BRI Wealth Management PLC

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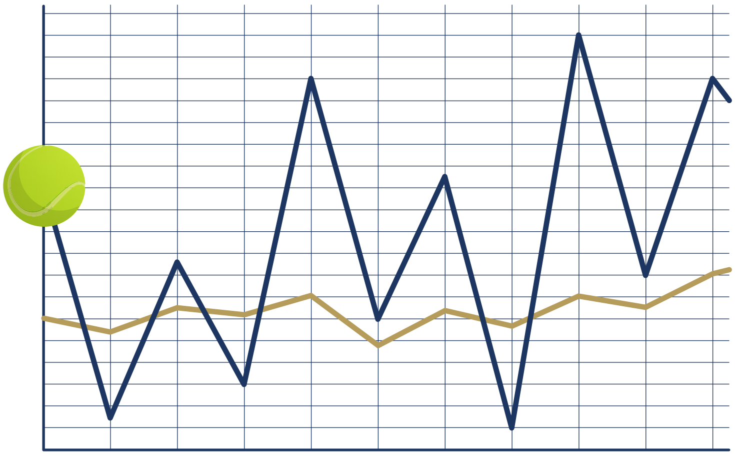
With the Wimbledon Tennis Championships in full swing at the time of writing this, I sit back watching the ball go back and forth between two players. I find watching tennis a calming activity and it gives me the opportunity to contemplate another interesting few months for markets. As I zone back in to watching the tennis, I start to notice a lot of similarities between the match and the events of the second quarter. The back and forth, back and forth in the financial news between inflation and the coronavirus could rival an Isner and Mahut marathon match. The themes of inflation and the coronavirus have jostled for pole position in the headlines throughout the last few months; and coverage of neither shows any sign of abating.



What is pleasing to see is that despite all this noise it appears that the vaccination roll-outs are winning: fifteen-love. Global equities advanced in Q2, supported by the positive outcomes the vaccines have had in reducing hospitalisations and deaths across the world. The continued highly accommodative fiscal and monetary policies and strong economic growth continued to override the noise of inflation fears and the new Delta variant of coronavirus.

The second quarter was strong for US equities; the S&P 500 reached a new all-time high in late June, returning 7.2% in sterling terms over the quarter, the most of any developed market. The FED surprised markets in its median forecast, which showed two interest rate hikes in 2023 (in contrast to previous estimates of no hikes until 2024). This caught the market by surprise; however, it was short-lived.

Overall, the economic picture remained rosy. Retail sales remained strong, Q1 GDP grew at 6.4% and industrial activity as measured by the US composite Purchasing Managers' Index (PMI) moved from 59.7 in March to 63.9 in June. The vaccination roll-out continued successfully with over 50% of the US population now fully vaccinated.

Inflation data, unsurprisingly, received a lot of attention. The Consumer Price Index (CPI) rose to 5% in May, up from 0.5% just a year ago; its fastest pace in more than 12 years. The vast amounts of government stimulus, the surge in personal savings and pent-up demand that have built up over the last 18 months are bound to drive prices higher over the short term as lockdown restrictions ease. However, despite the dramatic rise in inflation, equities climbed to record highs over the quarter, with cyclical sectors such as value and small cap leading the gains. Further reflecting the bullish sentiment, at the end of

June the VIX index (which measures stock market volatility) hit its lowest level since the start of the pandemic.

UK equities performed well over Q2. Markets were largely driven by lowly valued and economically sensitive sectors during April and May, continuing a trend we've seen since November. Small and mid-cap equities outperformed. 2021 has seen the busiest start to the year for private equity-backed bids since 2012; and Q2 was no different. Takeovers of London-listed companies have soared, as cash-rich buyout firms search for under-priced businesses to acquire. The low valuations of UK-listed companies will be a familiar story to investors, as the London market has been weighed down by the twin blows of Brexit and COVID-19, coupled with a weak currency as sterling still trades at a discount in relation to its historical average.

Even as a successful vaccine roll-out fuels a rebound in the economy, the FTSE 100 is trading lower than at the start of 2020. Buyout firms are therefore more likely to find a good deal in the UK than in the US. According to The Guardian, 'Private equity firms have announced 124 deals for UK companies (both takeovers and minority stakes) with a combined value of £41.5bn' so far in 2021. In June we saw Morrisons supermarket being one of the latest companies to be bid for. Other large takeovers we have seen in Q2 include UDG Healthcare, John Laing Group and St Modwen's. I suspect the bids will continue over Q3.

Eurozone shares gained in the quarter, supported by a strong corporate earnings season and an acceleration in the pace of vaccine roll-out in the region. Many European countries saw COVID-19 infections fall over the quarter and were able to loosen lockdown restrictions. Economic data pointed to a strong rebound in activity in Q2. The European market recorded a positive return of 6.25% in sterling terms over the quarter.

Emerging market equities also registered a strong return over the quarter (+3.61%). This was despite a sell-off in May as a higher-than-expected spike in US inflation renewed concerns over the timing of global monetary policy tightening. Japanese shares underperformed other developed markets (-2.55%). Although the rate of COVID infections in Japan remained markedly below most other countries, the persistent increase in cases led their government to delay lifting their state of emergency until 20 June. Slow progress has been made with their vaccine roll-out as only 25% of the population have received one shot of the vaccine, damaging the credibility of the Suga administration.

In the bond markets, corporate bonds performed well, outpacing government bonds. US Treasury yields declined over the quarter, with the 10-year falling to 1.47% from around 1.77% recorded in March. Investors searched for yield and inflation hedges against a backdrop of low government bond yields and higher inflation.

Despite the Wimbledon tennis championships coming to an end on 11th July, I do not suspect the match between inflation and coronavirus will end any time soon; I believe this is a match that will continue for the rest of 2021. Inflation worries and the new variants of COVID are likely to contribute to market jitters. However, global recovery and vaccination roll-outs remain strong. As interest rates remain low and inflation moves higher, cash becomes less attractive to hold, making it more supportive of broader asset classes.

At BRI, we have positioned portfolios resiliently to weather these market jitters. We remain committed to stewarding your investments through the short, medium, and longer term.

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