...Saltus

Investment review for quarter ending 30 September 2021

"We shall not cease from exploration... And the end of all our exploring Will be to arrive where we started... And know the place for the first time"

T S Eliot in his poem ''Little Gidding''

The third quarter of 2021 was another one with oscillating sentiment, sharp price movements and a general sense that an important transition was underway amidst all the noise. Well over a year after lockdowns were first imposed, the success of vaccines in dealing with Covid has allowed investors to shift their focus away from the virus towards more fundamental economic matters. Investor attention is now largely absorbed by inflation rates as opposed to infection rates, and the issue is proving to be a tough one to position for correctly.

Initially, investors felt that inflation risk was more than priced into major bond markets, as evidenced by the strong performance and steady buying of early summer. The fact that this bond market rally occurred whilst inflation readings were coming in at record levels, just served to underline the consensus view that the issue would prove to be transitory in nature rather than 'sticky'. However, this sanguine view was increasingly challenged over the quarter, particularly as bottlenecks in the global supply chain fed through into some shortages in goods and price spikes in commodities. The prospect of these issues taking longer than expected to fix brought the 'sticky' inflation issue to the fore and as investors mindsets shifted nervously, market sentiment quickly deteriorated.

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One other contributing factor to souring sentiment was the confusing and changeable outlook for the Chinese economy which remains, alongside the USA, the most significant contributor to global growth. For many months the Chinese Communist party had been moving forward with it's ''common prosperity'' agenda, in effect an attempt to use regulation to deal with the social imbalances that rampant growth had delivered. Unfortunately this agenda has ended up being pursued at a point when the clean-up of the domestic property sector is simultaneously delivering its first casualties. The possible knock on effects of the bankruptcy of a huge property developer on consumer sentiment dented global risk appetite just at the point when the market was already confused about how to price increased regulatory risk. With this issue acting in concert with headline grabbing price pressures, news outlets had plenty of near term negative issues to focus on, helping to set the scene for a move downwards.

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By late September many of the gains of early summer had begun to be unwound in a steady, global selloff. In equites this largely took the form of aggressive profit taking and some shuffling in market leadership to more economically sensitive sectors. In the bond market, the selloff seemed to us to be more of an overdue recognition that as the Covid era was ending, monetary policy should be tightening and yields should be rising to reflect this new reality. Returning to 'normal' isn't quite a fait accompli yet, but it is perhaps close enough for markets to properly price in life without the scale of intervention we have seen. By the end of the quarter this process was well underway, with bond market yields returning roughly to the levels of early 2020, just before Covid intervened.

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The jury is still out on the global supply chain issue, but our feeling is that it is a fixable problem, which corporations who are in general awash with cash, will address via an uptick in capital expenditure programs. Consensus opinion already expects that inflation will remain high in the US and UK until the second half of next year, which leave some room for the corporate capex machine to spin up to address the issue. We would hope that the forthcoming Q3 earnings season will provide more evidence that this is what is actually happening, and act with other factors to provide a positive offset to the more recent gloom.

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Amongst the other factors which could impact the outlook positively is the steadily improving picture on Covid. Vaccine take up is continuing to broaden and act in conjunction with new therapies to blunt hospitalizations. This, in turn, reduces the risks of another lockdown and increases the chances that living with the virus will turn out to be much less of an issue than it looked to be only a few short months ago.

The Saltus Investment Team, October 2021

	UK Equities	US Equities	Europe (ex UK)	Japan	Asian	Other Equities	Property	Alternatives	Bonds	Cash
MAP 2	5.9%	15.5%	0.9%	3.1%	2.3%	11.4%	3.0%	25.8%	25.0%	7.1%
MAP 3	8.3%	24.0%	1.4%	4.8%	3.7%	14.5%	1.9%	17.9%	17.1%	6.4%
MAP 4	11.6%	32.7%	1.8%	6.5%	4.9%	19.1%	0.6%	14.9%	3.4%	4.6%

	Quarter	Benchmark Quarter	Year to Date	Benchmark Year to Date	Benchmark
MAP 2	0.59%	1.49%	2.98%	4.48%	CPI plus 2%
MAP 3	0.30%	1.75%	3.96%	5.26%	CPI plus 3%
MAP 4	0.37%	2.00%	5.63%	6.05%	CPI plus 4%

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