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Her Majesty Queen Elizabeth II 1926-2022

This September was a month that we will all remember for the passing of Her Majesty The Queen. She was a reassuring constant through many of our lives and we are deeply saddened by her passing. Her 70 years of service are a testament to her incredible strength, resilience, and dedication. Our thoughts are with the Royal Family and the nation as we collectively mourn the loss of our longest-serving British monarch.

Portfolio Review *September 2022*

They say a week is a long time in politics, but one could argue the same for financial markets at present. Since our last review we have had a new Monarch, Prime Minister, a new cabinet and entered a new era for UK fiscal policy. In a normal month we would review the 50-75 basis points of monetary tightening that we saw across the developed economies in September and discuss the outlook for inflationary pressures peaking, not least because energy prices are beginning to weaken, but we will no doubt revisit these themes in the months to come. Instead, we will focus on the new Chancellor's mini-Budget and the ambitious economic model ushered in by so-called 'Trussonomics' which, in just a matter of weeks, has had far reaching ramifications for global equities, government bonds and currencies.

Before we come to the Chancellor's statement, the first item on Liz Truss's agenda as newly elected leader of the Conservatives, was to outline an energy support package to help tackle the growing cost-of-living crisis. UK households were set to see their gas prices rise by a further 80% in October, on top of the 54% increase we saw in the spring. The substantial package of measures included a cap on the unit price of energy and short-term subsidies meaning households will now face a more modest rise in utility bills this winter. The exact cost of the measures is as yet unknown due to the uncertainty of the actual cost of buying gas, but it is expected to amount to around £100-£150 billion over the duration of the two-year freeze.

The energy support measures turned out to be the warm-up act to Chancellor Kwarteng's mini-Budget statement set forth on Friday 23 September. Although mini in name, the extent of the proposed policy changes were some of the most material ever announced in a budget. The statement contained a reversal of the previous increase in national insurance contributions and corporation tax, a reduction in the basic rate of income tax, abolition of the top rate of tax (which has since been reversed) and stamp duty cuts.

The government's big gamble is that these tax cuts and reductions in regulations will fuel strong growth, and in turn generate greater tax revenues. However, the measures announced will place a significant additional burden on the already stretched UK public finances and come against a backdrop of great economic uncertainty. No revenue raising measures or spending cuts were announced so in conjunction with the energy package, will be funded by an additional £90bn in borrowing this fiscal year, with the Chancellor indicating more tax cuts to come. Furthermore, the

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Chancellor's statement was delivered without the independent scrutiny of the Office for Budgetary Responsibility (OBR), the organisation that was introduced by the government to stop chancellors spending too much or putting the public finances on an unsustainable trajectory. The government has since pledged that the OBR will provide analysis on 23 November (or possibly before) and at this time the Chancellor will also set out fiscal rules.

Initial market reaction to the statement was severe, with sterling falling sharply and gilt yields increasing substantially. In short, investors believe the tax cuts and increased government spending could make the UK's economic situation even worse. UK borrowing costs rose so rapidly following the announcement of the fiscal package that the Bank of England (BoE) was forced to intervene to purchase long-dated government bonds at the end of September, pledging to buy bonds "on whatever scale necessary" in order to steady the markets. This served to effectively backstop the market, although the 10-year gilt yield still stands at over 4%, up from around 1% at the start of the year. Of course, a rise in yields has consequences not just for the government but it sets the basis for long-term borrowing rates for companies and households and we have seen turmoil in the mortgage market as lenders have pulled mortgage products as they scramble to reassess the outlook for interest rates.

It is perhaps ironic that on the thirty-year anniversary of Black Wednesday – when sterling crashed out of the Exchange Rate Mechanism in September 1992 – the pound reached its lowest level against the dollar since 1985, falling around 8% in September. Part of this is a function of dollar strength against global currencies, another part about rising concerns on the UK economic outlook and future policy-making. The dollar has been gaining strength all year with the Federal Reserve's rapid tightening programme and investor's flight to safety. Furthermore, unlike Europe and the UK, the US has its own energy reserves so has been more insulated both on energy supply and has no exchange rate risk when purchasing energy which is globally priced in dollars. Perhaps a more accurate comparison is to consider the fall in sterling against the euro, which was around 3.5% in September.

So where do we go from here? The narrative has now switched from the "cost of living crisis" to a "crisis in sterling and the UK economy". The focus remains on the BoE who find themselves in a difficult position of trying to actively slow down the economy by raising interest rates, but now finds itself in a situation where demand has been stoked up by the government, which may lead to interest rates having to rise by even more than previously expected. The Monetary Policy Committee next meet on 3 November and following the intervention in the gilt market it is unlikely we will see anything materially change until then.

These are not easy times for policymakers in any region. They face an uncomfortable balancing act to support demand and maintain popularity among their electorate, yet without stoking further inflation and losing credibility over the long-term sustainability of their plans. Words and actions will be heavily scrutinised as more details are announced. Market volatility witnessed since the mini-budget will ensure that policymakers provide sufficient assurance about medium-term plans to anchor credibility. But any misstep on monetary policy risks feeding a vicious cycle of tightening monetary conditions, deteriorating economic activity and further doubts about fiscal sustainability.

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Portfolios

September lived up to its historical standing of the worst month of the year, with equity markets falling across the board. The challenges of persistently high inflation, hawkish central banks and anxieties surrounding growth proved a toxic mix for investors. In the UK the FTSE 100 was relatively resilient in comparison to other major indices, falling 5.16%. Roughly 80% of the earnings generated by FTSE 100 companies are made overseas and therefore become more valuable when sterling declines. By contrast, the FTSE 250 generates 40% of its earnings domestically and saw a decline of 9.67% over the month.

In the US, the S&P 500 index closed down 9.25% in US dollar terms – its worst September since 2002 – as inflation remained unexpectedly high. However, due to currency movements for sterling investors the index was only down 5.40%, demonstrating the impact of currency moves on returns. Europe and Japanese indices posted similarly negative returns whilst Asia and emerging markets fared worse with the strength of the dollar acting as a strong headwind to assets in these regions.

The Beckford James portfolios followed the broad moves in equity and bond markets. The lower risk Growth portfolios marginally outperformed the higher risk profiles, but the spectrum of returns was very narrow (50 basis points between the top and bottom performing portfolios) as all asset classes experienced extreme volatility and negative returns. The JP Morgan Global Macro Opportunities Fund was the only fund to keep its head above water in September, with all other funds delivering a negative return. The largest detractors were the more interest rate sensitive funds such as Foresight Global Real Infrastructure, Goldman Sachs Global Millennials and Liontrust Diversified Real Assets.

The Income portfolio also suffered falls in line with the UK market owing to its high degree of exposure to UK equity income funds. Unicorn UK Income, Chelverton UK Equity Income and Premier Miton UK Multi Cap Income were the worst affected funds whilst the CT Property Growth & Income (previously known as the BMO Property Growth & Income) also saw hefty falls. It was a similar picture for the Ethical portfolio with the Liontrust Sustainable Future Corporate Bond, Unicorn UK Ethical Income and Liontrust Sustainable Future UK Growth suffering the worst of the falls. Losses were limited to some extent by some better returns for the JP Morgan Global Macro Sustainable fund and Alquity Indian Subcontinent fund.