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Portfolio Review *April 2022*

Following on from a difficult first quarter of the year, April proved no different for investors, with global financial markets continuing their recent declines. Volatility permeated equities, bonds and currencies as a perfect storm of tightening monetary policy, high inflation, slowing economic growth momentum and geopolitical uncertainty all contributed to the risk-off sentiment, giving investors little reason for optimism.

April concluded with no sign of resolution to the war in Ukraine, as fighting in the eastern and southern parts of the country intensifying. The impact on energy markets remains particularly notable given the difficulties faced by Europe in reducing its energy dependency on Russia and ending this reliance is now a matter of national security. In doing so, governments' timelines on "greening" economies to achieve net zero have been turbocharged. European gas prices cooled a little in April but still stand 42% higher year-to-date. There was also some welcome relief from a pause in that the recent rise in oil prices due to both the release of strategic oil reserves from the US and expectations of lower demand from China.

Global equities suffered four consecutive weeks of losses, with the MSCI World Index posting a 3.8% decline. Growth stocks led the sell-off, particularly among the technology sector, which is more negatively affected by rising rates, whilst small-cap stocks underperformed large-caps. The US was the worst performing market with the S&P 500 index down 4.3% while the more tech-centric Nasdaq Composite fell 9%, its worst monthly performance since the autumn of 2008 at the height of the financial crisis. Once again, the only relative bright spot was marginally positive returns for UK stock markets, given their more defensive make up. The commodity-heavy FTSE 100 rose 0.8% while the broader FTSE All Share index returned 0.3%. The FTSE 100 index remains one of the few key benchmarks in positive territory so far in 2022.

Elsewhere there were also losses in Europe, Japan, Asia and Emerging Markets. The latter was once again dragged down by China as markets priced in the impact of the now far-reaching lockdowns. Having kept Covid-19 infections under control for most of the past two years, Chinese authorities are now struggling to contain a major outbreak. The country has adopted a zero-Covid strategy which saw Shanghai spend all of April in full lockdown and reports have emerged that this could soon spread to Beijing as infection rates rise. This will undoubtedly challenge China's 5.5% growth target for 2022 and compound the already strained supply chain issues which are still struggling to recover from the initial wave of the pandemic.

Losses were not just confined to equities with bonds also losing ground as rising inflation and monetary tightening had an equally negative impact on fixed income assets. Bond yields continued to rise (meaning prices fell) as expectations of significant interest rate hikes increased. The only asset class to perform moderately well were commodities. However, even here the rally stalled towards the end of the month due to a strengthening US dollar and concerns that fading economic momentum will ultimately take a toll on commodity demand. The best performing areas were unsurprisingly energy and agriculture which offset weakness in areas such as industrial metals, livestock and precious metals.

Expectations for the path of monetary policy ramped up last month and there has been a material shift in these since the start of the year as inflation continues its rampant rise. Markets are now pricing in the prospect of interest rates over 2% in both the US and UK by year-end, while eurozone rates are expected to move into positive territory around October. There are now clear signs central banks are prepared to act seriously to tackle inflation. US headline inflation reached 8.5% in the year to March, up from 7.9% in February, whilst in the UK the Consumer Price Index (CPI) rose from 6.2% in February to 7.0% in March, the highest level since March 1992. These figures would appear to validate several members of the Federal Reserve stating their desire to take rates back to neutral as quickly as possible with markets moving to price in three 50 basis point hikes at each of the Fed's next three meetings, commencing in May. There were also expectations that the Bank of England, after raising rates by a quarter of a percent in April, would hike for a fourth consecutive time in May. Bond markets reacted sharply to the more hawkish tone coming from central banks and consequently bond yields rose significantly over the course of the month.

Outside of the Federal Reserve and geopolitical headwinds, April saw the start of the first quarter 2022 earnings season. Companies delivered exceptionally strong earnings growth last year rebounding from their Covid-lows, making year-on-year comparisons unusually challenging. On the whole results have been mixed and although a high proportion of companies have beaten analysts' expectations, earnings growth has decelerated. This dynamic is more pronounced in areas that benefited from the pandemic, like e-commerce, although trends such as cloud computing remain strong. For those companies that have missed expectations or published disappointing results the punishment has been severe and share prices have fallen considerably. This has been most evident amongst the big technology names such as Apple, Amazon and Netflix who all failed to deliver the knockout scorecards investors have become accustomed to. With the mega-cap stocks making up a large proportion of the benchmark, their combined profitability has a big influence on overall market returns.

So, where does this all leave us? The global economy entered 2022 with strong tailwinds but these have swiftly unravelled. While robust labour markets and large amounts of pent-up savings remain supportive, the macroeconomic picture is now more troubled than it has been over the past 18 months. Central banks face substantial challenges as they look to tighten policy to help bring down inflation back to target (around 2%) without tipping economies into recession. Against this backdrop, there is the potential for further pressure on equity valuations ahead. Companies that can maintain healthy margins thanks to strong pricing power will likely be relative outperformers. In fixed income, yields may still have further to rise as central banks push ahead with their tightening plans.

Portfolios

The Beckford James portfolios were not immune from the falls in equity and bond markets and all portfolios delivered negative returns during April. The Income portfolio fared best, falling just 0.5%, thanks largely to its higher allocation to the UK and predominance of equity income funds which tend to be invested in value rather than growth-type sectors and stocks. There were some strong performances from the likes of Vanguard Global Equity Income, GAM UK Equity Income and Fidelity Global Dividend which all delivered positive returns; however, these were not quite enough to offset falls from elsewhere in the portfolio.

The Growth portfolios also fell with Growth 3 down 1.1% for the month followed by the other portfolios in ascending risk order through to Growth 10 falling 2.4%. There were some positive performances from those areas of the portfolio which benefit from rising inflation – so-called real assets – such as the Threadneedle and L&G Property funds which rose 3.1% and 0.8% respectively, and the Liontrust Diversified Real Assets fund which was up 0.5%. However, as with the Income portfolio, these positive performances were offset by falls elsewhere with the US funds and those with a strong growth bias coming under particular pressure. Natixis Loomis Sayles US Equity Leaders, for example, fell 9.0% and Goldman Sachs Global Millennials was down 6.0%.

The Ethical portfolio fell 3.3% coming under pressure from its higher degree of exposure to the US and growth-type stocks, which were both weak during April. We will shortly be writing out with some suggested changes to this portfolio to help increase diversification away from these themes which we believe will improve the risk-return profile of this portfolio.