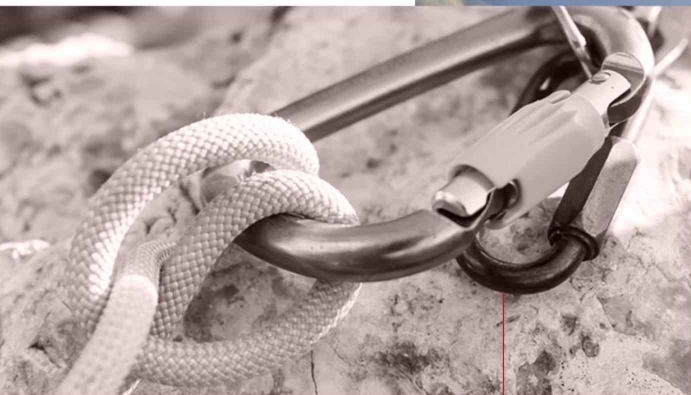


1. Macro and Rates
2. Fixed Income
3. Equity
4. FX and Commodities

Key Take-Aways

- With the lifting of Covid-19 restrictions around the world, February began on a rather optimistic note for the global recovery. But that was without considering Russia's invasion of Ukraine on the 24th of February.
- Markets reacted by sinking into negative territory, volatility increased and commodities, starting with energy, soared.
- While it is impossible to know the extent and final outcome of this conflict, international reactions were not long in coming, with unusually severe sanctions being imposed on Russia.
- The US economy is the least affected by the war in Ukraine. For this reason, we do not expect the Fed to be deterred from tightening rates. Given its energy trade balance, Europe is much more exposed and therefore, we should not expect any rate rise before 2023.
- Geopolitical risks have led to a flight in safe havens over the month. Yield of the 10-year Treasury bond has fallen from 2% to 1.68% and the German 10-year Bunds' yield has fallen back to negative territory.
- In February the S&P 500 fell by 3.1%, while the Euro Stoxx 50 lost 6.0%, bringing the year-to-date performance to -8.9% and -8.7% respectively.
- Russian MOEX Index lost 33.8% in February alone and Russian issuers have fallen to junk literally overnight on the back of the invasion. Eurozone equities were also particularly hit, namely the Euro Stoxx Banks Index (fell 11.7%) due to exposure concerns.
- Conflict in Ukraine has increased supply chain concerns and fueled inflationary pressures. Oil, along with others commodities, has spiked about 60% since the start of 2022, hitting its highest level since 2008.
- US inflation coupled with hawkish comments from the Fed, added even more positive pressure on the USD, with the Dollar Index trading +3.5% higher since the beginning of the conflict and at a 21 months high.

Review: February 2022

Russia and Ukraine

With the lifting of Covid-19 restrictions around the world, February began on a rather optimistic note for the global recovery. But that was without considering Russia's invasion of Ukraine on the 24th of February.

Despite the fact that this event materialized a tension that had been building for a long time, the markets all reacted by sinking into negative territory, volatility increased and commodities, starting with energy, soared. While it is impossible to know what the extent and final outcome of this conflict will be, international reactions were not long in coming, with unusually severe sanctions being imposed on Russia, putting the country in an unprecedented situation that will probably push it to default on its debt, at least because of its inability to make international payments.

The S&P500 closed the month down -3.14% and the Nasdaq down -3.43%, while the Russell 2000 was up 0.97%.

In Europe, the FTSE 100 was slightly down, at -0.08% and the SMI at -1.96%. The correction was more severe for the Eurostoxx50, which ended the month at -6%,

In the rest of the world, the Nikkei was down -1.76%, the Hang Seng -4.58% while Brazil was up 0.89%. The Russian index (RTS $) unsurprisingly ended the month down -34.72%.

In terms of US sectors, energy was the only sector to finish in the green, up 6.37%, while on the other hand, telecoms ended the month down 6.98%, followed by real estate at -5.09%.

The dollar index edged up 0.18%, the EUR/USD depreciated -0.13%, the USD/CHF -1.12%, the GBP/USD -0.19% and the yen -0.14%. The most significant decline was in the ruble, which depreciated by over 26% against the dollar.

The US 10-years yield closed the month at 1.82%, up 4bps. The Bund yield rose by 12bps, ending February at 0.14%. The Bloomberg Global Aggregate Index ended the month at -1.19%, the JPMorgan EMBI at -4%, the Bloomberg Global High Yield Index at -2.39% and the Bloomberg Core Developed Government Index at -0.89%.

Commodities continue to soar, with the Bloomberg Commodity Index up +6.20%. Once again, energy was the main driver, with WTI up +8.59% to end the month at $95.72 Volatility closed February at 30.2, up 5.32%.

Equity % Change	Price	1 day	5 days	MTD	QTD	YTD	EST P/E
S&P 500	4,374	-0.24	0.58	-3.14	-8.23	-8.93	18
Nasdaq	13,751	0.41	1.50	-4.58	-12.10	-12.10	24
Russell 2000	2,048	0.35	1.93	0.97	-8.78	-9.01	19
Euro Stoxx 50	3,924	-1.17	-1.54	-6.00	-8.71	-8.71	13
Stoxx 600 EUR	453	-0.09	-0.37	-3.36	-7.11	-7.11	13
FTSE 100	7,458	-0.42	-0.35	-0.08	1.00	1.00	11
SMI	11,987	-0.00	0.80	-1.96	-6.90	-6.90	16
NIKKEI 225	26,527	0.19	-2.19	-1.76	-7.87	-7.87	15
CSI 300 China	4,582	0.18	-1.14	-0.00	-7.26	-7.26	12
MSCI EM Index	1,172	1.48	-3.89	-3.00	-4.87	-4.87	11

Equity % Change	Price	1 day	5 days	MTD	QTD	YTD	EST P/E
S&P 500	4,340	-0.24	0.58	-3.14	-8.23	-8.93	18
UTILITIES	344	0.43	2.47	-2.32	-5.56	-5.56	18
ENERGY	535	2.57	3.91	6.37	26.54	26.54	13
TELECOM	233	-0.00	1.84	-6.98	-12.92	-12.92	16
CONS STAPLES	780	-1.32	-1.63	-1.50	-3.00	-3.00	20
REAL ESTATE	282	-1.77	0.87	-5.09	-13.19	-13.19	39
CONS DISCRET	1,395	0.60	-1.57	-4.06	-13.37	-13.37	21
MATERIALS	523	-1.18	-0.68	-1.43	-8.19	-8.19	16
HEALTH CARE	1,513	-0.75	1.94	-1.13	-7.95	-7.95	16
INFO TECH	2,677	-0.16	1.13	-5.02	-11.60	-11.60	22
FINANCIALS	640	-1.45	-1.72	-1.49	-1.57	-1.57	13
INDUSTRIALS	843	0.73	1.52	-1.10	-5.81	-5.81	17

Currency % Change	Price	1 day	5 days	MTD	QTD	YTD
DXY	96.704	0.10	0.70	0.18	1.09	1.21
EUR-USD	1.1219	-0.43	-0.80	-0.13	-1.32	-1.42
USD-JPY	114.96	-0.52	0.18	-0.14	-0.11	-0.06
USD-CHF	0.9169	-0.91	0.11	-1.12	0.44	0.44
EUR-CHF	1.0287	-1.43	-0.71	-1.23	-0.86	-0.78
GBP-USD	1.3422	0.09	-1.33	-0.19	-0.82	-0.95
EUR-GBP	0.8359	-0.50	0.54	0.09	-0.63	-0.63
JP EM FX Index	51.79	-2.30	-3.41	-2.91	-1.46	-1.46

10 yr Yield Bps Change	Price	1 day	5 days	MTD	QTD	YTD
US	1.82	-15	-11	4	31	35
Germany	0.14	-10	-7	12	31	31
UK	1.41	-5	0	11	44	44
SWITZERLAND	0.26	-6	1	16	39	39
Japan	0.19	-2	-2	1	12	12
US IG Spread	132	-4	2	16	32	32
US High Yield spread	370	-19	-11	20	100	100
EUR High Yield spread	443	-17	18	57	97	97

Commodity % Change	Price	1 day	5 days	MTD	QTD	YTD
BBG Commo Index	114.6	1.92	2.62	6.20	15.51	15.51
Gold Spot $/OZ	1908.2	1.00	0.10	6.18	4.32	3.84
Crude Oil WTI	95.7	3.38	5.11	8.59	24.33	24.33

Volatility	Price	1 day	5 days	MTD	QTD	YTD
VIX	30.2	2.56	2.40	5.32	75.09	12.93

Source: Bloomberg 2/28/2022

Macro and Rates: With no doubts, the Fed is Hawkish

As the Covid crisis has just began to fade, Russia shocked the world with a unexpected full invasion of Ukraine.

We won't comment on the conflict itself as we are not geopolitical experts. Instead, we will try to draw the global economic and monetary policy impact of the conflict.

First of all, the main impact is on energy.

Ukraine's GDP represents roughly twice the one of Luxembourg while Russian's one is slightly higher than Spain. Both countries make up only a small proportion of World GDP and the crisis should not be able to derail what continues to be a robust global growth. The economic fallout of the conflict appears manageable.

Nevertheless, the spike in commodities and oil prices in particular and the duration of this spike (in fact the duration of the war) will trigger, as a first-round effect, slower growth and more inflation in the coming months.

The first-round effect will not be global. Europe is the most exposed.

Indeed, 21% of the euro zone's energy imports come from Russia. On the other side of the trade, Russia consumes only 2.6% of euro zone's exports. This disequilibrium makes Europe vulnerable to its reliance on Russian energy and Russian gas in particular.

Also, Europe does have some exposure to Russia via its banking sector but this one is rather modest. The exposure of Austria, for example, whose banks have by far the closest links to Russia is limited to just 1.7% of GDP.

Despite Europe current strong economic data, we now expect the ECB to hold back on the removal of liquidity for some time. Inflation from higher commodity prices combine a hit to economic growth will prevent from any ECB tightening. European Consumer Confidence will for sure need to be monitored as the psychological impact of the war and the specter of nuclear war in Europe will for sure have an impact.

The US economy is another story. The vulnerability of the US economy to higher oil prices is considerably lower than previous spikes in 2007 and 2008.

At the time, the country ran a USD 30 billion monthly trade deficit in petroleum products. Today, thanks to the expansion of domestic production, the balance is flat. Therefore we expect the US economy to be the least affected by the war in Ukraine. For that reason, we do not expect the Fed to be deterred from tightening. While a 50 basis point hike looks unlikely (but not impossible), the trend clearly remains on track towards monetary tightening. As the above-trend US growth will likely remain immune to the war in Ukraine, we expect the Fed to be able to maintain its tightening campaign. However, aggressive rate hike anticipations like the one observed earlier this year won't likely repeat given the current environment.

The situation is terrible for Ukraine and the world, and dangerous for markets, which will remain volatile. Assuming some reasonable level of de-escalation, the current situation will nevertheless brings downside risks to growth and upside risks to inflation. However, US and Europe are not in the same positions. Given its energy trade balance, Europe is much more exposed and therefore, we should not expect any rate rise before 2023. In the US, the economy is comparatively more immune from inflationary pressure and therefore the Fed will keep the window opened to start its monetary normalization.

Fixed Income: Stagflation?

In February, Russia invaded Ukraine thereby sending commodities prices even higher. Especially soft commodities joined the general upswing in prices as supply from "Europe's breadbasket" will be hit.

The increased geopolitical risks have led to a flight to safe havens over the month. Thus, the yield of the 10-year Treasury bond has fallen from 2% to 1.68% and the German 10-year Bunds' yield has fallen back into negative territory on the first day of March after trading as high as 0.3% in February.

The US yield curve has flattened especially in the middle, e.g. the 3 to 10 year maturities. The short end moved less as the market continues to price-in a Fed lift-off on March 16. The probability of a 50bps hike, however, has fallen sharply and only a 25bps hike is priced-in. In a sense, the geopolitical situation has helped the Fed.

Macro economic data from the US continues to be mixed. While the last ADP Employment change, a lagging indicator, the ISM Services Index, a leading indicator, came in weaker than predicted by the survey.

While a certain slowing of the economy was to be expected following the extraordinary rebound after the pandemic, some indicators point to a much weaker growth for the coming months. The Atlanta Fed estimates that growth in the US will be zero in the first quarter of this year.

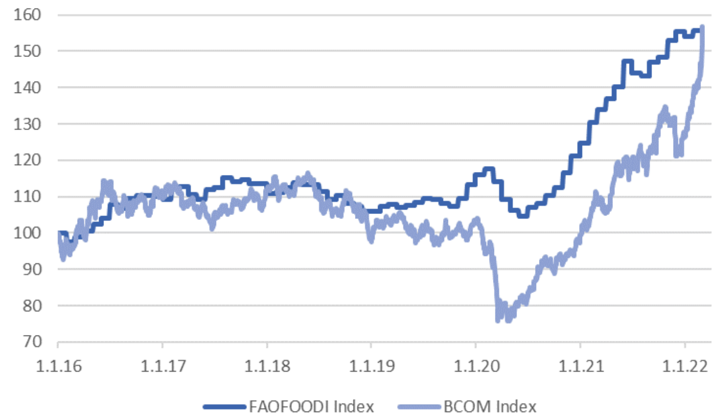
Currently we are witnessing two developments: on one hand inflation remains higher, and on the other hand growth dynamics seem to be stalling. Geopolitical risks may well accentuate these trends, and this is why the word stagflation is in everybody's mind.

February was also a month where holding "risk-free" government bonds helped stabilize portfolios under pressure from falling equities. Investment grade and high-yield spreads, however, continued to widen.

Russian issuers have fallen to junk literally overnight on the back of the Russian invasion of Ukraine. Other Emerging Market issuers have felt the pressure, too.

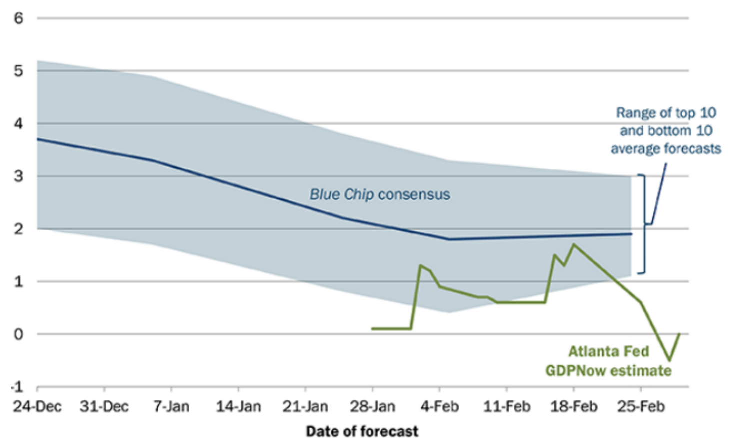
We recommend a careful stance in fixed income for now and to focus on "return of capital" vs. "return on capital".

UN Food & Agriculture World Food Price Index and Bloomberg Commodity Spot Index, rebased 1.1.2016



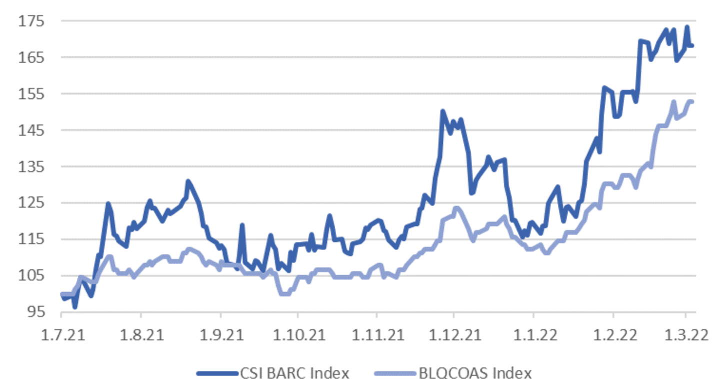
Source: Bloomberg

Evolution of Atlanta Fed GDPNow real GDP estimate for 2022: Q1



Source: Bianco Research LLC

US Investment Grade and HY spreads Rebased at 100 as of 1.7.21



Source: Bloomberg

Equity: The escalation of Russia-Ukraine conflict leads indices further into correction territory

With increasing interest rate expectations and as tensions between Russia and Ukraine deteriorated throughout the month, culminating in a full-scale military conflict on the 24th of February, markets reacted negatively with investors in a risk-off mode. In February the S&P 500 fell 3.1%, while the Euro Stoxx 50 lost 6.0%, bringing the year-to-date performance to -8.9% and -8.7% respectively.

Russia sanctions pressures foreign companies with exposure to the country.

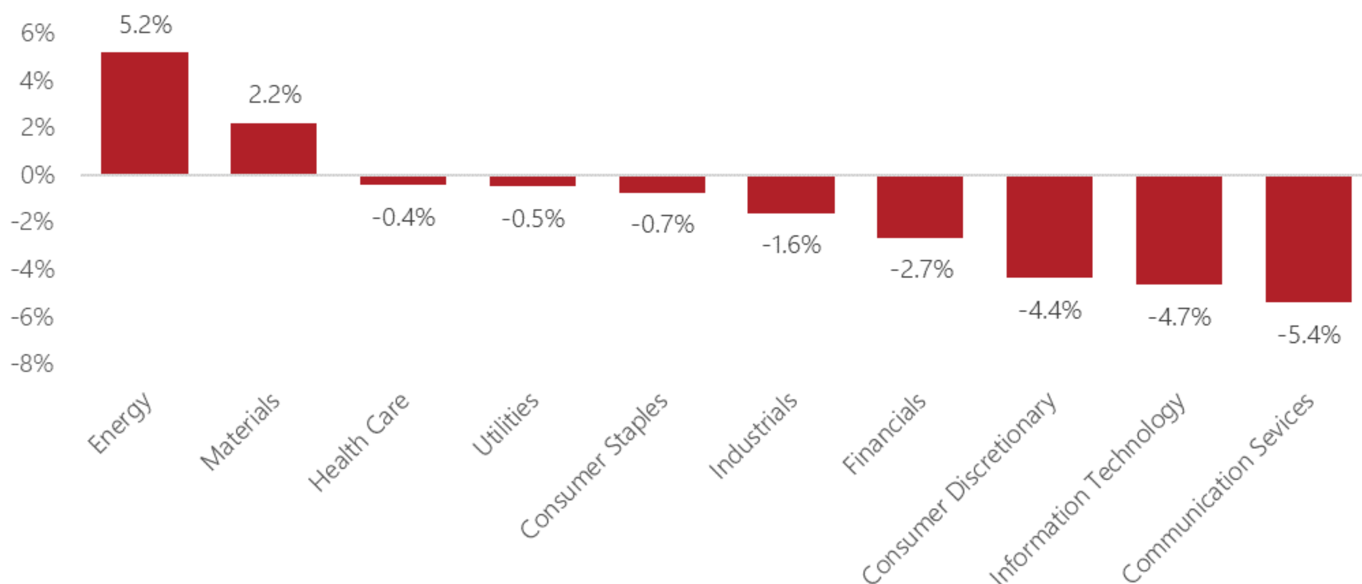
As a retaliation for invading Ukraine, most western countries announced strong sanctions against Russia, crippling the country's economy. As a result, the Russian MOEX index lost 33.8% in February alone. Eurozone equities were also particularly hit, namely sectors and companies with higher exposure to Russia. The Euro Stoxx Banks Index fell 11.7%, with Western European banks having approximately USD 91 billion total claims on Russian counterparties as of end-September 2021, according to the Bank for International Settlements (BIS). Société Générale (-21.7% in February) and UniCredit (-18.7% in the month) are two of the European banks with largest operations in Russia, which represent less than 5% of the groups' activity.

Geopolitical tensions outweigh a solid earnings season.

In a month that was dominated by tensions in Europe, the earnings season was quite solid with 76% of companies in the S&P 500 that reported earnings positively surprising and EPS on average growing 31% y/y (marking the fourth straight quarter of above 30% earnings growth). In Europe the tone was also positive, of the companies that presented results, 64% presented higher EPS than expected.

Energy and Materials sector in the green.

Disruptions in the supply chain have justified inflation reaching levels not seen in over a decade and have led to markets expecting several rate hikes this year by the Federal Reserve. The conflict in Ukraine has increased supply chain concerns, namely in the energy sector, as Europe rethinks its dependency on Russia. This led to significant increase in the oil price with the WTI ending the month at just under USD 100/barrel, marking the third straight month of strong gains. The conflict has also led to a rise in agriculture commodities, as Russia and Ukraine are responsible for more than 25% of global wheat exportations. This further fuels inflationary pressures and justified the good performance of these sectors in February.



Forex And Commodities: Seek Refuge in Safe Haven Positions, EUR/ CHF Reaches Parity

As the global economy was already grappling with inflationary pressures, Russia's invasion of Ukraine and harsh international sanctions have introduced geopolitical anxiety on global currencies and commodities, lifting up the Dollar, CHF, Gold and slumping EUR on the back of a Crude oil rise.

The Dollar index traded +3.5% higher since the beginning of the conflict (a 21 months high). As the intensifying war in Ukraine prompted safe haven flows, US inflation coupled with hawkish comments from Fed, added even more positive pressure on the USD. However, a decline in US dollar investor bullish sentiments is now observed. The value of the net long EURUSD position sees a net increase since December and tend to continue end of February. If the decline in USD sentiment should continue, it could put a slight break on the momentum in the greenback.

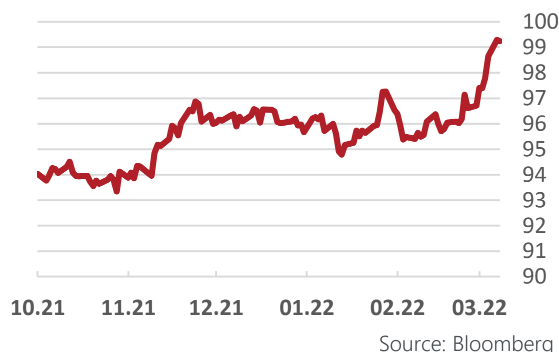
While the dollar strengthens, the euro slumped to a fresh low as soaring crude prices raised fears. Europe is vulnerable as it imports as much as 33% of its natural gas consumption from Russia and the EUR currency has become increasingly correlated with oil prices. The higher oil climbs, the more the euro shall fall as investors fret about higher inflation and the blow to the economy. The ECB will face hard decisions to make in rising price environment, it will likely decide in favor of a faster taper of its net asset purchases.

The euro also briefly sank below parity versus safe-haven Swiss franc for the first time in seven years as investors sought refuge in the Swiss currency. The CHF continues to be highly valuated and a drop below parity could be a danger for Switzerland's export-dominated economy. It could break plan from the SNB to retreat from negative interest rates in the short term. EM currencies are suffering drastically. JPMorgan Emerging Market Currency index, saw a decline of its value by more than 8% vs the USD.

Gold has skyrocketed above the resistance level of 1,950 per ounce, lifted by demand from investors nervous that the extension of war could spark losses in other investments classes. Investors prize gold for its stability in times of turmoil. Despite being shy at the beginning of the invasion, the sensitivity of the precious metal in now perfectly reflecting the current geopolitical tensions. Being driven by short-term tactical interest, the price of the ounce is likely to maintain above a 2,000 support in the upcoming days, its highest value since August 2020.

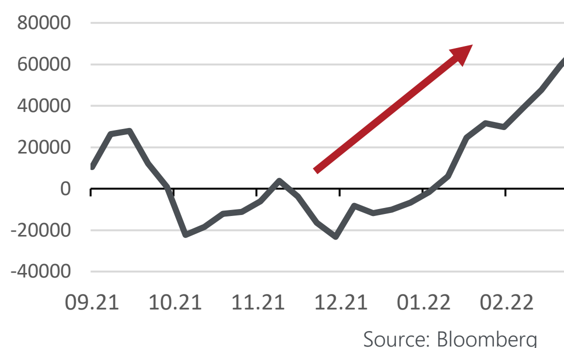
Oil, along with others commodities, have spiked about 60% since the start of 2022, hitting its highest level since 2008. There are no reasons to imagine a reverse of the situation in a short-term perspective as Russia represented nearly one third of world exportation and is now banning from import by world sanctions and new risk of embargo. If disruption worsen or continue in a longer period, we could see Brent moving above USD 150 per barrel.

US Dollar Index soon testing the 100 level ?



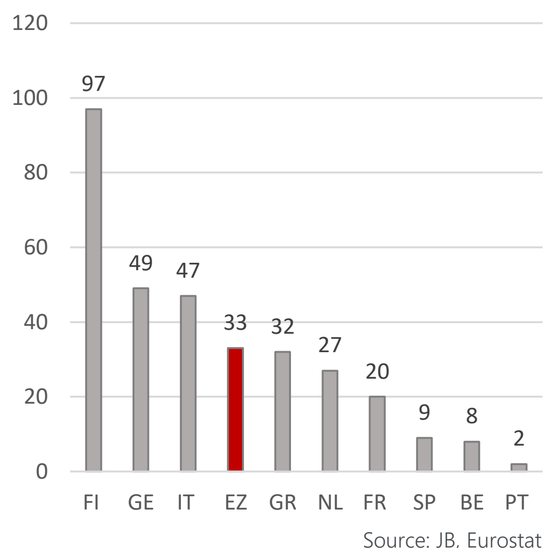
Source: Bloomberg

Net long EUR /USD position. Negative sentiment for USD ?



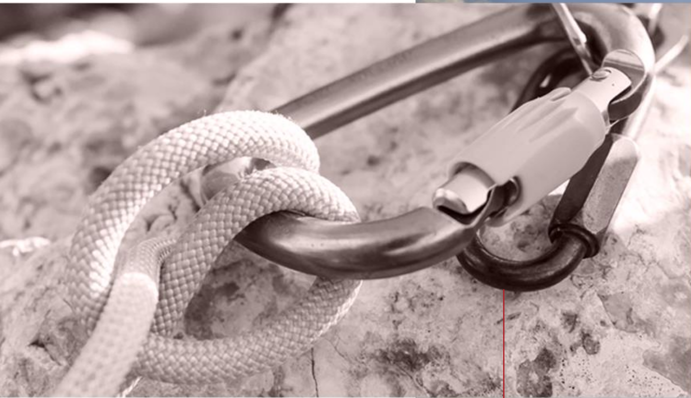
Source: Bloomberg

Eurozone gas import from Russia. Is the Eurozone too dependent ?



Source: JB, Eurostat

Source: Bloomberg , WSJ, Reuters



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