Our Ref: SC

Mr M Kearle
CBK Wales

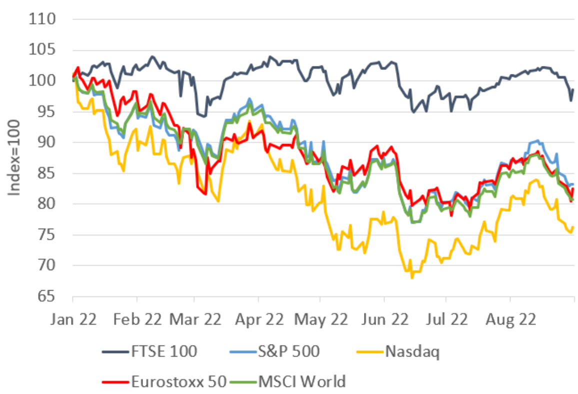
12th October 2022

Dear Mark

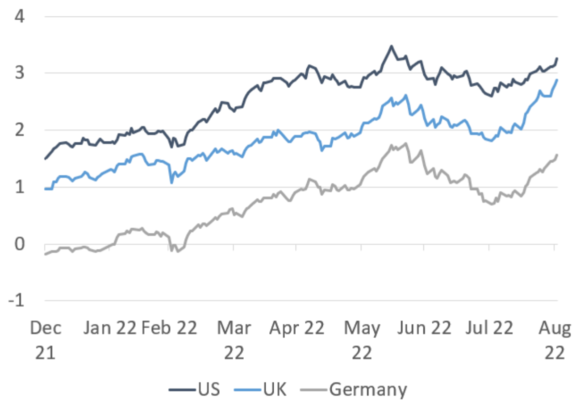
Market Commentary

I am sure it will not have escaped you that 2022 has and continues to be an especially volatile year for investment markets. You may recall, we came into this year with many major stock markets at all-time highs, with the US S&P 500 peaking at 4,796.56 points on 3rd January 2022. Bond yields also came into the year at historic lows, following years of ultra-low interest rates and quantitative easing.

Global equity indices (rebased level)



Global sovereign 10-year bond yields (%)



Source: Refinitiv Datastream.

While inflation was ticking higher throughout 2021, markets had initially been reassured by the narrative this would be transitory. Unfortunately, inflation has proved far more stubborn than initially believed with the war in Ukraine only exacerbating matters. This has resulted in the raising of interest rates by central banks, prompting weakness in both stocks and bonds and leaving limited places for investors to hide.

One of the few places to find positive returns this year has been in energy and commodities. The windfall profits for energy producers, alongside a substantial fall in the pound pushing up the value of overseas earnings, has helped the FTSE 100 be one of the best performing stock indices this year. However, we should point out the narrowness of this performance. Unless one was overweight energy companies, it has been difficult to keep up with the FTSE 100 this year, let alone outperform.

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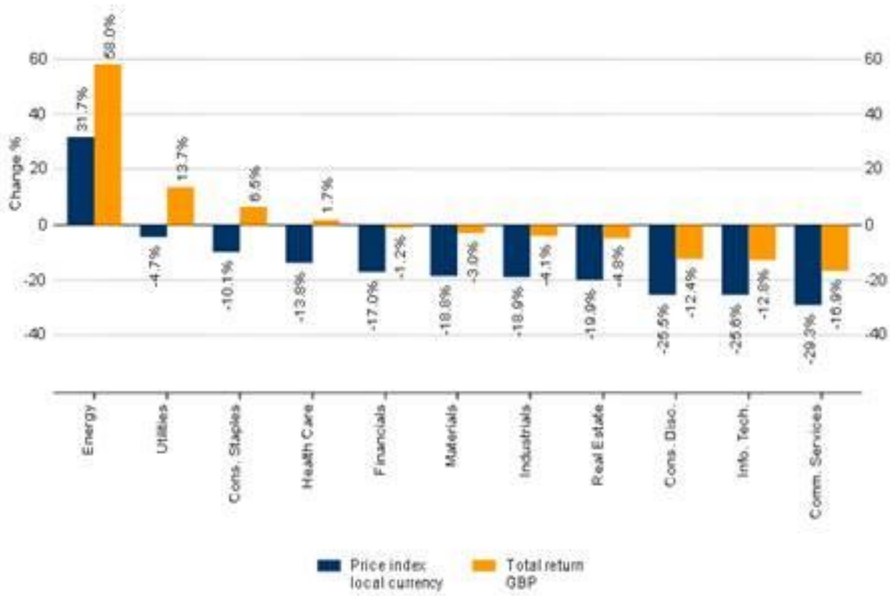
Sector

YTD Performance ending 31 August '22



Source: Refinitiv Datastream

While it may have been tempting to chase the outperformance of energy companies, we must keep in mind our long-term investment focus. Over the longer-term energy has underperformed the wider equity market and much of the gains of the past year have only resulted in the sector catching up. This, in part, gets to the crux of the issue we have seen this year. Many of the worst hit assets have been those which have performed so strongly over the last decade or so – US technology and growth stocks in particular.

We would also highlight that volatility is the price investors pay for seeking higher returns than those available on exclusively low risk investments. While predicting exactly when we are likely to experience volatility can be difficult, there can be no doubt that it will be experienced at some point in any long-term investment. However, history has demonstrated the rewards of sitting tight through periods of volatility; the chart below outlining long-term stock market returns, despite substantial periods of market weakness, is reassuring at times such as these.

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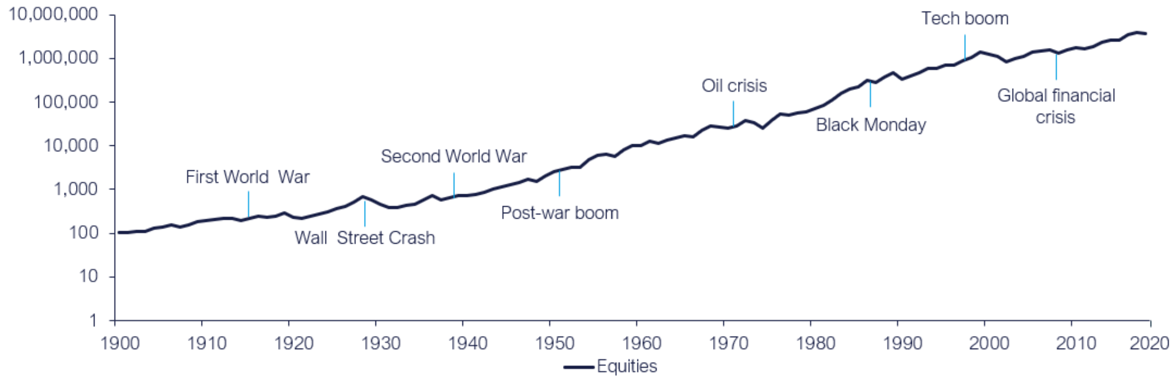

Looking forward, we expect markets to continue to be volatile until the future path for inflation and interest rises becomes clearer. We would, however, highlight that this picture could change as quickly as it has developed. We have seen some early signs that inflation may have peaked, with oil now some way off its high and retailers indicating they are likely to begin cutting prices to clear overstocked inventories and to continue to draw in increasingly stretched consumers.

We are also starting to see medium-to-long-term investment opportunities arising, with many high quality, well capitalised business in structural growth sectors trading at a considerable discount to last year. Similarly, value opportunities are cropping up in the bond market for the first time in many years – in reality, since before the financial crisis! One can now receive a gross annual yield of close to 5% on a UK government bond maturing in January 2025, something which would have been unthinkable only a matter of months ago.

It has clearly been a challenging 2022 thus far but I hope that it is clear from my email that not only do we understand why, but we are closely monitoring your investments with a view to taking advantage of market weakness where suitable. We also believe it is in your best interests to retain holdings where we perceive the weakness as overdone or where we consider the long-term structural drivers for growth to remain in place. When the markets are as volatile as they have been at present, it is rarely beneficial to make drastic changes, although we will, of course, continue to make adjustments as necessary.

Yours sincerely

Simon Chicken
Divisional Director

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