Albemarle
STREET PARTNERS

Monthly Commentary

November 2023

We have started our descent, but must tread carefully in this thin air.

Of those climbers who perish attempting to scale Mount Everest, some 53% reach the peak but die on the descent.

This unfortunate fact occurs for many reasons. Sometimes climbers literally give it all to reach the summit, leaving nothing for the way down, and of course the risk of falling only grows in a rapid descent, perhaps because the high altitude is proving so physically painful.

The problem is that a lot of Everest is so high that the lack of oxygen breaks down the body's internal processes. Time is your enemy at altitude, and it corrodes your body whether you have summited the peak or not.

This physical phenomenon is repeated in the economic world.

Here, the mountain we must all climb is the rising cost of money as interest rates go up. The more rates stay 'higher for longer', the longer companies and individuals must survive on thinner air.

Higher interest rates raise the risk of running out of the financial oxygen needed to finance company or personal borrowing, and discourage us from taking risks with expansion.

We could easily fall into the trap of thinking that because it seems interest rates may well now have peaked that we are out of danger. Not so. For the next year the key question is: can the economy survive the high-altitude portion of the descent? Because it is here rather than on the way up that the economy most often experiences a fall.

Our view remains that despite a resilient economy so far, particularly in the United States, we will see growth slow, and some real economic pain will be felt by households in the months ahead.

Yet we should not be discouraged as investors. The past two years have been challenging because in a rising interest rate environment both shares and bonds fall at the same time – a rare and unsettling experience. However, as interest rates begin to fall because the economy is slowing down, we can hope to see a rally in bonds whilst also expecting to see strong performance from high-quality equities.

The past month has brought with it more evidence that central banks will have a lot of patience with the economic data before they risk any further interest rate rises, and it is our firm view that in general the direction of rates is now down. Falling rates mean falling bond yields and rising bond prices.

Our portfolios stand ready to harness this opportunity, but we are not impatient. We are resisting the urge to rotate into too high-risk assets at this time, knowing that whilst we remain in the high-altitude zone our footsteps must be carefully paced. Our first step as we begin to descend will be to buy higher risk bonds that can benefit to a greater extent. We are also going to increase our exposure very gradually to active equity funds in areas such as Japan and Asia which look particularly well-placed to benefit from the recovery. Our final step will be to own higher risk shares such as smaller companies. But rest assured we will be waiting until the air is a little thicker before making such a move.

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