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Portfolio Review *October 2022*

Following a turbulent month and a half, a degree of political stability returned to the UK with the appointment of Rishi Sunak as Prime Minister. After just 44 days in office, Liz Truss drew a close to her premiership, resigning after losing the backing of her party and claiming the unenviable title of the shortest-serving prime minister in UK history. Truss's resignation was unsurprising after her low-tax post-Brexit vision for the economy came crashing to a halt, largely due to markets being unwilling to allow her to borrow hundreds of billions of pounds at a time of persistently high inflation and rising interest rates.

UK assets reacted positively to the news which helped to stabilise gilt yields and in turn, interest rate expectations. UK government bonds rallied 3% over the month, as yields fell back to pre-budget levels, while sterling rallied by a similar amount against the dollar. Sunak's fiscally conservative reputation and prior experience as chancellor, together with the retention of Jeremy Hunt as chancellor who has already reversed almost all of his predecessors 'mini-budget' also helped to restore calm to markets. The publication of the Autumn Statement has been delayed by a couple of weeks, most likely so that the economic projections can not only reflect the current slowdown in economic activity, but also to reflect the substantial reductions in debt cost projections from 5 weeks ago.

Whilst markets have reacted positively, Rishi Sunak has a difficult task ahead of him as he looks to reduce the fallout from recent political events. Significant challenges still remain for the UK economy, not least how the Bank of England will respond to this period of chaos while trying to lower inflation. In addition, UK macroeconomic data deteriorated last month, with the ONS confirming that the economy unexpectedly shrunk by 0.3% in August while business surveys suggested this weakness had continued into the autumn. However, there have been a few bright spots which seemed to slip under the radar while investors were distracted by the political situation; gas prices have collapsed from their August highs; we remain at almost full employment in the UK and profit levels are close to record highs.

While the media focused on political events at home, elsewhere October was rife with other geopolitical events. In China, President Xi Jinping was re-elected at the Party Congress for an historic third term, while the US announced broad export restrictions on semiconductors to China. Russia suffered more military setbacks in Ukraine and bombed Kyiv in response. North Korea launched a missile over Japan for the first time since 2017, Iran was shaken by protests and Brazil re-elected former President Luiz Inacio Lula da Silva.

On the economic front, data continued to hint at a global slowdown. While US GDP growth came in strong, this was mostly due to rising energy exports and falling imports, the latter indicating that the economy continues to slow. Data from the UK and Eurozone also indicated a weakening environment, although Eurozone GDP remained positive for Q3. The US dollar weakened in October against most major developed and emerging market currencies, with the exception of the Japanese

Yen and Chinese renminbi, as risk on sentiment reduced demand for safe haven assets, while sterling enjoyed a recovery rally on hopes for a return of political stability and fiscal responsibility.

Inflation rates in most major regions remain high keeping central banks on their tightening schedules. The European Central Bank hiked rates by 0.75% in October, and while the Bank of England and US Federal Reserve did not meet in October, they subsequently hiked rates by 0.75% in early November with minutes from the meetings highlighting concerns by policymakers, implying more potential hikes in the US albeit with Andrew Bailey hinting that the UK may not have as far to run in terms of hikes. Inflation rates in most major markets remain high, with annual rates exceeding 10% in both the UK (a 40-year high) and the Eurozone, 8.2% in the US and remaining at 3% in Japan, also an eight-year high. On a more positive note, supply chains continued to improve with container shipping costs across the Pacific returning to late 2020 levels.

The myriad of events across the world and weakening economic data did not however undermine the recovery rally in developed market equities after two consecutive months of declines. After a challenging two-month period there was limited bad news for markets to digest and although volatility remained high, this was lower than the elevated levels we had seen in September. Developed markets outperformed in a similar equity relief rally as in July on the back of positive third quarter earnings reports in spite of weaker macro conditions. Emerging markets underperformed developed markets, ending October with negative returns driven by double digit declines in Chinese equities. This came on the back of the export-ban of semi-conductors by the US and negative perception of the outcome of the Party Congress. Chinese equities, particularly those held by foreign investors, sold off amid fears of more autocratic rule and the potential for worsening frictions with trading partners. News that China would not be relaxing its zero-Covid policy anytime soon also weakened investor sentiment.

At a company level, investors have been focused on the all-important third quarter earnings season which, at the half-way stage, showed around three quarters of companies have delivered better-than-expected results. All sectors made gains, but the dispersion has been high. Energy stocks were broadly stronger following especially robust earnings. Some retailers were notably weaker, with investors anticipating pressure on consumer spending as the full effect of rate rises starts to take effect. The spotlight was on the mega-cap technology names, which exert and outsized influence on the markets. Meta, parent company of Facebook, sprang perhaps the biggest unwelcome surprise amid an advertising slowdown combined with rising costs. Amazon and Microsoft also disappointed forecasts, partly due to a slowdown in their cloud computing businesses. All three companies underperformed the wider US market last month. However, it wasn't a widespread tech sell-off as other stocks in the sector performed well such as Apple, which reported a slight rise in earnings, and Netflix where investors were excited about the new ad-supported subscriber offering and a resumption of growth in subscribers in Q3.

Returns from fixed interest were mixed. Government bonds in the US suffered from rising rates while in the UK they staged a recovery amid a significant decline in rates. High yield returns were strong as a substantial decline in credit spreads offset rising rates. Commodities had a strong monthly mainly due to a sharp rise in oil prices. Oil rose 8.9% following an announcement from OPEC that it would reduce output substantially to prevent prices from falling too much amid the global economic slowdown.

Portfolios

The Beckford James portfolios encouragingly delivered positive returns across the board in October. The top returning portfolio was the Ethical portfolio, up 1.74%, helped by some strong returns from the likes of EdenTree Responsible & Sustainable European Equity, Liontrust Sustainable Future Corporate Bond and Schroder Global Sustainable Value Equity. Detractors included Stewart Investors Asia Pacific Sustainability which came under pressure from exposure to China.

Turning to the Growth portfolios, the best performing portfolios were the lower risk profiles where the strong rebound in fixed interest during October thanks to falling yields drove strong performance from this asset class. Performance was positive across all risk profiles, ranging from 0.83% for Growth 3 to 0.47% for Growth 8. There were some strong performances from the likes of Vanguard US Equity Index and Atlantic House Defined Returns whilst at the other end of the spectrum JP Morgan Emerging Markets Income and Schroder Asian Alpha Plus detracted, again as a result of Chinese exposure.

Finally, the Income portfolio delivered a return of 1.12% with many of the value focused funds within this portfolio performing strongly. The standout performers during the month were Man GLG Income, JO Hambro UK Equity Income and Vanguard Global Equity Income, offset to a small extent again by emerging market exposure via the Fidelity Asian Dividend fund.