

# FEBRUARY 2023

## MONTHLY COMMENTARY

Following a strong start to the year, spurred by improving inflation data figures and growing hopes that the current global monetary tightening cycle was nearing its end, solid economic data released in February led to a sell off in both bond and equity markets. The Bloomberg Barclays global aggregate bond index closed the month in the red returning -3.3% underperforming global equity markets which rounded off the market with a return of -2.4%.

While the typical expectation is that markets would welcome strong economic data; the economic data released in February led many investors to re-evaluate the previous consensus views of where interest rates would peak and, more significantly, when rate cuts could be expected. If the economic picture remains strong, central banks have more slack to keep increasing rates in a bid to bring down inflation which is behaving more stubbornly than many expected. Markets began to price out a rate cut by the end of 2023 which punished equity and bond investors alike. Central banks in the US, UK and Eurozone remained united on the view that, in the battle against inflation, their job is not yet done.

### UK

UK equities performed well during February, returning 1.94% and the FTSE 100 index achieved a new record high owing to upbeat company earnings. The best performing sectors were energy, healthcare and telecom which benefitted from revived dollar strength as investors began to expect a higher peak in interest rates in the US.

The Bank of England (BOE) implemented a 0.50% interest rate increase to 4% in February which was expected by markets. Andrew Bailey, BOE governor, placated investors by claiming that inflation had turned a corner, a claim that was backed up by the Consumer Price Index data later in the month which reported inflation had fallen to 10.1%, continuing its downward trajectory.

The UK dodged a technical recession with the GDP (Gross Domestic Product) data for Q4 2022 showing the economy had not contracted (avoiding two consecutive quarters of decline following the contraction in Q3 2022). And the economic outlook appears to be improving. Although the BOE still expects the UK to fall into recession in 2023, the downturn is now expected to be much shallower than the previous forecasts made back in November when energy price levels were much higher.

### US

Over the pond in the US, the Fed (Federal Reserve) voted a further 0.25% increase in the interest rate to 4.75%. Chairman Jerome Powell delivered a warning that the disinflation process (a slowdown in the rate of inflation increases) will take longer, and further rate hikes will likely be required.

The Consumer Price Index data released in the US showed signs of stubbornness which sent shockwaves through markets and added more weight to Powell's comments. On a monthly

basis, inflation was faster than expected. It rose 0.5% percent from December compared to the previous report of 0.1%, owing in part to gas prices. Food prices and a range of service prices also climbed swiftly. Concerning inflation figures were coupled with a stronger than expected labour market report and retail sales data.

Markets wobbled as the narrative changed from January: inflation is showing a worrying amount of stickiness, even as it moderates from its peak.

Technology stocks performed the best with healthcare and communications sectors being the biggest detractors.

## EUROPE

European equity markets performed well during the month with major markets finishing flat-to-positive. This is likely due to the comparatively lower valuations, compared to their US counterparts, and the reopening of China's economy after the lifting of zero-COVID policies which is encouraging for consumer demand for European cars and luxury goods. Several of these companies make up a key component of our London & Capital core equity strategy. The European Central Bank (ECB) delivered a 0.5% interest rate increase with ECB president Christine Lagarde signalling an intention to increase rates again by 0.5% in March. The ECB cited concerns over persistent core inflation to justify the hawkish tone. Inflation data released in the month showed that headline inflation had fallen again but core inflation pushed up to 5.3%. With the Eurozone being highly affected by energy costs, the fall in energy prices brought reprise to both companies and households in the region which should help to boost consumer confidence and reduce risks of a deep recession. Furthermore, the European commission announced the Green Deal Industrial Plan, which aims to scale up the manufacturing capacity of green technologies. A move which reiterates Europe's commitment to accelerating the energy transition.

## CHINA

February proved a tougher month for China as the reopening post COVID-19 is proving to be uneven. Underperformance was driven in part by profit-taking after strong returns since October's lows and dwindling enthusiasm for the re-opening of the economy. Furthermore, increased geopolitical tensions with the US discouraged investors following the shooting down of a Chinese high-altitude balloon in US airspace.

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