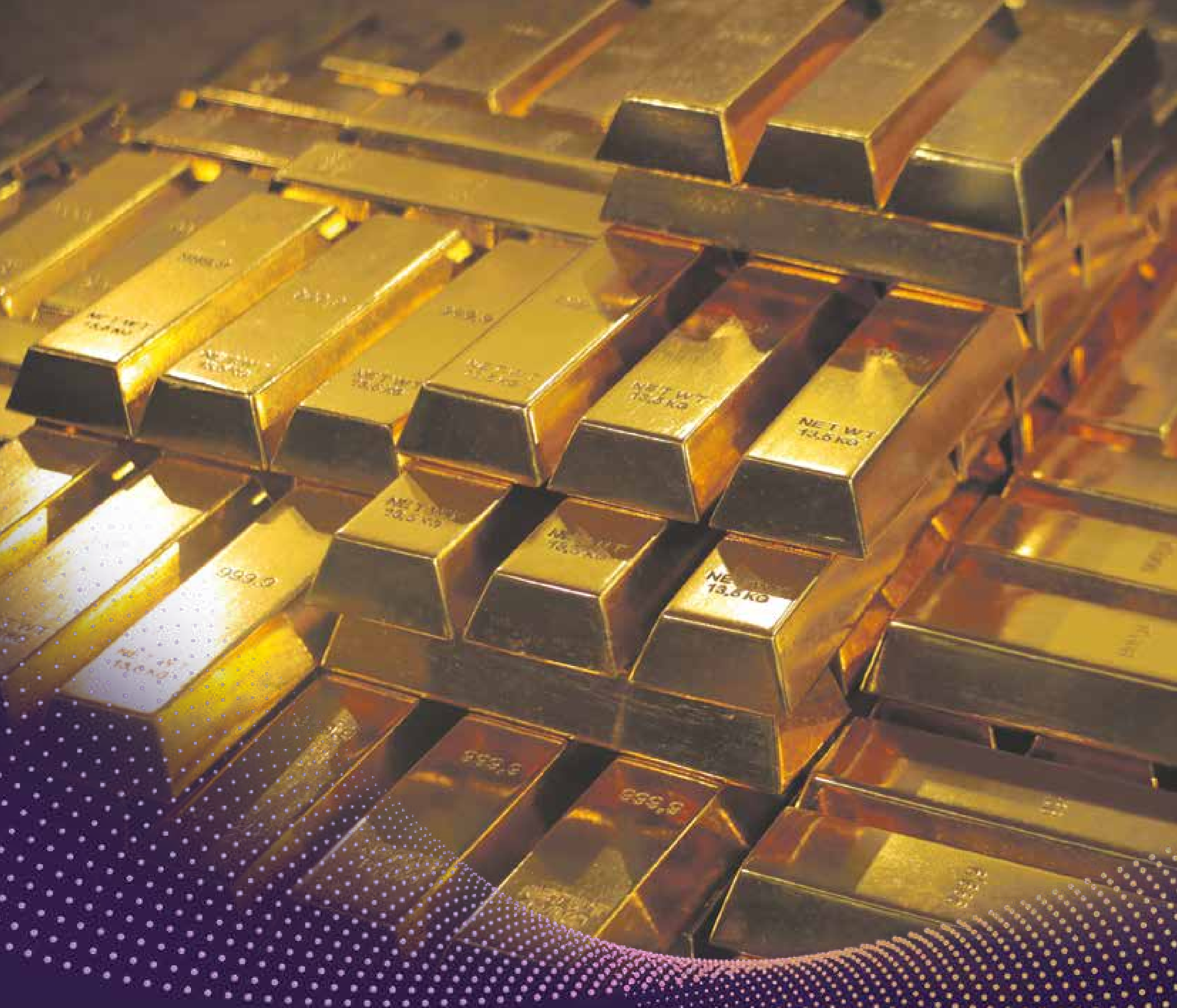

Investment Outlook

A monthly round-up of global markets and trends

May 2023

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Investment outlook

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A golden message for financial markets

April marked the 90th anniversary of President Franklin D. Roosevelt banning most private ownership of gold within the US. Individual ownership restricted the Federal Reserve's (Fed) ability to increase the money supply during the Great Depression because it needed to be backed by gold bullion. This limited the Fed's capacity to stimulate the US economy, which in turn dampened output growth. President Roosevelt's executive order forced investors to sell their gold holdings to the government. It wasn't until 1974 that this limitation on gold ownership was repealed. Fast forward to today and the bullion price has soared past $2,000 per troy ounce and to a record high during April.[1]

The recent gold price rally has been helped by foreign central bank bullion purchases following Western financial sanctions against Russia – see our May 2022 Investment Outlook. The private sector is also becoming more actively involved in the gold market. March's data from the World Gold Council showed the strongest investor demand for non-physical gold since 2019.[2] For investors, it is important to understand the implications of rising gold prices.

While it is open to interpretation, we see two main reasons why investors are buying gold. The negative take is that investors are buying gold because risks have risen, and bullion is widely considered to be a store of value in uncertain times. These could range from intensifying geopolitical headwinds to sluggish economic growth, banking sector issues and inflation concerns.

Alternatively, a more positive take is that investors are betting on an end to the Fed's interest rate hiking cycle. The expected pause in US interest rate rises is dragging down the US dollar, thereby alleviating money shortage concerns in the global financial system.

On balance, we side with the positive take, where the Fed lifts its foot off the monetary brake, for three reasons. First, in March, US annual headline inflation (CPI) decelerated for the ninth month in a row and is back down to a near two-year low. Base effects, which relate the current level of inflation to the level the prior year, should continue to drag down inflation given that prices were already elevated this time last year. Importantly, lead indicators, such as falling job openings and lower selling prices from the National Federation of Independent Business, a survey of small businesses, indicates that core inflation, which excludes food and energy, should continue to slow over the coming months.

Second, the Fed Funds base rate is now higher than the Fed's forecasts of underlying inflation for 2023 and 2024. This positive real interest rate over inflation indicates that monetary policy is already restrictive and should help to tame inflation further.

Third, the Fed is aware of the risks of tightening monetary policy too much. This risk became apparent in the banking sector, with the failure of Silicon Valley Bank and Signature Bank in March – see our April 2023 Investment Outlook. The Fed will also be conscious there are inflation drivers outside of its control (i.e. energy prices). OPEC's recent production cut has given a boost to crude oil prices and complicates the job of the Fed. So, despite the aggressive rhetoric from some members, the Fed will be reluctant to raise interest rates too far.

The Fed does not expect to cut interest rates later this year, in contrast to market participants who do. The Fed may be considering the risk that inflation remains persistent in the coming years given that many large multinational companies have demonstrated pricing power since the pandemic. For instance, Unilever, a British-Dutch multinational company that produces everyday consumer staples, saw the prices for its goods rise by 10.7% from a year ago in the first quarter of 2023, though it has slowed from a peak of 12.5% in the third quarter of 2022.[3] This corporate pricing power could mean that inflation is stickier in the future.

The bottom line is that slowing US inflation raises the likelihood of the Fed pausing on interest rate increases. However, other central banks like the European Central Bank are likely to continue to raise interest rates given they were slow to start hiking. Higher relative interest rates in Europe will increase the attractiveness of the region, and we believe global investors are likely to move capital there as they seek out the potentially higher returns on offer. This could lead to further US dollar depreciation against other major currencies (i.e., the euro). Essentially, if there are more dollars available outside the US it reduces the systemic risk of a shortage of money dragging down asset prices. This happened during the Global Financial Crisis (GFC), as banks made fire sales of their assets to meet their obligations.

Higher gold prices also suggest the US dollar is overvalued. According to data that goes back 50 years, the US dollar reached a record low against a basket of currencies (US DXY dollar index) in March 2008, but it then recovered sharply during the GFC. Today, the US dollar is now coming down from a 20-year peak reached in September 2022 and could well depreciate further from here – see our December 2022 Investment Outlook.

Ultimately, higher gold prices probably signify a weaker US dollar, which should provide a tailwind to drive the price of overseas equities and bonds.

Publication sources:

[1,4,5,6,7,8] Refinitiv Datastream/Evelyn Partners, data as at 30 April 2023

[2] www.gold.org/goldhub/research/gold-market-commentary-march-2023

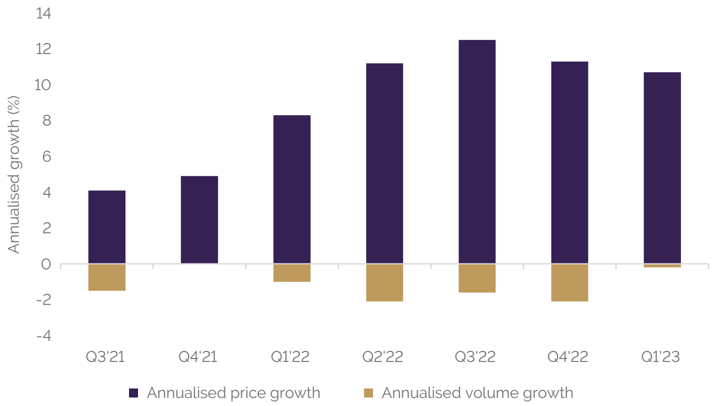
[3] www.unilever.com/investors/results-presentations/overview-q1-2023

Market highlights

Equities

Despite inflation beginning to slow in the US, UK and the eurozone, some corporations continue to maintain pricing power. Since inflation started to pick up at the end of 2021, Unilever, a UK based consumer goods company, has managed to maintain near double digit annualised price growth. This has more than offset rises in input costs, while volumes have stabilised, causing a large increase in overall sales growth for Unilever. However, while consumers remain willing and able to pay these higher prices, sales growth should remain above pre-pandemic levels.

Unilever underlying sales growth proves resilient

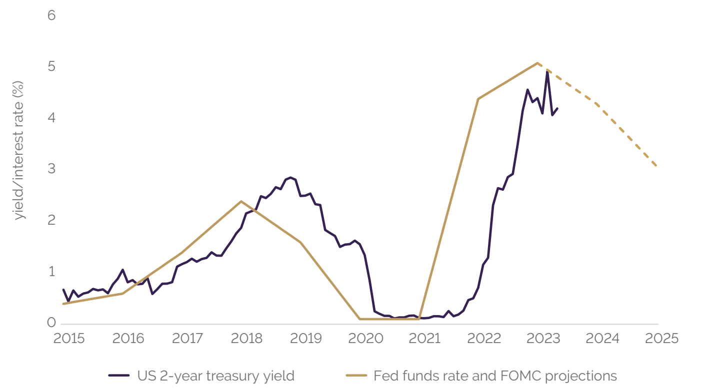


Source: Unilever/Evelyn Partners, data as at 27 April 2023
This is not advice to invest in this stock.

Fixed income

The US two-year treasury bond yield represents market expectations of where US interest rates, as set by the Federal Open Market Committee (FOMC), are headed. Following the collapse of several US regional banks in March, the bond market has lowered its interest rate expectations. Since then, US inflation has continued to slow - headline annual inflation (CPI) was 5.0% in March. US economic growth also decelerated. The first quarter real annualised GDP growth reported at 1.1%, compared to 2.6% in Q4 2022.[4] With inflation and growth slowing, the bond market continues to believe that interest rates will not need to remain as high as the FOMC are projecting.

US interest rate expectations remain volatile

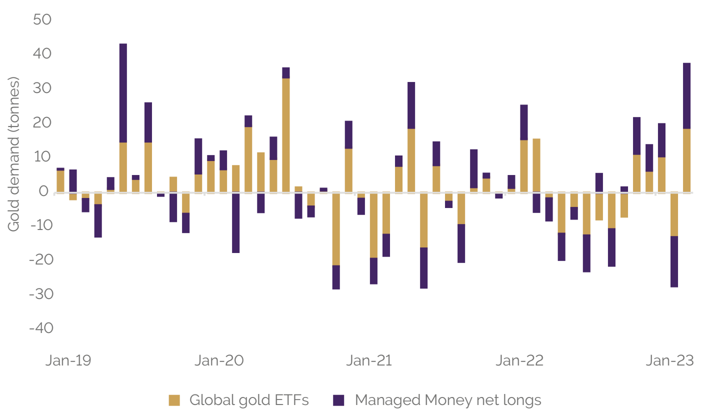


Source: Refinitiv Datastream/Evelyn Partners,data as at 30 April 2023
Future projections are not a reliable indicator of future performance.

Currencies/Commodities

Gold rallied in the first quarter of 2023, gaining 9.2%. This rally continued into the first half of April when the spot value of gold peaked at $2,040 per troy oz, marginally below its all-time high of $2,075.[5] This was driven largely by a shift in investor sentiment following the US banking turmoil, prompting an increase in investor demand for safe-haven assets like gold. The chart shows a steep increase in the quantity of gold bought by investors through exchange traded funds and net long positions in managed money (representing the overall exposure to gold in actively managed funds). This combination shows that investor inflows into gold in March increased at their fastest rate since June 2019.

Investors increased their gold exposure during March



Source: World Gold Council/Evelyn Partners, data as at 06 April 2023
Past performance is not a guide to future performance.

Market returns (Total return (%), sterling)	1 month	3 months	1 year	5 year
Equities				
MSCI All-Country World	-0.2	-0.4	2.5	57.8
MSCI UK	3.6	2.8	8.3	27.7
MSCI UK Broad	3.6	2.3	6.2	22.6
MSCI USA	-0.4	0.3	1.8	87.0
MSCI Europe ex UK	2.3	4.5	14.0	46.6
MSCI Japan	-1.3	-1.5	4.6	18.6
MSCI Asia Pacific ex Japan	-1.4	-7.7	-1.4	26.5
MSCI Emerging Markets	-2.7	-6.6	-6.2	5.9
Bonds				
iBoxx GBP Gilts	-1.9	-2.2	-16.2	-15.6
iBoxx USD Treasuries	-1.1	-1.0	-1.2	15.2
iBoxx GBP Corporate	0.3	-1.3	-7.4	-3.0
Commodities and trade-weighted currencies				
Oil Brent Crude ($/barrel)	-0.3	-6.5	-26.3	6.0
Gold ($/ounce)	0.7	3.2	4.3	51.6
GBP/USD	1.7	2.1	0.1	-8.7
GBP/EUR	0.0	0.4	-4.3	-0.1
EUR/USD	1.6	1.7	4.6	-8.6
USD/JPY	2.3	4.7	5.1	24.4

Market commentary

The MSCI All-Country World Index, a benchmark for global equities, ended the month down 0.2%.[6] Regional outperformance came from the UK and Europe, which recovered from a difficult March, to finish April up 3.6% and 2.3% respectively.[7] This contrasted with the underperformance in emerging markets, down 2.7% for the month, driven by China's reopening demand boost materialising more slowly than anticipated. Brent crude oil rallied at the start of April following the announcement of OPEC to cut oil production. However, this was more than offset by fears that an economic slowdown would reduce demand, prompting Brent crude to end the month down 0.3%.[8] The US dollar continued to weaken against the euro, sterling, and yen as the US Federal Reserve looks to be closer to the end of their rate hiking cycle than the European Central Bank or the Bank of England.

Key macro data	Latest	2023 Consensus forecast	Spot rates	30-Apr	Yields (%)	30-Apr
UK GDP (YoY%)	0.57	-0.20	GBP/USD	1.25	MSCI UK	4.30
UK CPI Inflation (YoY%)	10.10	6.50	GBP/Euro	1.14	MSCI UK broad	4.16
Bank of England Base	4.25	4.30	Euro/USD	1.10	10 Year Gilt	3.72

The market commentary, values and charts as at 30 April 2023. Total returns in sterling.
Returns are shown on a total return (TR) basis ie including dividends reinvested (unless otherwise stated).
Net return (NR) is total return including dividends reinvested after the deduction of withholding tax.
Source: Refinitiv Datastream/Bloomberg

Sources

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