INVESTOR INSIGHT

Autumn 2021 A look at the markets by **RSMR**

Welcome

Welcome to the latest edition of our 'Investor Insight' which provides high-level commentary on the global markets and how these might be affecting your investments.

We hope you find this useful.

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in association with:

GRAYSIDE FINANCIAL SERVICES

The global economy: What's going on?

Consumer surge triggers inflation fears

The main theme since the opening of economies following the launch of the Covid-19 vaccine programme has been a growing inflation risk. While central banks initially talked this down, current persistent high levels of inflation have led to tougher rhetoric.

This is coupled with concerns about global supply chains as manufacturers and distributors cannot keep pace with consumers' voracious desire for goods and services.

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This could be an early sign that the cheap loans era is coming to an end. The timeframe for increasing interest rates has shortened as various central banks, notably the US Federal Reserve (Fed), have issued more forceful statements.

Norway has become the first advanced economy to raise interest rates and four emerging economies followed in September.

The pandemic's unleashing of pent-up consumer demand is hard to ignore. Shipping costs have risen almost five-fold and raw material costs and food prices have soared. Prices are rising due to supply bottlenecks and Covid-19 outbreaks disrupting the smooth flow of goods.

As a result, a tougher stance on interest rate rises, especially from the Fed, is likely with a possible increase in 2022 and other central banks are likely to follow.

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The asset classes – a quick round-up

EQUITY MARKETS

Generally markets have remained positive, and the outlook is for continued but slowing, improvement.

The last quarter was flat as several issues dented the start of this year's investor optimism.

Japan has led returns, in local currency, and the US once again performed strongly.

Emerging markets and Asia have been weak as the after effects of the Chinese crackdown on certain economic sectors hit investor confidence.

Markets wobbled at the end of the last quarter following comments from the Fed, and ex-Fed chairpersons, which increase the likelihood of earlier-than-expected rate rises. A close to 3% equity market fall in late September was the largest for some time.

Current and continuing growth expectations suggest that areas of value should lead markets if they rise.

Many fund managers still believe that equities offer the best opportunities as fixed income and cash offer little return for increased risk if interest rates rise.

FIXED INTEREST

Inflation remains the biggest threat to bond markets. Its corroding effect on interest rates is crucial when financial assets have risen in value.

Central bank moves to prevent a Covid-19 depression by flooding the financial markets with money drove significant gains in asset prices.

This year has seen bond yields rotate quickly without any huge shift in the underlying economy.

The most recently available minutes of the Fed show that most members expect an interest rate rise in 2022 and three more in 2023. In the UK, a Bank of England rate rise is expected to happen between November and March.

All this suggests a weaker outlook for fixed interest assets' capital values, but it also has ramifications for other asset classes.

Value remains in emerging market debt and areas of high yield, but these carry more risk and would not represent the necessary anchor for defensive assets in balanced portfolios.

PROPERTY

There is strong demand for industrial premises and out-of-town retail is also recovering.

In the industrial sector, intense demand from online retail, coupled with low quality stock availability, continue to fuel the positive outlook for warehouses.

Investor confidence in offices has grown but home working and flexible employment is changing how they are used.

Economic factors look likely to support a bounce-back in 'bricks-and-mortar' retailing. Supermarkets, as well as warehouses, continue to deliver attractive returns.

The rest of the property market is flatter with city centres suffering from fewer shoppers and less spending.

The easing of Covid-19 restrictions, and a return to office working since July, are expected to lead to improvements at some shopping centres and 'tourism high streets'.

Retail's recovery looks long term with possible changes of use or multi occupancy coming to the fore. Rental income data has been stronger overall but very poor in pandemic-affected sectors such as travel and leisure.

Investors should concentrate on core, well-located retail space with secure and long-term income streams, underpinned by high-quality tenants.

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Global round-up

- The European economy is expected to expand by 4.8% in 2021 and GDP will increase by 4.4% in 2022, says Focus Economics.
- The Bank of Japan kept rates on hold at -0.1% at its September meeting.
- Many see the US market as overvalued with the UK and Europe offering better opportunities.
- US consumer price inflation has topped 5% for three consecutive months.
- Japan had the strongest stock market in the last quarter as markets welcomed internal political announcements.
- Uncertainty regarding regulation in China and its objectives for private enterprises have seen India benefit as a safe haven.
- US Treasury yields reached their highest level in three months, exceeding 1.5% for 10-year Treasuries.
- UK gross domestic product (GDP) remains 4.5% behind pre-pandemic levels but is improving.
- Brazil was the weakest market in the MSCI EM index as high inflation rose and the central bank hiked interest rates.

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So, what's next?

The third quarter started with markets performing strongly, encouraged by the belief that the benign economy, especially in the US, would continue.

Early economic data, including unemployment figures, tempered the breakneck pace of the recovery in Q1. This made investors believe that central bank policies would support markets while governments continued to back the early recovery.

This bolstered confidence in the prospects for a strong economic rebound but more recently markets retreated due to fears about rising inflation.

Towards the end of September, government bonds rose after tougher talk about inflation from central banks combined with oil price rises and rising fuel costs.

Investor positioning became more optimistic on the outlook for government bonds, but short-term raised interest rate expectations have hurt growth stocks, underlining how changeable markets have been in 2021.

Longer term consistent trends will continue to be an important influence on how investors should shape their portfolio but, for today's investors, the most important factor in portfolio construction is whether higher inflation is permanent or transitory.

If the answer is regarded as important but unknowable, constructing a portfolio which can avoid extreme outcomes may be the wisest course of action.

About RSMR

Independent specialist research.

RSMR was formed in 2004 to meet a growing demand from financial advisers for specialist and impartial investment research.

The RSMR team is made up of individuals with expertise from across all areas of the financial industry – from asset management, strategy and fund research through to business development, strategic planning and market research.

We are best known within the financial industry for our 'R' fund ratings – this rating is given to investment funds that meet our stringent research criteria. We don't limit ourselves to just looking at performance – we also look carefully at the people, processes and capabilities that are required to make effective investment decisions.

We work in partnership with your financial adviser, providing the benefit of our broad industry insight and rigorous research. This quarterly market summary is designed as a 'snapshot' of the more thorough and lengthy commentary that we provide to your adviser on a quarterly basis.

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