VT Tyndall Real Income Fund

Monthly Commentary | December 2022

TYNDALL

Review

After the extremely strong bounce in equity markets in November, December could not live up to expectations of a traditional ‘Santa’ rally and the iShares UK Equity Index tracker lost a modest -1.06% for the month.

The themes that have dominated investment thinking for most of 2022 remained at the front and centre of the debate during December, specifically the stickiness or otherwise of high levels of inflation, prospects for imminent recession, the outlook for further interest rate increases, the risks to corporate earnings forecasts, geopolitical upheaval and so on.

In the US the Federal Reserve increased interest rates by +0.5% at its latest meeting, down from previous increases of +0.75% at each of the last 4 meetings. Whilst this technically represents a slowing in pace of hiking, the Fed made it clear they remain extremely uncomfortable with the current level of inflation and have cautioned markets against expecting an easing of policy soon.

Elsewhere, the most significant news was almost certainly the complete U-turn in Covid policy in China. Following increasing (and rare) levels of social unrest in relation to nearly 3 years of strict lockdowns, the authorities appear to have abandoned the ‘zero Covid’ policy almost overnight, and now appear to be rapidly reopening their economy again. Whilst this should be good news for the global economy in due course, the transition will likely have some unforeseen consequences in the short term, given huge increases in Covid case numbers in China currently. Already, several countries are reintroducing testing requirements for travellers arriving from China.

Here in the UK, the primary focus has been on increasing levels of industrial unrest and subsequent strike activity across a whole swathe of public and private sector industries including the transport network, NHS, Royal Mail, Border Force and more. Given extremely high inflation levels and a ‘cost of living’ crisis this action is not entirely unsurprising and unfortunately will likely add to the difficulties currently facing the UK economy.

Fund performance / Activity

It was a solid month performance wise as the portfolio gained +0.66% (share class A GBP Net Accumulation), outperforming both the peer group average loss of -0.52% and the iShares UK Equity Index loss of -1.06%.

Outperformers came from a variety of different sectors of the market and included holdings such as Prudential, DS Smith, Ashmore, Keller, Vesuvius, WH Smith and Wickes. Having no exposure to oil giant Shell also proved beneficial as their share price relatively underperformed for the period. Detractors came from equally varied sources and included positions in EasyJet, Burberry, Ashtead, Bodycote, Howden Joinery and Dunelm.

December was a relatively quiet month for portfolio activity with no complete disposals or new additions during the month. We added modestly to existing positions in Vistry, Pagegroup and Hill & Smith funded via profit taking in Burberry and Melrose Industries.

Market Outlook

Just because we have reached the turn of a new year we do not believe, as tempting as it is, that this somehow necessitates a new outlook - it is, after all, just a date change. However, as we mentioned last month, several of the key 'trends' that have been dominating investor sentiment for the past year or so are showing tentative signs of changing. Specifically, inflation looks to be peaking alongside the US Dollar, Government bond yields and possibly even the oil price. Should these tentative signs develop into something more substantial, the investment landscape in 2023 may well look considerably different to the last 12 months.

At the risk of repetition, we still expect a degree of economic weakness in the near future, driven primarily by the lagged impact of the previously mentioned rise in interest rates, inflation, energy costs and the dollar. However, as we have argued many times, we expect that weakness to be less severe than many predict and our conviction in that view will likely increase if the trend reversals noted above continue to gain traction.

Additionally, from a global perspective the importance of the abandonment of the 'zero Covid' policy in China should probably not be underestimated. As noted earlier, there may well be some short-term implications of such a rapid policy change which may not be entirely favourable. However, from a medium-term perspective, having the second largest economy in the world learning to live with Covid and back to as fully an operational state as possible, will have important implications for global demand and supply across a whole host of economic sectors.

Market movements will likely remain volatile in the near term as investors wait for greater clarity regarding the outlook. Notwithstanding this uncertainty, we remain extremely enthusiastic for the upside potential for the portfolio, and we remain happy to purchase more shares, at attractive prices, in any further bouts of market weakness.

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Data source (unless otherwise stated): Bloomberg, FE Analytics

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