October 2021 Rebalance

General Overview

Asset/Region	Current Stance	Previous Stance
US Equities	Neutral View	Neutral View
UK Equities	Positive View	Positive View
European Equities	Selective Approach	Selective Approach
ROW Equities	Cautious View	Cautious View
Fixed Income	Negative View	Negative View
Property	Selective Approach	Selective Approach
Infrastructure	Positive View	Positive View

Since our last meeting, equity markets have suffered on the back of an expected tightening of monetary policy by central banks. The UK 10 year moved to over 1% for the first time since March 2020. Growth is slowing but is still above trend, and GDP figures from the UK and US have surprised to the upside.

The committee raised concerns over the global supply chain constraints and subsequent cost-push inflation pressures. There was a growing concern that inflation pressures are expected to be more entrenched; traditionally super-efficient global supply chains are unlikely to return in the same capacity, and companies will continue to see wage pressures for traditionally low-cost labour as shortages occur. We're anticipating quarterly reporting from companies to be the next pivot point for markets, and we plan to look out for margin squeezes and extra costs being absorbed.

To add to the aforementioned pressures on global production, there are growing concerns over energy supply worldwide. Both India and China have been reportedly experiencing blackouts as they run low on coal, and gas shortages in Europe are already straining EU relations.

Due to the above concerns, we're adopting a slightly more cautious view generally, especially in our cautious and defensive models where capital preservation is of greater importance.

USA

After non-farm payrolls fell short of economists' expectations in August, we anticipated September unemployment and growth data to have an influence on the Federal Reserve's decision around tapering of asset purchases, which they signalled could begin as early as November. Since the last IMC, non-farm payroll has disappointed again in September, but falling unemployment rates and rising wage growth acts in support of the policy changes desired by hawkish members.

The US debt ceiling was raised as a concern; failing to suspend the debt ceiling could have catastrophic consequences if the US government was forced to default on its obligations. Taking into consideration historic stand-offs between Republicans and Democrats over the debt ceiling, we anticipated a last-minute decision in favour (since this IMC, the debt ceiling has indeed been suspended until at least early December).

We continue to monitor the infrastructure bill, which is becoming increasingly intertwined with the social reform bill as moderate and progressive Democrats fail to agree on a course of action.

UK

A number of supply chain issues were discussed when it came to the UK, but these events are being witnessed further afield as well. Rising energy prices and HGV driver shortages were a couple of issues raised around the supply chain, and we remain vigilant to the possible blip in recovery as a result. This comes at a time then the Bank of England are becoming increasingly hawkish. Nonetheless, there was certainly a feeling that the UK was returning to normality.

As the furlough scheme ends, we expect the vast number of job vacancies to be partly filled by the circa 1 million people that would have previously been on furlough. Dependent on growth and unemployment figures, we anticipate the Bank of England to announce a tightening of monetary policy by the end of the year, but we expect this to be well-flagged and therefore well-received by markets.

EU

In Europe, there was the forementioned energy concerns; gas shortages could be eased with an increase in supply from Russia, but strained relations mean this hasn't happened as an immediate response. Supply constraints are being felt similarly in Europe, with concerns about a lack of HGV drivers growing across the continent.

The German election has been stealing the spotlight with a movement away from the status quo, attributable to a narrow win by the SPD party. We're anticipating the formation of a government to be quicker than expected by the media, with SPD likely to form a coalition with the FDP and Greens. The Greens would bring the focus onto environmental projects, which is an obvious plus.

ROW

Chinese authorities have continued on their journey to crackdown on certain sectors that do not align with the regime's long-term plans. Xi Jinping has also had the potential systemic risk from Evergrande's piling debt on his plate. We're witnessing a clash between Xi's determination to enact change with the constraints of dealing with a debt-fuelled real estate sector that, alongside property services, accounts for circa 29% of GDP. We continue to be insulated from China-specific risk, and we continue to favour having economic exposure rather than listing exposure. Any direct listing exposure is in companies that are operating in sectors that do not conflict with the regimes program, such as renewable energy.

Some committee members brought India to the attention of the meeting; a report was released on the morning of the IMC commenting on the red-hot market and the potential for big corrections. High expectations are built into Indian investments, and there are concerns that they might disappoint. As a result, we remain vigilant as it heads into reporting season, on the grounds of having some emerging market exposure in India.

Inflation and Global Interest Rates

As pre-mentioned, we're expecting to see a global tightening from central banks. The general view is tapering of asset purchases will come first, although base rate rises are certainly on the cards in a number of economies. Economic recovery from the pandemic has been varied by country, depending on vaccination access and vulnerability to Covid-19 variants. Therefore, central banks are taking tightening of monetary policy at different speeds; the Reserve Bank of Australia has already begun tapering, whilst the ECB still has some years to come as they remain wary of raising rates after struggling with their inflation target for a number of years. With regard to the UK and USA, we're anticipating announcements about changes in monetary policy to be as early as the end of the year.

Portfolio changes

In general, we have slightly lowered risk in portfolios, chipping away at broad equity exposure, and adding a small amount into bonds to capitalise on the move higher in yields.

As we noted in our quarterly report, we feel the post-COVID bounce is now priced in by equity markets and this was reflected in more subdued growth. At the same time, impact investments found themselves in the shade as the market focused on reflation. Whilst we regard this reflation as a more temporary, we see the long-term case for impact investments accelerating.

We have modified the asset allocation ranges of the Adventurous portfolio, increasing core equity exposure from 80% to 90%. This is because we expect the next few months to be more volatile, and also to accommodate our new Balanced Growth model portfolio that will sit between the Balanced and the Growth models. This also reflects our view that impact investments remain focussed on the future.

Whilst higher equity exposure favours more adventurous investors who can withstand fluctuations in the market, the current uncertainty means that in the medium term we would seek to lower risk for the lower risk investors.

Whilst it may seem counter intuitive to raise and lower risk in the same meeting, this reflects the uncertain times; our highest risk model is now a little riskier and our lower risk models are now a little more cautious in anticipation of higher general market volatility.

Company Information

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