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Everything Ethical Newsletter – January 2023

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Market Commentary

January saw a strong rally across markets as investors waved goodbye to a brutal 2022. They continued to pin hopes that central banks were near the end of their monetary tightening, whilst also seeing signs that the economy is facing a shallower recession than previously anticipated. The main US tech-heavy index rose over 10% in the month, the most since January 2001 and historically means it will gain at least another 14% this year, however January may wrong foot investors.

In the United States, the data continued to show that inflation is falling, the economy is slowing but the labour market remains strong. US CPI data was in line with expectations, seeing it slow to 6.5% but with core inflation remaining sticky. The Federal Reserve's (Fed) favoured measure of inflation, the PCE deflator, also came in line. Furthermore, manufacturing gauges came in much lower than expected, to levels that had not been seen since May 2020.

Despite this, the labour market remained strong with December's non-farm payrolls coming in slightly higher than had been expected. Yet, at the same time, average hourly earnings came in lower than had been anticipated. This, combined with the slowing inflation and economic activity, led investors to view on balance that the Fed was not far from the peak in its rate hikes. They also continue to bet that the Fed will start to cut rates before the end of 2023, despite officials speaking to the contrary, which fuelled January's risk-on attitude.

We think the market is due some consolidation given the moves, as the economy continues to hold up well and the Fed is willing to tip the economy into recession to get inflation back to target. This view was supported by January's non-farm data coming in much stronger than expected post month end.

The UK continues to find itself in a more difficult situation. The Bank of England will likely be forced to keep interest rates high, alongside a tight government fiscal policy, which will result in an intensifying squeeze on household income. Retail sales and consumer confidence metrics both came in lower than expected which reflected this sentiment. UK CPI did fall for the second consecutive month; however, core inflation remains sticky and unchanged. The UK is also suffering from a tight labour market and government neglect of public services, not to mention the damage done by Brexit to trade and the workforce. On the third anniversary since officially leaving, it has been estimated that Brexit is causing a £100 billion-a-year loss in output.

UK wages continue to add further inflationary pressure, with them growing at the fastest rate outside of the pandemic period at the end of 2022. However, the growth in the private sector was substantially higher than in the public sector, which only added to the tensions between government and unions. January saw further industrial action as public-sector workers demand fairer compensation, whilst the political circus continues to roll on. The sentiment towards the UK is so negative, we could potentially see an upside surprise moving forward, although we understand the reason for this pessimism.

Sentiment towards Europe is much more positive from a macro perspective, primarily driven by a warm winter that has helped alleviate concerns over energy supplies. As mentioned in last month's report, European energy prices are now below where they were before the Russian invasion of Ukraine. This, alongside the implementation of government support packages, has led to some dramatic falls in European inflation numbers. In a further sign of positivity, the Euro-Area economy grew 0.1% in Q4 when economists had expected a contraction of 0.1%. Several of our European stocks have performed well in January but we feel it is important to remain selective despite the top-down optimism towards the region. Structural issues still remain, for example the importance of the car industry in Germany, which is seeing increasing competition from China.

The sudden reopening of China is another factor that is driving improving sentiment toward the global economy compared to just a couple of months ago. As we anticipated in last month's report, this has caused short-term disruption due to a surge in illness but we are already seeing signs of this abating. Instead, we anticipate it to be a growth impulse felt through various sectors as supply chains continue to ease and Chinese people begin travelling internationally again.

Model Portfolio transactions in the month:

There were no changes made to portfolios during January.

Performance:

Funds MPS	January 2023
Defensive	**1.93%**
Cautious	**2.07%**
Income	**3.24%**
Balanced	**2.20%**
Balanced Growth	**2.41%**
Growth	**2.65%**
Adventurous	**3.01%**

Direct Equity MPS	January 2023
Cautious Green	**1.47%**
Light Green	**1.45%**
Mid Green	**1.98%**
Dark Green	**1.90%**

MPS Stock pick feature:

Eurofima is a supranational organisation that provides financing to European railway companies to electrify their networks. Eurofima is comprised of 26 shareholders (railway companies), from 25 member states, who are eligible to borrow at low rates. The use of this cheaper financing must only be used to purchase, modernise and refurbish Eligible Green Assets which include; electrical multiple units, electrical locomotives and passenger coaches when combined with electrical locomotives. Eurofima is therefore focused on climate change mitigation and the “greening” of the transport sector, with their bond issuances being 100% climate aligned with a green framework.

Ethical News

Toyota retained their position as the world’s largest producer of autos in 2022. However, it is only in recent weeks, following the appointment of a new CEO in January 2023, that they are beginning to warm to electric vehicles. They have historically been an advocate of the hybrid vehicles, questioning the focus on only EVs as the solution, arguing that hybrid gas-electric vehicles could be a solution, given the lack of infrastructure in place for electric vehicles. The new CEO, Koji Sato takes over in April, and will be behind the company’s new push, and it’s no surprise given the data; one in 10 vehicles sold in Europe and one in five in China were full electric.

Last year witnessed an important milestone in global efforts to decarbonise. Data suggests that for the first-time, investment into the energy transition equalled that of investment into fossil fuels globally over the year. **Investment into renewable energy**, electrification, energy storage and other technology reached **$1.1 trillion**. Whilst renewable energy saw record investment, electrification of transport is growing at the fastest rate, including into the infrastructure required for charging. For the first time, electric vehicles outsold their diesel counterparts in the UK despite the shortage of supply.

The UK government outlined new plans to protect and **restore wildlife in England** which builds on the 2018 25 Year Environment Plan. The plans cover how the government intends, amongst others, to create and restore at least 500,000 hectares of new wildlife habitats, incentivise farmers to adopt nature friendly practices and boost green growth and new jobs specific to a greener future. They also committed to every household having access to a green space or water within a 15-minute walk from their home. In a separate set of plans, the government also announced that new **log burners** would have to meet much stricter standards on smoke as they have become an increasing source of harmful air pollution in urban areas.

Redrow, one of the UK’s biggest housebuilders will install heat pumps in new homes as standard. This comes ahead of the likely ban on new gas boilers by the government in an effort to decarbonise homes (although the ban is not expected to kick in until 2033). Heat pumps work by running on electricity and drawing thermal energy from outside. This is the reverse of how air conditioners work, which extract hot air from a room and expel it outside. There are targets to install hundreds of thousands of heat pumps, although concerns remain over the likely shortage of engineers.

An investigation into **carbon offsets** used by large corporations have revealed them to be largely worthless and detrimental in the fight against global warming. Vera is the world’s leading standard for the offsets market, and it was revealed that more than 90% of their rainforest credits are likely to be phantom and not representative of genuine carbon reductions. Their credits are the most commonly used by companies and calls into questions carbon reduction claims that are made by the companies who use them.

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