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OUT OF THE ORDINARY

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Market reflection

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Overview

Despite the bankruptcy of the sixteenth largest bank in the United States (Silicon Valley Bank) and the fact that the second largest bank in Switzerland (Credit Suisse) had to be rescued by the biggest (UBS), equity markets put in a remarkably steady performance during March 2023, although there was a wide performance gap between the best and worst sectors.

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US Banks took the biggest hit, losing a quarter of their value in aggregate, as investors weighed up the prospects of lower profitability. Concerns also resurfaced about the quality of loans made to the commercial property sector amidst the downward shift in office attendance following the pandemic. Even so, we remain of the opinion that a rerun of the Great Financial Crisis is improbable, and we were encouraged by the speed with which central banks provided liquidity to the financial system when required. The MSCI World Index managed to grind out a small gain, consolidating the advances made earlier in the quarter.

Indices were buoyed by a strong performance from US large cap Technology shares, which were supported by lower bond yields as markets priced in an expectation that central banks will be quicker to cut interest rates now that the first major cracks have started to appear in the financial sector. UK equity indices lost some ground on account of their exposure to more cyclical sectors. The US 10-year Treasury yield, having briefly risen above 4% at the beginning of the month in response to “hot” economic data, fell back close to 3.5%. The 10-year UK Gilt enjoyed a similar performance. But with inflation remaining elevated, there were further interest rate increases from the Federal Reserve, the Bank of England and the European Central Bank amongst many other central banks, and they might not yet be finished with their policy tightening.

- The Bloomberg consensus for World GDP growth in 2023 remains at 2.4%, although there is considerable uncertainty about how the year will evolve. While the UK and Europe appear to have been remarkably resilient thanks to the reduction in wholesale energy costs, the pace of China’s recovery has been somewhat disappointing. The US economy has been remarkably resilient, but many indicators suggest a potential US recession later in the year. The turmoil in its regional banking industry only added to those fears, especially if banks become more cautious in their lending policies.

- We continue to await signs of weakness in company earnings, which we believe will occur as the year progresses. Although inflation remains elevated, the fact that it is falling from its peak levels will give companies less cover to increase prices, while their costs continue to increase. Wages could be a particular source of pressure for margins, with unemployment remaining very low as many employees appear to have left the workforce for good.

- The UK Chancellor delivered a Spring Budget characterised by his “safe pair of hands” strategy, which continues the task of rebuilding confidence in the Conservative administration. Savers with large pension fund balances were pleasantly surprised by the abolition of the Lifetime Allowance Cap, although the leader of the opposition immediately promised to reverse that decision should Labour prevail at the next general election. This must take place by January 2025 at the latest.

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