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global investment management

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Global Matters | Monthly

Market Review

February 2023

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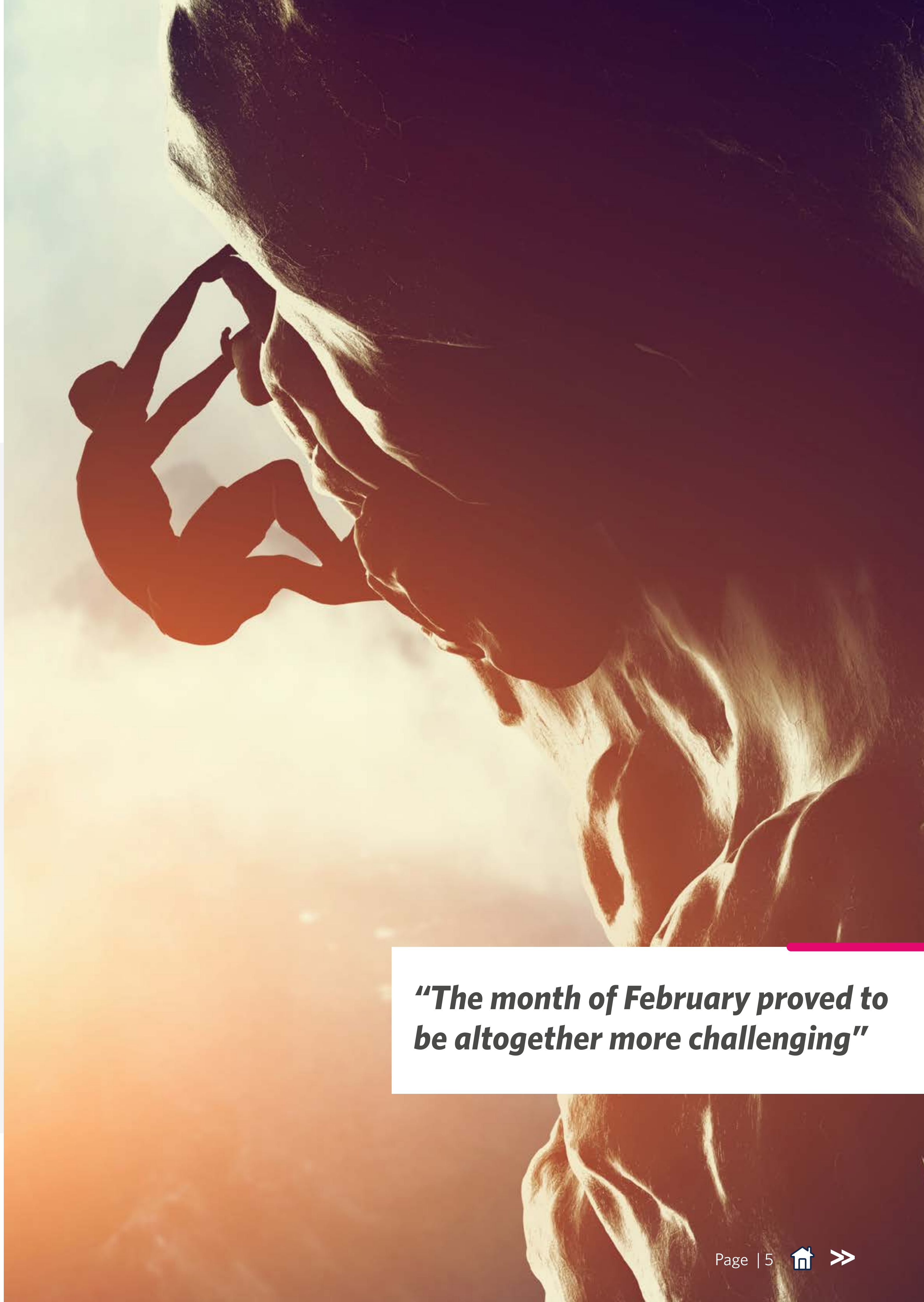
Global Market Review & Outlook

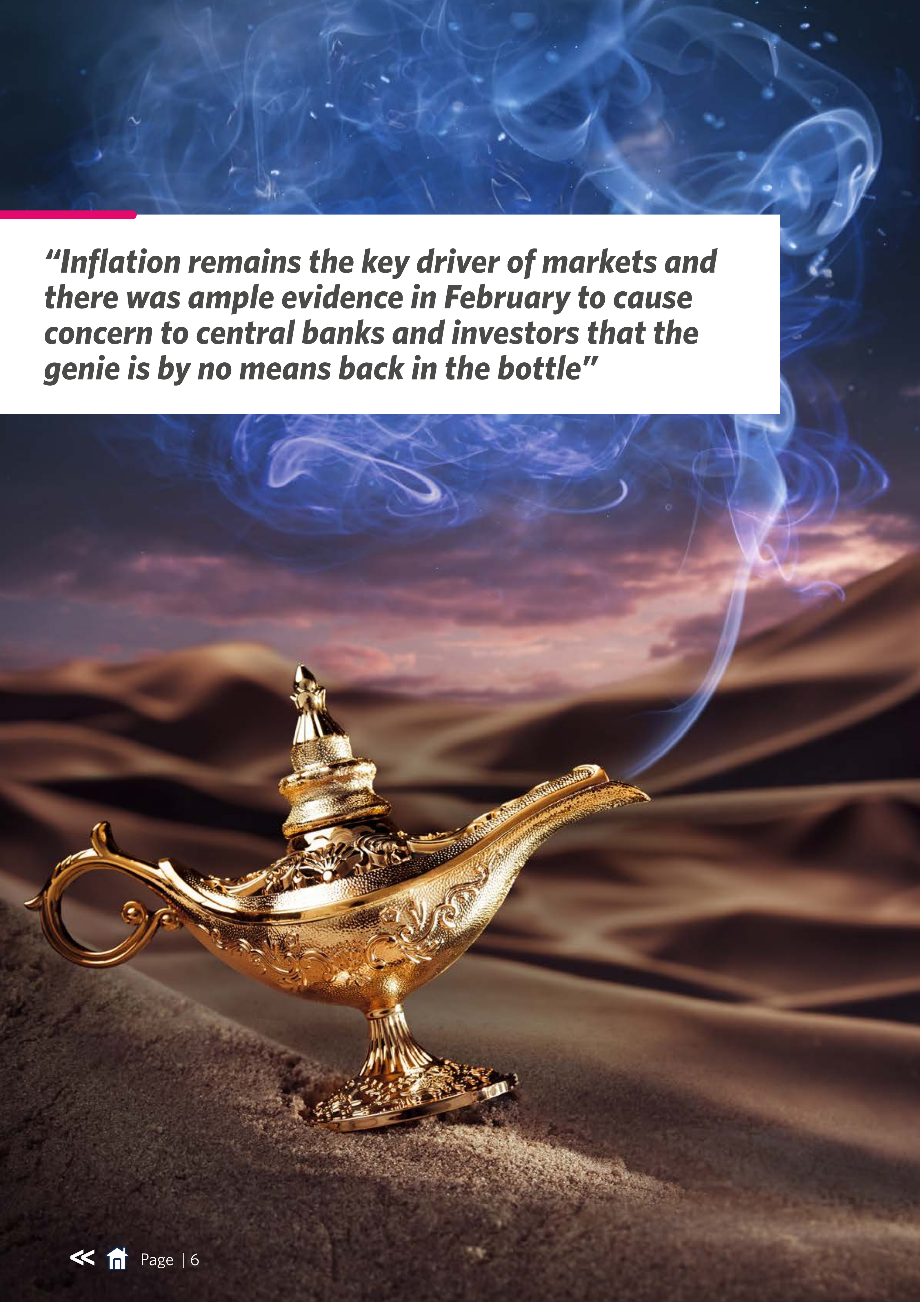
After a benign three months, February proved to be altogether more challenging. Bond markets suffered a big sell-off as the market substantially repriced interest rate expectations in line with the Fed's view. At the beginning of the month the Fed raised the Fed Funds rate by 25bps as expected, to 4.5-4.75%, and, while signalling further rises ahead, the accompanying statement was interpreted as somewhat dovish. However, any dovishness was quickly dispelled in the face of data showing inflation stickier than expected, the labour market remaining very resilient, retail sales surprisingly buoyant, and leading indicators of activity across the US, Europe and China stronger than expected. The Fed's rhetoric, along with the ECB and other developed world central banks, became increasingly hawkish and the market rapidly adjusted to the narrative of higher terminal rates and tighter for longer policy.

Market expectations for Fed Funds Rate in Dec 2023 rose sharply in February

Source: Momentum Global Investment Management, Bloomberg Finance L.P. as at 2 March 2023.



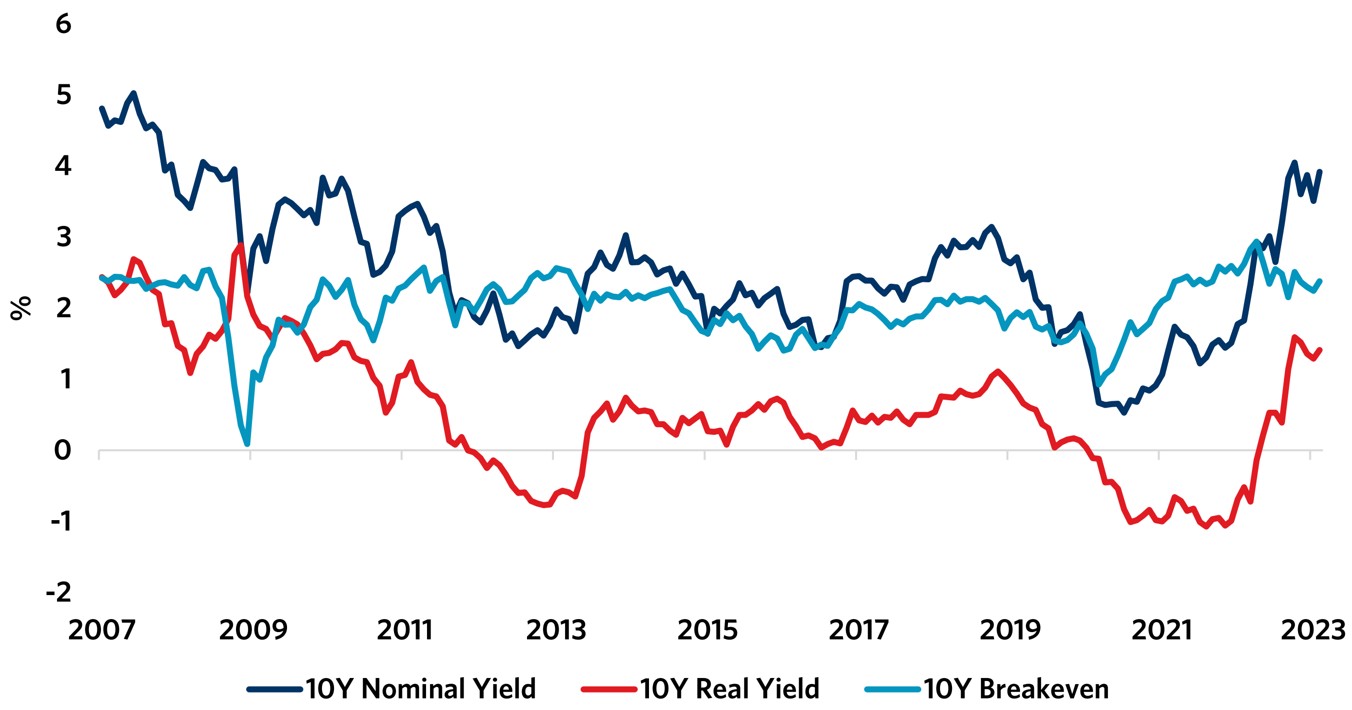
"The month of February proved to be altogether more challenging"



“Inflation remains the key driver of markets and there was ample evidence in February to cause concern to central banks and investors that the genie is by no means back in the bottle”

Over the month the market’s expectation for the Fed Funds rate at the end of this year moved up from around 4.5%, which had been broadly the same for the preceding four months, to 5.3%, with the peak rate in this cycle now priced at around 5.4% in H2 2023, almost 75bps higher than expected only a month earlier. Similar shifts in market pricing took place in Europe and the UK, and bond markets everywhere sold off, reversing all the sizeable gains in January. Yields rose across the maturity spectrum, with the biggest moves in shorter dated bonds: the yield on 2-year government bonds in the US rose by 62bps to 4.82%, and in Germany by 48bps to 3.12%, the highest level since 2008 (and which was in negative territory for most of the decade up to the end of 2021). The rise in yields at the front end of the curve was driven by a sharp shift up in inflation expectations, while at longer maturities it was rising real yields which drove the moves. The 10Y real yield in the US moved up by close to 30bps to 1.54%, a level which offers some valuation attractions after over a decade of extremely low or even negative real yields.

US Treasury bond yields offering value



Source: Momentum Global Investment Management, Bloomberg Finance L.P. as at 28 February 2023.

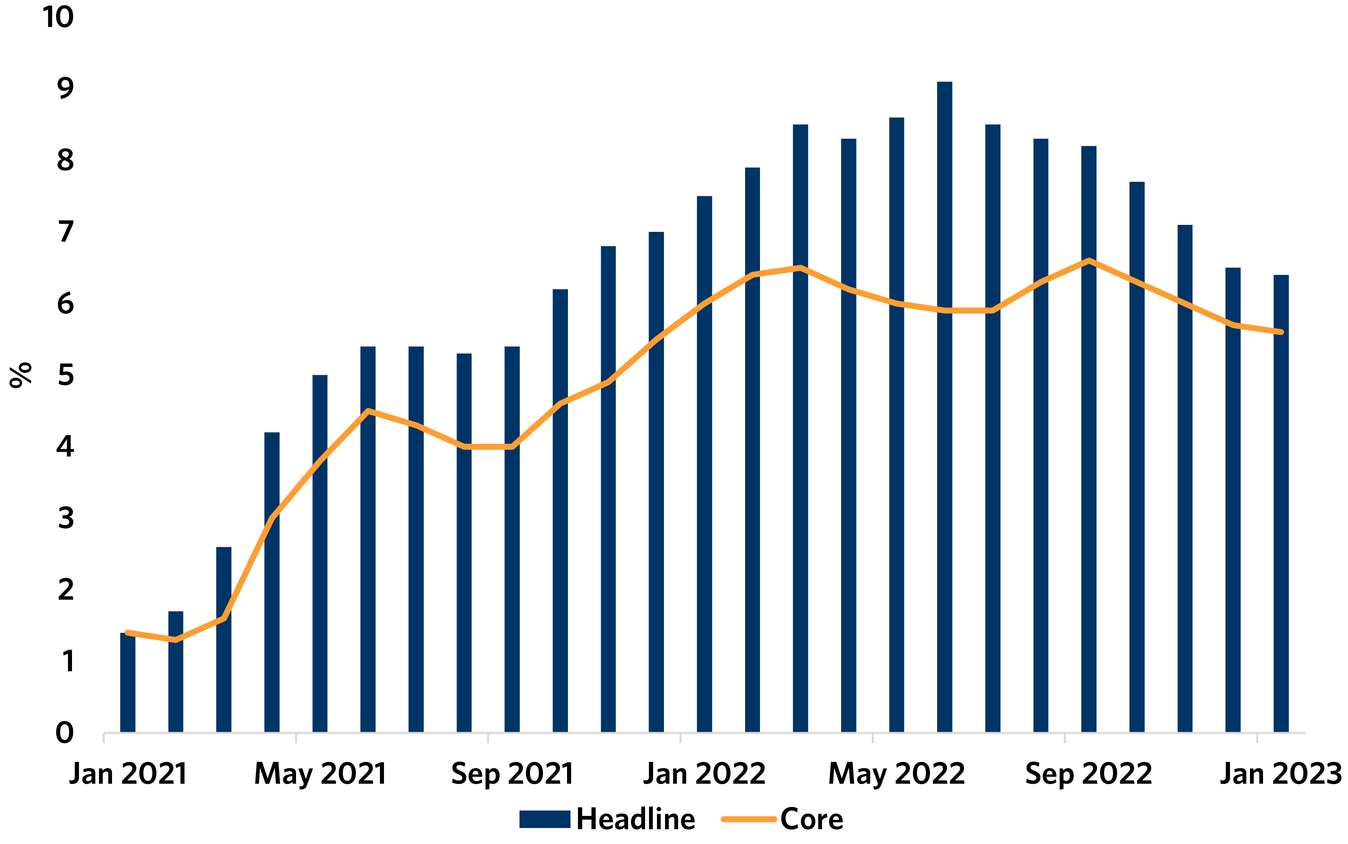
As a result, US Treasuries returned -2.2% in February and the JP Morgan Global GBI -3.2%, dragged down by a sharp rally in the USD, +2.7% on a trade weighted basis, reversing some of its falls over the preceding four months. Rising nominal and real yields along with a stronger dollar saw precious metals come under pressure, with the gold price retreating 5.3% in February. Equity markets were also impacted by the rise in risk-free rates, with the MSCI World index -2.4% and emerging markets -6.5%, held back by a fall of 10% in China following its sharp rally since October.

Inflation remains the key driver of markets and there was ample evidence in February to cause concern to central banks and investors that the genie is by no means back in the bottle. The January US Consumer Price Index (CPI) came in higher than expected at 6.4%, a rise of 0.5% in the month, while price measures which change only slowly and can be more difficult to rein in remained uncomfortably high: the Atlanta Fed sticky-price CPI was 6.7% in January, unchanged from December and at the high for this cycle. The labour market continued to show resilience with a surprise increase in payrolls in January of 517,000 and unemployment fell to 3.4%, heightening fears that the Fed has not yet tightened enough to cool the labour market, and a range of leading indicators in the US and elsewhere pointed to stronger growth and continuing price pressures. Global growth forecasts have been revised up, helped by China’s post-Covid reopening growth surge and the dramatic fall in natural gas prices in Europe, which to date has avoided a widely expected recession.

While of less immediate concern to markets, geopolitics arguably took a turn for the worse. President Biden's trip to Ukraine was perhaps not a Pearl Harbour moment when Churchill 'slept the sleep of the saved' but it surely took NATO ever deeper into the conflict. While it substantially increased the chances of Ukraine retaining its independence it also heightened the risks of a lengthy, attritional, costly and damaging proxy war, and potentially increases the risk of China aligning itself ever more closely with Russia, an outcome which would carry much greater threats for the West and the global economy. Any attempts by China to help Russia to evade Western sanctions or provide lethal weapons would be a serious escalation in the deteriorating US-China relationship.

likely, however, it will continue to be inflation, monetary policy and the extent of the economic slowdown necessary to bring inflation under control which will dominate markets in the months ahead. There is no doubt that headline inflation will fall sharply this year as base effects fall away, the energy price falls in recent months feed through, and supply chain improvements continue to ease pricing pressures in goods. But energy prices are unlikely to continue to fall at the same pace, and supply chain improvements are a one-off adjustment, so the focus will be on core prices and their stickiness. February has resolved one big uncertainty, the disconnect between central banks' views and the market's pricing of policy rates now removed by the repricing in the past month. But the impact of that repricing might not yet have worked its way fully through markets, and considerable uncertainties remain about the pace of the slowdown in core inflation, the strength of the labour market and wage-price spiral fears, and how long will tighter for longer mean in practice with the resultant possibility of policy overkill. Recession risks in the US and Europe have diminished in the short term but remain real as 2023 progresses, especially given the lags in monetary policy.

US inflation falling – but slower than expected



Source: Momentum Global Investment Management, Bloomberg Finance L.P. as at 31 January 2023.

The rise in bond yields in the past month is giving rise to valuation opportunities in government bonds, which, unlike credit and higher risk bond markets, would be beneficiaries of recession, while yields have improved to such an extent that cash is now a viable instrument to achieve target returns and manage risk in multi-asset portfolios. Equities also offer some valuation opportunities but are overhung by the sharp rise in the discount rate over the past month and by recession worries, and the period of consolidation in these markets which we anticipated last month is likely to continue. Recovery lies ahead and we are optimistic for markets over the next twelve months, but believe it is prudent to temper that optimism in the short term given the risks and uncertainties around inflation and recession. We are therefore taking opportunities to add to defensive assets in shorter duration bonds while biding our time before adding to risk assets.

"Recovery lies ahead and we are optimistic for markets over the next twelve months"

Market Performance - *Global (local returns) as at 28 February 2023*

Asset Class / Region	Index	Ccy	1 month	3 months	YTD	12 months
Developed Markets Equities						
United States	S&P 500 NR	USD	-2.5%	-2.4%	3.6%	-8.2%
United Kingdom	MSCI UK NR	GBP	2.1%	5.0%	6.8%	10.6%
Continental Europe	MSCI Europe ex UK NR	EUR	1.5%	5.4%	9.1%	4.4%
Japan	Topix TR	JPY	0.9%	0.6%	5.4%	8.5%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	-6.8%	0.8%	1.3%	-12.0%
Global	MSCI World NR	USD	-2.4%	0.1%	4.5%	-7.3%
Emerging Markets Equities						
Emerging Europe	MSCI EM Europe NR	USD	2.4%	12.3%	5.9%	-47.2%
Emerging Asia	MSCI EM Asia NR	USD	-6.9%	0.3%	1.2%	-15.3%
Emerging Latin America	MSCI EM Latin America NR	USD	-6.2%	-1.1%	3.1%	-0.3%
China	MSCI EM China NR	USD	-8.8%	-1.1%	-2.2%	-16.3%
BRICs	MSCI BRIC NR	USD	-10.4%	5.4%	0.2%	-16.1%
Global emerging markets	MSCI Emerging Markets NR	USD	-6.5%	-0.5%	0.9%	-15.3%
Bonds						
US Treasuries	JP Morgan United States Government Bond TR	USD	-2.2%	-0.4%	0.1%	-9.8%
US Treasuries (inflation protected)	BBgBarc US Government Inflation Linked TR	USD	-1.4%	-0.5%	0.5%	-10.9%
US Corporate (investment grade)	BBgBarc US Corporate Investment Grade TR	USD	-3.2%	0.3%	0.7%	-10.4%
US High Yield	BBgBarc US High Yield 2% Issuer Cap TR	USD	-1.3%	1.9%	2.5%	-5.5%
UK Gilts	JP Morgan UK Government Bond TR	GBP	-3.3%	-4.8%	-0.7%	-20.9%
UK Corporate (investment grade)	ICE BofAML Sterling Non-Gilt TR	GBP	-2.2%	-0.5%	1.3%	-12.3%
Euro Government Bonds	ICE BofAML Euro Government TR	EUR	-2.3%	-4.5%	-0.3%	-15.9%
Euro Corporate (investment grade)	BBgBarc Euro Aggregate Corporate TR	EUR	-1.4%	-1.0%	0.7%	-9.6%
Euro High Yield	BBgBarc European High Yield 3% Constrained TR	EUR	-0.1%	2.3%	3.0%	-3.8%
Japanese Government	JP Morgan Japan Government Bond TR	JPY	1.2%	-0.4%	0.9%	-3.5%
Australian Government	JP Morgan Australia GBI TR	AUD	-1.7%	-1.2%	1.3%	-7.2%
Global Government Bonds	JP Morgan Global GBI	USD	-3.2%	-0.4%	-0.5%	-15.2%
Global Bonds	ICE BofAML Global Broad Market	USD	-3.2%	0.0%	-0.2%	-14.0%
Global Convertible Bonds	ICE BofAML Global Convertibles	USD	-1.7%	2.8%	4.2%	-8.8%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	USD	-3.4%	0.1%	0.1%	-11.6%

Asset Class / Region	Index	Ccy	1 month	3 months	YTD	12 months
Property						
US Property Securities	MSCI US REIT NR	USD	-4.8%	-0.4%	5.2%	-12.8%
Australian Property Securities	S&P/ASX 200 A-REIT Index TR	AUD	-0.8%	1.3%	7.3%	-10.6%
Asia Property Securities	S&P Asia Property 40 Index NR	USD	-5.5%	-1.7%	-3.1%	-11.6%
Global Property Securities	S&P Global Property USD TR	USD	-4.7%	0.6%	3.3%	-14.8%
Currencies						
Euro		USD	-2.6%	1.6%	-1.2%	-5.7%
UK Pound Sterling		USD	-2.4%	-0.3%	-0.5%	-10.4%
Japanese Yen		USD	-4.5%	1.4%	-3.7%	-15.6%
Australian Dollar		USD	-4.6%	-0.9%	-1.2%	-7.4%
South African Rand		USD	-5.2%	-6.3%	-7.2%	-16.3%
Commodities & Alternatives						
Commodities	RICI TR	USD	-4.1%	-4.7%	-4.0%	-1.9%
Agricultural Commodities	RICI Agriculture TR	USD	-3.5%	-0.6%	-1.2%	-3.2%
Oil	Brent Crude Oil	USD	-0.7%	-1.8%	-2.4%	-16.9%
Gold	Gold Spot	USD	-5.3%	3.3%	0.2%	-4.3%
Hedge funds	HFRX Global Hedge Fund	USD	-0.4%*	1.2%*	1.3%*	-1.4%*

Interest Rates	Current Rate
United States	4.75%
United Kingdom	4.00%
Eurozone	3.00%
Japan	-0.10%
Australia	3.35%
South Africa	7.25%

Source: Bloomberg Finance L.P. , Momentum Global Investment Management. Past performance is not indicative of future returns.
**estimate.*

Market Performance - *UK (all returns GBP) as at 28 February 2023*

Asset Class / Region	Index	Local Ccy	1 month	3 months	YTD	12 months
Equities						
UK - All Cap	MSCI UK NR	GBP	2.1%	5.0%	6.8%	10.6%
UK - Large Cap	MSCI UK Large Cap NR	GBP	2.0%	3.8%	5.1%	13.9%
UK - Mid Cap	MSCI UK Mid Cap NR	GBP	1.4%	8.6%	11.4%	-5.3%
UK - Small Cap	MSCI Small Cap NR	GBP	1.0%	5.5%	7.3%	-6.3%
United States	S&P 500 NR	USD	-0.7%	-3.7%	3.6%	1.6%
Continental Europe	MSCI Europe ex UK NR	EUR	0.9%	6.9%	8.0%	9.4%
Japan	Topix TR	JPY	-1.4%	1.9%	1.7%	1.8%
Asia Pacific (ex Japan)	MSCI AC Asia Pacific ex Japan NR	USD	-5.0%	-0.5%	1.3%	-2.6%
Global developed markets	MSCI World NR	USD	-0.6%	-1.2%	4.5%	2.6%
Global emerging markets	MSCI Emerging Markets NR	USD	-4.7%	-1.8%	0.9%	-6.2%
Bonds						
Gilts - All	ICE BofAML UK Gilt TR	GBP	-3.4%	-5.1%	-0.7%	-21.4%
Gilts - Under 5 years	ICE BofAML UK Gilt TR 0-5 years	GBP	-0.9%	-0.3%	0.0%	-3.8%
Gilts - 5 to 15 years	ICE BofAML UK Gilt TR 5-15 years	GBP	-2.8%	-3.0%	0.1%	-14.7%
Gilts - Over 15 years	ICE BofAML UK Gilt TR 15+ years	GBP	-6.0%	-10.5%	-2.3%	-35.5%
Index Linked Gilts - All	ICE BofAML UK Gilt Inflation-Linked TR	GBP	-4.8%	-6.8%	-1.7%	-33.5%
Index Linked Gilts - 5 to 15 years	ICE BofAML UK Gilt Inflation-Linked TR 5-15 years	GBP	-1.6%	-3.2%	0.6%	-15.7%
Index Linked Gilts - Over 15 years	ICE BofAML UK Gilt Inflation-Linked TR 15+ years	GBP	-8.5%	-11.1%	-3.7%	-45.9%
UK Corporate (investment grade)	ICE BofAML Sterling Non-Gilt TR	GBP	-2.2%	-0.5%	1.3%	-12.3%
US Treasuries	JP Morgan US Government Bond TR	USD	-0.6%	-2.1%	-0.6%	0.0%
US Corporate (investment grade)	BBgBarc US Corporate Investment Grade TR	USD	-1.5%	-1.4%	0.1%	-0.7%
US High Yield	BBgBarc US High Yield 2% Issuer Cap TR	USD	-1.3%	1.9%	2.5%	-5.5%
Euro Government Bonds	ICE BofAML Euro Government TR	EUR	-2.3%	-4.5%	-0.3%	-15.9%
Euro Corporate (investment grade)	BBgBarc Euro Aggregate Corporate TR	EUR	-1.4%	-1.0%	0.7%	-9.6%
Euro High Yield	BBgBarc European High Yield 3% Constrained TR	EUR	-0.1%	2.3%	3.0%	-3.8%
Global Government Bonds	JP Morgan Global GBI	GBP	-1.4%	-1.7%	-0.5%	-6.2%
Global Bonds	ICE BofAML Global Broad Market	GBP	-3.2%	0.0%	-0.2%	-14.0%
Global Convertible Bonds	ICE BofAML Global Convertibles	GBP	-1.7%	2.8%	4.2%	-8.8%
Emerging Market Bonds	JP Morgan EMBI+ (Hard currency)	GBP	-1.6%	-1.2%	0.1%	-2.1%

Asset Class / Region	Index	Local Ccy	1 month	3 months	YTD	12 months
Property						
Global Property Securities	S&P Global Property TR	GBP	-2.9%	-0.7%	3.3%	-5.8%
Currencies						
Euro		GBP	-0.2%	1.9%	-0.6%	5.2%
US Dollar		GBP	2.5%	0.3%	0.5%	11.6%
Japanese Yen		GBP	-2.2%	1.6%	-3.2%	-5.8%
Commodities & Alternatives						
Commodities	RICI TR	GBP	-2.3%	-6.0%	-4.0%	8.6%
Agricultural Commodities	RICI Agriculture TR	GBP	-1.7%	-1.9%	-1.3%	7.1%
Oil	Brent Crude Oil	GBP	1.1%	-3.1%	-2.4%	-8.1%
Gold	Gold Spot	GBP	-3.5%	2.0%	0.1%	5.9%
Interest Rates				**Current Rate**		
United Kingdom				4.00%		

*Source: Bloomberg Finance L.P. , Momentum Global Investment Management. Past performance is not indicative of future returns. *estimate.*

Asset Allocation Views

Score	1	2	3	4	5	6	7

Score	Change	1	2	3	4	5	6	7
MAIN ASSET CLASSES	▲/▼/—							
Equities	—				■			
Fixed Income	—				■			
Alternatives	—					■		
Cash	—				■			

Our Overall View

We have upgraded fixed income to a more neutral view following the fall in bond prices this year, and pockets of value appearing. Equity valuations have also improved but an upgrade feels premature with policy still exhibiting a firm tightening bias. Alternatives remain attractive for their diversifying qualities and return potential, and whilst cash yields have improved markedly, the sharp 2022 repricing warrants a downgrade from the previously overweight view.

Score	Change	1	2	3	4	5	6	7
EQUITIES	▲/▼/—							
Developed Equities	—				■			
UK Equities	—						■	
European Equities	—				■			
US Equities	—			■				
Japanese Equities	—						■	
Emerging Market Equities	—					■		

Equities offer improving return potential after 2022's weakness. Financial conditions have tightened, but by historical standards are not restrictive, and excess savings and strong labour markets should support the consumer in the near term. Nonetheless, recession is all but expected to follow and equities are likely to remain challenged until policy tightening abates. We favour the UK and Japan on valuation grounds, with the latter also offering the accompanying (cheap) Yen exposure. European equities have cheapened but fundamental risks, notably around energy pricing, caution against increasing today. The US likely has room to cheapen further as earnings compress.

Score	Change	1	2	3	4	5	6	7
FIXED INCOME	▲/▼/—							
Government	▲				■			
Index-Linked	▲				■			
Investment Grade Corporate	▼				■			
High Yield Corporate	▼			■				
Emerging Market Debt	—					■		
Convertible Bonds	—			■				

Bonds offer increasing opportunities following 2022's historic repricing. Concerns around a slowdown in global growth have also improved the appeal of higher grade issuers, both sovereign and corporate. Although inflation expectations have all but normalized, real yields in some markets are attractive against the backdrop of weaker growth. In credit we prefer short duration bonds, including emerging markets. Core high yield is arguably premature as defaults pick up, but valuations have improved. Convertible bonds are less attractive with equities and credit both presenting reasonable opportunities today.

Score	Change	1	2	3	4	5	6	7
SPECIALIST ASSETS/ALTERNATIVES	▲/▼/—							
Commodities	—				■			
Property	—				■			
Infrastructure	—				■			
Liquid Alternatives	—				■			
Private Equity	—						■	
Specialist Financial	—					■		

Real assets and alternatives continue to look attractive on both fundamental and valuation grounds. Commodities remain volatile but with a slowdown in growth expected in the year ahead, gains in aggregate will be harder to come by. Private equity has been challenged in recent months and offers attractive discounts at current levels. Infrastructure continues to enjoy structural tailwinds from digitalisation and energy transition initiatives.

Score	Change	1	2	3	4	5	6	7
CURRENCIES vs. USD	▲/▼/—							
GBP	—					■		
EUR	—				■			
JPY	—					■		
Gold	—				■			

Sterling and Yen are mildly favoured as they remain cheap versus long term valuation metrics. The latter's (usually) diversifying qualities also retain some added portfolio attractiveness, and the Bank of Japan's recent relaxing of the yield target range adds to the positive outlook for the Yen. The Euro will probably continue to struggle in the face of relative rate expectations and more localised economic and political considerations. Gold has inflation protection qualities vs. the fiat currencies, plus haven qualities that are attractive in this elevated geopolitical climate.

The Asset Allocation views are as of March 2023 and are updated quarterly unless otherwise stated.

"Alternatives are attractive for their diversifying qualities and return potential"

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