FOR PROFESSIONAL ADVISERS ONLY

2023 Market Round-up

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Remembrance

It would simply not be right to speak on portfolio or market performance in 2023, before first remembering the many lives that have been lost in the year due to natural disaster and conflict. Life is precious and should be protected at all costs. Our thoughts go out to all of those that have been affected.

2023 Summary

- Despite volatility, 2023 concluded on a much stronger note to where it began.
- Global inflation continued to cool.
- The US Central Bank expressed a more optimistic outlook for their economy.
- Improvements to the US economy often lead to improvements elsewhere in the world.
- Economists and markets alike are entering 2024 with a more positive outlook than last year.

Market review: From gloom to boom

At the start of the year, global inflation was at historically high levels (although decreasing), and there was a pessimistic sentiment and outlook from central banks, economists, and markets worldwide. Fast forward 12 months, and we ended the year with the world's largest stock market (US: S&P 500) experiencing an almost 20% increase, with most markets around the globe showing strong performance. Additionally, the US Federal Reserve, the world's largest central bank, expressed satisfaction with their progress.

The head of the US Federal Reserve, Chair Jerome Powell, also said that should inflation continue to cool, and conditions continue to improve, interest rate cuts were likely in 2024. The US market responded in earnest to this positive news, recording a new all-time high on the 22nd of December.

This is important because:

The US leads the way - Usually, the United States is at the forefront of economic advancement. If the actions and monetary policies of their Central Bank have a positive effect on the economic situation there, it is probable that other central banks worldwide will emulate their approach.

Interest rates drive investment returns - Financial markets are highly affected by interest rates. When rates decrease, companies have more capital to spend and consumers have more disposable income. This often leads to a new phase of economic growth. Conversely, when Central Banks raised rates aggressively in early 2022, it caused a significant decline in markets during the first half of the year.

Interest rates drive cash returns - Interest rates drive the rate of returns available within cash deposit accounts, and with interest rates being so high recently, many investors have been enticed to divest from their investments and put their money into cash. Not only are rates set to fall, but many portfolios are already beating cash deposit rates. In fact 75% of portfolios available via a Managed Portfolio Services in the UK outperformed cash in 2023, net of all investor charges.

We started 2023 how we ended 2022, with gloom and worry about the year ahead. The year then had its ups and downs, and the media fanned the flames as much as they possibly could to bait our clicks, but inflation continued to cool and Central Bank sentiment improved, and markets and models finished the year in a much better place as a result.

Despite a positive end, 2023 was for the most part a volatile period for investors. Whether it was the averted US Banking crisis in March, the US banging its head on the debt ceiling in April or volatility through October in response to the conflict in Israel and Gaza. There was much negative news to drive portfolio behaviour in the short term.

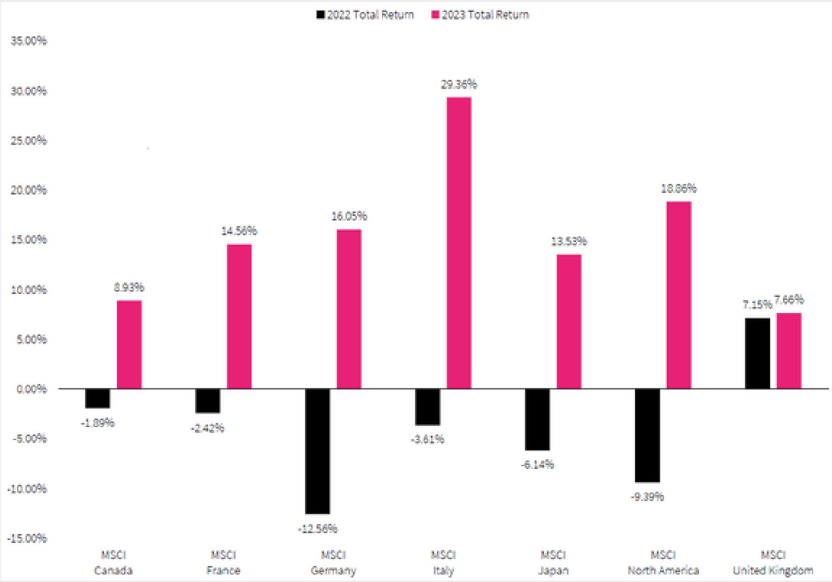
Fortunately, global inflation has been kept in check due to actions taken by Central Banks, and influential voices are now expressing a more positive outlook. This has led the markets to recognise that the underlying fundamentals remain strong and that the future holds a more supportive environment for growth.

Although the US market index had a fantastic year, only 1.4% of S&P 500 companies (otherwise known as the ‘Magnificent 7’) drove 90% of the return. A key theme driving their success was the adoption of Artificial Intelligence (AI) and the new opportunities for efficiency and profitability that it represents. This is a good sign if we study historic market behaviour, as any strong and sustained period of growth is usually started by a handful of companies that represent a new and more profitable way of operating, which the broader market soon adopts.

A great example of this was Henry Ford’s introduction of the assembly line in the early 20th Century. He and the Ford Motor Company served as a ‘proof of concept’ in how much more efficient and profitable an organisation can be with this new approach. Fast forward 10 years and companies across all manufacturing industries around the world had introduced them, and a new wave of profitability and growth ensued.

2023 Summarised in Four Charts

Returns from G7 Stock Markets in 2023

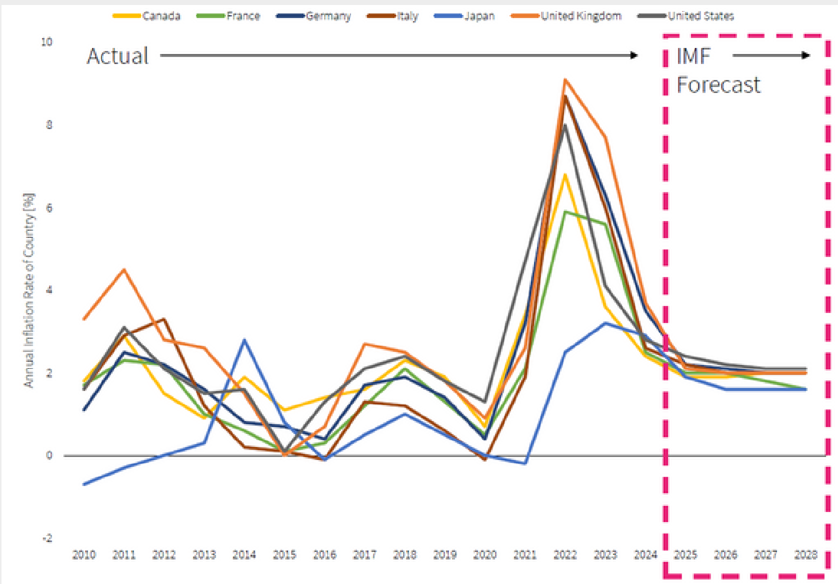


Market returns stronger in 2023

Source: FE FundInfo & MSCI. Data accessed 06/01/2023.

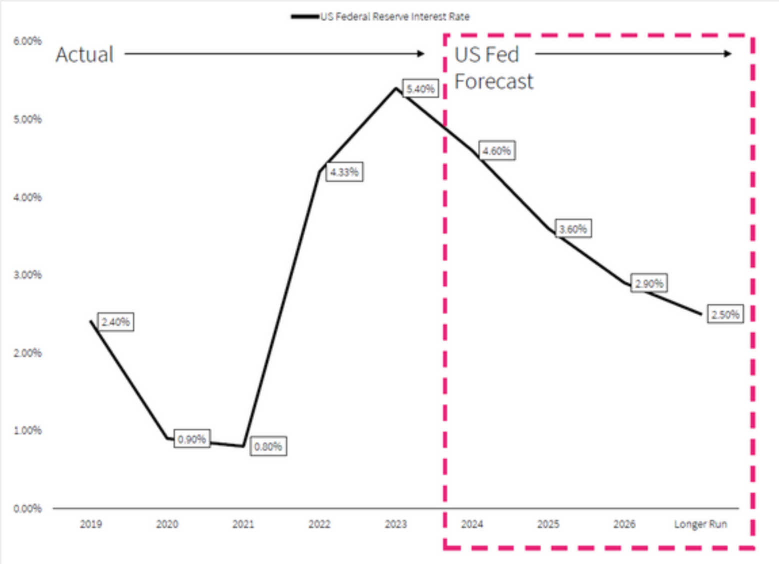
IMF Annual Inflation Data of G7 economies

Global inflation cooled



Source: International Monetary Fund database. Data accessed 07/01/2023.

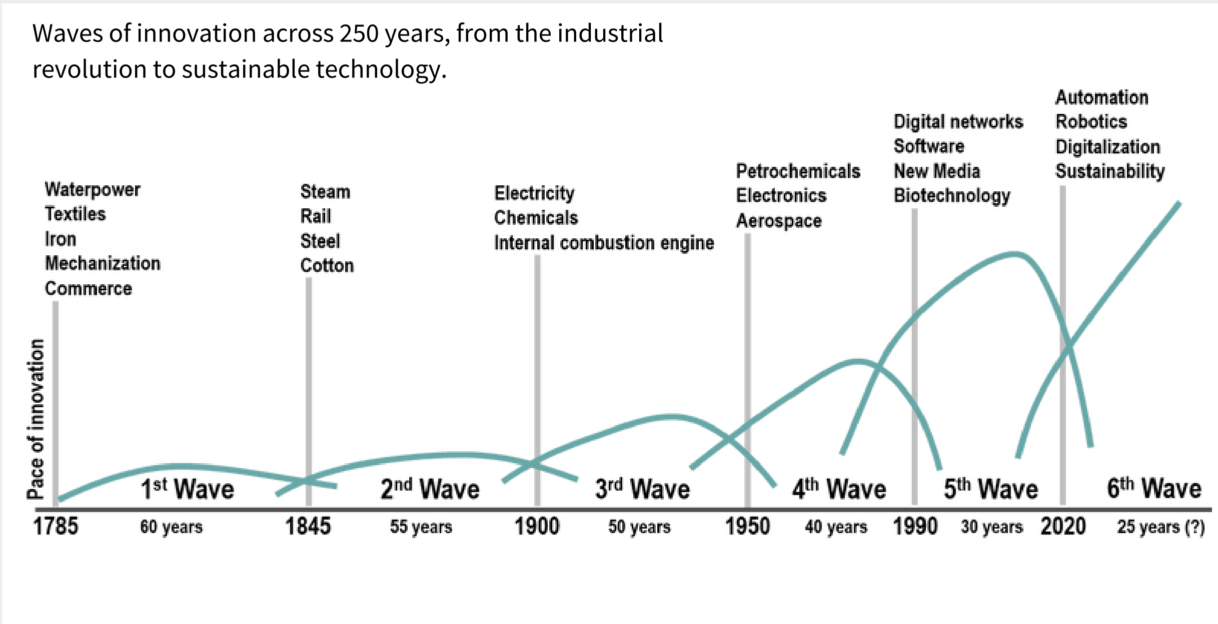
US Fed Interest Rate - Median dot plot projection



US Reducing Rates in 2024

Source: US Federal Reserve website. Data accessed 07/01/2023

Innovation Cycles



Source: Adapted from Hargroves, K. and M. Smith (2005) Natural Advantage of Nations:

- The big moves in the US market, and specifically the Tech sector, are being driven by expectations that AI will have a dramatic impact on global productivity and company profits.
- Tech companies invest a lot in R&D and with interest rates set to come down, the cost of capital will reduce and encourage greater investment and greater advances.
- The beginning of any innovation cycle begins with a handful of firms that serve as a 'proof of concept' to the rest of the economy.
- Henry Ford's introduction of the production line soon became the single biggest driver of manufacturing productivity globally.
- Will widespread adoption of AI be the next big driver of productivity?

Risk Warnings

The value and income from investments can go down as well as up and are not guaranteed. An investor may get back significantly less than they invest. Past performance is not a reliable indicator of current or future performance and should not be the sole factor considered when selecting funds. Our funds invest for the long-term and may not be appropriate for investors who plan to take money out within five years. The fund will be exposed to stock markets and market conditions can change rapidly. Prices can move irrationally and be affected unpredictably by diverse factors, including political and economic events.

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