ESTATE CAPITAL INVESTMENT PORTFOLIOS
OUTLOOK

EDITION 38 Winter & Spring 2023

In This Edition:

The bond market runs Britain.

An overshoot is as likely as a pivot.

Xi is in total control of China.

Once inflation falls, bonds and equities will stabilise.

US inflation looks to have peaked.

Gilts have lost -25% this year.

ESTATE CAPITAL

Central banks have not yet reached the point of pivot.

Central banks are approaching the point of maximum danger as they attempt to both curb inflation without tipping economies into a painful recession.

With UK inflation at 11.1% and eurozone at 10.7%, central banks are expected to react to this through higher interest rates, but there are growing signs of economic contraction, credit demand is falling and savings rates improving, showing that business and households are tightening their belts.

Having taken far too long to appreciate that inflation was far more than 'transitory' both the BoE and the Fed have prioritised getting prices under control. The Fed has done more than most with rate rises of 0.75% at each of the last four Federal Open Market Committee (FOMC) meetings. This has been an aggressive tightening exercise but one that the USA could manage. The Fed has been bold in countering inflation because the US economy is in good shape.

The annual inflation rate in the US slowed for the fourth month running to 7.7% in October as compared to 8.2% in September and lower than the market forecast of 8.1%.

The US unemployment rate fell to 3.5% in September 2022 but increased to 3.7% in October to match market expectations in another sign that overall labour market conditions in the world's largest economy remain tight.

The BoE and ECB have been far more cautious in their approach to rate hikes. The ECB must respond to differing priorities from its member states.

Some G7 central banks are becoming more sensitive to over tightening and have started to rein in on rate hikes, even the hawkish Fed is starting to talk about reducing the pace and size of future rate rises and to assess the impact of policy changes prior to another step.

In the UK, Ben Broadbent the BoE Deputy Governor has suggested that UK interest rates may not rise as high as analysts are expecting given the damage high interest will do to mortgage holders and the wider economy. This has been interpreted that the BoE are increasingly concerned that high rates will deepen a recession and cause a crisis in the housing market.

UK base rates are currently 3.00% and expected to now rise by 0.5% at Decembers MPC meeting. Markets are predicting a peak of between 4.5% and 5% by June. Previously markets had predicted a peak interest rate of 5.25% in order to control inflation. The BoE own modelling suggests a rate of 5.25% will reduce GDP by 5% which is considered overly severe. Goldman Sachs are predicting UK CPI inflation will hit 11.9% by next April.

While the UK has mainly recovered from its currency and gilt yield spike, there have been other countries that have endured financial pressure. These stresses are fundamentally emulating from liquidity in the US treasuries market. The Fed has moved from a policy of loose money which has fuelled inflation to one of monetary tightening. All central banks are collectively draining liquidity from the international system as they withdraw monetary support. It is this squeeze on capital that is making currency and credit markets sensitive.

It is not just the GBP that has weakened against the mighty US$ this year. All currencies have been devalued relative to the US$. The US$ is now stronger in relative terms than it has been for many decades.

Due to the strengthening of the US$ the draw on capital has been strong. The pull of money to the USA is leaving other countries under pressure to attract international capital. The result being that the values of the Euro, Yen, Renminbi and Sterling have fallen substantially.

As a result of a strong US$ and US treasury yields currently at 3.79%, the rest of the world is experiencing a shortage of cheap capital. When the UK government ask investors to buy UK gilts to fund our energy cap policy and unfunded tax cuts, the market reacted by wanting a higher yield. This further explains why markets are sensitive.

The US economy is far better insulated from recession than other nations. Despite the rises in US interest rates, US economic data is quite positive. Business and consumer confidence remain strong and spending is being maintained. The reason for the easing of US inflation is that oil prices are falling as is the cost of imported goods.

The Fed is still of a view that the US labour market is still tight. The Fed would like US unemployment to rise from 3.7% to around 4.5%. At that level of unemployment, the rate of wage inflation would be modest. The US jobs market created 315,000 new positions in August and then another 263,000 in September and a further 239,000 in October. There are no strong signs that new job numbers significantly subsiding so we can expect US interest rates to continue for a while perhaps until a fall in new job numbers.

The one issue that all investors would like to see is US yields starting to fall. There are signs that US inflation peaked in June and that US inflation currently at 7.7% is now expected to fall to 7% in December and then to 5.5% in Q1 and to 3.25% by Q2. After a period of aggressive rate tightening by the Federal Reserve, US interest rates currently stand at 4.00% and are expected rates to hit 5.0% with a 0.5% rate rise at the next two FOMC meetings in December, and January.

Monetary contraction in the US is now at a concerning rate. The Fed is removing US$1.1tn of cash from the economy and commentators are feeling that this is over doing it and creating recession. Fortunately, the Fed has seen this danger and is talking of reducing the pace and size of quantitative tightening. The actions of the Fed over the next four months will be significant to the future of stable money. What will prompt an ease in tightening is a fall in core inflation and a rise in US unemployment. US 10-year Treasury yields have come down from 4.33% last month to 3.79% in mid-November.

The easing of US Treasury yields has also coincided with the US$ slipping in value against other major currencies giving some prospect of the easing of global financial conditions. Markets feel rate rises will be less than expected in the US so have revalued the dollar accordingly. An overly strong US$ brings inflation and capital imbalance to the rest of the world economy. Any sign of the transatlantic mis-balance narrowing is a good sign.

Central banks have not yet reached the point of pivot but it is getting closer and markets are feeling it.

Stock markets are not expected to deteriorate much more.

The global economy is heading for recession, the depth of which may be quite shallow in the USA but deeper in the UK and Europe. It is the spectre of inflation that has driven central banks to tighten monetary conditions which are in themselves recessionary and the root cause of all the equity losses and bond price falls this year.

Stock markets have priced in the known news over inflation and there is a growing view that headline inflation in the most influential market, the US, has peaked and therefore a new threat is that the Fed will over shoot with rate rises.

Jerome Powell, The Federal reserve Chair will be focussing on US data to make future policy calls. Expectations are that while core inflation has not yet reduced, when it does, there will be a faster fall in overall inflation. Some Fund Managers and analysts suggest US inflation currently at 7.7% will be back to 2.5% within 12 months.

Stock markets are not expected to deteriorate much more from current values as the expected recession could be relatively mild and stock markets have priced this in already. Bonds have been mispriced due to near zero interest rates and have now reacted to yields rising to match the market demands of an inflationary world. For a safe asset, gilts and bonds have been incredibly volatile especially long dated credit. Once bond yields stabilise, we will have far more attractive investment conditions.

The US housing market is showing pressure from the Fed rate rises. US mortgages rates are up and this is impacting new house sales. The current US mortgage rate is 6.81% while a 30-year fixed mortgage is 6.92%.

The last housing crash in America was in 2007/08 and was promoted by massive oversupply and very easy money. This year there is far less stock available therefore the lack of supply will protect prices.

In 2008, subprime lending was high but this has changed now. Subprime lending is hard to obtain and accounts for a small proportion. The superprime sector is now predominant. This is supported by a robust and well capitalised US banking system.

The US economy is still creating jobs. There were 315,000 new vacancies in August, 263,000 new jobs in September and 239,000 in October. Unemployment was 3.7% in October. Everyone who wants a job can get one as only half of vacancies are being filled.

The Fed is watching the unemployment rate in order to predict wage inflation. With job vacancies still strong the Fed will not rush pausing rate rises. Any increase in unemployment will likely mean that interest rate rises will be less as wage inflation will be reduced. A cooling economy will be better for rate hikes.

The US markets are better placed to weather the recession storm and therefore likely to be the first economy to lead the way out of recession. For this

reason, we are retaining our overweight position in US equities and will be re-introducing some US treasuries to the portfolio.

Europe is focused on getting through this winter's gas demands by filling its gas storage capacity and so can avoid being reliant upon Russian energy supplies. Russian gas is being replaced by US LNG as well as Algerian and Norwegian gas. US LNG is being supplied to the UK and then piped to European storage as the UK has so little storage capacity. European gas storage is now full.

If the winter is a normal one and so far, weather forecasts are suggesting a relatively mild winter, then black outs are expected to be avoided. The funding of gas storage has been expensive as will be the energy price cap policy of the UK and German governments. The German government plan could cost €200bn, while the original 2-year Liz Truss energy cap plan was expected to cost up to £150bn. This has since been reduced in scale as gas prices have fallen and the government is wanting to reduce its debt costs.

Both the UK and German government want to shelter the public from excessive gas prices. This has been seen by markets as vital to the economy and will help avoid a deeper recession.

The position of the UK government has shifted dramatically since Jeremy Hunt took charge of the Treasury. This has only been further reinforced when Rishi Sunak become Prime Minister. Jeremy Hunt has the support of the BoE and is seeking significant cost reductions in government budgets and reversed nearly all the tax cuts in order to balance the UK budget over the years to come while reducing the nation's debt pile of £2.54tn which as a percentage of annual GDP is 95.6%. This will be hard in the face of a recession and a cost-of-living crisis.

September's failed mini-budget put the UK's finances under the spot light and has resulted in higher borrowing costs. Consumer spending and therefore corporate earnings are expected to fall and that the UK will underperform other G7 countries in 2023. Despite this outlook, UK unemployment is only 3.6% and the employment rate is 75.5%. There are 1.2 million unfilled job vacancies and 1.5 million people unemployed so almost everyone without a job could have one. Since Covid 500,000 people have left the workplace either due to a lifestyle change, ill health, early retirement or just not working.

The UK stock market has been far more resilient than most other markets this year. Starting January 2022 at 7384 points it now stands at 7474. All predictions are for a recession in Europe and that stock prices reflect a relatively mild recession. The impact of wage inflation over the next year will have an influence over interest rate policy and a fall in employment would be healthy for lower borrowing costs. That does not at this stage look obvious in the US with new job vacancy numbers still strong.

The Fed remains focused on addressing elevated inflation through monetary tightening.

On 2nd November, the Fed FOMC raised interest rate by 0.75% to 4.0%, which was broadly in line with what the economic consensus had expected. This is the fourth consecutive time that the FOMC has raised interest by an aggressive 0.75%.

Fed Chair Powell sounded hawkish saying that he preferred “to overtighten” and then “use our tools to support the economy later on.” Powell expressed that “if we failed to tighten enough, inflation would become entrenched and that would be a much bigger problem.” In other words, the Fed continues to remain focussed on addressing elevated inflation through monetary tightening.

In the near-term, the Fed remains hawkish. Nevertheless, given that the FOMC has raised rates at a rapid pace in a short period of time, there is potentially room for a future step-down in tightening. The Fed Futures market is now looking for the FOMC to raise interest rates by 0.5% at its December meeting, before stabilising at around 5% in 2023.

The risk for the Fed is that inflation surprises on the upside. This could come via a tight labour market that drives up costs and pushes wage inflation. However, the latest Employment Cost Index for the third quarter was reported in line with economists’ expectations and stabilised at 5.0%, the same rate as the previous quarter. Importantly, this was the first time since the pandemic that the annual rate of wage inflation growth stopped accelerating and suggests that higher wages may not be getting entrenched in the labour market.

Another concern for the Fed is that inflation upside could come from higher energy prices. The latest developments from Organization of the Petroleum Exporting Countries, known as OPEC+ (which includes Russia) to reduce oil output by 2 mbd in October is not encouraging. What makes this a highly unusual decision is that the West had called on the Middle East-led oil cartel, and particularly the Saudis, to keep crude oil flowing during this energy shortage.

The official reason given for the OPEC+ production cut is that it is a response to rising interest rates and declining global growth expectations in advanced

economies. Nevertheless, it is possible that OPEC+ egged on by Russia, is pushing back against the desire of the West to lower energy prices. After all, OPEC+ is a profit maximising oil cartel with material pricing power. In short, energy is increasingly becoming weaponised. Brent Crude oil prices stand at US$85pb and has been trending down from a June high of US$123pb.

As it stands, money markets forecast US short-term interest rates to peak at around 5.0% early next year. Should interest rate expectations stabilise it should provide an opportunity for equities to recover from deeply oversold levels and low valuations.

On 3rd November, the day after the Fed announced a 0.75% rate rise so did the Bank of England. The Bank lifted the UK interest rate to 3% from 2.25%, the biggest increase since 1989. This takes borrowing costs to their highest since 2008, when the UK banking system faced collapse.

This rise in UK interest rates to 3% was expected and was voted on a 7-2 majority. Two members of the MPC voted for a 0.5% rise. This worried markets as it indicates that policy makers are concerned about the economy and recessionary pressures enough to prioritise a lower rate above inflation control. The BoE has warned the UK will see its longest recession since records began and will face a “very challenging” two-year slump. It also warned the unemployment rate will nearly double. The Bank believes by raising rates it will make it more expensive to borrow and encourage people not to spend money so easing pressure on prices.

The risk for the Fed is that inflation surprises on the upside.

At this stage an overshoot is as likely as a pivot.

The central outlook from fund managers is that the world will fall into recession but that it may be shallow. If we use the two quarters of negative GDP growth as the definition of a recession then the USA has been in recession this year already. However, a recession is usually accompanied by a meaningful pick up in unemployment and this is far from the case. The current unemployment rate is 3.7% and new job openings have been strong every month.

Other indicators of a downturn such as business confidence surveys and inflation show a different story, one of stagflation. Equities usually suffer during economic slowdowns as corporate profitability is hit by weaker growth and rising costs from higher wages and interest rates. The magnitude of equity losses this year has been greater as compared to past slowdowns despite the maintenance of corporate earnings. This is due to the high level of monetary tightening. The contraction in economic activity has come after the very sharp recovery from Covid lockdowns.

The S&P 500 started the year at 4766 and in late November stood at 4003, a fall of -16% while US interest rates have risen from 0.25% in January to 4% in November.

With US inflation currently at 7.7%, comparisons are being made to the stagflation period of the 1970's when inflation soared due to an oil price shock but was not managed well as inflation returned for much of the decade. The Fed has learned that lesson and is more likely to push down on inflation harder and longer which is itself a recession worry.

While the 1970 inflation surge was caused by oil hitting US$150pb, this is not the case now. Inflation is the result of an imbalance between supply and demand for goods after the ending of Covid lockdowns and this has since been magnified with the invasion of Ukraine by Russia and the resulting sanctions as well as the impact on supply chains by China's brutally restrictive and ineffective zero

Covid policy. Another factor of this slowdown is the number of workers who have withdrawn from the work force which has created a tighter labour market.

In the USA there are 10.6 million unfilled job vacancies and 5.7 million unemployed seeking work. While early retirement, health or family circumstances may account for a meaningful number of people not seeking work, it is now likely that with inflation impacting the cost of living, that more will seek work. As it is there are currently two jobs for each job seeker. The recession may cut the number of vacancies and higher wage growth may be an incentive to return to work.

Any easing in the job market will be seen as positive by analysts as this takes the pressure off the Fed to continue to raise rates. However, the US economy is still creating jobs. There were 315,000 new vacancies in August, 263,000 in September and 239,000 in October. Unemployment was 3.7% in October.

There has been talk of the Fed 'pivoting' to a softer position on interest rate rises. While US headline inflation looks to have peaked, but key parts of total inflation still look sticky and nothing is likely to change policy until the sections such as housing, core services and food inflation fall and job growth declines. Unemployment is still at one of its lowest levels for several decades. The labour market matters most for inflation due to its impact upon wage growth. Low unemployment usually means higher wage growth.

Markets have been aware that the Fed may, with improving inflation data, ease the rate of expected rate rises but as of early November the Fed is focussed on addressing elevated inflation through monetary tightening.

In the past a policy 'pivot' has been the result of an event rather than just deteriorating economic numbers. The Fed hopes to rein in inflation through tighter financial conditions. We may not see any easing of rate rising until there is confidence in a victory over inflation and that is likely to happen in the USA first.

The opposite of a rate pivot is that the Fed over hikes in its desire not to repeat the errors of 1972 and raise and retain rates more than is needed, that creates a recession. At this stage an overshoot is as likely as a pivot.

US rising inflation looks to have peaked.

There were three big market-moving stories in early November: the US midterm elections, the latest crash in the unregulated world of crypto currencies, and the release of US inflation data for October. By Friday, it was the lower-than-expected inflation data that dominated in terms of market activity.

The inflation report from the Bureau of Labor Statistics revealed annual consumer price index (CPI) inflation slowed to 7.7% in October, below the 8% expected by most economists, and the lowest level since January. This was a very good piece of news and better than expected.

It looks as if US inflation has peaked and is now declining. While it is still too early to assume the US Federal Reserve will pivot away from its monetary tightening policy, the market euphoria following the data release was quite significant. Not since the market confusion in the early days of the Covid pandemic have we witnessed so much movement in both equity and bond markets. Observers could have got the impression that all 2022 dominating market trends had reversed with the tech-led Nasdaq gained 7.5% and US 10-year Treasuries rallied as yields fell 0.3%.

While we may not have reached the actual turning point in terms of reversing market and economic tides, perhaps last week's activity confirms that there is a widespread belief in markets that the current economic downturn is more likely to be shorter and shallower than some scaremongers including Andrew Bailey, the Governor of the Bank of England, would like to suggest.

What has led to the slight decline in US consumer price inflation is a reversal of the price of goods. Supply chain disruptions have largely disappeared as time has allowed production processes to realign themselves. Freight prices have normalised, and China has once again become an exporter.

This is good news indeed for shoppers, especially with Christmas approaching, but is clearly no longer the primary focus of central banks, who are more concerned about secondary inflationary pressures, namely tight labour markets leading to wage inflation.

Expectations that Fed Chair Jerome Powell will get more dovish are premature until labour markets ease. Should the Fed raise rates at its December meeting by less than the a 0.75% as they have in their last four meetings, Fed members may as well tell markets that they are indeed pivoting. So, it is likely and even probable that external cost pressures in the overall inflation dynamics will be easing over the coming weeks and months (goods prices in the US and energy prices in Europe), but that is not yet sufficient to realistically expect central banks to take their foot off the monetary brakes.

The Fed's December meeting may well cause yet another turn in market sentiment and the underlying corporate profit development, coupled with thinning seasonal liquidity from institutional investors, leaves us facing some more potential volatility before the year ends. However, the outlook for asset markets over the near term into 2023 is certainly getting better.

It is the rise in interest rates that has driven the US$ to new highs against other leading currencies. The US$ is up 16% against a basket of global currencies this year. This is driven by uncertainty and US interest rates. These rate rises have attracted foreign capital with investors seeing the US$ as a safe haven.

While US stock markets have seen declines this year, UK investors in US markets have been cushioned from these declines due to the pound falling at the same time and the conversion of US assets back to Serling is better.

The S&P 500 is down -16% so far this year but in GBP terms that is only -4% due to the relative reduction in sterling value this year. When US stocks recover, then the gain can be in both equity and currency.

The same principle has worked for FTSE 100 companies, who collectively make over 70% of their earnings overseas and are only modestly exposed to the UK domestic economy. They benefit from translating mainly US$ earnings back to Sterling reported profits and dividends.

What is good for the US$ is usually a problem for the rest of the world in times of downturn. The US economy is sucking up global capital that is proving to be a drain on credit costs.

Xi is in total control of China.

The much-heralded 20th Communist Party Congress took place in early October and President Xi Jinping was confirmed as President for a further five years. In accepting the confirmation, he announced new policies but one that did not change was the zero covid lockdown policy which has cost China so much in liberty and growth.

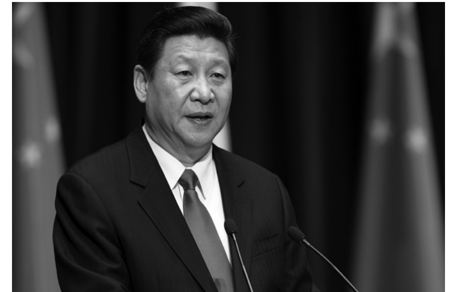
China has endured the world's strictest lockdown that have destroyed lives and livelihoods and there is no guarantee that this will not continue with Xi Jinping having been handed an unprecedented third term in office. Xi is in total control of China and is determined to enforce China's cultural and military dominance even at the expense of the economy. With the zero Covid policy continuing and another Shanghai lockdown in operation, the opportunity for a big economic growth stimulus package looks some way away until China is free of Covid.

Over the past 5 years, we have seen policies that de-risk the Chinese economy such as the crackdown on shadow banking, property development, local government debt and fin tech. There has been a refocus on 'common prosperity' and a cut back in private education companies. Xi has signalled that he will continue to pursue his common prosperity programme and in doing so will take on the financial elite in China. Hence the wealthy are leaving and their money is flowing out.

The Communist Party Congress appointed a new Politburo Standing Committee which will set the tone for the next five years. With the lowering of Chinese growth numbers, the pressure on ordinary people in a low growth economy with growing levels of unemployment and lack of investment will soon be evident.

The Chinese system of government relies on the good will of its population for its success. Hence, the new Politburo will need to address these issues so we should expect some form of Covid vaccination policy and a growth stimulus package.

China is in a very different position over inflation and interest rates. The country has the capacity for growth once the authorities allow it. Chinese inflation is currently 2.8% and interest rates are 3.65%



We are however concerned about the policy of Xi Jinping over culture and geopolitics and it is this that is frightening off international investors. As a comparison, Russia's share of world trade is only 1.5% and that has fallen due to oil and gas sanctions while China's share of world trade is 15.5%. China is far more engrossed and needing of export trade than Russia, which could be lost if China was to seek to recover Taiwan as a province of China.

The newly elected Politburo will be overwhelmingly dominated by Xi loyalists, while well respected economic reformers are retired. Their replacements are less experienced, close confidants or bureaucrats who will prioritise a state model of economic management.

The market reaction to the Communist Party Congress outcomes was negative. Stocks on the Heng Sang slumped and the Renminbi weakened against the US$ over concerns that Xi will continue with his ideological policy at the expense of the economy. Investors are repatriating capital due to the growing concerns over China withdrawing into a more dictatorial regime. This will hamper economic growth.

Official Chinese figures for GDP growth for Q3 were 3.9% beating expectations and were a strong bounce back from 0.4% growth in Q2 when many cities were in lockdown. However, these latest growth figures are high compared to all developed countries but well below past Chinese growth rates. The delayed disclosure of the Q3 GDP figures did not reassure markets either. The main concerns are that the property sector continues to slump, retail sales and labour markets are weak and any stimulus support looks some way off.

Some observers are hoping that China will initially stand by its zero Covid policy but will take incremental steps towards easing the policy. China must re-open and will need to stimulate growth. This is not universally accepted as there are concerns that the Secret Kingdom will revert to exactly that.

We hope that Chinese leaders will begin to re-engage with their global counterparts in other countries after a prolonged lockdown. This will be a signal of the approach the new government takes and so far, it is not looking encouraging.

Xi Jinpings' reaction to the covid protestors will be his biggest test. The demonstrators may be suppressed but the zero covid policy then relaxed.

One thing we can learn from this fiasco is that the bond markets govern Britain.

A week is a long time in both UK politics and the UK economy as markets punished ex-Prime Minister Liz Truss and ex-Chancellor Kwasi Kwarteng for a non-costed tax reducing budget.

Announcing a fiscal stimulus package contingent upon economic growth to replace tax revenue, before explaining where the growth was coming from was not well received. Markets did not appreciate this policy when Britain has a vulnerable currency, a large national debt and trade deficit and is a major energy importer with very little winter gas storage capacity.

Tax cuts to stimulate economic activity is a sound policy, historically tax revenue has risen when tax rates cut, unfortunately the timing was wrong. This in hindsight should have waited untill after gas prices were falling, inflation in decline, interest rates falling and national debt falling as a % of GDP.

Liz Truss felt she could pull off a major turnaround in the UK fortunes over the next two years, but the Treasury, Bank of England, Office of Budget Responsibility, and the City did not. The opinion of City analysts and traders is instantly visible in the foreign exchange and bond markets. The latter has control of the personal finances of the public.

The government had to reverse all three tax cutting aspects of the mini budget. The cut in 45% highest income tax rate to 40%, the cutting of basic rate income tax from 20% to 19% and the stop on corporation tax rising from 19% to 25%. The ending of the 2.5% national insurance increase has remained.

On 23rd September, the day of the mini budget, Sterling stood at US$1.14 only to fall to US$1.035 but then recovered to US$1.11 when the Bank of England stabilised gilt prices on 28th September. Sterling was at this value when Kwasi Kwarteng stood down as Chancellor. Over that same time frame UK 10-year gilt yields were 3.7% prior to the mini budget but lifted to 4.5% soon after, fell to 3.85% when the BoE stepped in and are 3.1% in late November.

Kwasi Kwarteng's career has taken the hit for a poorly considered budget, but he was not wrong about the need for the UK to correct long term weaknesses and deficiencies in the economy. Sadly, for what was positioned as an important growth budget focused on creating an investment focus for the UK with lower taxes and less regulation, instead has resulted in higher borrowing cost for business and home owners. This has for many wiped out any NIC savings.

There were claims that this budget has been unfairly treated by international investors as UK debt to GDP is lower than the majority of the G7 nations. The post Brexit opportunities for investment and regulatory reform which could have seen a Brexit dividend have so far come too very little including the reversal of this growth focus budget.

Unfunded tax cuts at a time of a pending recession

and a cost-of-living crisis were always going to be a hard sell especially if not backed up by an independent audit from the Office of Budget Responsibility (OBR).

Fundamentally, Truss and Kwarteng did not trust the orthodoxy of the Treasury or the OBR as they held different economic visions. They wanted to challenge the economic orthodoxy that has run western economies for decades in order to stimulate growth. The Truss government thought they could beat this orthodoxy but they did not understand the power of the city.

The ending of the governments' immediate plans to reduce taxes was confirmed by Jeremy Hunt and brings budgetary discipline back to government finances. This decision was in part forced upon Jeremy Hunt by the Bank of England (BoE) not offering an open-ended commitment to gilt price underpinning. The BoE gilt purchasing programme ran only till 14th October and so Hunt's hand was forced.

It makes little sense for the BoE to be purchasing gilts when they are seeking to run down their QE bond assets by selling them back to the market in order to tighten money supply and head off inflation. Around the world, central banks are seeking to control the inflation that was built up from low interest QE stimulus.

The budget U turn in higher rate tax and corporation tax reductions were welcomed by the Governor of the Bank of England, Andrew Bailey to bring back balance to the UK books. He said 'Flying blind is not a way to achieve sustainability.' This has been interpreted as a criticism of Kwasi Kwarteng and by association Liz Truss.

The problems for the Government have not been helped by the slow to act BoE. Andrew Bailey, has a long-standing reputation for slow and ponderous decision making and has been criticised in many quarters for being far too slow to raise UK base rates when inflation was building. The BoE were still buying bonds up until December 2021 when inflation was accelerating. The BoE pumped £400bn into the UK economy between 2020 and 2021 as they thought inflation was only temporary.

The Monetary Policy Committee that Bailey chairs, has not risen interest rates at a pace to have brought inflation under control and therefore are now more likely to have to raise rates even more to catch up for their inaction. UK base rates were raised by 0.75% on 3rd November MPC meeting.

The size of the shortfall in the UK budget is £62bn which Jeremy Hunt must find in order to regain market confidence in the UK government. The £62bn will be needed for the 2026/27 fiscal year in order to stabilise Britain's debt to GDP ratio. This gap could be filled by reasonable growth in the economy but analysts do not see where that growth is coming from in the short term.

One thing we can all learn from this fiasco is that it is the bond markets that govern Britain.

UK base rates are expected to hit 4.5%.

There is something profoundly efficient in the UK's unwritten constitution. It has been able to remove a failed Prime Minister and start again as if nothing had happened quickly and quite ruthlessly. We can certainly say that we live in interesting times, but times that are serious and concerning to our people and our economy.

Liz Truss wanted to give tax cuts to both business and individuals and use borrowing to offset the lost revenue. The potential for growth through incentive was clear, the outcome however, was that the resulting interest rate rises negated any benefits business may have received.

Liz Truss bowed to the inevitable, but despite her rapid downfall, she did ask some important questions about the future of the UK economy. Past governments of all colours have with the support of the Bank of England, (BoE) borrowed huge sums to support public spending assuming growth was constant, but it is not and we need to find some.

With national debt standing at £2.45tn, declining productivity and a growing trade deficit, Britain's growth outlook is not strong. For many, Brexit was seen as an answer to change course but so far, any such opportunity has been largely missed and our trading relations weaker. Our next few governments will have to answer the key question over how we raise productivity, create new jobs and new industries to replace those in decline, achieve greater efficiencies with public money, reduce our trade deficit, move to reliable and sustainable energy and control inflation. These are tough challenges for the next decade at least.

UK inflation is currently 11.1% which is five times higher than the BoE inflation target. The BoE are very aware that acting only to control inflation with higher rates will only deepen and prolong any recession and punish mortgage holders and business. Higher interest rates will also cost the government more to pay the interest servicing costs of our national debt.

The UK base rate is currently 3% and is expected to rise in December by 0.5% to 3.5%. Rising interest rates from historically low and near zero levels to somewhere closer to normal rates is starting to show how fragile some areas of the economy are. The BoE Deputy Governor, Ben Broadbent has stated that the BoE is very aware of the impact that high interest rates will have upon the economy. Analysts are predicting that the highest rate of UK base rate

interest is now likely to be 4.5% rather than 5.25% as previously thought. This reduction will filter through in lower mortgage costs.

New Prime Minister Rishi Sunak, has already restored some economic confidence to the UK. Since Sunak entered No 10 sterling has risen to US$1.20 up from US$1.095, while 10-year gilt yields have fallen from 4.43% to 3.1%. One could easily think that the most turbulent month experienced by bond markets since 2008 and the Premiership of Liz Truss never happened.

Rishi Sunak's new government is focused on fiscal prudence and a different winter lies ahead for households and businesses. For example, the energy price cap protection is now to be reviewed after six months and not last for 2 years. The current mild weather has reduced gas demand and that near-term energy prices have fallen. This is a welcome outcome as the imports of LNG mainly from the USA shows that the redistribution of global gas to cover the loss of Russian supply to Europe has been a success and achieved sooner than expected. There is in fact an over-supply of LNG as storage capacity in Europe is full and tankers are waiting to be unloaded.

The Sunak government are taking a hugely different approach to fiscal matters and one that he maintained consistently throughout this summer's Tory leadership campaign.

The Treasury has warned that everyone will have to pay more tax to put the UK's public finances on a sustainable footing and that spending cuts alone would not be enough to ensure the government meets its targets on spending and debt. The Treasury has not put a figure on what it calls the "fiscal black hole" facing the UK, but has suggested it may be at least £50bn.

What is commonly called a "black hole" in the public finances refers to the amount the government would have to raise taxes by, or cut spending, to meet its medium-term financial targets. The projections are dependent on estimates about how much the economy will grow. The size of the shortfall has shrunk slightly since Mr Hunt reversed most of the measures introduced at last month's mini-budget. At the time, the Institute for Fiscal Studies estimated it could be as much as £62bn.

A big part of the deterioration in UK standing has been due to global forces. We should not ignore however, that there has been a relative underperformance of UK assets since the June 2016 Brexit Referendum and that the decision to leave the EU will remain a weakness until trade deals and relations with the EU improve. Britain is less resilient to shocks and self-inflicted shocks are ones we should avoid.

Investment losses of 25% are not associated with government gilts.

At the end of October, the price of a 'safe' 10-year UK government gilt has fallen by 25% and that of a 30-year gilt by 50%, while the price of an index linked 15-year gilt has fallen by 60% over a 12-month period.

Investment falls of these magnitudes are always associated with high-risk private equities not government gilts. This crash in gilt prices has been coming for many years ever since the BoE started of quantitative easing (QE) which pushed down yields and as a result overvalued the gilt price. The BoE kept buying up bonds to place cash into the economy and this has continued up until recently when the BoE started selling off their balance sheet of bond assets.

We have enjoyed a 40-year bull market in cheap money, low inflation, and low interest rates. Governments around the world have cut rates and stimulated economies with borrowed money, and we are witnessing the consequences.

The Bank of England is tasked with the control of inflation while also avoiding financial crisis. In September we saw these objectives being stretched and pulled in opposing directions.

With exceptionally high inflation of 11.1% and expected to rise even further to around 12%, the UK requires significant monetary tightening. The BoE has been criticised for being so slow to act and not get ahead of rising inflation early enough and therefore, we face tougher medicine now.

Septembers failed mini-budget was seen as fuelling inflation with tax cuts, while the BoE were seeking to suppress inflation with interest rate cuts and quantitative tightening. The BoE response to support pension funds in need of margin call liquidity was to offer lender of last resort cover through purchasing gilts. The Bank had to suspend the selling of gilts in order to buy gilts for a period of two weeks. Anything longer would undermine monetary tightening and for this reason the BoE could only have supported the gilt price for a short emergency period. Long term 30-year gilts yields rose from 3.6% to 5% at the mini budget only to fall back to 3.85% on the BoE intervention. They are now standing at 3.26%.

Treasury and BoE policy makers want to minimise volatility but they do not want to minimise yields as this would be seen as yield curve control. The Treasury authorised the BoE to purchase up to £100m in the gilt market in order to create stability. In the end only a fraction was used as the threat was in its self, sufficient.

The last 15 years has seen us become used to near zero yields, however with the world now

experiencing shortages in supply of gas, food, semiconductors, and labour, it is only to be expected that interest rates will have to move higher to establish the balance between supply and demand.

Higher inflation has necessitated central bank action and that higher yield levels are needed to be attractive to investors. A higher yield is paid for in the bond price and these have fallen heavily in response to rising yields. Once inflation is seen to have peaked, yields can stabilise along with prices so that the interest in bonds will improve.

The selloff in gilts was not because of gilts themselves but through the need of pension funds to liquidate assets in order to pay margin calls on their derivative investments.

Ironically, higher gilt yields are a positive for any fund with long term liabilities. With rising bond yields, the discount factors for liabilities goes up and current valuation of future liabilities goes down.

Over the longer-term UK corporate and government bonds look like a good buy as yield based returns are looking better than has been the case for over a decade. This year we have started a down turn in bond prices after nearly 40 years of rising prices. When the bull market for bonds started in the 1980's the 10-year gilt yield was 16% it is now 3.1%.

Equity markets are very influenced by bond markets and are not likely to rally until global bond markets stabilise. Bond markets are perhaps now reasonably priced and yields will only rise if interest rates and inflation push higher than expected. A key moment of change will come when US core inflation declines. At that point yields should stabilise.

US 10-year treasury yields hit 4.3% in October but are now 3.79%. This was aided by the US economy growing in Q3 by 2.6% as compared to market expectations of 2.4% and returning to growth after both Q1 and Q2 were negative. The Fed hiked interest rates by 0.75% in November but is now expected to hike by 0.5% in December and 0.5% in January before stabilising at 5%. The UK is expected to stabilise at 4.5%.

We have enjoyed a 40-year bull market in cheap money, low inflation, and low interest rates.

The energy cap is a massive financial commitment by the Government.

The government's policy to cap the price of energy will have a marked impact on the cost of heating homes this winter.

The cap will result in an average heating bill of about £2,500 but without the cap families would have been facing bills of an average of £5,000. This policy in itself is counter inflationary and because of it, UK inflation is now expected to peak at a lower level which will reduce pressure on the Bank of England over interest rate rises.

The energy cap policy was a massive financial commitment by the Government. The original policy could have cost up to £150bn or 5% of GDP. The full impact will not be known as the future price of gas is market lead. The current trend is that gas prices are falling. The cost to the Treasury will ultimately depend upon the price and supply of gas as well as weather conditions and demand. Despite the commitment made by the government, markets were very happy with the policy as it was essential to households and business.

The current price of UK Natural Gas is £285 thm while the 10-year average has been around £75 thm. Prices peaked at £635 thm at the end of August and have fallen back since then despite the restrictions on gas supply from Russia into Europe.

The planning for gas storage to see Britain and Europe through this winter is essential. Europe has been building up storage of gas supplies ready for this winter's demand and Britain has been acting as a bridge for US gas imports into Europe. As Britain has so little storage capacity of our own, we have been exporting gas stocks to Europe. European stocks are now full. However, storage capacity is only 25% of the winter usage so ongoing supply is needed.

Centrica obtained regulatory approval for the re-opening of the Rough gas storage facility off the Yorkshire coast back in August but the site is still not factored into the National Grid's winter outlook for UK gas supply. The Rough site could at full capacity store sufficient gas to meet winter demand for 10 days which is 70% of the UK storage capacity. Rough is now not likely to help this winter but with a long-term agreement yet to be finalised between Centrica and the government it could support future winter needs.

The closure of Rough in 2017 in order to save costs has left the UK with little storage capacity and more reliant upon global gas markets. The decision to close Rough must now be seen as reckless.

The National Grid has warned of the possibility of blackouts this winter if Britain cannot secure sufficient gas to power gas fired power stations. National Grids base case is that Britain has sufficient electricity supply to get through the winter but this outlook is based upon imports from the continent being undisturbed. The reality is that our success in getting through the winter without electricity rationing will largely depend upon the weather. If temperatures fall, we may be facing black outs. We can all remember back to February 2018 when supplies ran dangerously low as the Beast from the East battered Britain with extreme weather conditions.

To ensure Britain can maintain reliable supplies of gas, the government is seeking to sign a 20-year gas supply deal with Norway. Norway is the UK's largest supplier of natural gas but this is being challenged by demand from other countries.

The German government has acted in the same way as the UK government in capping gas prices for households and business. The cost of this scheme is thought to be around £176bn. However, this policy has come under criticism from other EU countries as not being European or acting as one. Germany is Europe's best source of stored gas due to its large storage capacity.

The recent indefinite shut down of the Nord Stream 1 gas pipeline by Gazprom was supposed to be the Kremlin's big weapon against the West. Interestingly since the shutdown, gas and electricity prices have fallen from €335 mwh in August to €156 mwh now. A fall of 53%. The Russian share of EU gas imports has also fallen from 40% to just 9% since the start of the Ukrainian war.

Confidence is growing in Europe as gas storage facilities are now full that the continent can get through this winter without a severe hit to the economy. The ending of the war between Russia and Ukraine will be very welcome but will not change the need for Europe to invest in reliable clean energy and move away from over dependence upon Russia. The post war long-term implications are that Russia energy exports will be severely reduced impacting the Russian economy.

Eurozone inflation has hit a record 10.7%.

Eurozone inflation hit a record 10.7% in October, up from 9.9% in September and higher than expected. This rise was driven by energy prices higher than the previous 12 months. These figures came out at the same time as Eurozone GDP growth figures which showed the continents economy expanded in Q3 by 0.2% down from 0.8% in Q2.

The new inflation figures put pressure on the ECB to work harder to bring down inflation. The ECB had already risen interest rates by 2% over its last three meetings and is now expected to hike by another 0.75% at their next meeting in December.

Analysts feel that core inflation which takes out volatile elements such as food and energy is likely to remain uncomfortably high at 5%.

Business surveys in Europe point to a downturn and fall in output in Q4 and Q1 2023.

The ECB need to be very aware of the impact of higher interest rates will have upon the economy. Over hiking will only worsen conditions with Europe on the cusp of a recession. The ECB are still expected to prioritise price stability in the near term.

Higher borrowing costs will impact residential and commercial property values.

Mortgage costs have been in the headlines recently after the rise in the UK gilt yield. Lenders pulled mortgage products in expectation of a sharp increase in base rates. Many mortgage products have now been re-introduced but at three times the interest rate cost.

The implications of higher borrowing costs will have an impact on residential property prices and commercial property funds as well as the stock value of house builders. It has already been forecasted that house prices could fall by 8% in 2023.

We have seen property funds and house building stock fall more heavily than the FTSE All Share index. Both had done well after the end of lockdown due to higher consumer savings and property deals taking place. The sharp contraction in money supply since the start of 2022 has seen the property sector suffer significant losses.

Property values are tied to interest rates as property transactions are the most often geared investment as individuals and companies borrow to build or buy property. The loan to value matrix a vital factor. If borrowing costs are rising and valuations are falling, then losses are inevitable. The fact we have been living through over a decade of ultra-low interest and inflation rates brings this more into focus.

One sector that is showing the pressure of interest rate rises is Real Estate Investment Trusts. (REIT's). These funds are unusually leveraged and that borrowing costs will be now more expensive if not stressful. This sector has seen £100m withdrawn out of commercial property funds since the mini-budget. Therefore, funds are also suffering from liquidity issues and borrowing costs.

It is not a surprise that commercial property is a focal point of this credit cost increase. Particularly as occupancy levels of offices has not been fully recovered and that hybrid working is more common. In the UK commercial property market there will be strains for some time. However, in London there has been a building boom and supply is strong. The demand for space is holding up and rent defaults are low.

It is against this background we make our recommendations.

24th November 2022

INVESTMENT PORTFOLIOS

The second half of 2022 has been a more challenging period for investment than the first, given the aggressive interest rate rises of the US Federal Reserve and other central banks as inflation topped 10% in many developed countries. Inflation continues to be the dominant force in global finance. The period of massive government stimulus and public spending that saw the world through the Covid pandemic has now created the environment for high inflation.

The loose money years have now been turned on their head with central banks draining liquidity and tightening monetary policy to bare down on inflation. The consequences of high public spending and huge national debts are now hitting consumer confidence and spending with a recession ahead. The cost of living is putting pressure on wages and creating wage demands while business costs are rising so that profits and jobs are under pressure. Higher interest rates will influence mortgage costs and therefore property values.

Despite these fears, the outlook for stock markets has improved since US inflation looks to be now falling. In the past 5 months US CPI has come down from 9.1% in June to 7.7% in October. With falling inflation there is less pressure on the Fed to continue to rise interest rates more than is already expected. For this reason, US 10-year treasury yields have fallen from 4.22% in October to 3.79% in late November. With falling yields comes price stability and investor confidence.

We are living in particularly sensitive times and markets so easily over react to any new announcement which only increases volatility and investor nervousness. However, markets do know about all the bad news. If it is in the press, it is in the price holds true. Prices are generally starting to get better as markets see beyond what is currently expected to be a relatively shallow recession. Sadly, the UK is expected to be worse hit than most equivalent economies.

From the start of 2022 the world leading stock markets have performed quite differently. Please see below the % returns from 1st January to 23rd November 2022

UK	FTSE 100	+1.2%
	FTSE 250	-17.4%
Europe	EuroStoxx 30	-8.3%
USA	S&P 500	-16%
India	BSE Sensex	+5.5%
Hong Kong	Hang Seng	-25.1%
Japan	Nikkei 225	-2.9%

The difference between the FTSE 100 and FTSE 250 is that the FTSE 100 contains large global businesses but the FTSE 250 represents the domestic UK economy and as such has fared much worse this year.

With the expectations of further interest rate rises, inflation pressure and a shallow global recession we have amended our portfolio selections.

We have continued with our hybrid portfolio blend of both active and passive funds that we established in Edition 37. Edition 38 will see a slight rise in the allocation to active funds particularly in the bond section where we feel active oversight may be worthwhile. Performance has over the recent past has been above benchmark and we seek to maintain that advantage for investors.

The decline in US inflation has been a key improvement for our investment outlook. Inflation in the US is expected to be 7.40 % by the end of this year projected to trend around 2% at the end of 2023. The Fed will be pleased that their aggressive 0.75% increase in interest rates over each of the last four FOMC committee meetings has worked. We now expect the Fed to continue to hike but at 0.5% in December and 0.5% in January. They may then stop raising rates and see how the economy responds. Business and households faced with higher borrowing costs will be encouraged by the potential of no more near-term rate rises.

The labour market in the US remains strong with new jobs being taken up at the rate of 261,000 in October, 315,000 in September and 292,000 in August. The expectation is for around 250,000 new jobs will be filled each month in 2022 but fall to a new monthly target of 170,000 in 2023.

If the number of new job vacancies starts to fall then the Fed will be further encouraged that the US economy is slowing and that their interest rate rises have done their job. We expect another 1% increase in US interest rates as they will want to be sure inflation is beaten. If there are any signs of inflation raising then the Fed will take further action on rates.

We are happy to maintain our overweight position in the US as we do not expect a recession and that the US will recover first and fastest of the developed world. We have an emphasis towards low-cost US index trackers and active value funds with HSBC American Index Trust and Threadneedle US Equity Income Fund held in the portfolio.

We are concerned about the outlook for the UK due to labour shortages and high inflation. The UK's trade position is weakened and holding back investment and growth. With UK inflation at 11.1%, the BoE are expected to rise interest rates from the current 3% up to 4.5% over the near term in order to combat inflation. However, the Bank is sensitive to the impact that interest rate hikes will have upon borrowing costs, mortgage costs, and consumer confidence. Due to these concerns the BoE has hinted it will not likely go higher than 4.5%.

The UK is expected to enter a recession but perhaps not as severe as Andrew Bailey has predicted. Never the less, we have trimmed our UK exposure and invested in low-cost HSBC FTSE 100 and Vanguard FTSE All share index trackers. In doing so we are holding large UK based international businesses.

We see an improving outlook for continental Europe

due to a few factors, not least the success of the Ukrainian army in pushing back Russian forces in the Black Sea and South Eastern regions under Russian occupation. The conflict may endure for many more months and could at anytime take a desperate turn but the success of Ukraine should be supported as potentially the quickest way to a settlement.

European gas storage is now full and with alternative sources of LNG from the US and gas from Algeria and Norway, the threat from the Kremlin to cut off Europe's energy source has weakened. This was Russia's main play for the West to buckle but has been neutralised in a material way. Energy prices are still elevated but demand looks to be less as so far, the weather has been mild. A mild winter will likely mean that black outs or gas rationing are unlikely and European stock markets have responded positively.

Just like the BoE we expect the ECB not to go hard on rate hikes in fear of crashing the economy. With an outlook of lower-than-expected rate rises and sufficient energy to see the winter through, Europe is looking more attractive. We therefore have marginally increased our holdings in BlackRock European Index.

China has had a major impact upon global growth and inflation. China has adopted an aggressive zero covid lockdown policy which is still in force and has had a major impact upon manufacturing exports and supply. The lack of production has led to increased demand resulting in global inflation. President Xi Jinping has been confirmed in office for a further five years and has announced he will maintain the zero covid policy. Critics see this policy as unsustainable with urban unemployment at 6% and rising as it will disadvantage China. Some analysts are suggesting that a controlled easing of isolation rules and lock downs will start along with further vaccinations. If this is forthcoming then a stimulus programme of investment could follow and get China growing again. For this reason, we have, despite this year's losses in Chinese equities, maintained our modest holdings in the FSSA Greater China Growth Fund and to the JP Morgan Emerging Markets Income Fund that also invests in China.

The progress of Japan and the Asia Pacific region has been influenced by China's lockdowns. The reduction in trading has had in impact on stock values in the region. Again, we are expecting improvements in outlook so have retained our holdings in Vanguard Pacific Index Trust and Fidelity Japan Index and introduced Jupiter Asian Income Fund.

The fixed interest market has been exceptionally challenged this year. After years of falling bond yields and elevated prices, we can now see what impact of rising inflation and interest rates have had on the bond market. Inflation and rate rises have forced bond yields to rise significantly and as a result prices have fallen heavily. This year has been the pay back year for decades of low interest rates and over priced bonds.

The UK Conventional gilt index has over the past twelve months suffered a loss of -20.36% as yields have risen to meet market expectations. These are the type of losses sometimes seen in speculative private equity holdings not UK government gilts.

We have not held any long-dated bonds in our portfolio for some editions now so our portfolios

have not been exposed to these types of losses. We do hold a blend of short dated, inflation linked bonds along with some hedged bonds and floating rate notes. The short-dated inflation linked bonds and short dated high yield bonds have fallen by around -5% over the past year, while the hedged bond fund is down -1.5% and floating rate note down -2.5%.

We have a more positive outlook for bonds now that it looks like yields will stabilise. US 10-year Treasury yields are now 3.79% down from a high of 4.22% in October. UK 10-year gilt yields are now 3.1% having fallen from a high of 4.45% in October.

Within Edition 38 we have moved from holding inflation liked bonds to conventional bonds. We have continued to select short dated credit but also introduced some strategically managed bond funds in the form of the Jupiter Merian Global Strategic Bong, the Dodge and Cox Global Bond Fund and maintained the Royal London Diversified Asset Backed Securities Fund and M&G Global Floating Rate High Yield Fund. Our actively managed bond funds have increased in allocation as we feel that some active bond management is beneficial at present.

As far as the specialist sectors are concerned, we have been happy to maintain our holdings in sectors that have done well. The Polar Capital Global Insurance Fund has been particularly strong with a one-year return of 23.83%. We have retained Guinness Sustainable Energy Fund but have also added the Gravis Clean Energy Income Fund. The Clearbridge Infrastructure Fund has been replaced by M&G Global Listed Infrastructure on cost and trading grounds. We have halved our iShares Global Property Securities Index Fund holdings as we feel that higher borrowing and mortgage costs will impact property values. We have maintained our holdings in the JP Morgan Natural Resources Fund that has enjoyed on the back of energy and commodity prices a 39.58% return over the past 12 months.

We held in Edition 37, the Polar Capital Technology Fund, T. Rowe Price US Large Cap Fund and L&G Global 100 Index Fund but all three have not been included in this new Edition. We remain concerned about some aspects of the Tech sector and the Mega Tech sector in general. Our emphasis in Edition 38 is value not growth stock as we consolidate.

We are not holding any gold in the portfolio other than that held within the JP Morgan Natural Resources Fund.

We feel that a year of heavy re-pricing of values in almost every asset class and sector is coming to an end and while a recession can bring further sensitive volatility, we can be at last more confident about bond yields stabilising and an improving environment for investors.

As of the 14th November 2022, the best performing funds in our portfolio over the past six months have been;

Guinness Sustainable Energy Fund	24.89%
Polar Capital Global Insurance Fund	15.06%
JP Morgan Natural Resources Fund	10.57%
JP Morgan US Equity Income Fund	9.93%
Vanguard Global Small Cap Index	9.59%

As of the 14th November, the worst performing funds in our portfolios over the past six months have been;

Vanguard Global Bond Index	-5.45%
Fidelity Global Inflation Linked Bond	-3.92%
JP Morgan Emerging Markets Income	-3.51%
BlackRock Global Property Securities	-2.85%
T. Rowe Price US Large Cap Fund	-2.74%

As far as the 38th Edition is concerned, across all five portfolios, 10 new funds have entered the selection of which some are re-joining while 10 existing holdings have been dropped or substitutes for performance, ratings, or cost reasons.

The funds that have been removed are:-	TER
Franklin Templeton Clearbridge Global Infrastructure Income	1.59%
JP Morgan US Equity Income	0.92%
Royal London Short Duration Global High Yield Bond	0.69%
Schroder Asian Income	1.07%
Fidelity Asia Pacific Opportunities	0.93%
Fidelity Global Inflation Linked Bond	0.55%
L&G Global 100 Index	0.15%
Royal London Short Duration Global Index Linked Fund	0.27%
T. Rowe Price US large Cap Growth	0.95%
Vanguard Global Bond Index	0.31%

The funds that we have added are;	TER
Threadneedle US Equity Income	0.79%
Jupiter Merian Global Strategic Bond	1.17%
Jupiter Asian Income	1.13%
Vanguard FTSE All Share Index	0.07%
BlackRock Overseas Government Bonds	0.13%
Dodge and Cox Global Bond Fund	0.57%
M&G Short Dated Corporate Bond Fund	0.40%
Royal London Short Dated Gilts	0.29%
Gravis Clean Energy Income Fund	1.36%

PORTFOLIO PERFORMANCE

The Estate Capital Investment Portfolios

The balance of investments across different asset classes is the primary driver of portfolio returns.

The Estate Capital Investment Portfolios now offer five risk related investment strategies designed for medium to long-term investors seeking capital growth and income from a portfolio of leading investment funds. The individual funds that make up our diversified portfolios are selected on the quality of the fund manager and both the quality and consistency of past performance.

There is a wide range of asset classes across global markets available to investors. Our portfolios bring together a diversity of global equities, fixed interest securities, cash deposits, commodities, precious metals, infrastructure, and property. The global balance of investments across differing asset classes is the primary driver of portfolio returns.

Our asset allocation is built using a fully modelled asset allocation tool. This system is powered by research from actuaries Willis Towers Watson and investment data from Financial Express.

This modelling system offers us great accuracy to build and test the most efficient blend of assets for our five model portfolios. Each new edition of our portfolios is published on our website with fact sheets, performance figures, risk ratings and range of returns.

We benchmark and publish our portfolio performance against the most relevant national averages and are happy to say that our selections have enjoyed an enviable track record.

Cumulative Portfolio Performance from 14th November 2022.

Below are the past five year's gross investment returns for each of our portfolios from 14th November, 2022.

Portfolio	*6 months*	*1 year*	*2 years*	*3 years*	*5 years*
Cautious	0.75%	-5.43%	-0.36%	3.26%	11.03%
Conservative	1.36%	-5.97%	1.00%	7.15%	
Balanced	1.97%	-6.92%	6.34%	15.63%	25.26%
Strategic	2.82%	-3.29%	10.44%	15.30%	25.25%
Speculative	2.90%	-7.34%	4.80%	15.11%	26.92%

Discrete Portfolio Performance from 14th November 2022.

Below are the gross investment returns for each of our portfolios for each 12-month period over the last five years from 14th November, 2022.

Portfolio	*2022*	*2021*	*2020*	*2019*	*2018*
Cautious	-5.43%	5.36%	3.64%	6.11%	1.34%
Conservative	-5.97%	7.41%	6.09%	7.03%	
Balanced	-6.92%	14.25%	8.73%	7.37%	0.89%
Strategic	-3.29%	14.20%	4.40%	8.87%	-0.22%
Speculative	-7.34%	13.10%	9.84%	8.42%	1.70%

The above performance tables are produced by data from Financial Express Analytics. The tables are a proxy to our actual portfolio performance as they do not include adviser, manager and platform charges nor accurately reflect the actual dates that individual investor portfolios are rebalanced from one edition to another. The rebalance lag could amount to 8 weeks per rebalance. The proxy portfolio performance reflects the fund selection in each consecutive edition of our portfolios.

The value of investments can fall as well as rise. Past performance is not a guide to future performance. Cumulative and discrete performance charts show % growth from 14th November, 2022 calculated using bid prices with income reinvested into the fund net of tax.

Asset Allocation January 2023 - Edition 38

Portfolio	*Risk*	*Money Markets*	*Fixed Interest*	*Property*	*UK Equity*	*US Equity*	*Europe Equity*	*Asian Equity*	*Japan Equity*	*Global Equity*	*Other Assets*
Cautious	3	28%	34%	4%	7%	12%	2%	3%	1%	2%	7%
Conservative	4	26%	29%	3%	6%	17%	3%	3%	1%	5%	7%
Balanced	6	15%	20%	4%	8%	23%	6%	5%	2%	8%	9%
Strategic	7	12%	19%	3%	9%	29%	7%	5%	4%	7%	5%
Speculative	8	10%	13%	3%	11%	32%	7%	6%	4%	7%	7%

Perspective Range of Return & Volatility

Portfolio	*Risk*	*Return*	*High*	*Low*
Cautious	3	4.22%	15.72%	-7.29%
Conservative	4	4.99%	20.73%	-10.75%
Balanced	6	6.36%	29.70%	-16.98%
Strategic	7	7.06%	34.30%	-20.19%
Speculative	8	7.79%	39.22%	-23.64%

Investment Ratios

Portfolio	*Risk*	*Beta*	*Alpha*	*Sharpe Ratio*	*Info Ratio*
Cautious	3	0.87	0.16	0.00	0.99
Conservative	4	0.76	0.12	0.00	0.41
Balanced	6	0.81	0.19	0.06	0.52
Strategic	7	0.90	0.17	0.04	0.75
Speculative	8	0.91	0.15	0.00	0.42

Maximise your returns with a level of risk you're entirely comfortable with.

Financial Advice & Wealth Management

7 Uplands Crescent
Swansea
SA2 0PA

Phone: 01792 477763
Email: mail@estatecapital.co.uk
www.estatecapital.co.uk

Authorised and regulated by the Financial Conduct Authority.