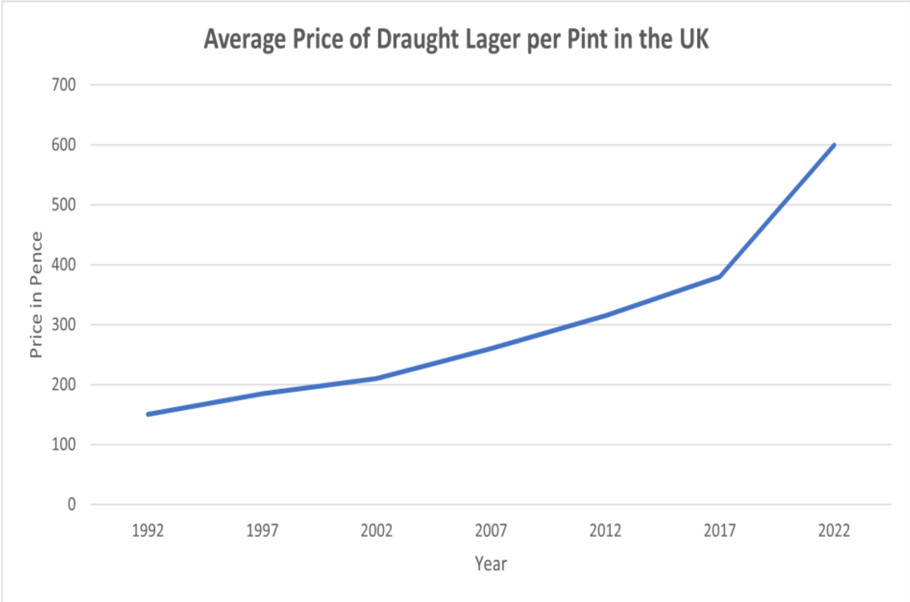
Newsletter - Fourth Quarter 2022

PRAISE MY SOUL THE KING OF HEAVEN

Looking back, it has been a unique quarter. The Queen's death produced a period of reflection and recollections of her unprecedented rule. In keeping with the tone, I learnt that she much admired the hymn "Praise, my soul, the King of Heaven" originally published in 1834 as a paraphrase of Psalm 103. I can remember singing this as a child without much thought to its meaning. However, reading through it again, the undertones of healing and forgiveness are all too apparent. Somewhat ironic given the mood and geo-political backdrop in the world we live in today.

ASSET ALLOCATION MUSINGS

I'm not sure there's an appropriate place to start this newsletter. Do we focus on the monarchy, politics, ongoing conflict, extreme weather, strikes, cost of living - there is a vast array from which to select. We will channel our thoughts on what is in front of us, and as we see a challenging winter that lies ahead, despite wanting to be contrarian, it's hard to be right now. Listening to the radio this morning, it appears the shoe that just dropped unnoticed (that will further impact the cost-of-living crisis) is the sharp rise in the price of carbon dioxide. The Energy and Climate Intelligence Unit reported that the price of liquid carbon dioxide has risen by 3,000% over the last 12 months and it's the food and drink sector that will be footing the bill. CO_2 is a key input into meat production, soft drinks, beer, plastic packaging and fertilizer. Maybe we should be alert to the constant scare mongering from journalist quarters, however the constant left field threats from all sides have us scratching our heads. As much as a I like a pint of beer at my local establishment, as you can see from the chart below, the price inflation in this category has me thinking it could be time to hunker down at home and dust off the home-made damson gin from my 2016 vintage for the cold dark nights ahead.

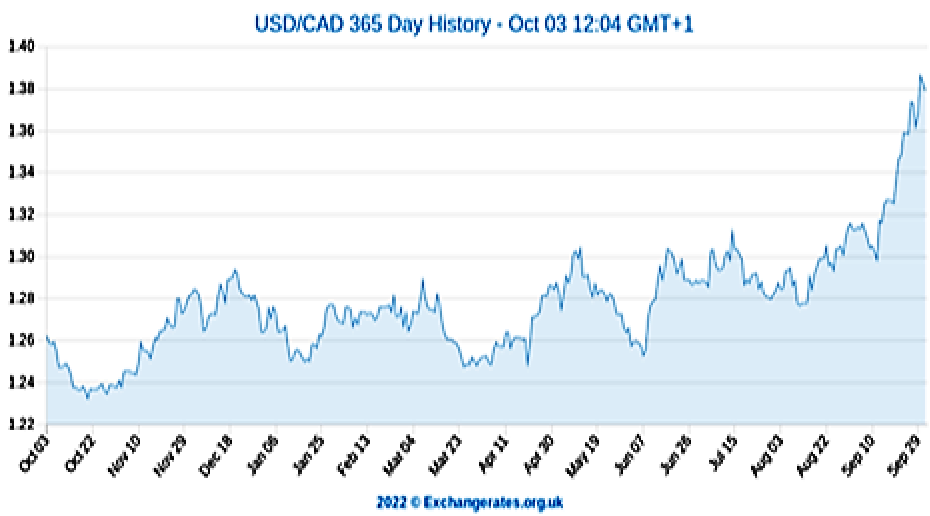


IT FEELS LIKE IT'S JUST THE UK

With political tensions running at breaking point, it was somewhat ironic that the two main political parties had their own conferences last month amid turmoil. What a difference a year makes. Roll back a year and Boris et al were basking in their apparent Covid success, detracting their audience from Boris-gate, whilst Keir and Co. were left to try and score some cheap political points. Roll forward a year and a change in Tory leadership and a government mini-budget, that went down like a cup of the proverbial in our humble opinion, no doubt had Labour's activists and it's PR machine having to rewrite their conference posters and speeches overnight. The sheer deluge of criticism from all corners of the financial world got us thinking whether the UK were alone in the financial quagmire. This is a snapshot of what we unearthed:

Did you know the Thai Prime Minister has been suspended for six weeks after supposedly over-staying his welcome (term restricted to 8 years) having rewritten the consititution without having been formally elected in 2014. Makes Boris look saintly don't you think? The barrage of negative comments from our European cousins regarding the mini-budget was probably less surprising. However did you know that Germany unleashed its own equivalent fiscal package, the third of its kind, in response to the impact of higher energy prices and without the fiscal adjustments required to pay for the package (sound familiar?).

Greenback (US dollar) vs Loonie (Canadian dollar)



Mark Carney, the UK's previous Bank of England Governor, was also quick to cast his critical eye on the mini-budget. Anyone with a sense of financial prudence will recall how his policy as Canada's Central Bank Governor, pushing interest rates down too far and for too long in our opinion, acted as a pre-cursor to the troubles they now face. Canada has excessive debt, especially at the consumer level, and a property market that has begun to falter; try and ask a Canadian for their views on Mr. Carney and you may be surprised by their response.

Ironically, the UK pound has now recovered back its post-mini-budget losses versus the US dollar. Despite the IMF's edicts about the currency, it may not be quite the emerging market basket case we were led to believe. Was it pure journalistic scaremongering at play? Only time will tell.

WANT TO OWN A PORSCHE BUT CAN'T AFFORD THE PRICE TAG…

Volkswagen (VW) pressed ahead with the listing of its Porsche subsidiary despite dislocations in stock markets, pricing the deal at the top end of expectations last month. VW raised €19bn in the process to enable more resources to be channeled into electric vehicle manufacturing. The prognosis for shareholders in Porsche looks less appealing if the run rate of new listings over the last 12 months is anything to go by. Additionally, having Emma Raducanu as a brand ambassador at a time when her form has slipped may be a bad omen. However, at €81 per share (below issue price), it is at least a cheaper way to own the Porsche brand than the latest Taycan model...!

HERE'S OUR TWO PENNIES WORTH ON THE GOVERNMENT'S ECONOMIC POLICIES

Although it appears as if the mini-budget announced at the end of September is now subject to populist revisions, we thought it would be sensible to outline our thoughts on current government economic policy. Prior to Kamakaze Kwasi's economic stimulus package we were curious as to how the Treasury and Chancellor were stepping in to promote growth and help ease the burden of the cost of living crisis, whereas the Bank of England (BoE) was attempting to take the heat out of the economy with interest rate increases aimed at tempering inflation. This is akin, in our eyes, to the government pressing their foot down on the accelerator at the same time the BoE slamming on the brakes (as employment levels are near full and output gaps are pushing prices ever higher). The results, from our perspective, being a muddled mess as both the current account and budget deficits continue to expand.

As we have alluded to previously, the issue of running monetary policy too losely in the first instance was, in our eyes, naive (i.e. interest rates were kept too low given a stable economy, strong employment data and a buoyant property market). This was the time to gently raise rates when the economy was robust, not as is now the case, when the economy is suffering under inflationary duress and may even be in recession.

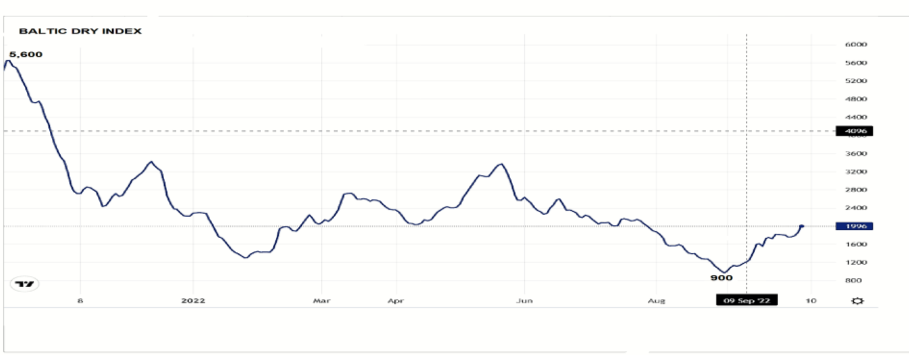
There are clearly no quick fixes, either in the UK or elsewhere around the world where the same problems co-exist. However, we are not in the camp that reacted before deploying the brain matter. The various measures were to some extent required given the ongoing squeeze in people's living standards, and many of the policies were supported on both sides of the political spectrum. The government's debt profile looks similar to many developed economies (US, Canada, Europe, Japan, Australia..), so the end game may be a unified action to remove areas of debt deemed too unjust (student debt springs to mind). This is a subject matter for another newsletter, you'll be glad to know. As to how the Conservative Party recover lost confidence in their elector base, this may be an even stiffer task.

INTERESTING FACT

Searches for " real estate market crash" exploded by 284% in the US as of September 2022 – the highest level in Google Trends history. So, despite having a currency that's as safe as houses, it appears the houses aren't built on as solid a foundation.

LOOK TO THE SHORT TERM TO FIND ALTERNATIVE NARRATIVES

Last quarter we looked at why avoiding the near term noise and focussing on the long term fundamentals can be a useful exercise (why equities are the standout long term asset to own). This quarter we look at some of the near term indicators which support growth assets in the longer term. Financial markets are quick to discount bad news, meaning that the stock market is likely to have factored in a recession long before it hits home. It's hard to find any positive news out there right now, and you probably won't have noticed that several key commodities' prices have fallen a long way from their recent peaks. Wheat prices have retraced over one third, gasoline futures (oil indicator in the US) are down almost 40%, the copper price peaked in March and has fallen 30%, the steel price is down almost two-thirds and the stand out winner - international shipping costs – are down 70% from the highs (see the chart below). Perhaps the inflation story is beginning to unwind, and with this the markets should eventually adjust to a brighter outlook.



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