DART CAPITAL

Market Commentary

November 2021

It was a mixed month for equity markets, with the announcement of a new COVID variant, and tweak in monetary policy guidance by the US Federal Reserve, serving to push volatility higher later in the month whilst government bond yields declined. In this environment, the moves we made to portfolios over recent months have proven to be beneficial, with the addition of longer duration UK government bonds and an increase in overseas currency exposure, most notably in the Japanese Yen and US Dollar, helping to bolster portfolio resiliency.

COVID-19 Update

The discovery of the Omicron variant rocked markets late in the month, with initial reports that it had the potential to evade vaccines enough to cause a flight to safety across all major markets as markets quickly priced in a re-imposition of COVID restrictions across economies. However, the subsequent news flow on the new variant was more positive, with indications from southern Africa, where it is believed to have originated, suggesting that it is less virulent, albeit potentially more infectious, than previous variants with generally milder symptoms.

Whilst a tightening of restrictions is inevitable over the near-term, we believe that most western countries are in a far better position than they were heading into last winter. For instance, almost one-third of the UK population have now received three vaccine jabs (which likely provide some, albeit not full, protection from new variants), and there are now a number of treatments which are available for those patients which do require hospitalisation. Given the above, we're optimistic that hospitalisations should peak at lower levels than previous COVID waves.

UK

The upcoming meeting of the Bank of England's (BoE) Monetary Policy Committee is set to see a tight vote on whether to raise the base rate, with markets currently pricing in an evenly split between a rate rise of 15 basis points to 0.25%, and no change. The case for a rate rise was bolstered by labour market data released over the month which showed a record high number of job vacancies which quelled some concerns over the impact of the end of the furlough scheme, as well as inflation figures which were higher than most economists expected with year-on-year increase in the CPI (Consumer Price Index) of 4.2% in the 12 months to the end of October 2021. However, given concerns over the spread of the Omicron variant and potential restrictions over coming months, a rate rise is by no means a certainty.

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Even with the inflationary pressures, we believe that the BoE will take a cautious approach to raising borrowing costs, particularly given high household debt levels, with only small incremental increases over the next 12 months should the macroeconomic data allow it. Gilt yields moved down over the month as traders reduced the speed of expected rate hikes, with the yield on the 10 year Gilt declining 25 basis points to the end the month at 0.81%. Despite fairly weak sentiment towards UK equities, we saw strong corporate results from domestic businesses such as ITV and Marks & Spencer, the former of which generated record advertising revenue over the third quarter. MSCI UK All-Cap ended the month down 2.5% in capital return terms.

US

On the back of his reasonably positive outlook for the US economy and inflation which has proven to be more persistent than his committee had expected, Federal Reserve Chairman Jerome Powell pointed to a slightly quicker pace of monetary tightening in his comments at the end of November. Pressure to bring forward the end of the tapering process increased as inflation figures rose to 6.2% year-on-year in October 2021, according to figures released over the month. US equities remained close to all-time highs, although the gains were largely concentrated in small pockets of the market, with traders chasing exciting themes such as electric vehicles (a phenomenon which we discussed in more detail in our recent piece – link here). The S&P 500 ended the month down 0.8% in US Dollar terms.

Europe

Survey data indicated that the Eurozone economy lost some momentum over October 2021, with the prospect of rising COVID cases affecting consumer confidence and its subsequent knock-on effect on the services sector, whilst supply chain bottlenecks continued to impact the manufacturing sector. MSCI Europe ex-UK ended the month down 2.6% in local currency terms.

Asia

Chinese stocks remained weak over the month, as weaker than hoped for earnings releases from the country's technology champions, led by Alibaba and Tencent, served to mute market sentiment. Both companies are re-investing heavily in their businesses, partly in what's thought to be an attempt to under-state their profitability in the current stringent regulatory environment. MSCI China H ended the month down 3.9% in local currency terms.

Amidst the generally risk-off market mood, Japanese stocks also slipped, although the return was far stronger in sterling terms owing the strengthening of the Yen over the month. Despite this, the news on the ground in Japan was far more positive, with a strong corporate earnings releases and positive corporate news-flow. This is well demonstrated by three businesses: security firm Secom, construction business Hazama Ando, and property firm Toppan Forms, all of which delivered positive news over the month.

Hazama Ando – held in Buy List fund Jupiter Global Value - saw its shares rally 20% on the news that the management have committed to driving a 100% total return from the shares over the next two years. Management aim to achieve this through a combination of share buybacks and raising dividends, both of which are relatively easy to carry out given Hazama's extremely cash-rich balance sheet. The ambitiousness of management's targets is unusual for a Japanese company, however this attitude is changing, and will hopefully provide a lead for other companies to follow. Toppan Forms – held by Polar Capital Japan - received a bid from its parent company at a c.50% premium to its current share price, with the deal being the latest of a long-list of acquisition bids from parent companies seeking to incorporate their subsidiary businesses. Secom (a top 10 holding in the Polar fund) announced record third quarter profits, on the back of which management raised the dividend by 6% (to a level which well exceeds its 2019 pay-out). Despite this, Secom's shares are still well below their pre-COVID levels, which doesn't feel warranted given the continued growth of the business. MSCI Japan ended the month down 2.9% in Yen terms.