asia Ex Japan	Asia	556.58	-13.2%	-14.8%	-30.5%	-9.9%	-15.8%
MSCI Emg Mkts (£)	Emg Mkts	598.09	-7.2%	-3.0%	-12.4%	4.6%	10.7%
MSCI World Index (£)	Global	2401.32	-8.6%	-5.7%	-20.1%	10.2%	20.0%
UK Conventional	Gilts	2940.45	-8.9%	-13.7%	-24.0%	-26.8%	-16.5%
UK Index-linked	Gilts	3915.00	-14.6%	-16.6%	-31.8%	-31.2%	-17.4%
AES Property Index	Property	134.75	-1.2%	-2.3%	6.7%	-0.1%	4.8%
FTSE All-Share Real Estate Investment Trust Index	Property	1874.71	-21.6%	-23.8%	-32.6%	-30.8%	-29.8%
WTI Crude ($/Barrel)	Oil	81.53	-9.0%	-22.9%	8.7%	50.8%	57.8%
Gold Spot $/Oz	Commodities	1666.67	-2.6%	-7.8%	-5.1%	13.2%	30.2%
£1 = US$	Currencies	1.1084	-4.6%	-9.0%	-17.7%	-9.8%	-17.3%
£1 = €	Currencies	1.1355	-1.8%	-2.3%	-2.4%	0.7%	0.1%
£1 = Yen	Currencies	160.14	-0.8%	-3.1%	6.8%	20.6%	6.2%

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

Index	Region / Asset Class	31/08/2022	1 Month	3 Months	1 Year	3 Years	5 Years
FTSE All-Share Investment Companies Index	Diversified	11,019.32	-8.0%	-3.4%	-20.3%	4.0%	13.8%
Latest Weighted Average Discount	-16.5%						
Previous Month Weighted Average Discount	-10.1%						
12 Month Weighted Average Discount	-5.1%						

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

General Comments

September was a month dominated by its final few days. The latest Chancellor's so-called "Mini Budget" seemed to mark the start of a tumultuous time in many markets. However, quite how much of the volatility can be ascribed purely to this political event remains uncertain even now. It is likely less to blame than many journalists who seek simple cause-and-effect solutions would lead people to believe though, as many technical factors and longer-term trends were at play.

Somewhat unusually for a period dominated by headlines of market distress, equities were fairly calm. In fact, the areas of pain were traditionally lower risk assets and currency markets. UK government bonds in particular had an eventful month, or few days at the end of it. Furthermore, defensive assets such as Infrastructure and Property also struggled, arguably as a result of government bond yields rising. Meanwhile, sterling grabbed headlines for sharp moves but, as explained later, currencies almost across the board lost value against the US dollar.

Once again, the ARC Private Client Indices struggled as a result of the bond exposure hurting the lower risk mandates, while the relative outperformance of equities helped the higher risk portfolios to not fall as hard.

Please note the date of publishing and that not all markets will have closed for the month at time of writing. Please therefore forgive any small statistical errors, things have moved very quickly in the past few days and continue to do so.

UK Commentary

As mentioned above, Kwasi Kwarteng's first acts as Chancellor were not well received by most markets, commentators or even many of his own MPs. While we will always be hesitant to get drawn on political issues, it is worth noting that whatever one may think of these policies, that the timing of them may be ill advised. Perhaps the best reflection of this is not in fact any market volatility, but the fact that Labour surged to their biggest lead in YouGov polling ever. A thirty-three-point (this is not a typo) lead is quite remarkable, especially given the Conservatives had a roughly ten-point lead last autumn. This is quite the swing and obviously a huge challenge for new Prime Minister Liz Truss.

As quickly as politics can move though, markets can move quicker, and September certainly proved that in the UK. Government bond yields saw their sharpest ever recorded daily move & sterling managed to lose several pennies against the US dollar in a matter of days, and then recovered. More on these issues below.

Also, the Elizabethan era came to an end as HM Queen Elizabeth passed away. Much has changed since she ascended to the throne in 1952. As we discuss later, it is worth considering the global prosperity in that time and remembering that that the long-term progress in recent decades has been astounding.

North America Commentary

The US dollar is often seen as a 'safe haven' and seems to have proven so once again in September, continuing the pattern of this year. The fact that this happened despite US CPI inflation coming in at 8.3% rather than the predicted 8.0% really shows the strength of the dollar at the moment.

This may be partially explained, however, by the Federal Reserve's decision to increase their base rate to 3 to 3.25%, meaning US treasuries (their government bonds) now offer investors a fairly attractive return. This offers further support to the dollar.

One interesting and perhaps under-reported story came as conglomerate Amazon announced they aim to be able to run all operations on 100% renewable energy by 2025. They are undertaking 71 new renewables projects to try and achieve this.

Europe Commentary

European equity markets were generally quieter than American and Asian markets over the month (you can include the UK in this as well) as stocks outperformed on a local currency basis. However, once again, the strength of the US dollar means this European outperformance was masked by currency losses.

Italy has a new right-wing coalition government headed up by Giorgia Meloni, whose allies include names such as Berlusconi and Salvini. She has also previously praised Mussolini and had some very choice words to say about French President Emmanuel Macron. This election followed Sweden's similar vote to elect a right-wing block earlier in the month.

Elsewhere, there were battlefield victories for Ukraine as they reclaimed land from Russian invaders. This led to mobilisation & conscription from Russia and seemingly rising internal tensions.

It is also worth highlighting that Swiss consumer goods giant Nestlé (who own the likes of Nescafe, Cheerios and Häagen -Dazs) posted record profits in the UK this year despite rising costs, as they have managed to increase prices over 10%. This highlights, once again, the advantage of having strong brands and pricing power, especially in an inflationary environment.

Asia Commentary

Japan intervened in currency markets to prop up the yen against the US dollar for the first time since 1998. They are also now the only country in the world to retain negative interest rates.

Meanwhile, China's state bank actually cut base rates for the first time since 2015. This was widely considered an attempt to promote growth in response to disruptive COVID-related lockdowns and a struggling property market. The World Bank obviously agree with this as they cut their GDP growth predictions for China to 2.8% next year. Meanwhile, for the first time since 1990, many regional developing countries in Asia are projected to grow faster than China.

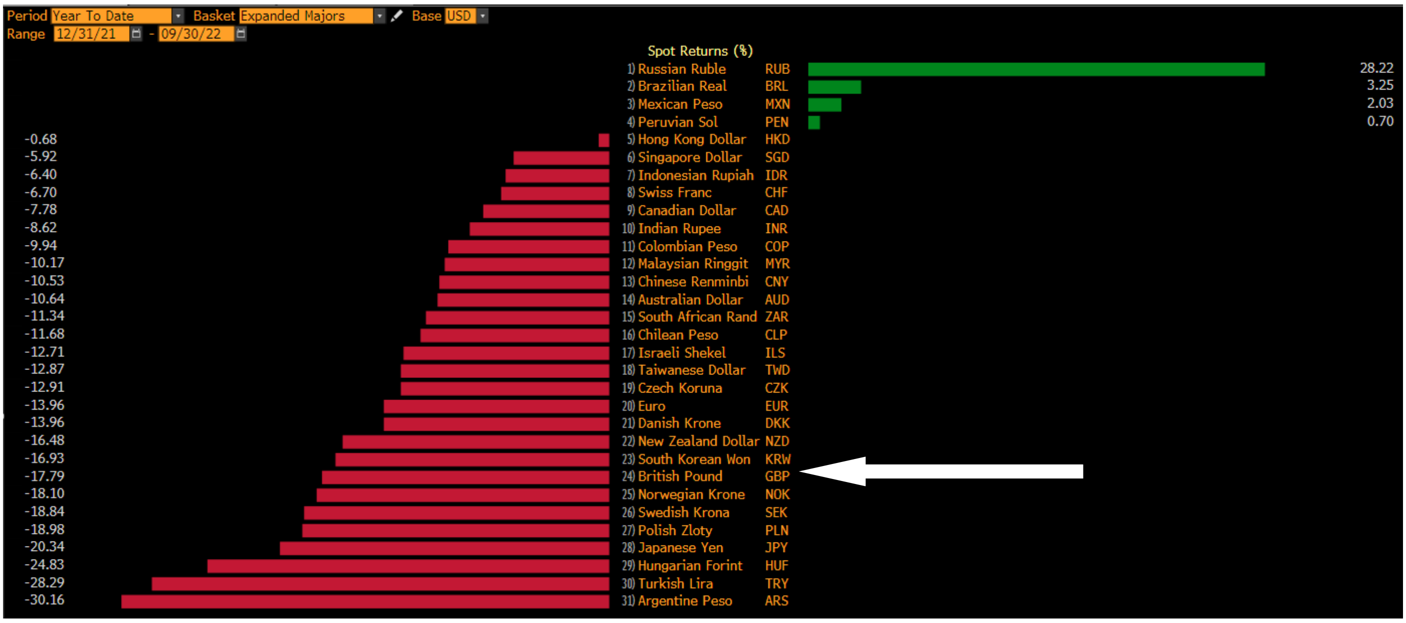
Emerging Market Commentary

Turkish inflation topped 80% for the first time in 24 years, but their central bank went against convention and actually cut interest rates.

Elsewhere, in Brazil it looks like the incumbent president Bolsonaro may be displaced by former president Lula. Brazil is the world's tenth largest economy and feeds around 10% of the world's population with its agricultural exports, so this is important to keep an eye on.

Charts of the month

Foreign Exchange Rates Vs The US Dollar



The above chart from Bloomberg shows the performance of the 31 major global currencies against the US dollar since the start of 2022. Please note the Russian Ruble is no longer freely traded.

We believe this highlights the fact that sterling (highlighted with a fairly rudimentary arrow) is not alone in losing value against the titan that is the US dollar. While many blamed Kwarteng, this data paints a broader picture. For example, and just considering September, the Norwegian Krona lost significantly more ground against the US dollar in the month than sterling did (nearly twice as much, in fact), which cannot be much to do with the actions of the UK's Chancellor. In fact, sterling was 17th out of these 31 currencies in September, actually improving its relative performance this year so far.

Sterling did momentarily hit an all-time low against the US dollar in the month, around $1.035 per pound. That is significant and was likely partially a reaction to recent government policy announcements. However, it was back to it's pre "mini budget" levels around $1.12 a matter of days later.

The US dollar is often in demand during times of risk-off sentiment, as they have a large and typically stable economy. Many commodities, such as oil, are also priced in dollars. Furthermore, their central bank has been fairly aggressive in increasing their interest rates and one can now receive a roughly 4.2% return for holding US government debt for two years, a fairly sizeable return compared to most other developed nations.

As we alluded to in our previous monthly commentary, US dollar strength across the board is rational. That does not make individual moves of no consequence or not interesting, far from it, but it is worth considering the context.

The Gilt Market – What happened in the last few days

The above graph from the Financial Times shows the yield on a 30-year UK government bond (gilt). A one-week move this month saw a roughly 2.7% move in the yield from bottom to top and back again. This is remarkable.

While yields have been rising pretty much everywhere this year as inflation continues and central banks raise interest rates, the activity in the last few days of September did seem to be one focussed in the UK markets, following the Chancellor's announcements. Without going into too much depth on the issues here, it is something that has been brewing for a while and not an issue entirely of the Chancellor's making. However, the action in the markets in the days following his speech was remarkable and was obviously related to the policies announced. We saw a sharp fall in the value of the pound and, importantly here, a sharp rise in gilt yields.

In short, large pension funds are required by the regulator to buy gilts. They then enter into various different contracts with banks to match liabilities (also known as Liability Driven Investing, or ensuring there is cash for when people take their pensions), to borrow against these gilts to enhance returns, or to hedge against any fall in the value of these gilts. When the price of these gilts fell so suddenly, these pension funds were left in a position where they were required to pay more to the banks. Simply put, these contracts became more expensive. In order to fund this, they had to sell what liquid investments they had. As liquid securities themselves, gilts were sold, which in turn drove down their prices further and exacerbated the problem, creating a spiral which could have had serious repercussions had the Bank of England not intervened. The Bank stepped in to buy long-dated gilts, thus providing a buyer for those who need to sell and driving the price of bonds up (yields down) and preventing this cycle from continuing. The intervention seems to have been successful as both gilt prices and the value of sterling stabilised somewhat.

Ultimately what this means it that the Bank of England now joins the Bank of Japan and the European Central Bank in having to print money despite high inflation, in order to support markets in their own bonds. However, The Bank of England were planning on reducing the size of the balance sheet, not increasing it. This also contrasts directly with their own policy of increasing interest rates to fight inflation, as they are now borrowing at ever more expensive rates.

Interventions like this are not unprecedented, but they are rare. It is even rarer that a significant catalyst for this intervention seems to have been the government's own policies.

Investment Profile – Havelock Global Select

Havelock Global Select was launched a little over four years ago now by boutique investment manager Havelock London. Fund manager Matthew Beddall, as CEO, was instrumental in the founding of the management company and the launching of the fund, having previously spent over seventeen years at Winton Capital Management where he served as Chief Investment Officer for over nine years.

The fund has a broad global equity remit but is a concentrated one, with 33 holdings in the portfolio. It is the only strategy Havelock London currently run, so all resources are directed at this single strategy. The style can be described as ‘quality value’ as the managers focus on finding businesses with “a track record of strong operating performance, financial discipline and a purchase price that does not require undue optimism about the future”. This process has led them to invest in companies such as Warren Buffett’s Berkshire Hathaway, Swiss engineering group Bucher Industries and speciality chemicals business Johnson Matthey.

While it is perhaps too soon to fairly judge the fund’s performance, it is worth noting that it is a top quartile performer in its sector over 3 years. This is a fund which is also liked by our Model Portfolio Service team, who recently added it to their portfolios.

Investment Team’s thoughts

As touched upon above, the progress humanity saw during the reign of HM Queen Elizabeth is quite remarkable. Medical advancements have come and gone, replaced by newer, more effective drugs and technologies. The internet has revolutionised the world as we know it. Humans landed on the moon seventeen years after her coronation and now we use satellites for anything from crop monitoring to communications.

To try and put some numbers to it, the Elizabethan era saw the population of the UK increase by around one third, from 50.5 million to 67.5 million. The global population has risen much faster from 2.6 billion to around 8 billion today.

Looking at financial markets during this time, it is hard to find an equity market index that stretches back the entire period in question. The UK's FTSE 100 was established in 1983 and has returned around 1,370% since then in sterling terms, while the MSCI World Index (tracking the largest companies in the world) was established in 1969 and has returned approximately 4,510% since in US dollar terms.

One index that does have a long enough history, the US's S&P 500, has returned around 128,000% (this is not a typo) in local currency terms since 1952. Comparing that to US inflation data, which has seen the dollar devalue roughly 2,890% in the same period, shows a huge amount of real terms wealth generated from investing in the stock market.

We believe that at times where market volatility is making headlines it is important to remember the long-term progress that has been made by humanity and how this coincides with investment returns. While much of this commentary talks of recent short-term moves, we endeavour to look through this and attempt to see the long-term view. We hope this enables us to capture positive returns from disciplined investing with a more appropriate time horizon, focussed well beyond daily movements.