Investment commentary

September 2021

Market overview

After a strong summer period, world equity markets declined around 4% in September although US dollar strength, and some weakness in sterling, did serve to alleviate some of these losses for sterling-based investors. The change in sentiment was driven primarily by lowering growth forecasts and concerns over the potential impact of supply disruptions and rising inflationary pressures.

Comments from the US Federal Reserve ('the Fed') were perceived as more hawkish and median expectations in relation to interest rate rises in the US have edged up to three (modest) hikes in 2023 and a further three in 2024. The Fed has also indicated that it expects to slow the pace of its asset purchase program, possibly from next month, and to bring it to an end by the middle of next year. It brought its growth forecast for the current year down by just over 1% to 5.9% and its inflation estimate up to 4.2%.

The Bank of England also put forward a more hawkish tone, hinting at an earlier than expected rate rise although the consensus remains that it will not move rates before its quantitative easing program stops, which is scheduled for the end of the year. Fuel shortages and continued hikes in energy prices caused significant disruption and the broad-based consumer price inflation ('CPI') increased 3.2% in August, the highest level for a decade. In Europe, the European Central Bank also signalled that it would be prepared to retreat from its accommodative policy stance, albeit likely in a more gradual process.

On the back of these developments bond yields rose significantly, with the 10-year Treasury yield nudging 1.5% and the 10-year Gilt rising just above 1% by the end of the month. The supply disruption and shift in growth and rate expectations also led to some divergent returns between equity market sectors. The energy sector was the clear winner on the back of the rise in prices while the prospect of higher rates benefitted sectors such as financials but impacted on sectors such as utilities and real estate.

The Chinese market has faced several headwinds recently with concern over greater government regulation, slowing economic growth numbers and the potential impact of the financial woes of real estate developer Evergrande. This has weighed heavily on emerging markets more broadly, which underperformed again over the month.

Strategy positioning

Although the pace of economic recovery has been tempered by the Delta variant, the prospect of continued stimulus, impressive progress on vaccinations and the wider recovery in corporate earnings (likely to be aided by increased pricing power) give us confidence to maintain the strategies at the upper end of their corresponding Dynamic Planner risk profiles. Any setbacks are expected to be short-lived as investor cash continues to accumulate and needs a better home to combat the vagaries of inflation.

Inflation could move higher still before low base effects from 2020 and short term supply pressures fall out of the statistics, but it seems increasingly likely that some inflation will become slightly stickier than originally forecast, particularly if current labour shortages also contribute to higher wage inflation. The recent trends of weaker activity, combined with higher inflation and still elevated unemployment levels, are complicating the picture for the world's major central banks – their talk of tapering asset purchases and the general removal of monetary stimulus has increased, but so far markets continue to be reassured by their measured reactions and their ability to perform a more complicated juggling act.

As things currently stand, it seems likely that central banks' policies will remain highly accommodative and that this backdrop will continue to be supportive for risk assets for the remainder of 2021 and into 2022.

Our broad geographic equity allocations, with a bias to the US and Asia, remain unchanged. Despite regulatory market challenges in China, Asian markets still seem well placed to deliver superior long term economic growth. The US economy and market look more mature on the surface, but there is still plenty of long-term growth potential and value opportunities to make further headway.

Our reduced exposure to interest rates (duration) within our fixed income allocation has provided protection against recent rises in bond yields. We believe that flexible strategic bond funds, which can pivot quickly as conditions change, along with inflation-linked bonds and 'market neutral' equity/bond 'alternative investments' should continue to act as good portfolio stabilisers and sources of return.

Risk warnings

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