



CARTLIDGE MORLAND

INDIVIDUAL WEALTH MANAGEMENT

INVESTMENT COMMENTARY



28 MAY 2021

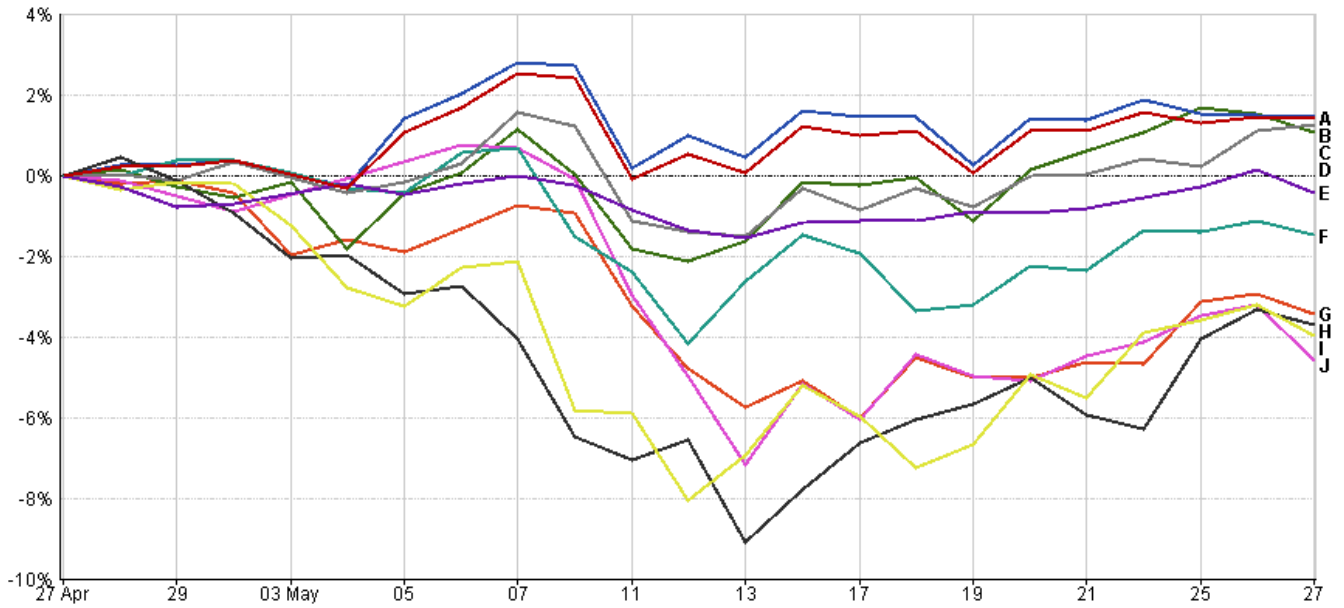


OVERVIEW

After some very strong performances in the last six months, equity markets have seen more muted returns in the last month. The principal concern for investors is increasing inflation – the US inflation rate shot up to 4.2% pa in April whilst inflation in the eurozone hit 1.6% pa and 1.5% pa in the UK. Markets fear that the US Federal Reserve (Fed) will have to take action to curb the economy overheating by increasing interest rates and reducing its bond purchase programme, as inflation is well above target. However, after reacting negatively to mid May US inflation news, equity markets ticked up, buoyed by the prospect of improving earnings as economies start to reopen due to vaccination programmes picking up pace and pandemic-related restrictions being loosened.



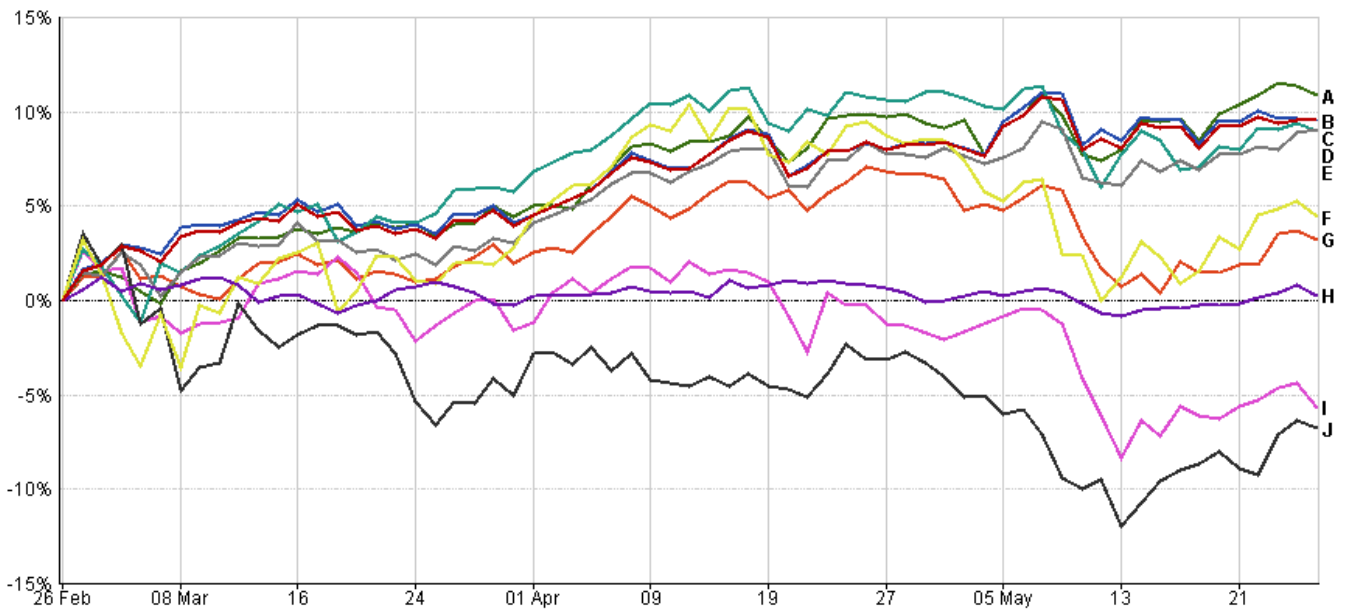
ONE MONTH INVESTMENT MARKET STERLING RETURNS



- A - FTSE 100 TR in GB [1.44%]
- B - FTSE All Share TR in GB [1.43%]
- C - FTSE 250 TR in GB [1.25%]
- D - FTSE World Europe ex UK GTR in GB [1.07%]
- E - FTSE Actuaries UK Conventional Gilts 10-15 Years TR in GB [-0.40%]
- F - S&P 500 GTR in GB [-1.47%]
- G - FTSE World Asia Pacific ex Japan GTR in GB [-3.41%]
- H - MSCI China GTR in GB [-3.68%]
- I - Nasdaq 100 GTR in GB [-3.97%]
- J - Nikkei 225 in GB [-4.56%]

27/04/2021 - 27/05/2021 Data from FE fundinfo2021

THREE MONTHS INVESTMENT MARKET STERLING RETURNS



- A - FTSE World Europe ex UK GTR in GB [10.89%]
- B - FTSE All Share TR in GB [9.57%]
- C - FTSE 100 TR in GB [9.56%]
- D - FTSE 250 TR in GB [9.07%]
- E - S&P 500 GTR in GB [8.98%]
- F - Nasdaq 100 GTR in GB [4.43%]
- G - FTSE World Asia Pacific ex Japan GTR in GB [3.20%]
- H - FTSE Actuaries UK Conventional Gilts 10-15 Years TR in GB [0.28%]
- I - Nikkei 225 in GB [-5.72%]
- J - MSCI China GTR in GB [-6.73%]

26/02/2021 - 27/05/2021 Data from FE fundinfo2021

The actions of the Fed are key to the global economy, equity and fixed interest markets. The Fed believes that higher levels of inflation are likely to be transitory as the economy re-adjusts in the aftermath of the pandemic. Initially, consumer demand is expected to be high as the country emerges from virus restrictions stoked by money from the US Government in consumers' pockets. With pressures on supply side in particular affecting commodities and currently recruitment, prices are likely to rise over the short term and then fall closer to target as the economy normalises and manufacturing bottlenecks ease. The alternative narrative is that higher inflation persists over the longer term and bond yields and interest rates continue to rise. Consequently, corporate and personal debt financing costs would increase so making debt more expensive to service and values of future earnings would be marked down - not ideal for equity markets. The Fed has urged patience in looking through these temporary hikes in inflation. However, when the economic recovery is firmly established, the Fed and other central banks will be intent on increasing rates gradually and winding down their asset purchase programmes so that they have sufficient monetary tools available when the next economic downturn occurs.

In common with the Fed, other central banks also believe that it is too early to withdraw the emergency monetary stimuli as economies start to recover following the lifting of pandemic restrictions. Such views from members of the European Central Bank (ECB) have kept European bond yields low and some still negative. The ECB plans to maintain its bond purchase programme until at least March 2022. The Bank of England kept interest rates at 0.1% at its last meeting and maintained quantitative easing at £895bn. It is expected that UK interest rates may start to rise in 2022 as growth expectations are increased and unemployment is expected to peak at 5.5%.

Economies have also been supported by vast amounts of fiscal stimuli. The US has already adopted colossal stimulus packages to support individuals and companies and to restart the economy. President Biden has laid out a \$6trn annual budget proposal to fund large-scale infrastructure and social investment programmes. The €800bn 'Next Generation' EU economic relaunch package is expected to start making payments through the second half of 2021. As economies around the world re-open, exporting countries such as China, Japan, Germany and many emerging markets should benefit from stronger demand.





The CM Investment Commentary is compiled by Angela Cooper, Managing Director of Cartledge Morland's Investment Services team.

Angela runs the firms' investment management propositions, with over 30 years' experience in investment research working for investment companies, leading UK national IFAs and wealth managers. Angela graduated from the London School of Economics and is a Chartered Insurance Practitioner.

OUR VIEW

We expect to witness continued volatility in investment markets as investors are pulled between the prospect of higher inflation and statistics pointing to improving economic and earnings growth. We maintain our diversified portfolios but with more emphasis on equities which should continue to benefit as economies around the world re-open, as vaccination programmes become more global and the number of Covid-19 cases reduce. There is concern that current vaccines may not be effective against new Covid-19 virus mutations, which is one of the reasons for maintaining fixed interest exposure, albeit at a lower level than previously, for the protection it offers in the event of equity market volatility and not ignoring the fact that geo-political strains could intensify.

UK commercial property funds have been severely affected as a result of the pandemic as countries locked down and offices, non-essential shops, restaurants and leisure facilities closed. Surveyors were unable to meaningfully value properties so the UK commercial property funds were suspended during the first 2020 lockdown. Most funds have now reopened as restrictions were eased but those with greater exposure to the hard hit retail and leisure sectors took more time to reopen as managers needed to raise liquidity for possible withdrawals when their funds reopened. However, the Aviva UK Property fund has not been able to reopen due to the relatively small size of the fund - 12 properties and cash valued at around £378m - and its high exposure to the leisure and retail sectors. Its managers have announced that the fund will close in July 2021 with cash already held within the fund, together with proceeds from the sales of the properties being returned to investors over time. We continue to hold commercial property funds which invest across a broad range of sectors for the diversification that they bring to portfolios as well as their income streams. We believe that commercial property will evolve - reflecting trends in the economy, meaning opportunities exist where sectors have been oversold. The yield from the asset class is currently above that of a 10 year gilt and high quality corporate bonds. Where appropriate, we continue to maintain core exposure at a lower level than has been typical.

Lastly, inflation cannot simply be ignored. The central banks are no doubt correct in resisting reaction to temporary inflationary factors caused by demand for

OUR VIEW continued

goods and services surging as lockdowns ease and the resultant supply side pressures. These are short term problems of misalignment between demand and supply – using blunt fiscal instruments to suppress demand would simply extinguish the economic growth which the central banks wish to encourage. Unfortunately, a different type of inflation is also lurking – yet to emerge in response to the massive increase in the global money supply – which has resulted from the central banks' actions in providing consumers and businesses with untold quantities of cash. Adding fuel are the huge savings consumers have accumulated during lockdown.

The central banks are relying upon careful withdrawal of stimulus and gradual increases in interest rates to curb growth in the money supply, to hold down inflation and ultimately to restore the interest rates policy lever by taking them back to levels which can be cut if needed. This is a very delicate balance between nurturing sustainable growth alongside modest inflation and encouraging either 'boom' or 'bust'. If the central banks get it wrong then 'boom' seems more likely than 'bust' presently, which will favour assets such as equities. Elevated inflation is toxic to fixed income and therefore to bonds, which makes portfolio risks more difficult to manage than usual.

If you have any queries
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