JOHN RAISIN FINANCIAL SERVICES LIMITED

Independent Advisors Report

Market Background April to June 2021

April to June 2021 proved to be yet another positive Quarter for financial markets with the MSCI World Index advancing almost 8% (in $ terms). Significant progress in vaccine rollouts in developed markets combined with the ongoing reopening of economies and the easing of social restrictions supported by both continuing ultra loose monetary (central bank) policy and fiscal (government) stimulus doubtlessly buoyed markets. Interestingly the outperformance of Value stocks over Growth stocks which was a notable (and long awaited) aspect of the previous Quarter was not repeated. During the April to June period the MSCI World Growth index advanced by 11% (in $ terms) while the MSCI Value Index advanced by less than 5%. The debate over future inflation trends continued but both the US Federal Reserve and Bank of England continued to indicate a belief that inflation above 2% would be transitory in both the US and UK.

As in the previous Quarter the period April to June 2021 saw further significant progress in the US COVID-19 vaccination programme and both economic data and sentiment continued along a positive trend. On 27 May the US Bureau of Economic Analysis estimated US GDP increased at an annual rate of 6.4% in the first Quarter of 2021 compared to 4.3% in the final Quarter of 2021. Quarter 1 corporate earnings reports were, overall, clearly positive. Consumer spending was facilitated by the arrival in later March of the $1,400 direct payments to individuals from the latest Federal stimulus package. Consumer sentiment as measured by the University of Michigan was slightly higher at the end of June compared with March. Unemployment was 5.9% in June compared to 6.0% at the end of March 2021. Further significant fiscal stimulus was proposed by President Biden which by June had resulted in an agreement with a bipartisan group of Senators to support a package worth about $1 trillion to upgrade infrastructure over an eight year period. The estimate issued by the US Bureau of Economic Analysis on 26 August indicated that GDP increased in the period April to June 2021 (Quarter 2 of 2021) at an annual rate of 6.6%. US equities enjoyed a clearly positive Quarter with the S&P index advancing to new highs during each of April, May and June closing at 4,298 on 30 June an increase of over 8% during the Quarter.

At both its April and June meetings the Federal Open Markets Committee (FOMC) of the United States Federal Reserve maintained the extraordinary measures to support the economy and financial markets introduced during 2020. An issue of discussion for the FOMC, market commentators and the press continued to be the level and future trend of US inflation. The CPI index which had been at +1.7% in February 2021 reached 5.0% in May leading to press headlines when this was announced in June. However in any debate about US inflation it must always be remembered that it is not the CPI or Core CPI rate (issued by the Bureau of Labor Statistics) but rather the Core PCE (Personal Consumption Expenditures Price Index, Excluding Food and Energy) issued by the US Bureau of Economic Analysis (BEA) that (to quote the BEA website) *"is closely watched by the Federal Reserve as it conducts monetary policy."* May Core PCE was 3.4%.

The FOMC remained cautious regarding a genuine inflationary trend with the official press release issued after both the April and June meetings including the statement that *“Inflation has risen, largely reflecting transitory factors.”* However, in its “Summary of Economic Projections” issued after the June 15-16 policy meeting the FOMC indicated that interest rate increases could begin in 2023, earlier than forecast in the projections issued after the March 2021 period. This led to immediate financial market uncertainty causing the Federal Reserve to have to stress, in the following days, that it remained cautious regarding both the future inflation and the wider economic outlook. During testimony to a Select Sub Committee of the US House of Representatives on 22 June Federal Reserve Chair Jay Powell stated that *“Inflation has increased notably in recent months”* caused by *“transitory supply effects”* but that as these *“abate, inflation is expected to drop back toward our longer-run goal”* Chair Powell further stated that *“We will not raise interest rates pre-emptively… we will wait for actual evidence of actual inflation or other imbalances.”*

European Equities (as measured by the MSCI EMU index) advanced 6% (in Euro terms) during the period April to June 2021. In addition to continuing government fiscal and extensive central bank monetary policy support the Quarter saw increasing vaccine rollouts, reducing restrictions on economic and social activity and positive Quarter 1 corporate earnings results all of which were favourable to the financial market environment. The European Central Bank (ECB) continued its ultra supportive monetary policy approach at both its April and June 2021 policy setting meetings. Unemployment continued to reduce from 8.1% in March to 8.0% in May and 7.7% in June (which was, of course only confirmed after the Quarter end). At her April 2021 press conference European Central Bank President Christine Lagarde was cautiously optimistic regarding the Euro area economy referring to a potential *“resumption of growth in the second quarter.”* This optimism was confirmed by the “preliminary flash estimate” of GDP for the April to June Quarter issued by Eurostat on 30 July 2021 which reported a 2.0% increase in GDP in the Euro area compared to the previous Quarter.

Euro area inflation (as measured by the Harmonised Index of Consumer Prices (HICP) and reported by Eurostat) finally reached the (then) ECB inflation goal of inflation near but below 2%. The HICP figures were 1.6%, 2.0% and 1.9% for April, May, and June 2021, respectively. However at her press conference following the June meeting of the ECB Governing Council Christine Lagarde the President of the ECB expressed extreme caution regarding longer term inflation stating *“Inflation has picked up over recent months, largely on account of base effects, transitory factors and an increase in energy prices. It is expected to rise further…before declining as temporary factors fade out…”* and *“…euro area annual inflation increased from 1.3 per cent in March to 1.6 per cent in April and 2.0 per cent in May 2021… Headline inflation is likely to increase further towards the autumn, reflecting mainly the reversal of the temporary VAT reduction in Germany. Inflation is expected to decline again at the start of next year as temporary factors fade out and global energy prices moderate.”*

The FTSE All Share index advanced by approximately 5% during the Quarter. A successful vaccination programme and easing of lockdown measures, together with positive economic data, supplemented the ongoing stimulus provided to financial markets and the wider economy by both the continuation of Government fiscal policy (introduced in the context of COVID-19) and the Bank of England’s highly accommodative monetary policy approach.

The Bank of England expressed confidence in the UK economy going forward at its May 2021 Monetary Policy Committee (MPC) meeting. The "Monetary Policy Summary" issued after the meeting included the statement *"GDP is expected to rise sharply in 2021 Q2"* and that *"GDP is expected to recover strongly to pre-Covid levels over the remainder of this year."* The estimate of UK GDP for the April to June Quarter issued by the Office for National Statistics (ONS) on 12 August 2021 supported the Bank of England's confidence with the ONS estimating that UK GDP increased by 4.8% during the Quarter. Unemployment moved slightly lower with the ONS announcing a rate of 4.7% for the period April-June.

There was a notable increase in inflation over the Quarter. CPI which had been 0.7% in March rose to 1.5% in April, 2.1% in May and 2.5% in June. The Bank of England (like the US Federal Reserve and European Central Bank) was, however, of the view that inflation clearly above the 2% target would be transitory. The "Monetary Policy Summary issued after the June MPC meeting stated *"Twelve-month CPI inflation rose from 1.5% in April to 2.1% in May, above the MPC's 2% target…Building global input cost pressures have increasingly been passed through…CPI inflation is expected to pick up further above the target…and is likely to exceed 3% for a temporary period…"* However, the MPC's *"central expectation"* is that *"inflation will fall back"* and *"the Committee judges that UK inflation expectations remain well anchored."*

Japanese equities not only underperformed other developed markets but experienced a negative return over the April to June Quarter with the Nikkei 225 down over 1%. The Bank of Japan continued its longstanding approach of huge ongoing monetary stimulus. However, Japan saw poor COVID-19 vaccine rollouts during the Quarter and a State of Emergency in Tokyo and some other cities for a significant part of the April to June period. Deflation (which has persisted since October 2020) continued with the Japanese CPI index at -0.5 for June 2021.

Asian and Emerging Markets saw modest overall progress during the Quarter. The MSCI AC Asia (excluding Japan) index advanced by approaching 4% and the MSCI Emerging Markets index by 5% (both in $ terms). Although COVID-19 vaccination rollouts globally were doubtlessly a positive factor the overall pace of COVID-19 vaccination in Asian and Emerging Markets was generally slower than in the US, Euro Zone and UK. High commodity prices, however, particularly benefitted some Emerging Markets including Brazil and Russia.

Overall, it was a good Quarter for the leading Government Bonds. The 10 Year US Treasury yield reduced (strengthened) from 1.74 to 1.47 and the 10 Year UK Gilt yield reduced from 0.85 to 0.72. The German 10 Year Bund retained its negative yield but weakened slightly from -0.29 to -0.21. The statements of the US Federal Reserve, European Central Bank and Bank of England indicating that they believe inflation will fall back to or below their 2% targets and their continued stated commitments to low interest rates and asset purchase programmes will surely have helped support the leading Government Bonds during the Quarter. Corporate Bonds – both Investment Grade and High Yield - performed well during the Quarter. The clear evidence of economic recovery (including lower expected defaults which are especially relevant to High Yield) will have been positive for Corporate Bonds.

In conclusion, April to June 2021 was yet another positive Quarter for financial markets. The issue of inflation, however, remained highly topical given its potential major implications for both financial market and wider economic behaviour and performance. The major Central Banks robustly maintained, and sought to justify, that the increasing levels of inflation experienced recently are merely "transitory" and that inflation will not remain clearly above 2% over the longer term. While the reasoning of the US Federal Reserve, European Central Bank and Bank of England is clearly logical and would seem likely to be proved correct this is certainly not the view of all commentators and market participants some of whom have stated that Central Bank statements regarding long term inflation look increasingly questionable.

Perhaps the situation was well articulated, in a speech to the Institute for Government in June 2021, by Andy Haldane the outgoing Chief Economist of the Bank of England who while not stating longer term inflation above 2% was likely put forward a logical case that it was clearly possible. In this speech Mr Haldane stated *"…While the essentials of inflation-targeting are as strong as ever, the regime is being tested as never before…There is no evidence so far of inflation expectations, in the UK or elsewhere, becoming durably or significantly de-anchored from target... But it is early days. Overall, inflation expectations and monetary policy credibility feel more fragile at present than at any time since inflation-targeting was introduced in 1992…By the end of this year, I expect UK inflation to be nearer 4% than 3%. This increases the chances of a high inflation narrative becoming the dominant one, a central expectation rather than a risk. If that happened, inflation expectations… would shift upwards, not only in financial markets but among households and businesses too."* Clearly, therefore, both inflation trends and how the major Central Banks respond to these in policy terms may potentially prove to be major factors affecting individuals, businesses, and the wider economy, as well as financial market asset values going forward

John Raisin

26 August 2020