Where evolution meets tradition

A Month in the Markets

MARCH 2022

In this latest edition our Head of Systematic Research for TAA and Alpha, Stefano Amato, looks at how the increased geopolitical tensions have impacted investment markets alongside focus primarily on inflation and rising interest rates.

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Market Overview

Global stock markets as a whole declined in February,[1] continuing the increasing volatility experienced in January[2]. We had already seen investment market focus being driven primarily by two key risks: inflation and rising interest rates, but Russia's invasion of Ukraine has not only added a third geopolitical risk, in our opinion it is also likely to put pressure on both of these risks through rising commodity prices.

At the beginning of the month, the prospect of persistently high inflation and tighter monetary policy from the US Federal Reserve (Fed) were already taking their toll on stock markets.[1] They were sent spiralling when Russia followed through with its invasion of Ukraine.[1] Resulting in major global stock markets falling in February, with Europe and China seeing the sharpest declines.[1] This was followed by falls in emerging markets, the broad Asia Pacific region and Japan.[1] Russia's stock market was one of the worst performers in February, falling by more than 35% over the month.[1]

UK and Europe

For the most part, the economic situation in the UK and Europe improved in February as disruptions related to the Omicron variant of COVID-19 began to ease.

In the UK, activity in the private sector accelerated at its fastest pace for eight months.[3] On the European continent, the services sector - which includes restaurants and leisure companies – rebounded, while the manufacturing sector

[1] Refinitiv Datastream, 28/02/2022
[2] FE Fund Info, 31/01/2022
[3] Markit Economics, 21/02/2022

improved[4]. Nevertheless, inflation remained an ever-present concern, with consumer price inflation running at 5.5% in the UK[5] and 5.1% in the eurozone[6].

At the beginning of February, the Bank of England (BoE) sought to temper higher inflation by raising its benchmark interest rate from 0.25% to 0.5%.[7] It was the first time since 2004 that the BoE raised interest rates at consecutive meetings.[8] This raised expectations that it paves the way for a further increase in the coming months.[9]

US

Much like the UK and Europe, business activity rebounded in the US as COVID-19 disruptions began to ease. The US economy was in fairly good shape in February, with increased activity in the services and manufacturing sectors[10]. Throughout February, companies announced corporate earnings reports for the fourth quarter of 2021. While many companies beat estimates, they were not as strong as previously expected.[11] Inflation continued to be a focal point for investors throughout the month. With consumer price inflation hitting 7.5%[12], it is broadly expected that the Fed is readying to raise interest rates in the coming months.

Global

While high inflation and imminent interest rate hikes were omnipresent concerns for investors in February, these issues were mostly overshadowed when Russia invaded Ukraine. The move sent stock markets tumbling and caused the price of safer-haven assets, such as gold, to spike. The price of gold briefly reached more than $1,970 per troy ounce on the day of the invasion. It subsequently fell back to a level around $1,887 per troy ounce.[13] Oil prices also surged, on fears that countries reliant on Russian oil and gas would face supply issues. The price of Brent Crude broke above the US $100 per barrel barrier for the first time since 2014.[14]

The European Union, along with the North Atlantic Treaty Organisation (NATO) and other key allies in the West, responded to Russia's move by announcing a series of economic sanctions[15] placed on the Russian government, government officials and private citizens. Along with this, several Russian banks were cut off from the SWIFT messaging system[16]. The US and UK also cut off Russia's major banks, as well as its central bank, from dollar and sterling clearing.[17] The asset management industry is working together with the UK Government to support their efforts, whilst collectively working to put in place measures to mitigate impacts for investors.

Outlook

Given the sudden resurgence of geopolitical tensions and the uncertainties that this has created, we have a cautious view of the months ahead. COVID-19 is no longer the primary risk on the horizon, having been replaced by inflation, rising interest rates and the Ukraine crisis.

We expect that interest rates around the world will continue to move higher in 2022, which will have a short-term impact on stock markets. Rising rates have already taken the wind out of the sails of high-growth areas of the market, such as technology companies,[1] and we see this continuing in the months ahead. Overall, we expect to see a higher degree of market volatility in the coming weeks and months. We also anticipate heightened political tensions as governments around the world seek an end to the aggressions.

Considering this investment landscape, we believe our portfolios are currently well positioned and we will continue to monitor the landscape and how these major risks progress, and will make any adjustments as necessary.

All data as at 28 Feburary 2022.

[4] Markit Economics, 21/02/2022
[5] Office for National Statistics, 16/02/2022
[6] Eurostat, 2/03/2022
[7] Market Watch, 3/02/2022
[8] Market Watch, 3/02/2022
[9] Reuters, 23/02/2022
[10] Markit Economics, 22/02/2022
[11] CNBC, 3/02/2022
[12] Trading Economics, 28/02/2022
[13] Reuters, 25/02/2022
[14] CNBC, 23/02/2022
[15] BBC News, 27/02/2022
[16] Swift, 1/03/2022
[17] City A.M. 28/02/2022
[18] Reuters, 31/12/2021