JOHN RAISIN FINANCIAL SERVICES LIMITED

Independent Advisors Report

Market Commentary July to September 2023

In contrast to the previous three Quarterly periods the July to September 2023 period saw a decline in Global Equities. After a positive July both Developed Markets and Asian/Emerging markets suffered declines in August and September with the MSCI World Index declining by over 3% (in $ terms) over the Quarter. An increasing realisation that interest rates will likely remain higher for longer (based on major Central Bank actions and statements) despite it appearing that interest rate rises are drawing to an end, and concerns over the Chinese economy were surely two notable contributory factors. Overall, the major Government Bond markets also declined over the July to September period.

In the US, on 12 July, the Bureau of Labor Statistics announced a sharp drop in the headline US CPI index from 4% in May to 3% in June. However, CPI rose to 3.2% in July and was 3.7% in both August and September. The Core PCE (Personal Consumption Expenditures) Index which is closely observed by the US Federal Reserve when determining monetary policy remained stubbornly above the target of 2%. Core PCE was 4.3 in June (reported in July), 4.3% in July, 3.8% in August and 3.7% in September. Unemployment remained very low but increased over the Quarter to 3.8% at September compared to 3.6% in June.

The June 2023 meeting of the US Federal Reserve Federal Open Markets Committee (FOMC) had held interest rates for the first time since March 2022. At its meeting which concluded on 26 July 2023 the FOMC again increased the Federal Funds rate, this time by 0.25%. The Press Release issued after the July meeting included the statement that *"Job gains have been robust in recent months, and the unemployment rate has remained low. Inflation remains elevated… The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. In support of these goals, the Committee decided to raise the target range for the federal funds rate to 5-1/4 to 5-1/2 percent."* At the FOMC meeting which concluded on 20 September 2023 the FOMC determined not to raise interest rates notwithstanding continuing *"elevated"* inflation and *"low"* unemployment. This more cautious approach was not surprising given the extent to which the FOMC had increased rates over the previous 18 months.

At his press conference following the September FOMC meeting Chair Jay Powell made the following statement regarding the future approach to monetary policy "*Since early last year, the FOMC has significantly tightened the stance of monetary policy… We've covered a lot of ground, and the full effects of our tightening have yet to be felt… Looking ahead, we're in a position to proceed carefully in determining the extent of additional policy firming that may be appropriate. Our decisions will be based on our ongoing assessments of the incoming data and the evolving outlook and risks."*

US Equities were negative over the Quarter with the S&P 500 declining over 3%. The increase in CPI in July (reported August) and particularly August (reported in September) together with the stubbornly elevated Core PCE inflation raised the possibility of further interest rate increases or the existing rates remaining for longer than perhaps expected/hoped for by markets. Statements by the US Federal Reserve also inclined towards a “high for longer” approach to interest rate policy.

As in the previous Quarter Eurozone inflation as measured by the Harmonised Index of Consumer Prices (HICP) continued to fall from 5.5% in June, to 5.3% in July, 5.2% in August, and 4.3% in September. However, it still remained clearly above the European Central Bank target of 2%. Core inflation also fell from 5.5% in June, to 5.3% by August, and 4.5% in September. Despite eight interest rate rises by the European Central Bank (ECB) between July 2022 and June 2023 Eurozone unemployment remained historically low. Eurozone unemployment was 6.5% in September 2023 only marginally up from the all time low, in the history of the Eurozone, of 6.4% as at June 2023.

The European Central Bank continued its clear policy of monetary tightening to bring inflation under control and back to the ECB target of 2%. To quote the first two sentences from the Monetary Policy Decisions statement issued after both the July and September 2023 monetary policy meetings *“Inflation continues to decline but is still expected to remain too high for too long. The Governing Council is determined to ensure that inflation returns to its 2% medium-term target in a timely manner.”* Therefore, at both meetings the ECB increased its benchmark interest rate by 0.25%. Following the September meeting this was at record level of 4%. However, there were clear indications that the ECB may be coming towards the end of its ongoing monetary tightening approach. The Monetary Policy Decisions statement issued after the September meeting including the comment that *“Based on its current assessment, the Governing Council considers that the key ECB interest rates have reached levels that, maintained for a sufficiently long duration, will make a substantial contribution to the timely return of inflation to the target.”* Furthermore, at her press conference following the September meeting ECB President Christine Lagarde, in response to a question, indicated that there had been a split in the Governing Council of the ECB over this latest rate rise stating “*there are a few members in the Governing Council who would have preferred a pause...”*

Eurozone Equities experienced a negative Quarter with the MSCI EMU index falling by over 4% (in Euro terms). News on inflation received during the Quarter (the June, July, and August figures) indicated only a slight downturn while GDP data released by Eurostat showed weakness with figures for the second Quarter of 2023, released on 7 September, indicating that GDP grew by only 0.1% in the Euro area the same as for the first Quarter of 2023. Corporate earnings reports for the second Quarter of 2023 were also disappointing.

In the April to June Quarter UK Equities, in contrast to other major developed market Equities had declined. In the July to September Quarter UK Equities again performed contrary to (most) other developed markets, this time gaining. The FTSE All Share gained almost 2% driven by the performance of the FTSE 100 (mega cap) Index which gained over 2%. The weakness of sterling versus the US dollar boosted returns for those (mainly) large UK listed companies which account/report earnings in US Dollars. The significant weighting of the FTSE All Share to Energy and Basic Materials stocks which had been weak in the previous Quarter clearly contributed to the positivity in the July to September Quarter which saw them rebound.

Fundamentally, however, there are significant questions regarding the FTSE All Share in the long term. This is in a context of, for example, the lack of big technology companies in the index, the weighting of oil and gas in the index, the movement of pension fund investors away from UK equities, and some large companies listing/moving their listing overseas and away from the London Stock Exchange.

There was a further clear decline in UK inflation reported during the Quarter although it remained far above the Bank of England target of 2% and clearly in excess of inflation levels in both the United States and the Eurozone. The June CPI inflation figure (reported in July) was 7.9% compared to 8.7% in May and the July figure (reported in August) was 6.8%. August and September saw CPI at 6.7%.

At the meeting of the Bank of England Monetary Policy Committee (MPC) held on 3 August 2023 the Committee raised Bank Rate (interest rates) by a further 0.25% to 5.25% (a fifteen year high) with 6 Members voting for this increase, two Members for a 0.5% increase and one Member for no increase. In relation to the view of the majority of the Committee who voted for a 0.25% increase the Minutes of the meeting included the statement (at Paragraph 24) that *"Six members judged that a 0.25 percentage point increase in Bank Rate, to 5.25%, was warranted at this meeting… Although the monetary stance was weighing on economic activity, a 0.25 percentage point increase in Bank Rate at this meeting was necessary to address the risks from greater inflation persistence."*

Bank Rate remained at 5.25% at the MPC meeting on 2 September 2023 following a 5 to 4 vote finally determined by Governor Andrew Bailey's casting vote. The other 4 Members voted for a 0.25% increase. The Minutes of the meeting indicated that the decision making at this meeting had indeed been difficult with (even) 4 of the 5 Members who voted to hold rates considering the decision was *"finely balanced."* Paragraph 44 of the Minutes included the following *"Five members judged that maintaining Bank Rate at 5.25% was warranted at this meeting. There were signs that the labour market was loosening… headline and services CPI inflation had fallen back and were lower than had been expected. Regarding activity, contacts of the Bank's Agents had become more downbeat, and the output PMI in August was now consistent with falling GDP. For most members within this group, the latest developments meant that the judgement to keep Bank Rate unchanged at this meeting rather than increase it was finely balanced."* However, the MPC was clear that monetary policy would remain tight and that further interest rate rises could occur – with Paragraph 48 of the Minutes stating "*The MPC would continue to monitor closely indications of persistent inflationary pressures and resilience in the economy as a whole, including the tightness of labour market conditions and the behaviour of wage growth and services price inflation. Monetary policy would need to be sufficiently restrictive for sufficiently long to return inflation to the 2% target sustainably in the medium term, in line with the Committee's remit. Further tightening in monetary policy would be required if there were evidence of more persistent inflationary pressures."*

Japanese inflation continued to exceed the Bank of Japan's target of 2% at 3.3% in July, 3.2% in August and 3.0% in September. Core inflation was 3.1% in July and August and 2.8% in September. The Nikkei 225 Index (which measures the performance of 225 large publicly owned companies) declined by 4% over the Quarter (having increased by over 18% in Yen terms in the previous Quarter).

At both its July and September monetary policy meetings the Bank of Japan, yet again, maintained short term interest rates at -0.1% and continued to be the only major Central Bank to retain negative interest rates. However, at the meeting which concluded on 28 July the Bank made a small but symbolically significant alteration to its monetary policy approach. While maintaining the 10 Year Japanese Government Bond Yield target of 0% with range of around plus or minus 0.5% the Minutes of the meeting stated that the Bank would *"conduct yield curve control with greater flexibility, regarding the upper and lower bounds of the range as references, not as rigid limits, in its market operations. The Bank will offer to purchase 10-year JGBs at 1.0 percent…"* What this means is that in effect Japanese Government Bond Yields will be allowed to move as high as 1% rather than 0.5%. As at the April monetary policy meeting the Bank of Japan under its new Governor, Kazuo Ueda, signalled, at its July meeting, that the long running ultra loose monetary policy approach of the Bank of Japan may change. However, this will not happen until the Bank is clearer that inflation will remain around the Bank's 2% target over the longer term.

Asian Markets (excluding Japan) and Emerging Markets, overall, performed broadly in line with developed markets as a whole. Both the MSCI Emerging Markets Index and the MSCI Asia (excluding Japan) Index declined by approximately 3% (in US $ terms). Chinese Equities experienced another Quarter of decline in the context of concerns regarding the Chinese economy – particularly property (which accounts for a sizeable proportion of all Chinese economic activity) and the extent of government measures to stimulate the economy. The situation regarding China and questions over the global economic outlook and the potential that US interest rates would remain higher for longer were all factors weighting against Asian and Emerging markets more widely.

Overall benchmark Government Bonds (US, UK, and Germany) experiencing another negative Quarter with yields rising and prices therefore falling. Over the Quarter the 10 Year US, UK and German yields all rose. The US 2 year yield also increased while the German 2 year yield remained static and the UK 2 year yield declined. Announcements from the major Central Banks while indicating that monetary policy tightening was drawing to a close, but that rates would likely stay high, was surely a clear factor weighing against benchmark Government Bonds. On 1 August Fitch (one of the three major credit rating agencies) downgraded its rating of US government bonds from AAA to AA+ Summarising the downgrade Fitch referred to "*expected fiscal deterioration over the next three years, a high and growing general government debt burden, and the erosion of governance relative to 'AA' and 'AAA' rated peers over the last two decades that has manifested in repeated debt limit standoffs and last-minute resolutions."* The major Corporate bond markets outperformed benchmark Government Bonds with High Yield again (overall) posting positive performance.

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