RICHMOND HOUSE
INVESTMENT MANAGEMENT

# Investment commentary

**January 2023**

## Market overview

2023 has begun brightly for investors with developed market equities rising nearly 5% in sterling terms in January. Market sentiment was buoyed by further evidence that inflation is falling in key regions and the consequent hope that central banks may soon be able to end their cycle of rate hikes. Generally better than expected economic and corporate data also provided support.

Inflation (CPI) in the US fell from 7.1% to 6.5%, driven primarily by lower energy and food prices. Markets were also encouraged by stronger than expected GDP numbers (2.9% on an annual and seasonally adjusted basis) and by a slightly cooling labour market.

Inflation also receded in the eurozone, falling to 9.2% in December, while economic data indicated that the region had narrowly avoided recession in Q4 with growth just positive at 0.1%. Concerns over the energy supply crisis in Europe alleviated further, helped by a combination of a mild winter to date, government support and falling gas prices.

The UK market also produced a strong return, albeit lagging other key regions. CPI fell modestly from 10.7% to 10.5% although core inflation was unmoved and the expectation of the UK facing 'higher for longer' inflation than most of the developed world remains as strong wage growth appears to be putting pressure on the services sector in particular. Economic indicators continue to point to recession being likely in 2023 with heavily negative real (above inflation) wage growth and a squeeze on many mortgage holders exposed to sharp rises in repayment costs expected to weigh heavily.

Returns from emerging market equities were even higher over the month (6.1% in sterling terms). In addition to the improved sentiment globally this was also driven by a strong rebound in the Chinese market, which rose 12% in local currency terms. Investor optimism was also buoyed by the economic boost stemming from the relaxation of covid restrictions, slightly better than expected economic data and the promise of further policy support for ailing sectors such as real estate.

Heightened expectations of a shift away from tightening central bank policy boosted growth stocks in particular, which are generally more sensitive to rising rates. Having dramatically underperformed their value counterparts last year (by more than 20%) 'growth' outperformed 'value' by 5% over the month led by sectors such as technology and consumer discretionary.

The continuing evidence that inflationary pressures are receding and expectation of a slowdown in the cycle of tightening rates sent bond yields lower (and prices up), particularly at the longer end of the yield curve. The yield on the 10-year Treasury bond fell from 3.9% to 3.5% while the 10-year Gilt yield fell from 3.7% to 3.3%. Corporate credit across the US, UK and the eurozone performed better still given lowered concerns over recession.

Broad commodity indices fell over the month, pulled down by lower energy and agricultural prices.

Our exposure to the US dollar provided a valuable hedge against falling asset prices over 2022. The US dollar was weak against most currencies in January, however, and fell over 2% against sterling which slightly impaired returns on our dollar-denominated assets. Looking ahead we continue to favour holding dollar-denominated assets based both on our view of the comparative outlook for the UK and US economies and the continued potential benefits of the dollar's reserve status.

## Strategy positioning

We have been well positioned to capture the strong returns from equity markets in January and continue to favour equities as an asset class. Greater visibility on inflation moderating and on the likely peak in rates across key markets is improving sentiment and equities remain our preferred asset class for potential real returns going forward. It has also been encouraging to see that corporate earnings have to date proved more resilient than many have expected.

We have high conviction in terms of our equity positioning and are targeting areas of relative economic and corporate strength. This includes the US and Asian markets, as well as sectors such as infrastructure and sustainable energy.

We have also benefitted from the recovery in fixed income markets and added targeted exposure to higher quality corporate credit over the month. As opportunities arise, we may look to add further to fixed income, potentially recycling more assets from our alternative strategies.