JOHN RAISIN FINANCIAL SERVICES LIMITED

Independent Advisors Report

Market Background October to December 2020

The official press release issued after both the November and December 2020 meetings of the monetary policy setting Federal Open Markets Committee (FOMC) of the US Federal Reserve included the statement *"…The COVID-19 pandemic is causing tremendous human and economic hardship across the United States and around the world…"* At his press conference following the December 2020 FOMC meeting Jay Powell the Chair of the US Federal Reserve stated *"Economic activity has continued to recover from its depressed second-quarter level…Even so… the path ahead remains highly uncertain."* Despite this, buoyed by huge monetary stimulus from Central Banks, material fiscal intervention by governments and optimism regarding vaccine development both US and financial markets worldwide enjoyed another positive Quarter. The MSCI World Index was up over the Quarter 14% (in $ terms) and 16% up for the calendar year 2020 despite COVID-19.

As with the two previous two Quarters the period October to December 2020 was clearly positive for US equities. The S&P 500 Index which had closed at 3,363 on 30 September closed at 31 December at 3,756 an increase of over 11%. All 11 sectors within the S&P 500 experienced a positive Quarter. Information Technology had yet another positive Quarter returning over 11% (and 42% for the calendar year making it the best performing sector in 2020). The Financial and Energy sectors which had suffered particularly as a result of COVID-19 experienced a clearly positive Quarter. Financials returned over 22% which did much to mitigate the earlier losses of 2020. The best performing sector was Energy which returned approaching 26% over the Quarter although such were the losses incurred earlier in 2020 that the sector ended the year at minus 37%. Despite COVID-19 the S&P 500 as a whole gained over 16% in 2020 with the Information Technology (+42%), Consumer Discretionary (+32%) and Communication (+22%) sectors all achieving particularly positive returns.

The Federal Open Markets Committee (FOMC) continued the extraordinary measures it had introduced earlier in 2020 to support both financial markets and the economy. At the December meeting the FOMC provided reinforced guidance on its asset purchase programme announcing it would to continue to purchase at least $80 billion of Treasury securities and at least $40 billion of mortgage-backed securities per month *"until substantial further progress has been made toward the Committee's maximum employment and price stability goals."* In December both Congress and President Trump approved a further $900 billion fiscal stimulus including payments of up to $600 for an individual, $1,200 for a married couple and $600 per dependant child.

Following the Presidential election on 3 November 2020 it became apparent that President Trump had been defeated by (former) Vice President Joe Biden. This did not appear to perturb markets with the S&P 500 climbing steadily from 3,369 on 3 November to 3,756, an increase of 11%, by 31 December.

US gross domestic product (GDP) increased at an annual rate of 4.0% in the fourth quarter of 2020 (equivalent to 1% growth compared to the previous Quarter) according to data released by the Bureau of Economic Analysis (BEA) on 28 January 2021. The BEA release stated this reflected *“both the continued economic recovery from the sharp declines earlier in the year and the ongoing impact of the COVID-19 pandemic, including new restrictions and closures that took effect in some areas of the United States.”* GDP was, however, estimated to have declined by 3.5% in 2020.

The unemployment rate which had been 7.8% (revised) in September was down to 6.7% in December. Although much below the April high of 14.7% this is still almost double the pre COVID level of 3.5% as at January 2020. Inflation continued to be clearly below the US Federal Reserve target of 2%. Inflation as measured by the Personal Consumption Expenditures (PCE) index was 1.3% in December while Core PCE (which excludes changes in consumer energy prices and many consumer food prices) was 1.5%. The FOMC does not see a swift path to its inflation target, but it does see a path, with Chair Jay Powell stating at his December 2020 press conference that *“the median inflation projection from FOMC participants rises from 1.2 percent this year to 1.8 percent next year and reaches 2 percent in 2023.”* The University of Michigan Index of Consumer Sentiment was very slightly higher in December (80.7%) than September (80.4%) and therefore remained very clearly above the levels recorded following the outbreak of COVID-19 (71.8% in April and 72.3% in May).

Eurozone Equities had a successful Quarter with the MSCI EMU Index increasing by approaching 13% (in Euro terms) in contrast to the previous Quarter when it had been almost flat. As in the United States the financial and energy sectors which had fared particularly badly following the outbreak of COVID-19 were clearly positive this Quarter. There were encouraging announcements from November regarding vaccine development, together with further monetary policy stimulus by the European Central Bank (ECB), and an agreement by EU leaders in December which overcame objections from Hungary and Poland which were holding up enactment of the 750 billion Euro Recovery Fund to be allocated amongst European Union states initially agreed in July.

While the Governing Council of the ECB did not extend its monetary policy initiatives at its October meeting it clearly signalled further likely loosening with the press release stating *“In the current environment of risks clearly tilted to the downside…a thorough reassessment of the economic outlook”* would be undertaken and that *“the Governing Council will calibrate its instruments as appropriate…”* In December the Governing Council introduced a number of initiatives to stimulate the eurozone economy. These included a further expansion of the Pandemic Emergency Purchase Programme from 1,350 billion to 1,850 billion and extending it from June 2021 to *“at least the end of March 2022”* as well as the extension of financing to banks to encourage further lending.

In Q4 2020 the Eurozone performed less robustly than other major economic areas. In contrast to both the United States and the UK where economic activity expanded (by 1%) the Eurozone contracted. Eurozone GDP decreased by 0.7% in Q4 2020 according to data released by Eurostat on 2 February 2021. Worryingly too deflation continued in the Eurozone throughout the Quarter with inflation at minus 0.3% in October, November and December 2020. Achievement of the ECB policy goal of inflation below but close to 2% over the medium term appears far away! Eurozone unemployment remained steady during the Quarter and was 8.3%, again supported by broad furlough schemes which have, so far, avoided significant expansion in unemployment in the Eurozone and will hopefully facilitate economic recovery going forward.

The FTSE All Share advanced over 12% during the Quarter with the bounce back by financial and energy sectors clearly contributing. Positive news regarding vaccine progress and market optimism during the Quarter that the UK and EU would avoid a no-deal Brexit (which they ultimately did on 24 December 2020) buoyed the UK equity market particularly the UK focussed FTSE 250 which advanced by over 18% over the Quarter. Notwithstanding a positive final Quarter UK equities experienced a poor year in both absolute and relative terms with exposure to financials and energy and an under exposure to information technology weighing against positive performance. While world equities (as measured by the MSCI World Index) advanced by 16% in $ terms (and 12% in £ terms) the FTSE All Share was down 10% (in £ terms). However, going forward, the UK market appears undervalued compared to other major markets and therefore a source of potential opportunity.

The Office for National Statistics announced on 12 February 2021 that UK GDP for the period October to December 2020 *“is estimated to have grown by 1.0%, following revised 16.1% growth in Quarter 3.”* However, the release goes on to state *“Despite two consecutive quarters of growth, the level of GDP in the UK is 7.8% below its Quarter 4 2019 level.”*

UK unemployment was 5% for the period September to November 2020 compared to 4% prior to the first COVID-19 lockdown in March 2020. The furlough scheme first introduced from March 2020 was extended in November 2020 to April 2021. In this respect the Minutes of the December meeting of the Bank of England Monetary Policy Committee (MPC) stated that *“the extension of the government’s employment support schemes is likely to limit significantly the near-term rise in unemployment, although a substantial further increase is still likely over the next few quarters.”* Consumer Price Inflation (CPI), which had been 1.5% in March 2020 continued to remain well below the Bank of England target of 2%. CPI which had been 0.5% in September was 0.7% in October, 0.3% in November and 0.6% in December. The Bank of England continues however to take the view that 2% inflation is possible in 2 years’ time.

The Bank of England MPC extended its support to the economy at its November meeting by increasing its planned purchases of *“UK government bonds by an additional £150 billion”* thereby increasing the planned level of quantitative easing from £745 billion to £895 billion. This further easing of monetary policy was in the context of clear concerns by the MPC, as expressed in the Minutes of their November 2020 meeting, regarding the UK economy and economic activity.

Japanese Equities (as measured by the Nikkei 225 Index) gained 18% over the Quarter. Over 2020 as a whole the Nikkei 225 gained 16%. Likely positive influences included COVID vaccine news and the election of Joe Biden as US President which is likely to result in both more predictable and traditional US foreign policy than under Donald Trump. In addition, the Japanese government announced a large fiscal stimulus in December to both combat COVID-19 and provide for long term investment including in clean fuels and digital technology.

At its December 2020 meeting the Bank of Japan further expanded its already huge monetary stimulus and, significantly announced *“the Bank will conduct an assessment for further effective and sustainable monetary easing, with a view to supporting the economy and thereby achieving the price stability target of 2 percent.”* This review which is likely to be finalised in March 2021 was initiated *"given that economic activity and prices are projected to remain under downward pressure for a prolonged period due to the impact of COVID-19."* Japan remained in deflation with Core CPI which had been minus 0.3% in September reaching minus 1.0% by December. The Bank of Japan target is plus 2% inflation.

Asian and Emerging Markets enjoyed a particularly positive Quarter partly facilitated by continuing US dollar weakness. For Emerging Markets, in general, rising commodity prices were also a boost factor. The MSCI AC Asia (excluding Japan) returned over 18% (in US $ terms) and the MSCI Emerging Markets Index approaching 20%. South Korea, Taiwan and India were all notable positive performers. While the Chinese market rose it underperformed Asia/Emerging Markets generally. The US government imposed further sanctions on Chinese companies while Alibaba was made subject of a monopoly probe by the Chinese authorities. Overall, 2020 was a positive, if volatile, year for Asian and Emerging Markets with the MSCI AC Asia (excluding Japan) returning 25% (in US $ terms) and the MSCI Emerging Markets Index 18%.

The extensive and further increasing monetary policy initiatives of the major Central Banks were supportive of the continuing low yields of the leading Government Bonds – despite the contrary pull of potential or agreed fiscal initiatives by governments. The 10 Year Gilt Yield fell from 0.23 to 0.20 and the 10 Year Bund Yield fell from -0.52 to -0.57. The 10 Year US Treasury Yield remained below 1% but did rise from 0.68 to 0.91 with market commentators citing concerns regarding the prospect of increased fiscal stimulus under a Democrat President and Congress as a clearly contributing factor. Both investment grade and high yield corporate credit enjoyed another positive Quarter.

In Conclusion the October to December 2020 Quarter was clearly positive for financial markets. The calendar year 2020 saw, despite the huge human and economic cost of COVID-19, further clear advances in asset prices. Ultimately the credit for this must go to the huge stimulus initiatives of both the Central Banks and governments. The greatest benefit of these measures has however been in providing support and protection to both business and individuals in the face of an unprecedented worldwide challenge. This was in contrast to support provided by governments in the 2007-2009 financial crisis which was focussed on businesses rather than individuals. The question remains whether all this Central Bank (monetary) and government (fiscal) intervention will indeed be genuinely inflationary and help facilitate the achievement of the major Central Banks 2% inflation targets. Or perhaps it might result in inflation levels significantly above Central Bank targets which could ultimately adversely affect asset prices?