NATIXIS INVESTMENT MANAGERS

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Market Review

Global Market Strategy @ Natixis Investment Managers Solutions

Economic & Political News

During the first half of the month, expectations for rate hikes across major central banks increased significantly as broad based inflation pressures continued to build. As such markets participants, started to worry about how much of an economic slowdown policymakers would have to manufacture in order to get inflation back again. Later in the month, Russia invaded Ukraine, triggering a significant humanitarian crisis and weighting on equites, particularly European's given the region's heavy dependency on Russian energy imports. As expected, the prices of the commodity complex rallied across the board, which, at least in the short term, has tilted higher inflation risk to the upside.

Numerous Western countries have rolled out harsh sanctions against Russia. While they vary across countries, sanctions have so far targeted Russian individuals and financial institutions. Doing business as usual with Russian companies has been largely disrupted and several major Russian banks have been removed from the Society for Worldwide Interbank Financial Telecommunication (SWIFT) platform, making it hard for lenders and companies to make and receive payments. In addition, the Central Bank of Russia's (CBR) ability to defend the Rubble by using its USD 630 billion of foreign reserves has been significantly curtailed after the unexpected and unprecedented step towards freezing its reserves held abroad. Noteworthy, Switzerland has set aside its usual policy of neutrality and also frozen the assets held by targeted Russian individuals.

Beyond the Ukraine-Russia conflict, the macroeconomic picture was broadly unchanged in February. US growth continued to be robust as the flash composite PMI jumped to 56 from 51.1 in January, and retail sales beat expectations and bounced back 3.8% month-over-month after a weak print in December due to Omicron's spread. Inflation surprised to the upside again, with the headline print increasing 7.5% year-over-year, its fastest pace since 1982, while prices for core goods and services have picked up. Although these price increases do not seem to be curtailing demand yet, the University of Michigan's print for consumer sentiment, the data of which was gathered before the Ukrainian crisis unfolded, continues to drop. Similarly, Eurozone's headline Harmonised Index of Consumer Prices (HICP) reached 5.1% year-over-year in January, its highest level on record, but, unlike in the US, over 50% of the headline HICP print came directly from energy inflation. In addition, the core HICP remained relatively contained at 2.3% year-over-year, while the equivalent figure stood at 6% and 4.2% year-over-year in the US and the UK, respectively. Moreover, despite tight labour markets across the US, the Eurozone and the UK, we have yet to start seeing the same wage pressure in the Eurozone, where wages were 2.4% higher in the fourth quarter of 2021 relative to the prior year, lagging behind the US (+5.7% year-over-year) and UK (+3.7% higher in the fourth quarter of 2021 relative to the prior year).

Against this background, which has been materially overshadowed after Russia's invasion, rate hikes expectations in the Eurozone in 2022, although they have not been taken off the table, have stabilised. Likewise, market's expectations have come down from seven Fed Funds rate hikes to five. In the meantime, though, the Bank of England (BoE) remained ahead and implanted its second 25bp rate hike of its tightening cycle.

Equities

Equity markets suffered across the board as investors' inflation and tightening concerns were obscured by Russia's invasion of Ukraine. Developed market equities declined 2.5% during the month but managed to outperform emerging ones, which fell 3%. However, emerging markets continue to be ahead year to date, being down 4.8% but still better than the 7.7% drop for developed markets. Global growth stocks were hit hard again in February, falling by 3.5%, while value outperformed but still fell by 1.6%. On a sectoral basis, global energy was the only sector to advance (+5.2%) as soaring oil and gas prices served as strong tailwinds, while global communications services (-5.4%) and information technology (-4.7%) were among the weakest.

Fixed Income

Sovereign bonds yields experienced quite a volatile month. In the first half of the month, yields rose rapidly on continued hawkish surprises from central banks. As such, during this first period, the 10-year US Treasury yield soared 26bp to just over 2%, the 10-year Bund yield jumped 30bp to 0.31% and the 10-year yield Gilt increased 28bp to 1.58%. But, around mid-month, as concerns about how much central banks may need slow growth to get inflation under control, coupled with increasing geopolitical tensions, yields peak and start declining. During the final days of the month, following the invasion, sovereign yields dropped further as investor sought for safety, but still finished slightly higher due to the increases earlier in the month. Hence, by the end of February, the 10-year US Treasury yield stood at 1.83%, the 10-year Bund yield at 0.14% and the 10-year Gilt yield at 1.41%.

Corporate bonds were hit hard again, particularly in Europe, registering negative total returns as spreads continued to widen. EM credit performed the worst, with IG and HY declining 5.6 and 6%, respectively. European HY followed, losing 2.8%, while US HY performed relatively better, declining just 1% given its high weight in the energy sector, which even saw a modest spread tightening.

Emerging Markets

Emerging market equities registered a 3% negative return in February, lagging developed markets, as increasing geopolitical concerns weighed on invertors risk appetite. Following the invasion and the myriad of strict sanctions implemented, the Russian Rubble collapsed by 26% to over 100 rubbles per US dollar for first time ever. Similarly, Russian equities crashed nearly 50% in US dollar terms as stocks became almost untradeable by foreign investors. Neighbouring equity markets, like the Polish and the Hungarian ones, were also severely impacted. In addition, Egypt, India and Turkey also underperformed the overall index as their economies present higher sensitivities towards elevated energy and food prices. In fact, the risk for social unrest in Egypt has increased notably given that the country consumes twice the global average of bread and that it imports about 85% of its wheat from Russia and Ukraine. By contrast, net EM commodity exporters, such as Saudi Arabia, Qatar, Brazil and Mexico, all generated positive returns and outperformed.

FX & Commodities

After hitting 97.2 in January, its highest level since mid-2020, the DXY index remained range trading during February, ending the month at 96.7. Much like sovereign bonds, the US dollar lost some strength during the first part of the month before regaining its ground as investors sought for risk haven assets. Conversely, the Euro weakened 2% to 1.12 US dollars per Euro from its monthly high as ECB tightening expectations decreased and the Ukrainian crisis unfolded. As expected, the Swiss Franc and the Japanese Yen strengthened significantly against the Euro following the invasion. The British Pound also followed suit and rallied against the Euro driven by BoE's second rate hike and FTSE 100 relative outperformance due to its significant weight of energy and mining stocks.

The commodity complex rallied sharply during February on the back of the Russian invasion. Following its 11.2% advance in January, the S&P GSCI index jumped 7.9% again during the month, with agriculture being the best performing component of the index, with strong gains for wheat given that Russia and Ukraine account for around 30% of global wheat exports —interestingly, the yellow section of Ukraine's flag represents wheat fields. The energy component also achieved solid gains in February, with strong price rises for WTI oil and Brent crude, which broke above USD 100 per barrel for the first time since 2014. Gold and silver rose in response to the invasion news and ended the month in positive territory, increasing 6.2% to USD 1,909 per ounce and 8.8% to 24.5 per ounce, respectively.

Developed Markets Equity - LC		Fixed Income Sectors - LC	
Top 3 Markets in February	**Return**	**Top 3 Markets in February**	**Return**
- TA35 Tel Aviv	2.9%	- GLOBAL INF-LINKED	0.3%
- OBX Norway	2.6%	- US HY	-1.0%
- S&P/ASX 200 Australia	2.6%	- US GOV	-1.1%
Worst 3 Markets in February		**Worst 3 Markets in February**	
- ATX Austrian	-11.8%	- EM Sov HC	-6.5%
- OMX Stockholm	-6.8%	- EM Corp HY	-6.0%
- Dax	-6.5%	- EM Corp IG	-5.6%

Emerging Markets Equity - LC		Forex and Commodities - USD	
Top 3 Markets in February	**Return**	**Forex**	**Return**
- FTSE KLCI Malaysia	6.5%	- DXY Index	0.2%
- Qatar Index	4.6%	- USD/EUR	-0.1%
- S&P BMV Mexico	4.0%	- USD/GBP	-0.2%
Worst 3 Markets in February		**Commodities**	
- Moex Russia	-30.0%	- Gold	6.2%
- S&P Merval	-3.2%	- WTI	8.6%
- EGX 30 Index	-3.1%	- Bitcoin	8.4%

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