BRI Wealth Management PLC

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To paraphrase Charles Dickens, it was the winter of despair, we had everything before us, we had nothing before us, we were all going direct the other way. Dickens' use of dualities can be reflected in the performance of global markets since the turn of the year. The shift from 'growth' to 'value' that began towards the end of last year continued during the quarter, leading to a significant style split with the MSCI World Growth Index sliding 9.6% in dollar returns, while the MSCI Value benchmark was more resilient, dipping 0.5%. Overall, global stock markets, as measured by the MSCI World Index, fell 5% in US dollar terms.

Looking at global equity sectors, with the price of oil leaping to a high of USD139 a barrel, energy stocks soared. Materials stocks, buoyed by rampant commodity prices, and utilities followed, with total dollar returns of 7.4% and 2.8% respectively. Consumer discretionary stocks struggled the most, falling 9.3%, closely followed by a 9% decline in IT companies. In respect of oil, what we have seen is a price shock not a supply shock, though that possibility remains if Russia, which is facing more severe sanctions, decides to turn off supply to Europe.

A big trend in the quarter was that of larger companies doing better than smaller ones, typified in the UK where the 'large cap' index rose 2.9% but the 'mid cap' index slid 9.5% and the Numis Smaller Companies Index shed 8.2%. The UK's Large Cap Index outperformed most of the world's major indices, precisely because of its over-representation in commodity and resource stocks and lack of technology companies.

For fixed income investors, the outcome was similarly disappointing, but this comes as no surprise to those who became increasingly concerned by the seemingly uncontrollable rise in inflation and the associated increase in rate expectations. The supposed safe haven of sovereign bonds suffered from their worst quarterly performance since 1980 – all maturity UK Government bonds fell 7.75% and US Treasuries by 4.6%. Russia's invasion of Ukraine has exacerbated the threat of high energy prices, rising food prices and disrupted supply chains and will likely prolong the period over which central bankers will exercise their judgement between fighting inflation and supporting growth.

Looking ahead over the next twelve months, we can see that US investors are positioned for a Fed Funds target rate above 2.5%, compared with the present 0.5%; this implies eight hikes. In the UK the picture is only marginally different: seven hikes and a rate of 2.5%. In the Eurozone there has been a significant shift, with tightening now expected in the second half of the year. In the UK we have the additional burden of a tax hike in the form of a rise in National Insurance contributions. While it is laudable that policy is directed towards increased funding for the NHS and Social Care, it comes when the forecast for GDP growth has fallen to 3.8% from 6% and when the Treasury has received an unexpected 'windfall' in tax revenues from the Oil & Gas sector.

While the general direction of travel was negative, it is pleasing to report that our basket of property investments delivered a collective positive outcome, albeit a small but quite significant number when compared to equities, bonds, and cash. Our position is largely the same as last year and we see no reason to change our view. Ecommerce and logistics continue to be the main drivers of returns, with the ability to soak up speculative build of distribution centres and warehousing.

We believe there are reasons to be optimistic. While we expected global growth to moderate from the post-lockdown surge in 2021, the consequences of the invasion are lower growth, with Europe taking the largest hit, and higher inflation. Even so, global growth this year should still be above trend, driven by the United States, the world's largest producer of oil and gas, and because China will most likely look to stimulate demand. This above-trend growth should support equities and commodities over bonds and cash. There is also the truism, which we have long supported, that there is no alternative to equities if your aim is either to protect your assets against the effects of inflation or to increase your spending power. There will always be moments of uncertainty, and these are to be endured rather than avoided by the long-term investor.

We expect inflation to moderate over the second half of the year as many of the factors leading to the current situation begin to fall out of the numbers – UK inflation is measured on a rolling 12-month comparison – and the hit to consumer spending takes hold (your author has just cancelled a contract to purchase a new car and will continue with the old jalopy for the foreseeable future). It won't be easy; but companies that continue to drive forward their earnings and their ability to generate cash will dominate.

Dickens' Tale of Two Cities is about a time of chaos, conflicts, and despair, and it tells us about a time of extreme opposites without any in-betweens. Today, we can see the same emotions at play in Ukraine and the return to a Cold War between Russia and the West. Only this time, it is more than just military. For investors, the rotation from growth to value has begun to unwind, and we feel that the next rotation – of extreme opposites, if you will – will be seen between equities and bonds where the latter, given the yields on offer today and interest rate rises priced in, are now priced at the value end of the range.

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