Monthly Markets Review

March 2022

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Key Observations:

- *Investor focus on central bank policy — particularly the Federal Reserve — was overshadowed by Russia's invasion of Ukraine in the last week of the month. Markets were broadly lower, with real assets the exception.*
- *Economic sanctions on Russia are likely to further pressure commodity prices and inflation globally.*
- *As 2022 evolves, the themes of inflation and market volatility remain evident, yet we maintain our positive view of global growth and see a near-term recession as unlikely.*

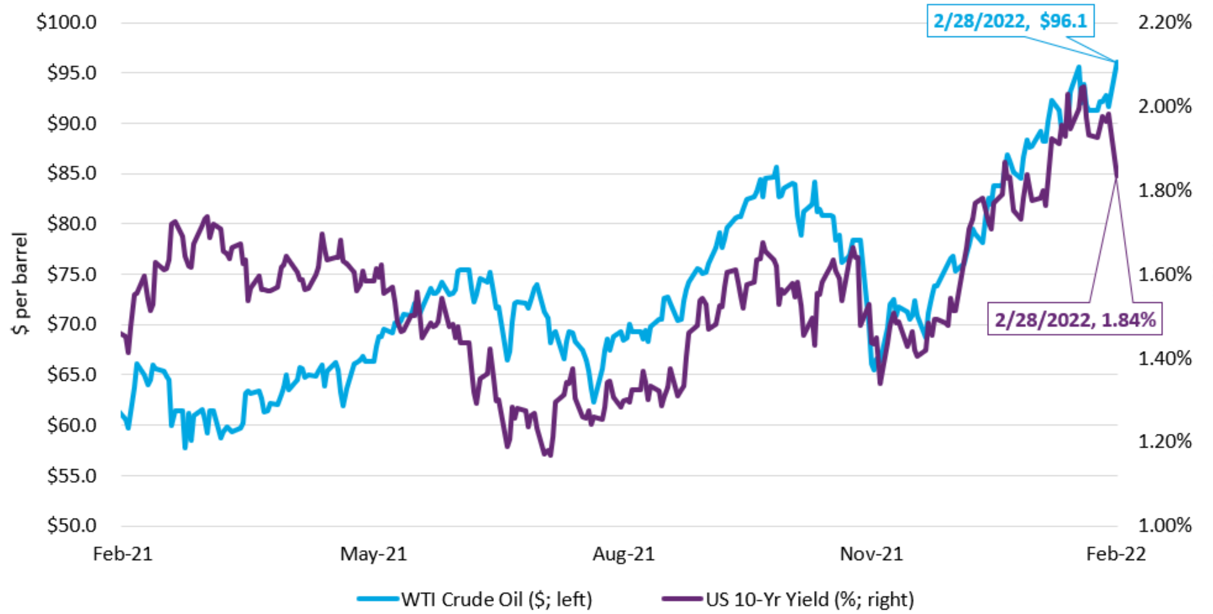
Market Recap

While February began with eyes on Federal Reserve (Fed) Chairman Powell's hawkish stance, inflation and a focus on the job market, the resounding theme was Russia's invasion of Ukraine in the last week of the month. As this evolved from a low likelihood event to a distressing reality, markets adopted a risk-off stance.

Markets trended lower in February, further adding to year-to-date losses across asset classes. Equity markets were mostly negative, with the S&P 500 Index and MSCI Emerging Markets Index each down 3.0%, while the small-cap Russell 2000 Index gained 1.1%. Lurking below these monthly numbers was significant volatility, as the CBOE Volatility Index (VIX) spiked to 31.0 from an intra-month low of 20.0. Fixed-income markets were lower in the first half of the month as interest rates rose, recovering some ground later; the Bloomberg U.S. Aggregate Index finished the month 1.1% lower. The U.S. 10-year Treasury yield reached a post-pandemic high of 2.05% but subsequently dropped to 1.84%, roughly in line with where it began the month. Notably, crude prices rose 8.6%, driven by uncertainty regarding sanctions on Russia, a major crude exporter. This pushed oil towards $100/barrel, the highest level seen since 2014. Energy and real asset names benefited from this acceleration in the prices of oil and other commodities, with the Bloomberg Commodity index gaining 6.2%[1].

[1] FactSet, Morningstar

Crude Prices and Treasury Yields Have Trended Together - Until Now



Source: FactSet as of February 28, 2022

> ***Oil prices rose toward $100/barrel, the highest level since 2014. The continued upward movement in energy prices will add momentum to inflation figures.***

Russia's Role in Portfolios

Although Russia is a major commodity supplier to the rest of the world, particularly Europe, its role in investment portfolios is muted. The drawdown in Russian equities has led to a halving of its size in the MSCI Emerging Markets index. Subsequently, index provider MSCI removed Russian equities from its indices, citing ongoing market closures that have made them entirely illiquid[2]. This will boost the relative size and importance of other regions in indices. Of note are Brazil and Saudi Arabia, which have benefited from the rise in crude oil and commodity prices. Their roles have been further magnified by weakness in other emerging markets.

Source: FactSet, Morningstar, as of February 28, 2022.

	Weight in Index (%)		Return (%)	
Country	**February 2022**	**December 2021**	**February**	**YTD**
China	31.8%	32.4%	-3.9%	-6.7%
Taiwan	16.1%	16.1%	-2.5%	-4.5%
India	12.4%	12.5%	-4.0%	-5.3%
Korea	12.3%	12.8%	0.8%	-9.4%
Brazil	5.0%	4.0%	4.7%	18.4%
Saudi Arabia	3.9%	3.3%	3.0%	12.5%
Russia	1.6%	3.6%	-52.7%	-56.8%
MSCI Emerging Markets Index	100.0%	100.0%	-3.0%	-4.8%

[2] WSJ: MSCI Signals Potential Exclusion of Russia From Influential Indexes (wsj.com)

While geopolitics remain at the forefront, the gears of the U.S. economy continue to churn. Despite the economic disruption wrought by the Omicron variant, the job market showed strength, gaining 467,000 jobs in January, more than three times the forecast of 150,000. The bulk of these gains came from the services sector, which added 440,000 new jobs. These positive trends were amplified by upward revisions for previous months' numbers. Strength in consumer spending was another positive factor, as retail sales grew 3.8% in January, compared to a -2.5% reading in December[3]. Given the central role of consumers in the economy, this bodes well for the continued recovery. Further evidence of strength in the economy was provided by the S&P 500 showing 30.7% earnings growth for the fourth quarter of 2021[4]. The January Consumer Price Index (CPI) number of 7.5% was both higher than the 7.3% forecast and December's 7.1% reading. Further prospects of high inflation will be a factor in the Fed's rate decision in coming months, especially given uncertainty regarding Russia, elevated market volatility and recent trends in commodity prices.

Outlook

Although elevated oil and natural gas prices will further stoke inflation, the heightened risk arising from the conflict in Ukraine may give the Fed and its peers grounds to temper their recently hawkish[5] tone. However, Chairman Powell already indicated the central bank still expects to begin its rate-hike campaign when it meets this month. Despite this, we recommend investors maintain their fixed-income allocations as part of a diversified portfolio. Our expectation for additional volatility over the balance of the year could limit the upside of longer-term rates, which could support fixed income in its role as a diversifier in the portfolio.

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[3] US Census Bureau

[4] FactSet

[5] Bias towards increasing interest rates to tamp down inflation over economic growth

Opinions are as of the date referenced and are subject to change based on market or economic conditions. There is no guarantee that any of these expectations will become actual results.

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