Market Commentary February 2022

A tightening of monetary conditions and heightened geopolitical tensions was carded to bring about volatility this year. However, many investors have been caught off guard by the speed at which both have developed.

Tighter monetary conditions were largely driving markets in the early stages of the month, with bond yields continuing to push higher and equity markets remaining volatile, with a particular sell-off in higher-growth investments.

Then, volatility jumped further in the closing stages of the month as Russia began a devastating invasion of Ukraine. Unsurprisingly, the move by Putin has caused widespread backlash from all walks of life, and various economic sanctions have been put in place.

Whilst still lower for the month, the selloff in bonds did reverse as we witnessed a flight to safety, with credit spreads continuing to widen, albeit it to more ‘normalised’ levels.

Sanctions such as freezing Russian assets will have an obvious impact on the domestic economy. We have already seen the Russian Central Bank more than double their benchmark interest rate to 20% as their currency has collapsed. However, there will be consequences for global trade far beyond Ukraine and Russia, as further strain is placed on supply chains, particularly if the violence is prolonged.

We have already seen the disruption of a higher oil & gas price. Whilst continuing its post covid bounce, the devastating attack on Ukraine has sent the price higher once more, highlighting the grip Russia has on energy supplies into Europe.

Whilst we see this as a positive in terms of accelerating the rollout of renewable projects (and have already seen renewable energy companies share prices react positively as a result), European powerhouses such as Germany are heavily reliant on natural gas from Russia, meaning further disruption in the manufacturing of goods.

Elsewhere, with their rich soil and land, Ukraine and Russia are big players in other commodity markets. Both countries are large suppliers of raw materials and machinery, including minerals and metals like nickel and copper, both of which play a larger part in the construction of green technologies such as EV batteries.

Russia and Ukraine provide around 29% of global wheat exports, and on top of this, Ukraine accounts for 16% of global corn exports and 18% of barley, which is where the country gets the ‘breadbasket of Europe’ label. Heightened and prolonged tensions pose significant risks for food security in Europe, Africa and the Middle East, but also countries such as China, who rely heavily on Ukraine for Corn. There are still a couple months before harvesting, but a concern nonetheless.

As with the oil and gas price, we have seen these commodity prices soar, further feeding through to the inflationary pressures globally that central banks are struggling to tame (the Bloomberg commodity index is up circa 19% year to date).

On top of the above, Ukraine is among the larger exporters of information-technology services. Coding from Ukrainians can be found in global banking systems, aeroplanes, cars and mobile networks. Whilst earning above average salaries domestically, they are a far reach from the salaries earned in Silicon Valley. As many coders have been displaced, some companies will either see project delays or seek more expensive alternatives.

Our portfolios have no direct exposure to Russia, and any exposure is indirect and minimal. The main consequences are the breakdown in global trade and subsequent supply issues, which has increased the uncertainty over central bank policy, particularly if there is a ramp up in escalations and the drag on growth becomes more severe.

No doubt it has implications to drag on the European economy more than the US. With the latter in a strong position to absorb the fallout. The US economy, is seeing an acceleration in service activity, from restaurants to hotels and airlines. This highlights the resurgence in part of the economy that had been hit so hard by the crisis and has led to some strong numbers being expected in February's US jobs report (consensus is for just over 400k jobs).

The situation is fluid and we will continue to update you and your clients should events move in either direction.

Intergovernmental Panel on Climate Change (IPCC)

At the end of the month, the Intergovernmental Panel on Climate Change (IPCC) produced the second part of its climate change report. The focus of the group producing this report was assessing the effects of climate change and how humanity can adapt to these. This part is therefore likely to be the most politically sensitive as it deals with the probable real-world impact of climate change whilst addressing contentious issues of how to adapt.

The UN Secretary General described the report as "an atlas of human suffering and a damning indictment of failed climate leadership." Extreme weather events are accelerating and wreaking increasing damage, with half of the global population living in highly vulnerable areas. Millions face food and water shortages induced by climate change, even at its current level. If we go above 1.5 degrees, there will be a sharp acceleration with some irreversible impacts. Hunger, ill-health, and poverty will worsen, and as these impacts hit hard international relations and geopolitics will likely become inflamed.

But the authors say that there is still a brief window of time to avoid the very worst. Dr Helen Adams, a lead author, said that the report shows that "things are bad, but actually, the future depends on us, not the climate." For the world to adapt, it is not just about spending on green energy which is now beyond obvious. The authors say that investing in education, health systems and social justice will help people to cope with the impacts of rising temperatures. If climate change is imposed on a society where rapid progress is being made on education, health and poverty, then the risk will be much lower. These are all themes of upmost importance for our portfolios, and this report shows that rapid investment is vital not just in renewable energy but throughout the sphere of sustainable investment.

Other Ethical News

Battery specialist **Zenobe** and transport operator **National Express** are teaming up to deliver 130 electric double-decker buses for use in Coventry, under a "pioneering deal". This deal will see over 130 double-deck e-buses, manufactured in Britain by Alexander Dennis Limited

(ADL) in partnership with BYD, enter service in Coventry from early 2023. This is part of the city's successful bid to become the country's first all-electric bus city and take it a huge step closer to replacing around 300 diesel vehicles by 2025.

Waitrose and **Lidl** are the most sustainable supermarkets, according to a study by consumer group 'Which?'. According to the research, in which Iceland finished last, it tracked supermarket policies on plastic waste and food waste, which shoppers have reported are the biggest issues for them; and greenhouse gas emissions, which most experts say poses the greatest environmental threat.

Scientists will begin work on four studies that will tackle key challenges facing the UK as it adapts to climate change and moves to net-zero emissions. Led by the **universities of Cambridge, Exeter, Glasgow, and Oxford**, each team will work to develop solutions to biodiversity loss, achieving net-zero cities, helping rural communities adapt to climate change, and provide timely data, analysis and evidence for policy decisions. The four programmes have each received £10m from the **National Environment Research Council** to bring together teams drawing on expertise from a range of disciplines.

Brompton, the UK's largest bicycle manufacturer has unveiled plans for the UK's largest bike plant on Kent wetlands in Ashford. Aiming to open in 2027, the state-of-the-art building will be situated within 100 acres of unused wetlands, 60 acres of which will be transformed by Ashford Borough Council into a rewilded public nature reserve and community cycle path with sustainability at its heart.

Finally, following on from the above, **AXA Investment Management** and energy giant **Engie** have acquired minority stakes in a new French company that plans to scale nature-based solutions within the forestry and agriculture sectors. **The Shared Wood Company**, which was created by experience forestry experts, specialises in preserving and restoring natural ecosystems to capture carbon for the long-term, mainly in LATAM, Africa and Europe – seen as key to tackling global warming.