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Just like the ribbon tied to a piece of rope and pulled by strongly competing forces, financial markets have shifted this way and that over April, but to nothing like the exaggerated degree witnessed over the first quarter of the year. Indeed, the UK stock and gilt-edged markets have displayed commendable resilience through a series of risk events and sometimes severe headwinds. The UK economy has matched that of other developed economies elsewhere, steadfastly refusing to wilt despite the twin pressures of stubbornly high inflation and eleven consecutive rounds of higher interest rates. The pound, too, has stabilised on the foreign exchanges as global investors have responded favourably to improved economic stewardship after a volatile autumn.

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As April came to an end, the world's most important central banks took the decision to reverse the provision of highly market-supportive emergency liquidity, thought necessary to provide stability in the wake of March's banking sector turmoil, from daily back to weekly operations. In so doing they have sent a clear signal that despite lingering fragility, especially in the US regional banking sector, the worst of the episode has been navigated successfully. However, it is the banking sector that serves as the interface between central bank monetary policy and the real economy and the lingering consequence

of events over March is thought likely to be a further tightening in credit availability. Thus, it is still too early to say that the pressure on activity, and by extension the financial markets, has eased.

On the other end of the rope, persistent inflationary pressures are serving to maintain the tension. Driven in no small measure by food prices at their highest level since 1977 and showing few signs of abating, the UK's inflation experience is proving more sustained than elsewhere, including in both Europe and the United States despite steadily receding energy prices after last year's spike in the immediate aftermath of Russia's invasion of Ukraine.

Why it should be that UK inflation is proving so much more enduring is the subject of much conjecture. One justification might lie in the post-pandemic jump in wholesale energy prices, exaggerated by the fallout from the war in Ukraine which was far more apparent in the UK and Europe than in the US. Beyond that, some European governments were quicker to cap prices than the UK. The regulator's price mechanism is serving to ensure that energy prices are now falling more slowly at home than elsewhere. Another justification might lie in the stickiness of the Bank of England's closely watched underlying price pressures, the consequence of stronger wage growth and a more persistent shortfall in the supply of labour than seen across other developed economies. Despite the confidence that these price pressures will gradually abate, the Bank of England has surely got more work to do if its aspirational medium-term 2% target is to be achieved and if that means forcing a recession then, think interest rate-setters, so be it.

Broadly diversified investment portfolios do not, of course, exist cocooned in a domestic vacuum and events in the wider world matter to just as great an extent as those at home. Beyond lingering concerns regarding the health of the banking

sector, the United States has plunged once again into a debt ceiling crisis. We have been here before of course and financial markets have dusted off the “playbook” last used a decade ago. So severe would the consequences of a US default be, even if technical, that some form of 11<sup>th</sup>-hour compromise is still the most likely outcome. But markets are not complacent given the highly adversarial nature of US politics, a fact reflected in a notable adjustment in short-dated Treasury bill pricing.

Not to be overlooked, geopolitical events are moving at warp speed. A Chinese economic rebound, the inevitable consequence of the lifting of highly restrictive “zero Covid” policies, has emboldened Beijing increasingly to confront the United States and its allies both militarily in Taiwanese waters and economically, a confrontation to which the West has responded robustly. Financial markets have historically struggled to price geopolitical developments, but when those developments enter the economic sphere and the world

appears on the brink of a profound fracturing, these issues are harder to ignore. The cleaving of the world into two distinct economic blocks would pose a new set of challenges and add a new dimension to financial asset pricing.

Yet for all these pressures financial markets have proved resilient. That this resilience will be challenged is an inevitable feature of the landscape and calibrating risk is just as significant a part of the investment process as assessing future rewards. Financial markets inhabit the future as much as they are informed by the present. Whilst the immediate outlook is opaque, the combination of slower growth and ebbing inflation should result in lower interest rates in time, a fact not lost on the bond market. Meanwhile, history confirms that whilst corporate profit and loss will likely reflect tough operating conditions in the near term, it recovers fast once the bottom has been reached. It is thus understandable that whilst the result of this show of strength contest is hard to predict, investors are right to hold the line.

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