RICHMOND HOUSE
INVESTMENT MANAGEMENT

# Investment commentary

**February 2022**

## Market overview

February was another challenging month for markets with developed market equities falling by 2.5% and emerging markets by 3%. Investor concerns were initially centred on the continued increase in inflation and how this might put further pressure on central banks to increase rates. The focus then turned to the escalation of the conflict in Ukraine. In addition to the destabilising effect of the conflict itself, the likely disruption to Russia's substantial commodity exports pushed the oil price above $100 a barrel and gas prices up a further 15% over the month. The impact was also felt in other areas of the commodity market where Russia is a key global supplier, notably metals and wheat, and this upward surge in commodity prices further fuelled inflationary concerns. A string of global sanctions are now serving to essentially cut Russia out of the world's financial system.

Growth stocks again declined more than their value counterparts while, in terms of regions, European equities fell most given the European Union's relatively high dependence on Russian oil (c.25% of total imports) and gas (c.40% of total imports). The UK market proved more resilient, aided by its relatively high exposure to commodities.

The current economic and geopolitical backdrop has left the outlook uncertain as to whether central banks might focus on easing policy to alleviate potential pressure on economic growth or tightening policy to try to combat inflation. Global bonds declined over 1% during the month and many now expect six rate rises in the US this year given inflation levels and the strength of the labour market. The 10-year Treasury yield reached 2% in the month before falling back to 1.8% while the 10-year Gilt yield rose from 1.3% to 1.4%.

The Bank of England raised interest rates by 25 basis points at the beginning of the month and UK rates are now expected to end the year above 1.5%. Given the expected hikes in energy bills coming in April most anticipate inflation in the UK to rise further from the current 5.5%.

## Strategy positioning

While all the uncertainty in terms of inflation and global growth might continue to impact the pricing of risk assets in the near term, we believe this commodity-induced inflation spike could be relatively short lived, as it has been in various previous energy-linked conflicts. Central banks will be mindful of this and therefore the chances that monetary policy will drift significantly off the expected path are relatively small at this stage. Given the rapidly evolving nature of the conflict in Ukraine, and the dramatic set of economic sanctions arising from it, we will need to keep reviewing this thesis carefully. However, we continue to favour a full exposure to equities in each of the strategies as earnings announcements remain positive, valuations do not look overly demanding and investor appetite is likely to return, particularly given the natural inflation hedge that equities provide.

Our bond positioning remains defensive and has limited exposure to the movement in interest rates, focusing on inflation-linked and absolute return focused vehicles. Similarly, our alternatives funds are non-directional and are targeting uncorrelated returns through market neutral, relative value strategies. These funds are proving their worth so far this year in the face of both equities and bonds losing value.

## Risk warnings