

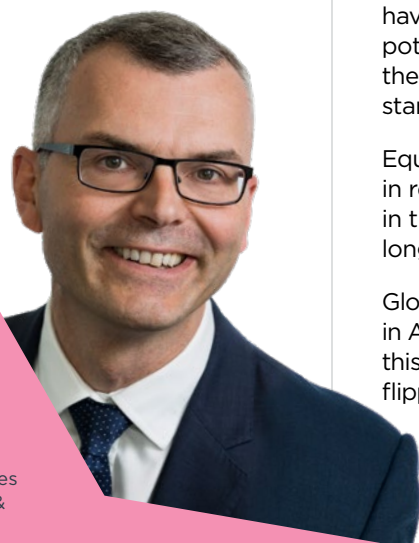
October
2023

XPS Investment News

Bringing you the latest investment news, insights and opinion
for charity and endowment clients

Quarter in brief

- The Bank of England ended its run of 14 consecutive rate rises in September as it voted to keep interest rates at 5.25% set in August
- Both the Bank of England and Federal Reserve warned that rates will remain 'higher for longer'
- High yield bonds were the best performer over the quarter despite rising default rates
- We expect most charities to have been broadly flat for the quarter, with the positive equity markets dampened by negative returns in other asset classes



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Corporate default rates are on the rise but credit markets remain sanguine

Falling inflation over the quarter may have signalled the near peak of interest rates around the globe but central bank policymakers have warned that interest rates are set to remain high for the foreseeable future.

The 12-month UK Consumer Prices Index (CPI) rate of inflation has fallen from 8.7% to 6.7% over the last 3 months. Prices are now rising at their slowest rate for almost 18 months. This was enough to prompt the Bank of England (BoE) to halt their run of 14 consecutive interest rate rises during September after most recently raising rates by 0.25% to 5.25% in August. However, the BoE did decide to increase the rate of quantitative tightening for the forthcoming year from £80bn to £100bn which would apply upwards pressure to gilt yields. Both the Governor of the BoE and the Chairman of the Federal Reserve (Fed) issued warnings that, despite hopes that interest rates had neared their peak, there is a long way to go in the fight against inflation before rates around the world would start to come down.

UK inflation exceeds the Euro area where the Harmonised Index of Consumer Prices fell to 4.3% in September and the US where CPI was 3.7% in August having risen slightly from its trough of 3.0% in June. Concerns over the potential for a recession brewing in the US continue to be hotly debated, with the US jobs market being a key focus. Weaker jobs data would lead to a softer stance by the Fed in relation to future rate rises.

Equity and corporate bond markets fared generally well over the third quarter in response to falling print inflation across major economies despite a setback in the final two weeks of the quarter resulting from central banks' "higher for longer" sentiment.

Global equities managed to deliver positive returns overall despite losing ground in August and September after a strong start to the quarter in July. However, this was primarily due to the depreciation of sterling which boosted returns and flipped them into positive territory. UK equities were broadly flat in the first two

months of the quarter but fared well in September to finish the period up, spurred on by encouraging inflation data and the Bank of England's surprise decision not to increase rates further in September.

Emerging market shares fared well, despite significant concerns over China, thanks to strong performance from tech stocks which make up a large proportion of emerging economies. China's property sector woes were compounded in September by the news that the chairman of Evergrande was under police surveillance and trading in its shares was suspended. Once the world's largest property developer, Evergrande is at the centre of the real estate crisis threatening to undermine the Chinese economy. Since it first defaulted on its debt in 2021 several other Chinese property developers have also struggled in the wake of the Chinese government's zero tolerance Covid approach and tight borrowing restrictions on property firms.

UK corporate bonds benefitted from a modest narrowing in spreads over the quarter, shaking off a slump in August. It remains uncertain how the expectation of

interest rates remaining higher for longer will impact companies looking to refinance their debt in the coming years. High yield bonds had a strong September to cap a stand-out quarter for an asset class that had struggled when interest rates have been rising given the increasing cost of financing putting pressure on underlying companies. However, most of this performance resulted from US dollar appreciation relative to sterling which fed into the global high yield index return.

The general stability of credit spreads seemingly stands at odds with observed default rates which have risen substantially for both high yield and investment grade corporate bonds this year and are expected to continue to rise in the coming months.

For charity clients, income levels were largely maintained although softness in capital values in property and bonds will have kept overall returns relatively flat for the quarter.

In case you missed it, [click here](#) to download a copy of our note on the recent changes to Charity Investment guidance in England & Wales.

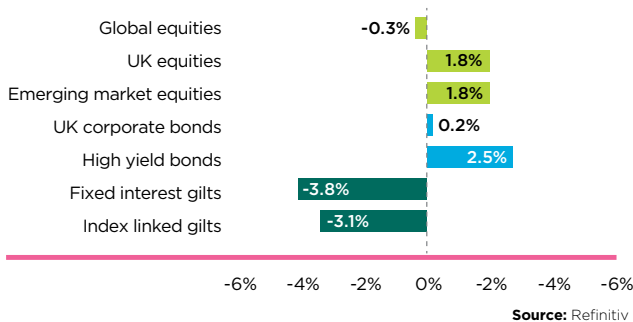


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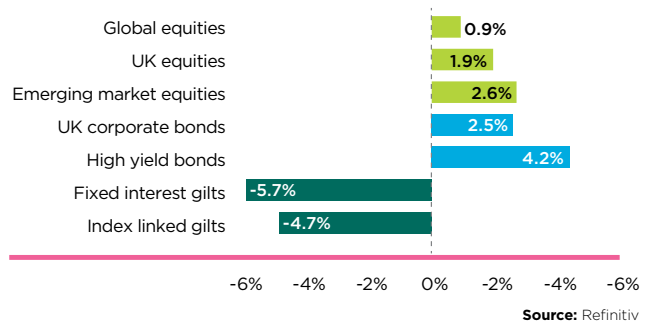
Market returns

High yield bonds were the strongest performer over September and over the quarter on the whole

1 month to 30 September 2023



3 months to 30 September 2023



XPS Investment asset class views

Asset class	Favourable	Neutral	Unfavourable	Movement
Developed equities		●		
Emerging market equities		●		
Investment grade corporate bonds		●		
High yield bonds		●		
Senior secured direct lending	●			
Balanced property (UK)		●		
Diversified private markets	●			
Private equity		●		
Cash	●			↑

Find out more

To discuss any of the issues covered in this edition, please get in touch with Alasdair Gill or Fraser Weir:



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