Hoyl Investment Committee

March 2022 Newsletter

The Russian invasion of Ukraine

Financial markets have endured a rough start to the year due to both rising inflation and interest rates. However, in recent weeks what many feared may happen came true with Russian President Vladimir Putin's full scale military invasion of Ukraine.

Clearly the most important concern with the continuing loss of life and huge number being forced to flee Ukraine is the human cost, rather than anything connected to investment markets. However, as the conflict continues it brings increasingly unpredictable consequences beyond Ukraine's borders, so it's understandable this geopolitical uncertainty will spark many questions.

President Putin's actions have caused untold misery to millions in Ukraine, while sanctions implemented by western nations since 3rd March, including freezing assets of the Russian Central Bank, removing selected banks from the Swift messaging system which enables the smooth transfer of money across borders, and the US, EU and UK banning individuals and businesses from dealing with the Russian Central Bank, are now causing financial hardship for the people of Russia.

Germany's recent decision to halt certification of the Nord Stream2 gas pipeline, which was completed in September last year, means it's now unable to begin commercial operations. This brings increasing pressure to secure alternative energy sources.

The sanctions imposed until now are designed to minimise the impact on energy supply, but energy prices will remain highly sensitive to further developments.

Along with government sanctions, various companies and organisations are severing their links with Russia.

Russia accounts for 13% of global oil production and 17% of global natural gas production. Given Russia's influence on global commodity production, escalating tensions have led to a sharp rise in energy prices, metals and agricultural commodities.

The European Union (EU), has a reliance on Russian energy, with around 25% of EU crude oil imports and 40% of natural gas imports currently coming from Russia. This means any disruption to supply could be significant.

There is limited opportunity for the EU to offset any disruption in supply by hastening imports from other sources, and recent volatility in the price of crude oil and gas have been intensified due to EU energy stocks having started the winter at depleted levels after an unusually cold autumn.

With ambitions to reach net zero emissions already putting pressure on European governments, these new concerns over energy security only add further pressure to transition away from imported fossil fuels towards domestically generated renewables.

We're all deeply saddened by the current situation in Ukraine. As with any conflict, the human toll is devastating and as the profoundly upsetting events continue to unfold, our thoughts are with the people of Ukraine and all those with family affected.

Looking at the financial markets

Prior to the Russian / Ukraine invasion, 2022 started with more poor inflation figures and multiple comments from the Federal Reserve on raising interest rates and the Bank of England raising interest rates in both December 2021 and February 2022.

In January, the S&P 500 had the poorest monthly performance since March 2020 and the poorest January performance since 2009. The NASDAQ underperformed the S&P 500 as the technology sector came under intense pressure due to rise in yields. The non-profitable technology stocks saw the biggest decline but this then affected the bigger (profitable) technology companies.

As public companies released their earnings in early to mid-January, companies missing their expectations have seen some sharp falls. For example, on 3 February 2022 shares of Facebook parent Meta plunged 26.4% (never before seen on Wall Street) on news that growth seems to have hit a ceiling point. This news wiped out more than $322 billion off Meta's market value and the S&P 500 fell 2.4%. A warning from Netflix of slowing subscriber growth saw their share price drop nearly 25% on the 21st January.

Fixed income (government gilts and corporate bonds) has also suffered during 2021 and of late, due to high inflation and rising interest rates.

Needless to say that the conflict in Ukraine war has only added to the volatility in the markets.

Your investment portfolio

As a loyal and valued client, who's placed your trust in us to look after your investments, it's only natural that you'll be concerned about how stock markets will react to current events and what it will mean for your investment portfolio.

We first need to remember that while the fall seen in the last few weeks isn't a comfortable experience, it is traditionally part of the journey for any long term investment.

Human nature tends to be risk averse, so any short-term dent in our investment portfolio can be a real concern. However, history has shown that attempting to sell assets in a panic not only leads to crystallising losses on exit, but also a risk of missing the right time to re-invest later on. Financial markets do fall, but will also recover. It's the time invested in the markets, rather than the timing of the markets, that will lead to the most positive return over time.

We expect to see more volatility within the UK and international stock markets going forward, and this will of course potentially affect your investment.

However, one of the advantages of investing through Hoyl's Model Portfolio investment strategies is the spread of risk across different asset classes such as cash, fixed interest, property and equities both in the UK and internationally, which is known as 'diversification'.

This is an important factor when investing to reach your long term financial goals, with one of the key benefits being how it helps to minimise the risk to the money you have invested in your portfolio. To explain this further, if one of your investment funds were to perform poorly over a certain length of time, your other investment funds may well perform better over that same time. This therefore reduces the potential losses to your investment, compared to if you simply had all your money invested in only the poorly performing investment fund.

We assure you our Investment Committee continue to monitor the situation, and will make any recommendations they feel are necessary.

United Kingdom

The Omicron variant of Covid-19 has affected the UK economy, especially in December when retail sales fell 3.7%. While conditions for consumers are likely to remain challenging over the coming months, with energy bills and taxes rising, a waning Omicron variant should be encouraging for overall economic activity.

However, while UK equities ended January slightly lower, they did outperform other developed economies due to higher exposure to certain industries which have had a recent uplift in performance, such as commodity stocks, financials, and low weighting to expensive technology stocks.

The Bank of England (BOE) voted to raise its bank rate by 0.25% to 0.50% at its 3 February meeting. The BOE's Monetary Policy Committee also voted to begin reducing the stock of UK government bond purchases and corporate bonds, financed by the issuance of central bank reserves, by ceasing to reinvest maturing assets, to be completed no earlier than towards the end of 2023.

We expect further rate rises during 2022, with a further possible increase following their next meeting on 17 March.

Fixed income investments, such as corporate bonds, are particularly sensitive to rising interest rates, as when rates go up the value of bonds will generally fall.

Headline inflation has increased to a 30 year high of 5.5% in the 12 months to January 2022, up from 5.4% in December 2021. The rising cost of utilities, such as electricity, gas and liquid fuels, has reflected a global surge in energy prices, with oil and gas prices especially driving these gains. We expect headline inflation to remain above 3.5% in 2022.

UK gross domestic product (GDP) is estimated to have increased by 1.0% in Quarter 4 (Oct to Dec) 2021. Compared with the same quarter a year ago, GDP has increased by 6.5%. Following the large 9.4% fall in 2020 because of the initial impact of the pandemic and public health restrictions, UK GDP saw an annual rise of 7.5% in 2021.

With rising interest rates, higher energy costs and inflation forecast to rise further it's predicted that UK GDP will be around 4% for 2022 from around 5%.

The UK unemployment rate remained steady at 4.1% in the 3 months to the end of December 2021 and just 0.1% above its pre-pandemic level. The average weekly earnings, which includes bonuses, grew at an annual pace of 4.3% over the same period, indicative of a tight jobs market.

United States

The US has experienced the fastest ever recovery since the recession in 2020.

While the discovery of the Omicron variant of Covid-19 shook markets late in 2021, there are expectations that the US economy will significantly outgrow most other developed economies in 2022.

Nonetheless, US Equities have declined sharply so far in 2022. The S&P 500 indices has declined about 10% in 2022, and the NASDAQ has lost about 13%. Investors negatively focussed on technology stocks in particular the more speculative companies.

The market reaction was mainly due to the uncertainty around the Federal Reserve (Fed) timeline for interest rate increases, talks on quantitative tightening and the outlook that inflation will continue to rise in 2022 was enough to spook the markets.

On 26 January the Fed voted to leave the target range unchanged at 0% to 0.25% but signalled an end to its pandemic asset purchase program in March (approving a final $20 billion in Treasury and $10 billion in mortgage-backed securities).

The Fed is expected to raise interest rates several times this year in its efforts to restrain surging inflation, beginning with its meeting to be held on 15-16 March.

However, full year 2022 growth forecasts (GDP) for the United States have been predicted to be around 3.5%. Growth is still predicted to be strong even after factoring in a series of rate rises. GDP for 2021 grew by 5.7%, compared with a contraction of 3.4% in 2020.

The annual inflation rate in the US surged to 7.5% in January, the largest such increase in 40 years. Inflationary pressure was broad based across goods and services.

Companies continue to face a variety of supply constraints, ranging from input materials, transportation and labour, and we foresee inflation peaking in the first half of 2022.

The US jobs market continues to be strong in January, with an unemployment rate of 4.0%, strong wage growth and 10.6 million job openings, which is close to full employment, and we believe the unemployment rate will continue to fall during 2022.

Europe

European equities are down as higher inflation, Covid related restrictions, the US Fed's monetary tightening, and tensions with Russia weighed on European stocks.

The European Central Bank (ECB) left its main deposit rate unchanged at negative 0.50% at its 3rd February meeting. However, following the announcement in a subsequent news conference, the ECB President Christine Lagarde did not rule out a 2022 rate hike, as she had on previous occasions.

On 16th December 2021 the ECB Governing Council decided to discontinue net asset purchases under the Pandemic Emergency Purchase Program at the end of March 2022. This therefore prepared the way for a rate increase in the second half of 2022.

The Eurozone GDP progressed to a record 5.2%, slightly above ECB estimates of 5.1% and following a 6.4% contraction in 2020. In 2022, the central bank expects the economy to expand by 4.2% while the European Commission sees it rising 4%.

Headline inflation in the euro area was confirmed at 5.1% in January 2022, the highest level since the euro's 1999 introduction.

Unemployment in the euro area continued its slow but steady decline, falling to 7.0% on a seasonally adjusted basis in December. Unemployment in the euro area is now below pre-pandemic lows. However, with slack in the labour market still evident, underemployment remains higher than it was before the pandemic. We anticipate the labour market will strengthen and that there will be wage pressure increases in the months ahead, although this will vary by country.

Emerging Markets

Emerging markets had a tough 2021, due to weakness in China and a deep downturn in construction and consumer spending.

Russian equities have fallen sharply on increasing geopolitical tensions following the Russian invasion of Ukraine, while energy prices rose on the prospect of lower Russian oil and gas supply following new western sanctions.

Central bank's monetary policy tightening to contain inflation is likely to continue to constrain growth in emerging markets during 2022.

We expect emerging markets growth in 2022 to be around 5.5%, down from around 7% in 2021.

Latin America and Central Europe could also face stagflationary scenarios, with high inflation and low growth.

Japan

Japanese stocks fell in January, amid rising concerns over a tighter monetary policy in the US and a sudden increase in the number of domestic new cases of Covid.

At the start of the year new Covid infections were less than a 1,000. However, by early February new Covid infections have increased to a record high of 80,000.

In response to this, the government expanded its state of emergency measures to 34 prefectures, including Tokyo. This then led to concerns over a slowdown in the economy.

However, despite the ongoing Covid-19 pandemic we remain optimistic on the outlook for Japan in 2022.

China

China's economy continues to struggle as global supply chains are being disrupted by its stringent zero Covid-19 policy.

Following the disruption caused by Covid the interventions from Beijing in relation to their goals of Common Prosperity have seen some sectors being de-stabilized.

China has had to contend with a slowdown in its property market, along with an overall slowdown in its rate of economic growth.

The China Evergrande Group, which is the second largest property developer in China by sales, has also been a drag on China's growth as the company defaulted on its debts. China's government is now considering a proposal to dismantle the company by selling the majority of its assets.

In January the People's Bank of China unexpectedly cut key interest rates for the first time in almost 2 years.

In contrast, China's exports rose by 20.9% year-on-year in December, ahead of the 18.2% consensus expectation.

China's economic and regulatory challenges have led to a significant sell-off in equities. In the past 12 months, Chinese equities were one of the worst performing sectors in the emerging markets.

We expect GDP Growth in China to be around 5% in 2022. We anticipate a weaker first quarter growth followed by a rebound in the second quarter due to an expected easing in monetary, fiscal and regulatory policies.

Hoyl Model Portfolios

We always keep a degree of caution when selecting funds for our model portfolios and only focus on investing in funds we believe to be the 'best of breed', which includes companies with strong balance sheets, which we believe are better positioned to cope in a challenging economic environment.

Historic Performance Comparison

Simply click on the link below to see performance comparison charts for our latest model portfolio investment strategies for the last 12 months and 3 years.

https://www.hoyl.co.uk/investment-committee-newsletter

Please remember that while these charts don't take the effect of plan charges into consideration, they clearly show the importance of remaining invested when there's a downturn in investment conditions.

Past performance is of course no guarantee as to what may happen in the future.

Thank you

Thank you for the trust you continue to place in us to help look after your investments and we trust you find our regular Newsletters interesting.

Please get in touch with your adviser if you should have any questions, would like to know more about anything we've mentioned, or need to discuss any financial matter.

We're always here to help and advise you, and please remember that you should always speak to your adviser if either your personal or financial situation changes.

Thank you again, and we wish you all the best for the months ahead.

You can contact your dedicated adviser on 01263 513016

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