JOHN RAISIN FINANCIAL SERVICES LIMITED

Independent Advisors Report

Market Background July to September 2021

Over the period July to September 2021 world equity markets were flat with the MSCI World Index, in US$ terms, at (almost exactly) the same level on 30 September as at 30 June. The Quarter however saw equity markets as a whole clearly advancing in both July and August before experiencing a fall of over 4% in September.

There was a clear difference in performance across geographies. The developed US, European, UK and Japanese markets all advanced by around 0.3% to 2.5% (in their own currency terms) while Asia (excluding Japan) and Emerging Markets fell by 8%-9% overall. Positive earnings results and high COVID vaccination levels reassured developed markets. All markets, but particularly Asia and Emerging Markets were negatively impacted by supply chain shortages, the Chinese governments intervention in the Chinese technology and private education sectors, and concerns about the ability of Evergrande, China's second largest property group, to service its debts.

Financial market concerns regarding inflation deepened in the context of supply shortages and energy price rises with an increasing view in financial markets that higher levels of inflation may be more than "transitory." The major central banks while acknowledging that inflation may be elevated for some time remained of the view that it would remain "transitory." There were, however, indications from the US Federal Reserve and particularly the Bank of England of future, but carefully considered and measured, interest rate rises in the context of judgements regarding achieving the 2% inflation target (and in the case of the US Federal Reserve their *"maximum employment"* target too).

In July and August US equities were supported by strong earnings results and by what markets took to be reassurances regarding the timing/circumstances of monetary tightening by the Federal Open Markets Committee (FOMC) of the US Federal Reserve by Chair Jay Powell at the central bankers annual Jackson Hole summit. The S&P 500 index increased from 4,298 on 30 June to 4,523 on 31 August and reached a (then) all time closing high of 4,537 on 2 September. September however proved to be a poor month for US equities. Possible factors influencing this slide include concerns regarding a possible default by the Chinese property group Evergrande, concerns whether Congress would increase the US debt ceiling in order to avoid the government defaulting on some of its financial obligations and renewed concerns regarding the future of monetary policy following the FOMC meeting of 21-22 September. The S&P 500 closed on 30 September 2021 at 4,308 which was 0.2% above its 30 June closing figure.

At both its July and September meetings the FOMC of the United States Federal Reserve voted, yet again, to maintain its main interest rate at the range of 0-0.25% and its asset purchase programme at $120 billion per month. However, there were increasing indications of approaching monetary policy tightening. The press release issued after the July meeting hinted at future reductions in asset purchases referring to *"progress towards"* achieving the Committee's goals of maximum employment and price stability. The press release issued after the 21-22 September meeting was clear that there could soon be a reduction in monthly asset purchases stating in relation to maximum employment and price stability that *"If progress continues broadly as expected, the Committee judges that a moderation in the pace of asset purchases may soon be warranted."* Furthermore, the "Summary of Economic Projections" issued after the September meeting indicated an increased expectation of interest rate rises during 2022 compared with the previous projections issued in June.

US inflation as measured by the Core PCE index (the Federal Reserves favoured index) remained clearly above the policy target of 2% with July, August and September all registering 3.6%. The FOMC indicated some heightened expectations regarding future inflation with the Minutes of the September 2021 meeting stating (page 8) *"…Participants marked up their inflation projections…Some participants expressed concerns that elevated rates of inflation could feed through into longer-term inflation expectations…"* The "Summary of Economic Projections" issued after the September meeting suggested Core CPI at 2.3% in 2022 up from the 2.1% issued following the June FOMC meeting. Unemployment continued to fall, to 4.8% in September compared to 5.9% in June.

US economic growth continued but slowed dramatically in the Quarter. On 28 October, the US Bureau of Economic Analysis estimated US GDP increased at an annual rate of 2.0% in the period July to September compared to 6.7% in the previous Quarter. This equates to growth of 0.5% over the July to September period. The University of Michigan survey of consumers saw a major fall, during the Quarter in consumer sentiment. The August Final Results release referred to consumers negative reactions citing *"the surging Delta variant, higher inflation, slower wage growth, and smaller declines in unemployment"* but cautioned that this *"does not imply an imminent economic downturn…"*

Eurozone equities enjoyed a clearly positive July and August supported by positive corporate earnings and high vaccine rates. However, in September Eurozone equities, as with world equities as a whole experienced a clear decline. The MSCI EMU index advanced by 0.3% in Euro terms over the Quarter.

On 29 October Eurostat issued *"a preliminary flash estimate"* of July to September Eurozone GDP growth of 2.2%. This was compared with the official estimates for the US of 0.5% and China of 0.2% for the same period. The Eurozone, however, remains behind the US and China in terms of its pandemic economic recovery. Euro area inflation as measured by the Harmonised Index of Consumer Prices (HIPC) and reported by Eurostat exceeded the new ECB inflation goal of 2% over the medium term throughout the Quarter reaching 3.0% in August and 3.4% in September. At her press conference of 9 September ECB President Christine Lagarde while referring to improvements in the euro area economy as a whole, increased consumer spending and an improving labour market struck a somewhat cautious note stating that *"We see the risks to the economic outlook as finely balanced…"*

On 8 July 2021, the European Central Bank (ECB) published its new Monetary Policy Strategy Statement which was last revised in 2003. The new strategy is modestly but clearly more tolerant of inflation. While the previous target was below but close to 2% the new target is 2%. In addition, the ECB indicated in a commentary also issued on 8 July (entitled “An overview of the ECB’s monetary policy strategy”) that while the old inflation target had led to a perception of aiming not above the target the new inflation target is a *“symmetric”* one where moderate deviations above and below the target were allowable on a temporary basis. This new Policy Strategy should therefore clearly reduce the chance of premature monetary tightening and make it more likely that the ECB will keep its ultra loose monetary policy approach for a longer period.

At the July policy setting meeting the ECB retained its previous ultra supportive monetary policy approach. At the meeting that concluded on 9 September the ECB maintained its ultra low/negative interest rate policy, forward guidance on interest rate policy, standard asset purchase programme at 20 billion Euros a month, its reinvestment policies and longer term refinancing operations. There was however a slight tightening of policy with the Press Release issued after the meeting stating *“Based on a joint assessment of financing conditions and the inflation outlook, the Governing Council judges that favourable financing conditions can be maintained with a moderately lower pace of net asset purchases under the pandemic emergency purchase programme (PEPP) than in the previous two quarters.”* At the press conference following the meeting Christine Lagarde, however, definitively stated that the ECB was not *“tapering”* but merely *“recalibrating”* the PEPP.

Compared with World equities as a whole UK equities enjoyed a successful Quarter. Not only were corporate earnings clearly positive but merger and acquisition activity also buoyed small and mid cap equities in particular. Notwithstanding market falls in September the FTSE All Share index ended the Quarter 2% up while the mid cap FTSE 250 advanced by 3%.

The UK unemployment rate was 4.5% for the June to August Quarter which was only 0.5% above the pre pandemic level. CPI inflation which had been 2.5% in June continued its upward trend recording over 3% in both August and September with further increases expected. The September Monetary Policy Summary issued by the Bank of England stated *“CPI inflation is expected to rise further in the near term, to slightly above 4% in 2021 Q4…”*

Both the August and September meetings of the Bank of England Monetary Policy Committee retained Bank Rate at its all time low of 0.1% and maintained existing policy regarding asset (bond) purchases. The MPC indicated potential future tightening of monetary policy at both the August and September meetings but this was clearly nuanced. However, given the overall content of the Minutes and Monetary Policy Statement issued after the 23 September meeting market commentators indicated expectations of an increase in interest rates (Bank Rate) by February 2022. Following a speech by Andrew Bailey the Governor of the Bank of England on 27 September the Financial Times printed an article (28 September 2021, page 2) entitled *“Bailey says MPC united behind rate increase this year if needed.”*

In contrast to the previous Quarter when Japanese equities underperformed world markets the July to September period saw the Nikkei 225 Index advance by over 2% which was clearly ahead of world markets. Deflation in Japan (which had persisted since October 2020) continued into July and August 2021, but September saw inflation return (just) with the CPI index at +0.2%. Unsurprisingly, in contrast to the US Federal Reserve and Bank of England, the Bank of Japan did not at all indicate that it was considering tightening its longstanding ultra loose approach to monetary policy at either its July or September meetings.

Asia (excluding Japan) and Emerging Markets appear to have been particularly negatively impacted by the Chinese governments intervention in the Chinese technology and private education sectors, and concerns about the ability of Evergrande, China's second largest property group, to service its debts. The MSCI Emerging Markets index declined by over 8% (in $ terms) while the MSCI AC Asia (excluding Japan) index suffered a decline in excess of 9% (in $ terms).

Chinese economic activity was constrained including by energy shortages and government action to control leverage in the property sector. Official Chinese Government statistics indicated that China's GDP only grew by 0.2% during the July to September 2021 Quarter.

The benchmark US 10 Year Treasury weakened slightly from 1.47% to 1.49% and UK 10 Year Gilt weakened from 0.72% to 1.02% over the Quarter. Both weakened clearly (but not dramatically) in late September. This was in the context of increasing financial market inflation concerns, and indications following their September meetings from both the US Federal Reserve and in particular the Bank of England resulting in markets anticipating they could soon tighten their monetary policy approach.

In conclusion the July to September 2021 Quarter saw a respite from the overall dramatic upward trend in Listed Equity prices seen since April 2020 but not an overall fall. This ultimately sideward move in markets occurred even in the light of significant concerns about China, supply side shortages, inflation (at least in the short term) and indications from two of the world's leading central banks of potential forthcoming monetary policy tightening. While both the Federal Reserve and Bank of England gave clear indications of likely future, but limited, monetary tightening this did not result in a "tantrum" in either Listed Equity or Bond markets. It remains, however, a matter of considerable debate as to whether inflation will remain clearly above 2% for a prolonged period or not. This is, of course, a matter of real concern and potential impact upon all of national economies, individuals and financial markets/asset performance going forward.

29 October 2021