Cantab
ASSET MANAGEMENT

Investment Comment

01 April 2022

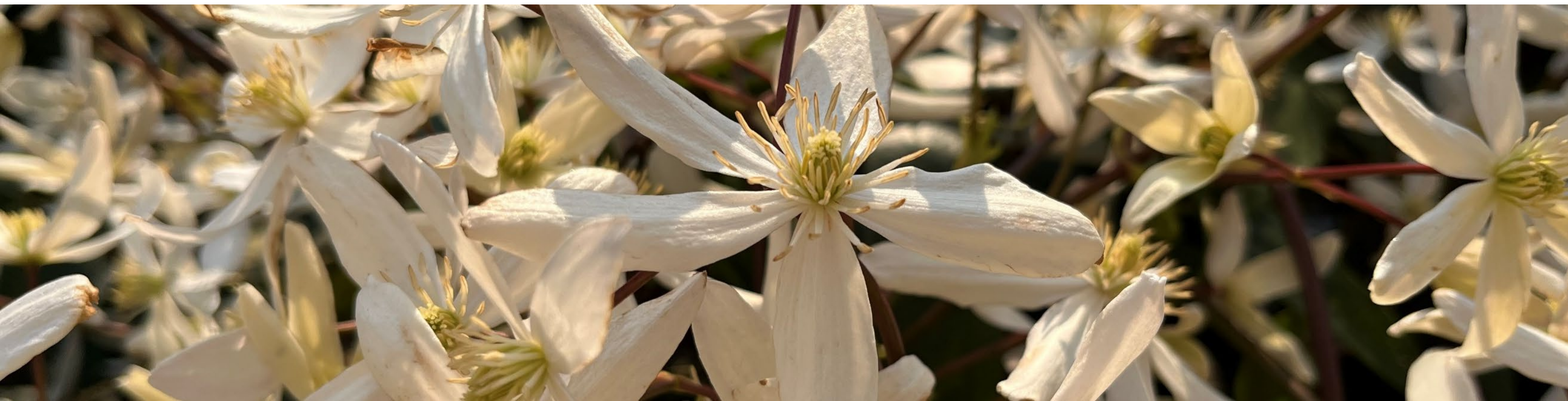
Sterling denominated returns of major indices	Q1 2022 %	Year 2021 %	Year 2020 %	Year 2019 %	Year 2018 %	Year 2017 %
Equities						
UK	1.7	18.7	-11.8	18.4	-9.8	13.0
World (ex UK)	-2.9	19.6	14.0	22.0	-3.5	13.3
Emerging Markets	-4.3	-1.6	14.7	13.9	-9.3	25.4
Fixed Interest						
Overseas Bonds (unhedged)	-3.9	-4.4	5.6	2.7	5.1	-2.3
Corporate Bonds	-6.2	-3.0	8.0	9.5	-1.6	4.4
Property	-1.9	20.8	-9.5	22.4	-7.8	8.1
Cash	0.0	0.0	0.0	0.0	0.0	0.0

Source: MSCI UK IMI, All Country World ex UK, Emerging Markets, UK IMI Liquid Real Estate, Cash Equivalent (GBP 1W LIBOR -1%); BofA ML: Global Broad Market+, Sterling Non-Gilts. Total Return, Sterling adjusted.

When a human crisis with terrifying consequences for millions of people is ongoing, commenting on the effect on markets can feel uncaring or even heartless. Like all, we are shocked and saddened by the Russia-Ukraine war and hope for a just peace as soon as possible. This Investment Comment will attempt to objectively consider the impact of the war on capital markets, whilst also assessing the other principal drivers of market movements over the first quarter of 2022. Commodity prices surged whilst fixed income sold off and global equities, as measured by the MSCI ACWI, fell by 2.64% over the period.

The MSCI USA Index posted a quarterly loss of 2.59%. Hawkish updates from the Federal Reserve in January triggered volatility in bond and equity markets, with both derivatives trading and the CBOE Volatility Index ticking up in the face of near two-year high treasury yields. Volatility remained elevated through February and March as the Russia-Ukraine tension escalated into a full-scale invasion, clouding global growth prospects and triggering the US to impose wide-ranging sanctions on Russia. The US also banned purchases of Russian oil, which will increase pressure on the 40-year high US inflation rate of 7.9%. To offset this import ban, President Biden announced an historic release of 180mn barrels of oil from the US Strategic Petroleum Reserve. Biden is hoping that this will soften soaring US energy prices, which increased 25.6% year on year in February. Towards the quarter-end, the Federal Reserve announced a single interest rate hike and US equities rallied following peace negotiations in Europe.

The MSCI Asia Pacific ex Japan Index fell 2.98% over the quarter, driven by Chinese equities. Covid-19 is still rife in Asia and China's 'zero-Covid' strategy, notably the two-stage 50-million-person lockdown in Shanghai, continues to weigh on growth in the region. China's Composite PMI in February indicated only marginal expansion whilst consumer prices rose just 0.9%, bucking the strong global demand and inflation trend. Chinese Premier of the State Council Li Keqiang's gross domestic product (GDP) growth target of 5.5% for 2022 was the lowest in 30 years, and it is likely that the People's Bank of China will continue easing and credit expansion to achieve this target.



The MSCI Europe ex UK Index posted a substantial quarterly loss of 7.40%, recovering somewhat from a drawdown exceeding 17% over the first 8 weeks of the year. Inflationary pressure and geopolitical tensions weighed on European equities even before Russia officially invaded Ukraine on the 24 February 2022. With Russian gas accounting for c.40% of the European Union's (EU) gas imports, the outbreak of conflict initially sent gas prices spiralling upwards by almost 70%. With such extreme energy price pressure on the already record high inflation rate of 5.9%, the European Central Bank announced a quicker scaling back of its stimulus programme than expected. Europe lags other major equity markets year to date, but rebounded strongly at the quarter-end following peace talks in Istanbul and the announcement of Russia 'dramatically' scaling back its military activities around Kyiv. The Ukrainian President, Volodymyr Zelensky, warned that Ukraine must remain vigilant and EU sanctions persist.

The United Kingdom was the only major region that posted a quarterly gain for equities, with the MSCI UK Index rising 1.67%. The 30-year high inflation rate of 6.2% prompted the Bank of England to implement its first successive rate hikes since 2004, lifting the base rate to 0.75%. Despite this monetary squeeze, UK equities have held up relatively well, reflecting the index's lower valuations and greater cyclical sector exposure, particularly to energy and mining stocks. UK house price growth is at a 17-year high, GDP data is strong and unemployment is low, but the Russia-Ukraine war of course creates uncertainty. UK sanctions have so far targeted Russian oligarchs, state media, propagandists, and military figures. Against this backdrop of a European war, UK Chancellor Rishi Sunak's quarter-end Spring Statement was a low-profile event, as he mostly kept to previously announced plans.

The MSCI Japan Index posted a quarterly loss of 3.92%. A sixth Covid wave forced eighteen prefectures, including Tokyo, Osaka and Aichi, into a quasi-state of emergency towards the end of January as daily cases approached 100,000. Prime Minister Fumio Kishida closed the country's borders for most of the quarter, with the manufacturing and service sectors suffering as a result. PMIs did pick up in March amid declining Covid cases and easing restrictions, however, wage growth remains lower than the 3% sought by Kishida. With respect to the war in Europe, Japan is coordinating with the G7 nations to impose sanctions on Russia. The quarter-end was marked by the Yen dropping to a seven-year low against the dollar as the Bank of Japan underscored its commitment to economic stimulus, holding rates at -0.5%. This has stoked speculation that the Central Bank could intervene to prop up the currency for the first time since 1998.

The MSCI Emerging Markets Index lost a significant 4.30% over the quarter, and the European war has created a fragmented outlook for developing economies. Eastern Europe will likely suffer most due to soaring energy prices, the direct impact on trade and the possibility of European economic deterioration, whilst net commodity exporters in the Middle East and Latin America may benefit from spiking commodity prices. Also at play are rising US treasury yields and a strengthening US dollar, making it more difficult for developing economies to attract foreign investment and service their pandemic-related dollar-denominated debt. Regulatory clarity and an economic recovery in China, as well as a resolution to the Russia-Ukraine war, could trigger a pick-up in Emerging Market equities in 2022, but the outlook is clouded.

As we move into the second quarter of the year, markets have recovered somewhat from recent lows. However, volatility remains elevated, macroeconomic challenges are significant and the global growth outlook uncertain. The principal drivers of capital markets over the next three months are likely to be developments in the Russia-Ukraine war, global inflationary pressure and the rate at which these factors catalyse major central banks' tightening of monetary policy. Now, as ever, the importance of remaining focused on long-term objectives is paramount.

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