Market 2 Market

A forward view of the global economy and financial markets

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The Coronation of a King

"Through God hath raised me high, yet this I count the glory of my crown: that I have reigned with your loves"
HM Queen Elizabeth I, 1601

Source: Wikipedia

We now know that the coronation of HM King Charles III will take place at Westminster Abbey on Saturday 6th May 2023. This gives the tailors plenty of time to change the cyphers on the uniforms of trumpeters and heralds. The other main beneficiaries of this early announcement are the manufacturers of souvenirs and general celebratory tat which will hopefully give some benefit to the china and glassware businesses in the UK.

The UK is the last country in Europe to hold coronations, the other countries with monarchies now hold inaugurations, which in the case of the Dutch monarch entails a ceremony before a joint session of the States General. We do things differently in the UK. Upon the death of HM Queen Elizabeth II proclamations were read out all over the Kingdom declaring the beginning of the reign of King Charles III. So why do we need a coronation?

British coronations involve two important aspects. The first is that the monarch is the head of the Church of England and central to the ceremony is the anointing of the monarch with holy oil. The quote from Elizabeth I refers to her being raised high, a statement which means that the monarch is above other men and women in the eyes of God. This view would certainly be open to challenge in our modern society. Indeed, we cut the head off the monarch in 1649 as he had tried to place himself above other men and women as a ruler by divine right.

The second part of the ceremony requires the monarch to swear that he or she will govern the peoples of the UK and the Commonwealth Realms "according to their respective laws and customs" which is the only part of the ceremony required by law.

The coronation of HM King Charles III is almost certainly going to be a shorter ceremony in comparison with the last coronation in 1953, which lasted three hours. We have already had some controversy over the crown that the queen consort may wear and over whether a bank holiday will be declared by the government. In the current scheme of things these may seem like trivial matters, but it does show how much interest there is in the ceremony and it will be a lavish state occasion with the UK putting its best forward to a huge global audience.

English coronations have traditionally been held at Westminster Abbey since 1066, before then monarchs have been crowned in Bath, Oxford and Canterbury or wherever it was convenient. The first recorded coronation of an English King dates back to 973 at Bath Abbey for the coronation of Edgar when an order of service was used that was based on ceremonies used by Frankish Kings. Coronations have evolved over the centuries and there is no rigid format that has to be adhered to. The coronation of HM Charles III is likely to be much more modern in its format, certainly shorter in duration and a careful eye will be kept to keep costs under control.

It will however, still be a day of pageantry and celebration, which we do so well in this country and I will certainly will be buying at least one item of celebratory tat which will go along with all the other T-towels, mugs and plates I have from other historic royal occasions.

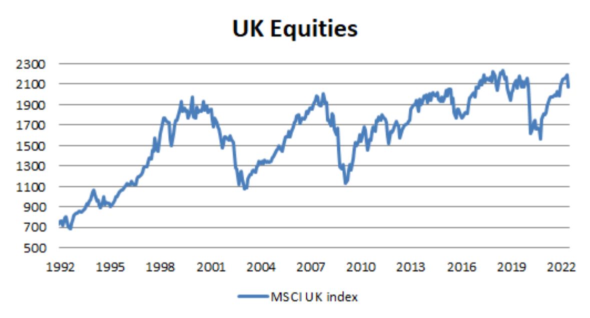
Richard Harper
Head of Asset Allocation
GHC Capital Markets Limited

Asset Allocation

In which **Tim Harris**, the Chair of our Asset Allocation Committee, describes the factors influencing our latest Asset Allocation decisions

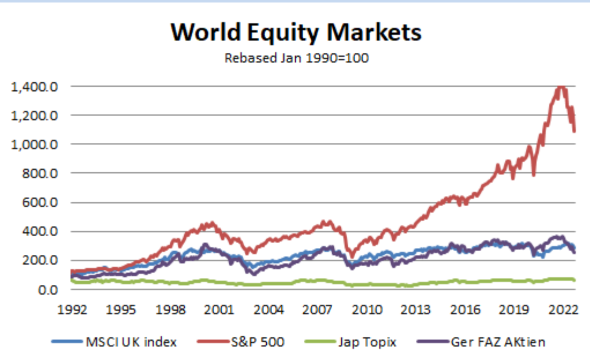
Too early to buy risky assets	Growth forecasts are down and interest rate forecasts have shot up. Global growth forecasts have slipped by 150bps since the start of the year. Consensus forecasts for US GDP growth are down to about 1.5%, while forecasts for the EU have improved modestly after governments capped the impact of higher energy prices. However, next year could be difficult**.** Market expectations of central bank tightening have moved up since mid-August, as the market realised that core inflation was going to be more of a problem than previously thought. German headline inflation hitting 10% and a surprise on US core inflation data have hit the markets hard.
Equities	Equity markets had a tough third quarter. The aggregate equity returns for the quarter hide the fact that global equities dropped 17% from their quarterly peak in mid-August. The S&P 500 volatility index shot up to 30% from 20% over those six weeks. Positive investor sentiment evaporated, as inflation rose sharply, forcing central banks to execute far greater tightening than the market had previously expected.
Bonds	Bonds were volatile, with a significant rally early in the quarter followed by a dismal drop in the latter half. In the early part of the quarter high yield debt did well, following the strong recovery in the equity markets, before retreating by about 10% from their peak levels. Nevertheless, global high yield quarterly losses are modest. UK gilts stand out for their dismal performance during the quarter. The UK government's mini-budget was anything but mini. The implied extra burden of debt put the skids under the gilt market, creating circumstances where the Bank of England had to step in to stabilise it.
Amidst the cross-currents of geopolitics	We believe that it is too early in this down leg of the global economy for a significant buying opportunity to be at hand. We have yet to see the recession that central bankers are seemingly trying to create. We are seeing the monetary tightening, but not the full consequence of the tightening. The recent mess in the UK is probably the most significant manifestation of unpredicted trouble so far. The three major debt rating agencies have put UK government debt on negative credit watch. This is not the global financial crisis of 2007-9, but a massive economic regime change from deflation to inflation. If we take central bankers at their word, their primary focus is squeezing inflation out of the system. At this stage, they are asking investors to take the rise in interest rates in their stride, as this will help provide a sustainable economy in the future. That said, we see opportunities emerging in some asset classes. We are keeping a close watch on assets that are near or nearing their extreme historical valuations.
European Equities	Eurozone equities have had a torrid time, but the valuations are now approaching the previous buying territory. The dividend yield of the market is close to 4% and the P/E of the market close to the 10x multiple low of previous cycles.
Japanese Yen and asset markets	The yen may be another asset class that is approaching a buying opportunity. The recent sell-off has been brutal, as the Japanese central bank left monetary policy loose even in the face of a collapsing currency and higher interest rates abroad. There is however, hope of a change in policy at the central bank level, considering inflation has picked up and activity is set to accelerate as the re-opening of the economy post COVID boosts growth. Economists are pencilling in 3.5% annualised growth this coming quarter as the economy re-opens. Inflation is already at 3.0%. A stable yen and a vibrant economy, with strong nominal growth should help the equity market. In local currency terms Japanese equities have been one of the best performers among global markets over the past twelve months, which we have captured on a currency-hedged basis. We maintain an exposure to Japanese equities in most of our Optimised Portfolio Service portfolios.
Global High Yield - too early but on the way to value	Yields have risen spectacularly since the mid-last year lows of 4.2%. Bond investors are concerned about the scale of the likely defaults as we go through a recession. We can only hope that the Global Financial Crisis will not be repeated. But, central banks now have more tools at their disposal to save the situation compared to the early days of the GFC. On a spread basis, the current 650bps is around half of the peak of the GFC.

Markets at a glance



Source: Lipper for Investment Management

The FTSE 100 index has taken much in its stride through the summer, given the Ukraine war, inflation, supply chain disruptions, heightened security risks and the extraordinary economic performance of the new UK government. Nonetheless, it is one of the better performing international indices, being down 7% year-to -date after 3-4 years of underperformance against its peers. The market's relatively modest valuation and the resilient performance of leading international companies have allowed some relative catch up. Despite a strong earnings and cashflow recovery from the lows of the COVID crisis, rising inflation pressure implies more tightening of monetary policy. This raises investment hurdle rates, which will keep pressure on valuations.



Source: Lipper for Investment Management

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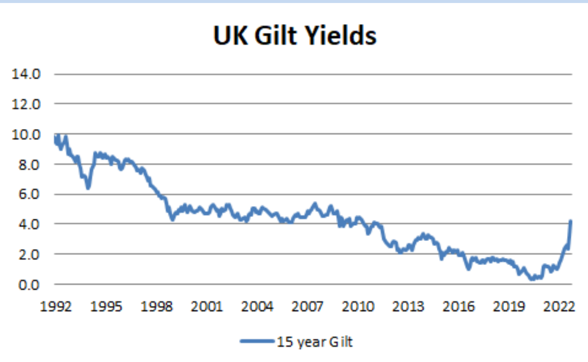
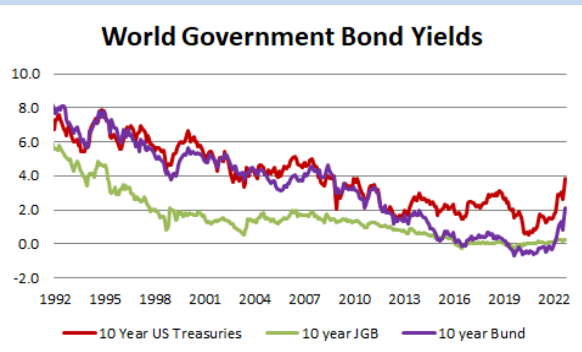


Source: Lipper for Investment Management

Gilt yields have now risen above 4.0% for the first time since the Global Financial Crisis. Inflation fears concern markets, but the loss of confidence in the new government's economic competence is a large contributor to this devaluation. All the major credit rating agencies now have UK government debt on negative watch. Inflation concerns reflect shortages of materials and wage pressures, given labour shortages in sectors, such as retail and hospitality. Real gilt yields are very negative, given high headline and core inflation. The Bank of England has promised a significant monetary policy response to recent fiscal expansion. There is little worse for a government bond market than policy error.



Source: Infront

We think the rises in global government bond yields have further to run. Government bond yields have typically peaked only shortly before the ends of central bank tightening cycles and we expect most major central banks to continue hiking rates over the next 12 months or so. The increase in government bond yields, as well as the threat of slowing global economic growth, will also keep corporate bonds, under pressure, although default experience is currently relatively modest. Aggressive rate tightening by the Fed is resulting in further strengthening of the US dollar against most currencies. Bond markets will only start to turn a corner when tightening cycles draw to a close, possibly a year away.

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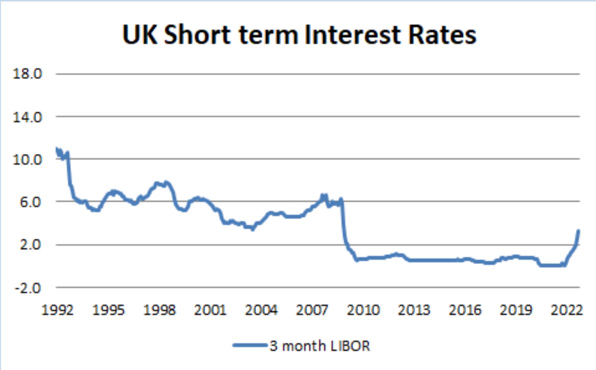
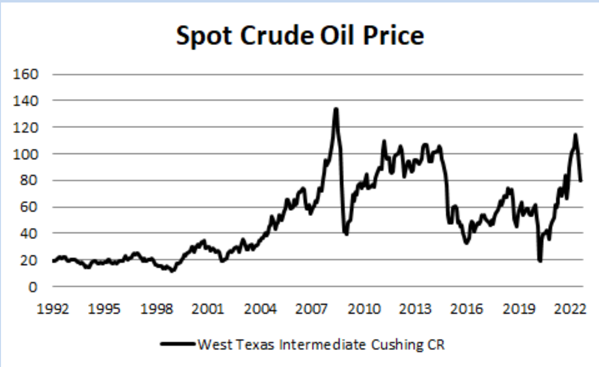


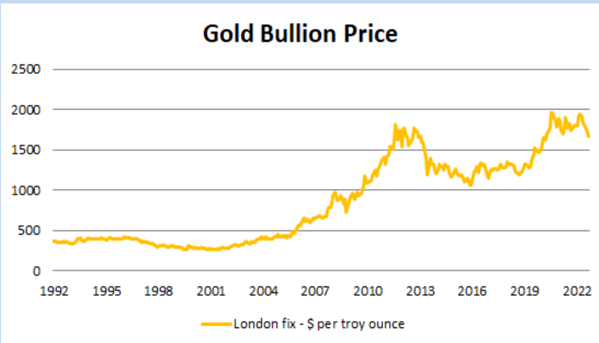
Source: Lipper for Investment Management

We forecast that the Bank of England will raise interest rates to a peak of 5% next year. There is a real risk of inflation becoming rooted in the UK economy and the Bank of England needs to be seen to be on top of policy. However, the Bank of England's greatest concern is to react to the inflationary push arising from the Government's major fiscal thrust, announced in the recent mini-Budget. We also expect the unemployment rate to remain low, wage growth to be high and the recent increases in prices to prove sticky. These will combine to keep inflation pressures elevated for a while and keep the Bank of England on a tightening tack.



Source: Lipper for Investment Management

Saudi Arabia and Russia have agreed production cuts that will likely underpin oil prices, which have drifted down from mid-year highs. The war in Ukraine remains a shadow over the market, as the West makes plans to reduce its dependence on Russian energy. This process is disrupting existing supply chains and prove costly. Meanwhile, there is little evidence that OPEC will increase supply in the short term. We do expect the price of oil to ease back into 2023, as recessionary forces respond to higher prices. But there remain major risks to the upside for energy prices, given the uncertainty surrounding the war in Ukraine.



Source: Lipper for Investment Management

As a real asset, gold is a safe haven in times of geopolitical uncertainty and inflation risk. Physical demand for gold has remained strong and investors are looking to this asset for portfolio insurance at a time when risk assets are suffering. In the near term, increasingly restrictive monetary policy will likely weigh on gold, but the mounting probability of economic pain should help to underpin prices. To gain conviction of material price upside, we need to see macro asset allocators pivoting back into gold, which could be driven by concerns over inflation becoming entrenched, escalating geopolitical tensions, the dollar rolling over from multi-decade highs or recession.

Note that where an MSCI Index has been used for illustration. This has been sourced with permission from MSCI Inc.

Quick facts

ISA Allowance 2022/2023	Stocks & Shares ISA Cash ISA Junior ISA	£20,000 £20,000 £9,000
Pension Allowance 2022/2023	The limit is the greater of £3,600 and 100% of salary, subject to the annual allowance of £40,000 (unless money has been accessed through flexi drawdown in which case the annual allowance is limited to £4,000).	

Tax facts

Income Tax	Personal Allowance 2022/2023	Up to £12,570
	Basic Rate @ 20%	£12,571 to £50,270
	Higher Rate @ 40%	£50,271 to £150,000
	Additional Rate @ 45%	Over £150,000
	Married couple's allowance: Older spouse born before 6 April 1935	Minimum £3,530 Maximum £9,125 Up to 10% of the appropriate Min/Max
Capital Gains Tax	Annual Exemption - Individuals	£12,300
	Basic Rate tax band (residential property)	18%
	Basic Rate tax band (other assets)	10%
	Higher Rate tax band (residential property)	28%
	Higher Rate tax band (other assets)	20%
	Business Asset Disposal Relief	10%
	Business Asset Disposal Relief limit of gains	£1,000,000
Inheritance Tax	Threshold up to £325,000	Nil
	Over £325,000	40%
Corporation Tax	Full Rate	19%
	Small Companies Rate (SCR)	19%

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