MFM

MIRANTE FUND MANAGEMENT

Market Overview

MARCH 2022

We believe in active management based on a structured investment process to ensure optimal diversification in terms of asset classes, types of financial instruments and geographic sectors. Risk management is an investment tool fully integrated into the portfolio construction process.

The benefits of this approach are numerous: the reduction of risk against significant market declines, as well as the potential to create increased value over the long term.

Frank Crittin, Chief Investment Officer

INFLATIONARY FEARS FANNED BY THE SOUND OF CANNONS!

This month, we have witnessed two events likely to generate significant changes in geopolitics and investment. One is the increase in inflation, and the other is the Russian invasion of Ukraine.

At the beginning of the month, macroeconomic figures confirmed the strength of inflation. Investors continued to bet on a faster monetary tightening by testing the credibility of central bankers. Rising rates will have a significant impact on the economy and investment strategies. At the end of the month, the worst-case scenario of a Russian invasion of Ukraine came to fruition. It had an immediate impact on commodity prices. This sudden increase will contribute, in the short term, to support a high level of inflation. Unprecedented economic sanctions have hit Russia extremely hard, wiping out much of its wealth. The Russian stock market fell by 38% on the invasion day. This was the most significant drop in any country's stock market index history. However, on the same day, the U.S. technology market (Nasdaq) ended up sharply by more than 3%, demonstrating the difficulty of predicting the impact of major geopolitical events on the financial markets.

Over the month, all asset classes fell sharply. The two main exceptions were commodities and inflation-linked government bonds. The direct impact of the Ukrainian war pushed all commodities to record levels, especially those related to energy. The immediate consequence of this increase has pushed up the prices of inflation-linked bonds.

On the equity side, the only sectors that managed to show a positive performance were commodity-related. Energy and materials performed spectacularly well. All technology companies were under pressure. They suffered from the impact of rising interest rates on their valuation combined with a drastic reduction in investors' risk appetite. In the consumer discretionary sector, travel-related companies benefited at the beginning of the month from the decrease in anti-Covid measures. The Ukrainian crisis then struck them. At the regional level, most regions contributed negatively to performance. Eastern Europe was naturally the main negative contributor, while South America showed a positive performance. Although in negative territory, Switzerland and Japan maintained their role as safe-haven markets.

At the bond level, the credit market showed signs of strain with the war and the weakening of Chinese real estate. Inflation-linked bonds managed to produce a positive performance. At the end of the month, government bonds rebounded dramatically after the invasion of Ukraine as investors looked for safe havens and were pleased with the current yield levels.

Real estate had a negative performance despite being theoretically defensive against rising inflation. Most regions contributed negatively to performance. At the sector level, despite a turbulent end to the month, the hotel sector benefited from the removal of Covid-related constraints. Office property also ended the month in positive territory. The most affected sector was the logistics sector due to the weakness of e-commerce.

NUMBER OF THE MONTH:

80%

Ukraine and Russia together account for 80% of world sunflower exports.

Russian shares listed on the London Stock Exchange have performed -99% since the beginning of the year.

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OUTLOOK: AN INFLATIONARY WAR?

While markets focus on the military manoeuvres in Ukraine and the consequences of sanctions, investors keep a close eye on the balance between overall economic growth and inflationary pressures. Historically, the short-term impact of armed conflicts on financial markets has been relatively marginal. However, in this case, the invasion of Ukraine is a new supply shock to the global economy. It drives up inflation through commodity prices while putting global growth at risk. Indeed, the economic consequences of sanctions will impact trade and the financial system. While the implosion While markets focus on the military manoeuvres in Ukraine and the consequences of sanctions, investors keep a close eye on the balance between overall economic growth and inflationary pressures. Historically, the short-term impact of armed conflicts on financial markets has been relatively marginal. However, in this case, the invasion of Ukraine is a new supply shock to the global economy. It drives up inflation through commodity prices while putting global growth at risk. Indeed, the economic consequences of sanctions will impact trade and the financial system. While the implosion of the Russian economy will have only a minor impact on the global economy, as Russia represents about 3% of the world's GDP, the side effects of these sanctions could be significant. Europe seems to be the most exposed, but the indirect impact of rising commodity prices and sanctions could affect global demand.

In terms of inflation, commodity prices will undoubtedly support it in the short time. However, most central bankers are trying to remove the impact of energy and food price movements from their inflation measures. Instead, they are most interested in whether consumer expectations of inflation are beginning to be incorporated into workers' wage demands. This could lead to a long-term price increase forcing central bankers to raise rates significantly. While it seems clear that the Fed will raise rates and withdraw liquidity to help cool the U.S. economy, the key question remains the speed of the increase. In this context, the war-induced economic slowdown in Europe could lead them to revise that pace downward.

In terms of bonds, despite the role of shock absorbers played by long-duration bonds (i.e. with a long maturity), we prefer to allocate risk in the area of credit, particularly in emerging countries. A measured allocation to TIPS allows us to hedge the risks linked to inflation partially. In the medium term, overcoming the temptation to opt for long duration after a phase of rising nominal yields will remain crucial.

Market corrections represent sharp movements in the prices of risky assets. They harm equity valuations. The current correction reflects investors' fears about inflation, rising rates and the war in Ukraine. However, recent data does not indicate an imminent recession. Although central banks will be tempted to raise rates, they may reasonably delay to preserve growth that is likely to be affected by the war. In China, before the Russian invasion, the government had already begun to stimulate the economy to offset the impact of the new Omicron wave and the violent turbulence in its property market. We remain opportunistic in terms of equity allocation without fundamentally reorienting our investment strategies. Specifically, we try to avoid being heavily invested in sectors, regions and supply chains exposed to the disruptions generated by the impact of economic sanctions. By observing its development and analyzing data, we could benefit from the situation if the expected returns on certain assets become sufficiently attractive to offset the risk.

The current inflationary pressure should positively drive real estate assets. Indeed, there are signs of a positive correlation between real estate companies' earnings, and thus their dividends, and inflation.

Our diversified investment approach, with a strong focus on the quality of the underlying assets, should allow us to withstand the strong movements of the main asset classes during market corrections. However, our primary challenge remains to mitigate inflationary risks in the short term while integrating the normalization of the global economy in the medium term. This calls for active management based on highly diversified portfolios, which remains central to cushioning the expected fluctuations in risk appetite.

In the longer term, the devastating sanctions used against Russia could redistribute the global balance of power and redefine the functioning of the worldwide economy. From a unilateral world dominated by Uncle Sam, we will move to a world divided between two economic blocs competing on ideological and technological levels. On one side, China and its allies and on the other side, the United States and its allies. Moreover, in the coming years, the major powers will try to protect themselves from the type of sanctions Russia is currently experiencing by promoting their «self-sufficiency» by promoting digital versions of their central bank's currency in world trade and finance. China is already testing a state-owned cryptocurrency.

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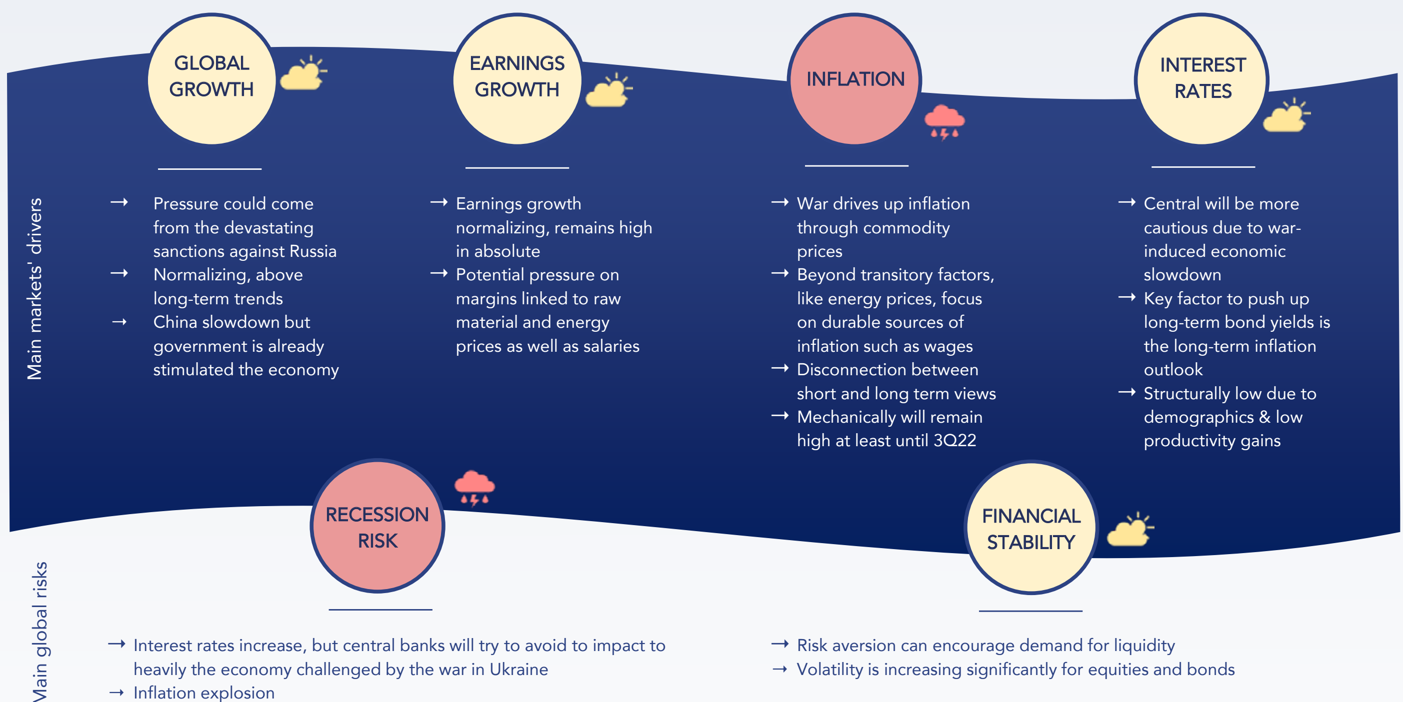
MAIN DRIVERS



SOURCE: MFM, March 2022

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MONTHLY PERFORMANCE, 28 FEBRUARY

Equities Market (Local currency)	
United Kingdom	0.78
Japan	-1.16
Switzerland	-1.93
Asia (ex-Japan)	-2.11
Emerging Markets	-2.38
World (all countries)	-2.65
Europe	-2.82
United States	-2.97
China	-3.92

Equities Sector (Local currency)	
Energy	4.89
Materials	1.54
Health Care	-0.64
Utilities	-0.68
Consumer Staples	-0.96
Industrials	-1.75
Financials	-2.91
Real Estate	-3.66
Consumer Discretionary	-4.47
Information Technologies	-4.70
Telecommunication Services	-5.43

Fixed-Income (USD Hedged)	
Global Inflation-Linked Bonds	1.03
Global Aggregate 1-3 Year	-0.39
Global Treasury	-1.02
Global Aggregate 5-7 Year	-1.03
Global Aggregate	-1.33
US Treasury Long Duration	-1.46
Global Convertibles	-1.95
Swiss Bond Index AAA-BBB (CHF)	-2.04
Global Corporate Credit	-2.12
Global High-Yield	-2.42
Global Aggregate Long Duration	-2.75
Emerging Market Hard Currency Aggregate	-4.59

Others (USD)	
Commo Global (ThomsonReuters)	6.20
Commo Industrials (CBR)	1.10
Hedge Funds	-0.11

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