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Market Commentary

March began as February left off, with economic data showing sticky inflationary pressure and the economy remaining resilient (sticky inflation referring to stubbornly high prices). This led to the market upwardly revising peak interest rate expectations. However, as the Silicon Valley Bank (SVB) news broke and the story developed to incorporate the wider banking sector, these expectations dramatically changed.

For reasons we highlighted previously, we have been defensively positioned over the last few months which has seen us at the lower end of our equity allocation and keeping cash allocations relatively high. We continued to be so into March, not quite seeing the clarity we desired before altering our asset allocation. This initially served us well as news in the banking sector saw a flight to safety and equity market sentiment sour further, continuing the downward trend it had been on since February.

Portfolios benefitted from having no exposure to the likes of SVB or Credit Suisse, as well as limited or no equity exposure to the traditional banking sector which shielded them from the gyrations to an extent. We have also been improving the credit quality of the debt within portfolios, favouring shorter dated and higher credit quality.

The deterioration in confidence witnessed an aggressive re-pricing of interest rate expectations, seemingly forgetting about the inflation fight that policy makers have been on for the last year. At the start of the Month, the Federal Reserve's (Fed) peak rate was expected to be around 5.5% in Q4 2023. Three weeks later, a peak of less than 5% was expected earlier in the year, followed by more aggressive rate cuts. This repricing saw longer duration assets benefit, but we remain confident in our current position. Inflation data has shown signs of stickiness and the labour market remains strong; we therefore felt this repricing was overdone.

In the UK, CPI came in to a surprise upside, remaining in double digits when it had been expected to fall below. Food inflation caught the eye, with prices increasing over 18% year on year despite global food indexes suggesting prices have fallen a long way from their peak. Elsewhere, headline CPI has been falling as base effects in sectors such as energy take hold, particularly in Europe. However, what is consistent and of more importance to policy makers, is that core inflation remains sticky globally, ticking up in several areas.

The view that the repricing was overdone was given further credence as eyes turned to the central bank policy makers. First up was the European Central Bank (ECB) who did not flinch under the pressure created by the banking sector and stuck to the 50bps hike, saying that inflation was projected to remain too high for too long. Next it was the Fed, where some economists were expecting no hike and one even predicting a rate cut. But like the ECB, they stuck to script and raised by 25bps and indicated that there may be more to come. Chair Powell also reiterated his view that he does not view a case for rate cuts this year. The Bank of England (BoE) rounded it off with a further 25bps hike, commenting that inflation was persistent and would require more hikes.

Subsequently, rate expectations have repriced once more, although not all the way back to the levels seen at the start of the month. For now, we anticipate higher for longer in terms of interest rate expectations. Arguably, the ECB still has the furthest to go with rate hikes given they had a lower starting level and started hiking later. The eurozone seems to be holding steady for now which will enable the ECB to do so without risking economic stability. However, post month end, the jump higher in the oil price adds to the uncertainty around inflation.

In addition to sticky inflation concerns, markets are also having to wrestle with shrinking central bank balance sheets. Cash is not only more desirable as an asset class, but also one where supply is falling, making life harder for more marginal investments. Whilst this has been talked about for some time, the recent banking issues are evidence that more demanding and disciplined capital allocation is hitting the streets.

Model Portfolio transactions in the month:

There were no changes made to portfolios during March.

Performance:

Funds MPS	March 23
Defensive	-0.66%
Cautious	-0.89%
Income	-2.00%
Balanced	-1.00%
Balanced Growth	-1.16%
Growth	-1.25%
Adventurous	-1.46%

Direct Equity MPS	March 23
Cautious Green	-1.28%
Light Green	-1.38%
Mid Green	-2.05%
Dark Green	-2.52%

MPS Stock pick feature:

Power Integrations Inc is a leading innovator in semiconductor technologies for high-voltage power conversion. Their products are key building blocks in the clean-power ecosystem, enabling the generation of renewable energy as well as the efficient transmission and consumption of power in a vast range of applications including appliances, mobile devices, computers and countless industrial applications. Their EcoSmartchips reduce energy waste when an appliance is in standby mode. Unlike traditional power conversion solutions requiring dozens of components, the company's integrated solutions reduce the bill of materials and the size of the integrated circuit board.

Ethical News

McDonalds is reportedly weighing up the pros and cons of rolling out reusable packaging in its restaurants worldwide. This assessment will look at the negative and positive environmental impacts of reusable containers, as well as comparison to other solutions, such as advanced recycling packaging. According to a 2021 study, **takeaway food and drinks packaging makes up 88% of the world's coastline rubbish**, so the move would seem a no-brainer. However, there are a number of considerations, including the assessment of energy and water use of the reusable containers, as well as consumer behaviour towards returning items which would need to be re-used multiple times before they are considered environmentally helpful, given the use of bulkier plastics.

March saw Chancellor Jeremy Hunt deliver his **budget for 2023**. As part of the plans, he committed to investing **£20 billion over the next two decades on low-carbon energy projects**, with a focus on carbon capture and storage. Interestingly, as it is a technology that splits opinion, he announced that **nuclear energy is to be classed as environmentally sustainable** for investment purposes alongside a promise for more public funding for it. There was the creation of what he called 'Great British Nuclear', which aims to bring down costs, and the launching of a competition to design small modular reactors. If the design is proven viable, there is potential for co-funding by the government.

RWE announced that its UK flagship offshore wind project Sofia, in construction off the North East coast, has signed an agreement with **Siemens Gamesa** to deploy recyclable blades on 44 of its 100 turbines. In total, 132 individual recyclable blades will be installed at the 1.4 gigawatts (GW) offshore wind project. This is the maximum available given the current market capacity for the new specialist resin used in the blades.

After almost 20 years of talks, **United Nations** member states agreed on legal framework for parts of the ocean outside national boundaries. The historic treaty is crucial for enforcing the 30x30 pledge made by countries at the UN biodiversity conference in December, to protect a third of the sea (and land) by 2030. Covering almost two-thirds of the ocean that lies outside national boundaries, the treaty will provide a legal framework for establishing vast marine protected areas (MPAs) to protect against the loss of wildlife and share out the genetic resources of the high seas. It will establish a conference of the parties (Cop) that will meet periodically and enable member states to be held to account on issues such as governance and biodiversity.