ALBERT E SHARP

INVESTMENT MANAGEMENT & STOCKBROKING

Market Commentary

October 2023

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MONTHLY COMMENTARY

OCTOBER 2023

Monthly returns and summary

Index	Portfolio Benchmark Risk Level	31/10/2023	1 Month	3 Months	1 Year	3 Years	5 Years
ARC Cautious	Low Risk	192.26	-0.8%	-1.3%	+1.2%	+0.4%	+6.4%
ARC Balanced	Medium Risk	235.46	-1.6%	-2.7%	+1.2%	+4.3%	+10.5%
ARC Steady Growth	Medium High Risk	281.29	-2.1%	-3.8%	+1.6%	+7.8%	+14.8%
ARC Equity Risk	High Risk	329.13	-2.8%	-4.8%	+1.8%	+10.9%	+19.1%

Source: Figures based on ARC estimates.

Index	Region / Asset Class	31/10/2023	1 Month	3 Months	1 Year	3 Years	5 Years
UK 100	UK	7321.72	-3.8%	-4.9%	3.2%	31.3%	2.7%
UK All Share	UK	3954.35	-4.2%	-5.8%	2.0%	25.5%	1.3%
Dow Jones Ind Avg	US	33052.87	-1.4%	-7.0%	1.0%	24.7%	31.6%
S&P 500 Index	US	4193.80	-2.2%	-8.6%	8.3%	28.3%	54.7%
Nikkei 225	Japan	30858.85	-3.1%	-7.0%	11.9%	34.3%	40.8%
MSCI Europe Ex UK	Europe	172.29	-3.5%	-8.3%	6.6%	25.5%	25.1%
MSCI Asia Ex Japan	Asia	580.91	-3.9%	-12.8%	10.9%	-20.7%	-0.5%
MSCI Emg Mkts (£)	Emg Mkts	585.57	-3.3%	-6.9%	5.1%	-4.8%	14.0%
MSCI World Index (£)	Global	2768.62	-3.0%	-9.6%	8.7%	20.7%	36.9%
UK Conventional	Gilts	2884.21	-0.4%	-1.7%	-5.8%	-30.2%	-19.3%
UK Index-linked	Gilts	3666.09	-1.3%	-5.5%	-9.9%	-36.3%	-25.8%
FTSE All-Share Real Estate Investment Trust Index	Property	1762.68	-3.8%	-9.9%	-13.0%	-17.7%	-32.9%
WTI Crude ($/Barrel)	Oil	81.02	-10.8%	-1.0%	-6.4%	126.4%	24.1%
Gold Spot $/Oz	Commodities	1983.88	7.3%	1.0%	21.4%	5.6%	63.3%
£1 = US$	Currencies	1.2153	-0.4%	-5.3%	6.0%	-6.1%	-4.8%
£1 = €	Currencies	1.1490	-0.4%	-1.6%	-1.0%	3.3%	1.8%
£1 = Yen	Currencies	184.36	1.2%	1.0%	8.1%	36.0%	27.9%

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

Index	Region / Asset Class	31/10/2023	1 Month	3 Months	1 Year	3 Years	5 Years
FTSE All-Share Investment Companies Index	Diversified	10,420.12	-5.2%	-8.9%	-7.3%	-7.5%	5.7%
Latest Weighted Average Discount	-16.1%						
12 Month Weighted Average Discount	-12.4%						

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

General Comments

October saw negative returns for most assets. Just about the only shining light was a shiny metal; gold, returning over 7% with investors arguably fleeing for the perceived safety of this commodity which has been used as a store of value for thousands of years.

Fixed income markets were down, but only slightly, while equities sold off more aggressively. The oil price fell significantly in the month, offering hopeful signs for inflation.

Unsurprisingly given these returns, multi-asset portfolios lost value, with the ARC indices continuing the pattern of recent months in trending downwards. Investment company discounts also remain stubbornly wide, although this does arguably represent an enormous opportunity on a long-term view.

UK Commentary

The latest UK GDP numbers showed a rebound from a weak July (which many blamed on strikes and the poor weather), coming in above expectations with 0.2% month-on-month growth. This has clearly been supported by strong wage growth. Although total pay growth slid to 8.1% year-on-year, this is still above CPI which was reported to be 6.7% on the latest reading, meaning consumers are currently experiencing real terms spending power increases.

The Prime Minister announced the cancellation of the northern leg of HS2. While this has always been a controversial project, and a divisive local issue for ourselves, it is another poor reflection on our government that they are unable to deliver part of one of the only major infrastructure projects ongoing in this country. Global markets value stability and politicians delivering on what they say they are going to do. Announcing major projects, only to continually revise and eventually cancel parts of them is only going to be seen negatively by major international organisations.

This plan announced at the Conservative party conference also didn’t help in the polls whatsoever, as Labour moved further ahead, and gained ground in parliament too with several by-election wins. One of these wins was in Scotland with a 20-percentage point swing catapulting Labour ahead of the crisis-ridden SNP. Labour winning SNP seats would give them a huge boost in their bid for a Westminster majority in the next general election, which is not too far away now. There were also two significant by election wins for Labour in Conservative heartlands Mid Bedfordshire and Tamworth. These constituencies going red would have been unthinkable to many Conservatives a few years ago.

North America Commentary

We also saw political drama in the US with the speaker of the house being ousted for the first time in American history, as representatives voted to remove Kevin McCarthy from the position. The following weeks had twists and turns, but ultimately the right wing of the Republican party got their way with the relatively unknown Mike Johnson being appointed. Johnson, a Trump ally, steps into the role at an important time given the upcoming funding deadline on the 17th of November.

US inflation for both producers and consumers came in above expectations. That said, they are at much more reasonable levels these days showing 2.2% and 3.7% year-over-year figures respectively. Much of this surprise was also down to the oil price spike in September, which has since reversed, as highlighted by the data table at the top of this piece.

In contrast, Canadian CPI came in below expectations at 3.8%. Consequently, the central bank opted to hold base interest rates at 5.0%.

In company news, energy giant Chevron agreed to buy oil and gas producer Hess Corporation for a sum of $53bn, payable in shares, while ExxonMobil acquired Pioneer Natural Resources for an enterprise value (equity plus debt) of $64bn. A recent meeting we had with boutique fund management house Smead Capital brought to light a wonderful quote on this topic from veteran oil investor T. Boone Pickens; “It has become cheaper to look for oil on the floor of the New York Stock Exchange than in the ground.” It seems energy majors have taken this to heart in recent times.

Europe Commentary

Eurozone Producer Price Inflation (PPI) fell to -11.5% in August, the latest figures showed. Yes, that is negative 11.5%, a significant contraction in prices. PPI is inherently a leading indicator for CPI (Consumer Price Inflation, the key inflation figure reported) so this is incredibly positive news for the future direction of inflation in the Eurozone. This is supported by various individual nations' data as well. For example, CPI in the Netherlands came in at 0.2% year-on-year, well below target.

Following these data, the European Central Bank decided to hold interest rates where they are at 4%, ending its unprecedented string of ten consecutive rate rises. This series of rate increases follows 15 years of the loosest monetary policy the world has ever seen, with central banks around the globe experimenting with negative interest rates and quantitative easing coming out of the 08/09 global financial crisis. It is not surprising that historic extremes in one direction have been followed by historic extremes in the other. We are hopeful though that we are now entering a period with a more normal interest rate environment and more stability of policy.

Asia Pacific Commentary

New Zealand has a new centre-right coalition government as the more left-wing Labour party was ousted after 6 years of rule, much of which was led by Jacinda Ardern, who jumped before she was pushed and stepped down shortly before this election defeat. Christopher Luxton will become the new PM.

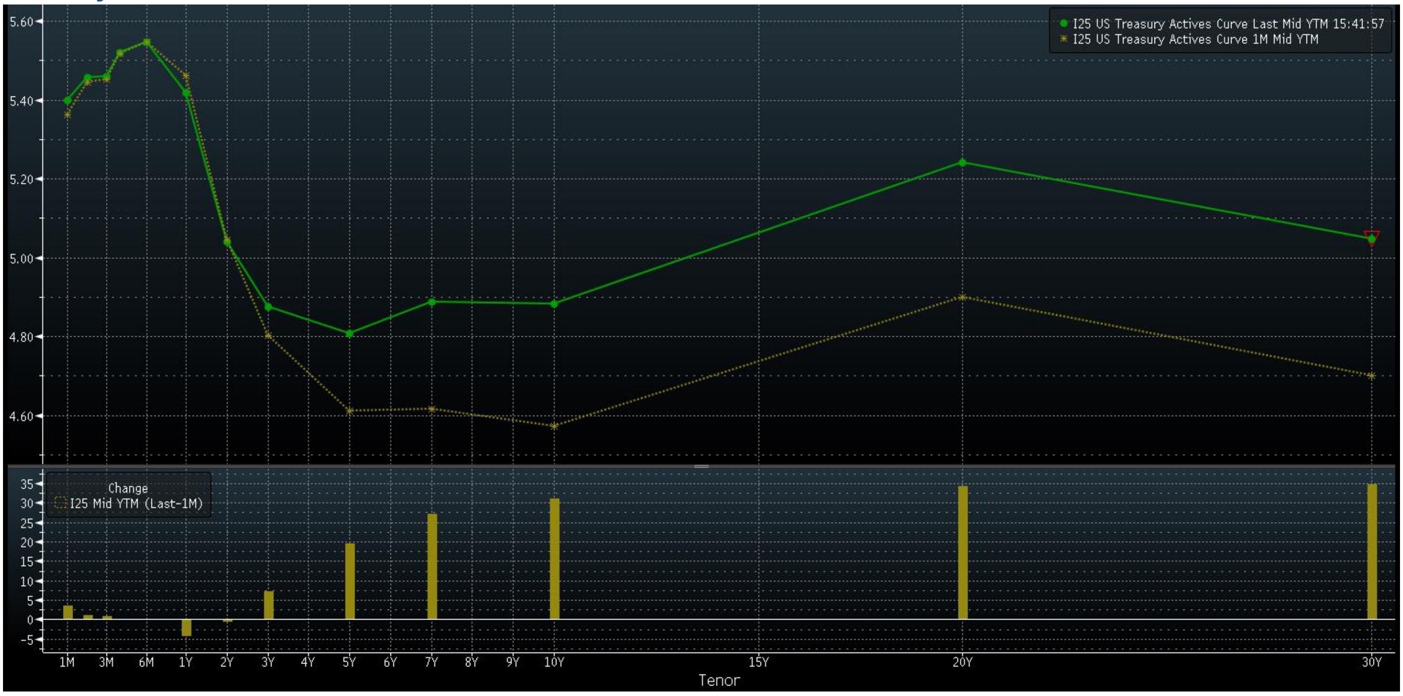
While we always take GDP growth projections with a pinch of salt, it is worth noting the World Bank predictions that India and its neighbours will grow faster than any other region this year. The bank lifted its projections to 5.8% for South Asia, while predicting East Asia will grow at one of the slowest rates in five decades. It predicts India will grow 6.3%, while China will grow 4.4%. As highlighted below, China may well outperform this forecast, however.

Emerging Market Commentary

Israel is certainly not an emerging market economy, with a GDP per capita noticeably above that of the UK. However, Palestine is very much at the other end of the spectrum. The ongoing conflict here is tragic in every sense. There are also obviously concerning geopolitical issues at play here which can impact markets. We hope for a resolution soon, although lasting peace has evaded the region for centuries so we are unsure what this may look like. While there are worries of spillover elsewhere and genuine concerns of escalating tensions worldwide, the Israeli market is a very small on in terms of global stock market capitalisation and trade flows, so we hope the global economic impacts of this war can remain muted.

Elsewhere, Chinese GDP surprised to the upside with 4.9% year-on-year growth. This was well above the 4.5% growth expected, showing signs that the economy may be recovering from the shadows cast by the property sector in recent times.

Chart of the month – US Yield Curve



The US yield curve moved significantly over the month, with the latest disposition (bright green) much flatter than previously (yellow/green). Perhaps of most significance is the change in the 2- and 10-year distribution, with the "inversion" almost disappearing. This is in part thanks to the 10-year treasury yield hitting 5% for the first time since 2007, largely as a result of strong economic data prompting investors to bet on the Federal Reserve increasing base interest rates further.

An inversion in the yield curve is a situation where shorter-term yields are higher than longer term yields. Usually, returns are better for those lending for longer, so an inversion is typically seen as abnormal. In fact, many see an inversion of the 2- and 10-year yields in the US to be a significant leading indicator of a recession in the US.

So far, with the significant US GDP growth mentioned above, this has not been the case. Now, we are close to this situation reverting to normal without a recession occurring. Given the 4.9% GDP growth, the US are a long way from a recession, so hopefully those who see this inversion as an indicator can be proved wrong once again. These are backward-looking data, so there is merit in any argument that points to other data painting a more recessionary picture for the coming year, however, 4.9% growth is certainly positive news for the strength of the economy.

Investment Profile – AXA Framlington Global Technology

Jeremy Gleeson and his team have been running this strategy for over 15 years now and have achieved some exceptional long term returns by investing actively in high quality global technology stocks. The portfolio is significantly different from the index, which is heavily dominated by some of the biggest companies in the world, and is arguably better diversified as a result of lower exposures to the largest companies. This active management has helped reduce volatility relative to the index.

The index is also somewhat flawed given the omission of some companies which would be considered by most to be technology stocks. Alphabet (Google), for example, is not in the index but is the second largest position in the fund. The exceptional returns generated for shareholders by this company would have been missed by a passive technology investor, despite the obvious technology exposure of the business.

The fund also offers a cheaper portfolio than the index, which is particularly significant in the often-expensive technology sector, with investors regularly willing to pay high multiples for stocks which they believe have the potential to generate high returns in the future, as they have in the past.

Investment Team's thoughts

October was another tough month for most asset classes. It recently emerged that NS&I hit their annual target for inflows in the single month of September, thanks largely to an attractively priced product which was pulled only a few weeks after release. In total NS&I attracted £7.7bn in September, a quite remarkable amount.

While this may be a drop in the ocean in the grand scheme of global markets, it does highlight a key issue for many markets as there is significant competition for capital now thanks to attractive returns on offer from low-risk investments. The flows of capital away from riskier investments towards other offerings is undoubtedly creating a significant drag on prices of risk assets.

This is, however, a good thing for investors. We can get attractive returns on low-risk assets, as well as being able to buy risk assets, such as equities, at incredibly attractive valuations. Throughout history, whenever other people are looking elsewhere, it has almost always been the best time for investors to look to purchase risk assets. We cannot guarantee history will repeat, but current valuations are incredibly attractive based upon decades and decades worth of data, so we are very optimistic about future returns from these depressed levels. Conversely, it is also a good time for the cautious given the attractive returns on offer from low (or even no) risk assets.

It may seem brash to be consistently upbeat in the face of continued poor returns, but we invest for the future on a long-term view, so are encouraged by the significant upside potential for markets from here.