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February 2018 Portfolio Review

The end of January saw the return of volatility to many capital markets, signifying the end of the steady rising equity market conditions that had prevailed through 2017. Expanding on that volatility, we concur with the view of many respected investment research institutions, that the return of more resilient global economic growth means that the end of the deflationary era has finally arrived. This will lead to a gradual normalisation of interest rates and bond yields away from the 'lower zero bound', but probably not higher than 3.5 - 4.5% over the remainder of this rate cycle. This reduces the relative attractiveness of equities and makes extended equity valuations less easily justified.

But it is unlikely that February's correction heralds a medium-term equity bear market because this shift in relative valuation is occurring as a consequence of economic growth and not fear of decline. However, it does mean that the relative attractiveness of different parts of the stock markets will be shifting. Those who particularly benefited from low cost of debt capital and investors' relentless hunger for growth prospects might suffer, while those who can sustain or improve their margins when input costs rise should now become more attractive. Over the shorter term this reorientation is likely to result in more market volatility, while over the medium-term risk asset markets retain upside potential in sync with further economic expansion.

During this period those parts of the market that have done best in the run-up to the correction are likely to come under the most scrutiny. Emerging market equities as well as US tech stocks are such areas as they could be seen as vulnerable in the upcoming market environment.

Elsewhere, the first public appearance of the new US central bank chair Jay Powell, who came across as more assertive than previous chief central bankers, appeared to confirm market concerns that they will no longer be able to rely on monetary support should stock markets wobble. They duly sold off again, not helped by president Trump's announcement regarding tariffs on steel and aluminium imports.

It is questionable whether he intends a 'trade war' with the rest of the world as opposed to simply re-iterating that he means business with his intention to secure better trading terms for the US. However, as the recent Florida shooting has shown, he can be swayed more by popular opinion than feeling tied by previous statements of principle. Expect a deal to be done, rather than a painful trade war to be fought.

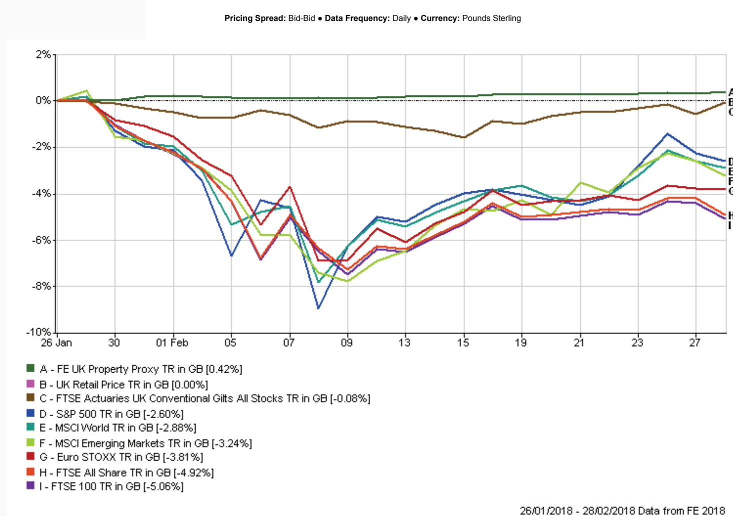
Similar bargaining tactics could be observed between the EU Commission and the UK government in the Brexit negotiations. The provocative language on both sides tells us that we may soon see more specific positions being teased out, which would be about time, given the beginning of the first potential transition period is only a little over a year away. Capital markets continue to indicate that they expect a 'muddle through Brexit' rather than a Hard Brexit or Remain.

Behind the political noise, economic data flow around the world told a story of continued strong and synchronised economic expansion, even if the rate of the expansion no longer seems to be accelerating further. The UK remains a special case due to Brexit, but even here construction and manufacturing business sentiment were reported at healthy expansion levels, although still considerably behind the Eurozone economies.

Portfolios

In a month where some of the major indices fell in excess of 4% it was refreshing to see that the diversification within our portfolios stemmed the largest loss (Income Portfolio) to half that.

Developed market index returns suffered heavy falls at the start of the month clawing back approximately 50% of the fall by the end. The UK and Europe faired worst with the FOOTSIE closing the period over 5% down.



Although the majority of indices had fallen over the period, 10 holdings across the Beckford James portfolios generated positive returns. The major holdings and those offering greatest support generally were the Natixis H2O multi-returns portfolio which gained 0.24% gross and the Vanguard UK Inflation Linked Gilt Index fund which gained 1.2%.

Notably, in a period of volatility, the Jupiter Absolute Returns fund also generated positive figures (+0.54%) and giving renewed confidence in its diversifying role.

As the committee meets for the March review, however, certain funds are under scrutiny having populated the 'watch' list for a few months. It is likely that these will be replaced in the upcoming portfolio update.

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