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1Q 2023 Commentary

Financial markets performed well in the first quarter of 2023, in spite of continued signs of inflation and central banks taking action by increasing interest rates, as well as the worrying developments in March in the banking sector when US lender Silicon Valley Bank (SVB) collapsed, and several other lenders came under significant stress. In light of this, banking sector stocks fell hard and have held back the performance of 'value' equities which had been performing well in the early part of the quarter. Investor money is clearly returning to 'growth' equities, and in particular technology stocks, with the Nasdaq rising over 15% in the quarter.

When the news of SVB's collapse hit the wires, the US central bank and the Federal Deposit Insurance Corporation moved swiftly to contain the erosion of confidence by guaranteeing customer deposits. This action helped to bring stability to the sector and to wider financial markets.

Despite the banking sector worries, the US Central Bank (the Federal Reserve) alongside other central banks, has continued to raise interest rates, as they focus on containing inflationary pressures. Analysts now expect that a number of Western countries are close to peak rates in this current cycle of interest rate increases.

While wage inflation will likely prove sticky, energy inflation should greatly subside in the coming months. Natural gas prices are back to the long-term trend, reverting to those prices before the pandemic and the Russian invasion into Ukraine. Oil prices have softened, due to good storage and to demand matching supply, and has led to OPEC+ recently announcing monthly production cuts.

China expects 5% economic growth over the course of the year, and the country's reopening following extensive lockdowns in 2022 should help global economic activity.

The US dollar has weakened over the quarter under review, and sterling has been among the best performing foreign currencies, having recovered to those levels seen last summer before the UK's disastrous mini-budget in September.

A recession is still forecast in 2023 for most economies, but with the pullback in energy prices the effects are expected to be mild. Employment remains robust, and while manufacturing data shows contraction, services data remains strong. Furthermore, the investment programmes in infrastructure and clean energy are expected to assist with mitigating some of the slowdown in industrial activity.

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Although there are still many uncertainties, especially concerning resolution to the Russian invasion of Ukraine, and there may still be ripple effects from the recent banking turmoil, risk assets are much more attractive than they were at the beginning of 2022.

With certain fixed income investments now providing attractive diversification in portfolios and a potentially steady interest rate environment ahead, equities should provide commensurate returns to investors.

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