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Where to hide?

April 2022

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# Global inflation pressures compounded by Ukrainian conflict

G10 inflation surprises make new highs – FAO food index continues to climb

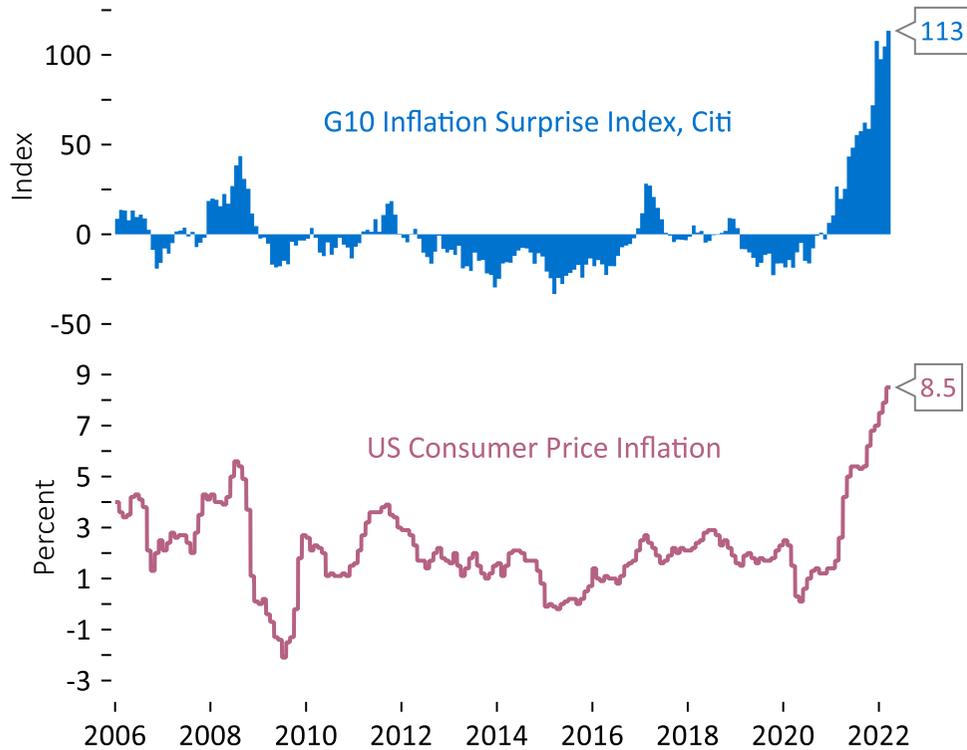


## Inflation surprises continue to climb across G10



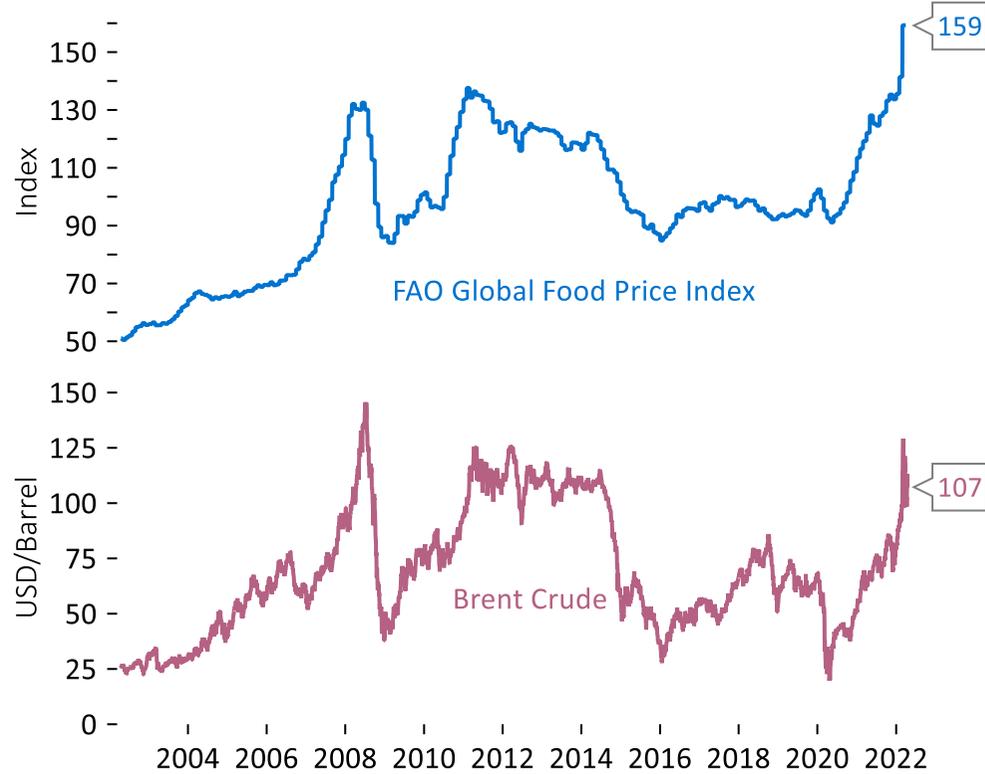
## Global food prices touch new highs

### Inflation surprise index and US CPI



Source: Macrobond, 20.04.22

### Food and oil prices



Source: Macrobond, 20.04.22

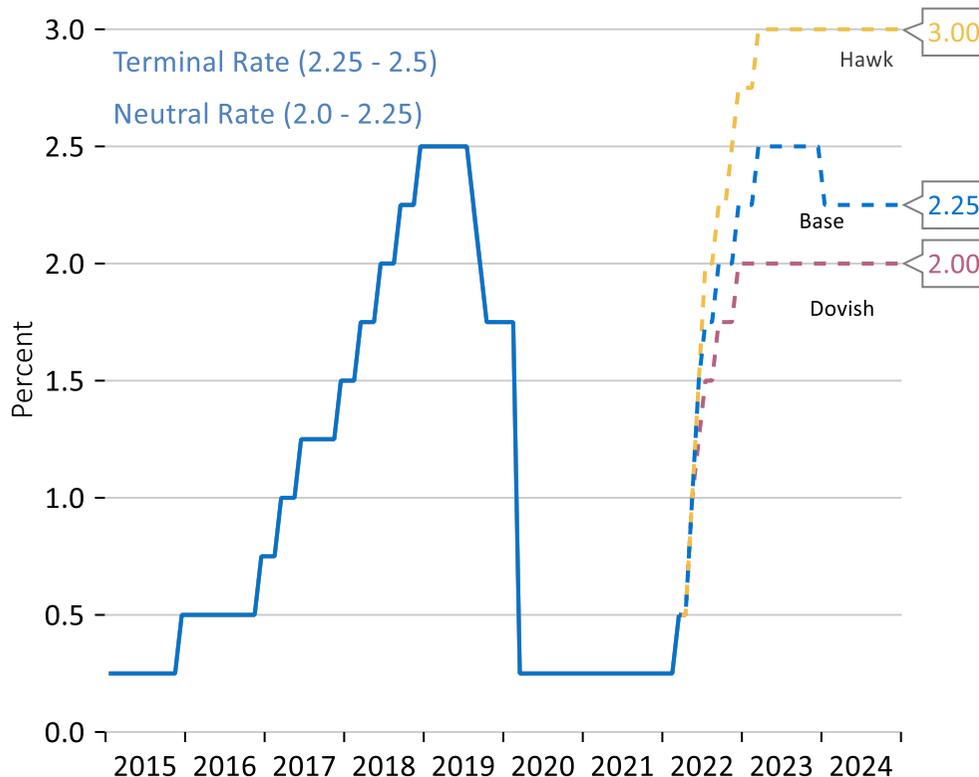
# Policy normalisation: Faster tightening- uncertainty prevails

A highly uncertain phase for policy



## Trajectory for US rates

### Path of policy normalisation in the US



Source: Macrobond, 21.04.22

## Assumptions

- **Neutral rate:** 2.25%
- **Base:** Economy slows to below trend (circa 1.5%) as Fed takes rates above neutral. Similar playbook to 2015 -2019
- **Dove:** Sharp slowdown in economy in 2023 prevents full normalisation. Economy slows to stall speed - below 1%.
- **Hawk:** Economy slows to trend (circa 2%) as Fed takes rates above neutral to bring unemployment back to natural rate.

## Unknowns

- *Impact of Balance Sheet unwind (QT)*
- *Monetary policy works with 'long and variable lags' as US is a highly dis-intermediated financial system*

# Asset class performance 2022-to-date

Equity recovery fades - bonds decline – Dollar stronger – volatility picks up modestly



Equities rally, bonds decline & gold leads returns



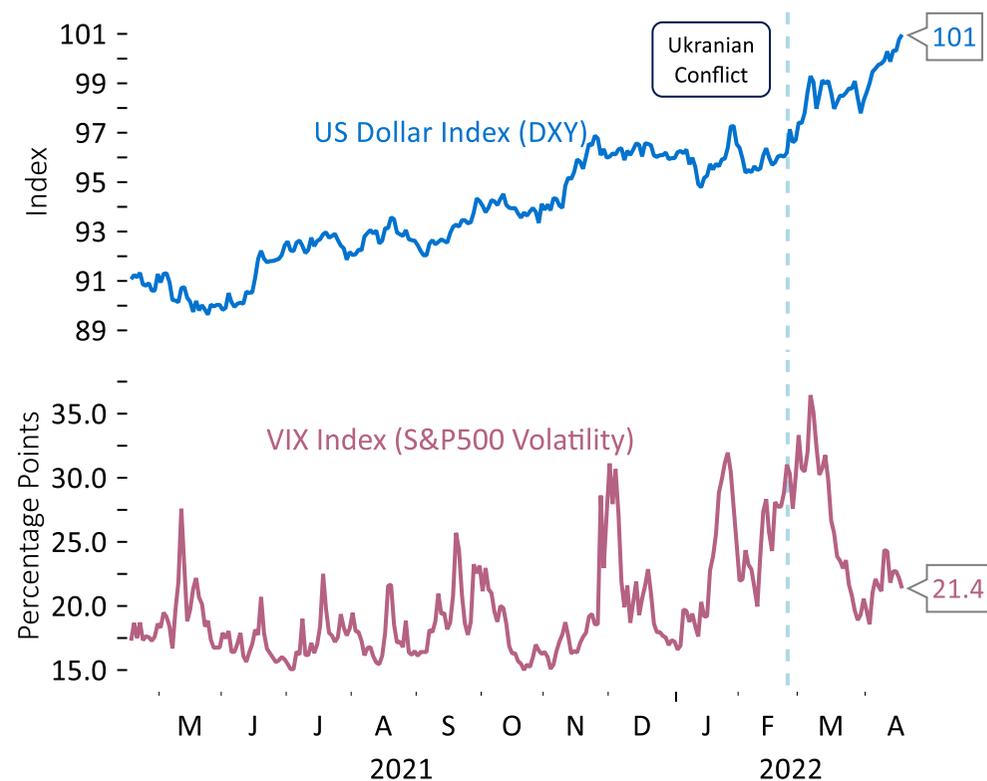
Dollar rally continues – volatility subsides

Global Asset Class Returns 2022 to date



Source: Macrobond, 21.04.22

US Dollar index and equity volatility (1Y)



Source: Macrobond, 20.04.22

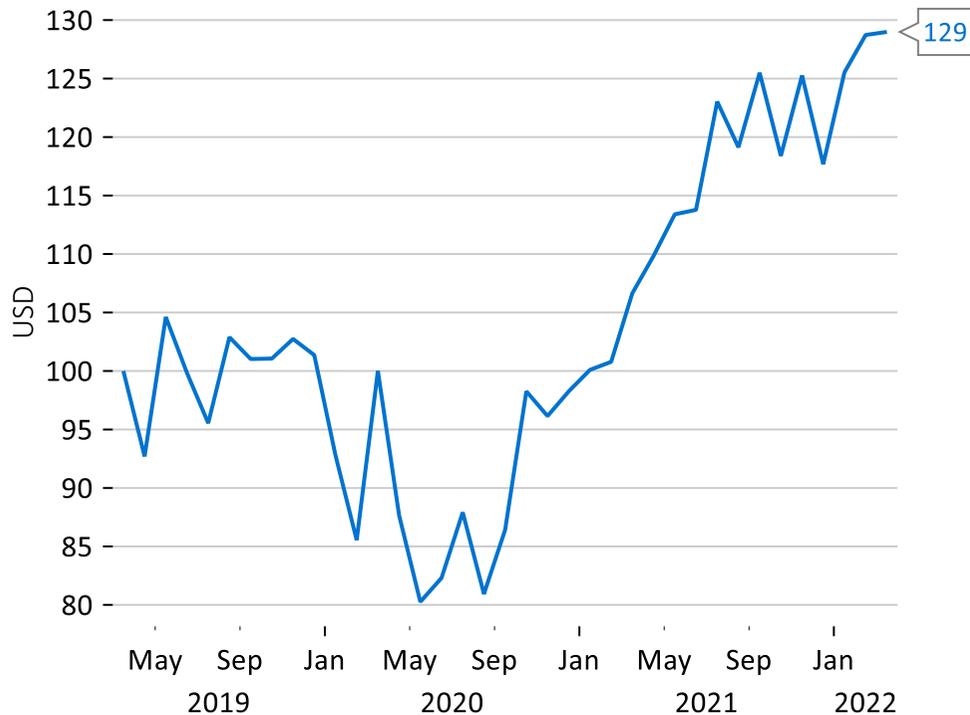
# Where do we see opportunities in risk assets?

## 1. Corporate earnings recovered rapidly in 2021 while valuations have moderated



Global earnings now well surpass pre-COVID levels

Global Earning Per Share (EPS) 1 year forward (FactSet)  
(Factset 31/12/2018 = 100)

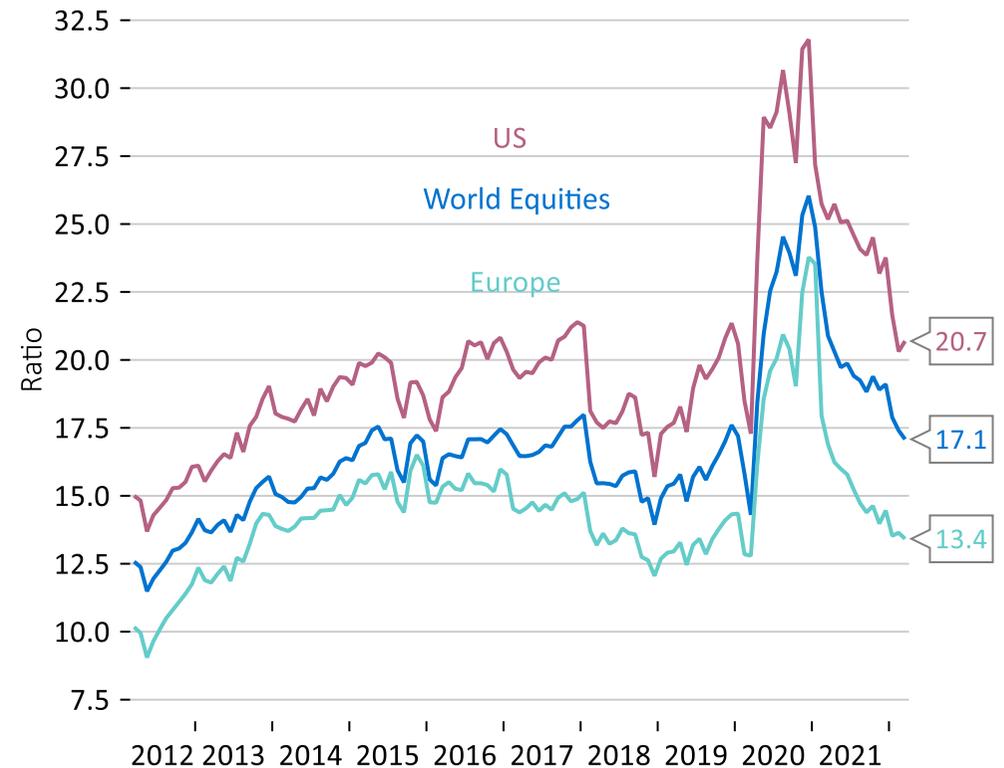


Source: Macrobond, 20.04.22



Equity valuations have moderated

Equity Indices 1 year forward PE (Factset)



Source: Macrobond, 20.04.22

# 2. Achieving net zero by 2050 will require a transformation of the global economy & unprecedented capital spend



Net zero 2050 needs \$9.2tn pa of spending on physical assets

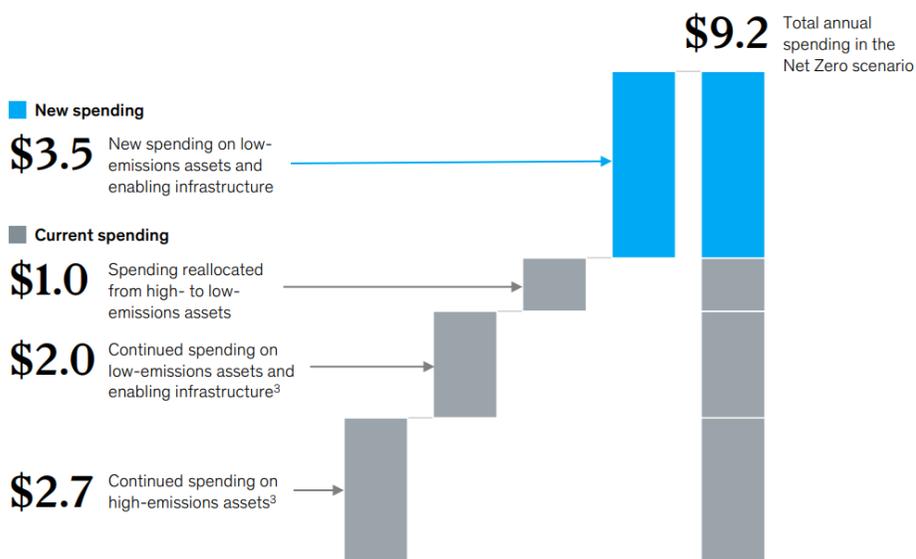


All global sectors will need to act together to meet 2050 goals

Exhibit E5

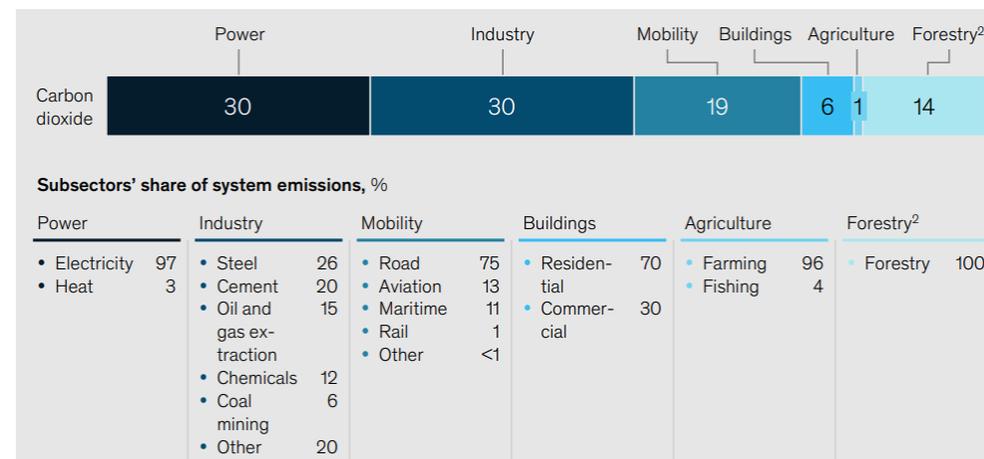
Spending on physical assets for energy and land-use systems in the NGFS Net Zero 2050 scenario would rise to about \$9.2 trillion annually, or about \$3.5 trillion more than today.

Annual spending on physical assets for energy and land-use systems<sup>1</sup> in the Net Zero 2050 scenario,<sup>2</sup> average 2021–50, \$ trillion



Power and industry are major energy consumers and together generate about 60 percent of CO<sub>2</sub> emissions.

Share of emissions<sup>1</sup> per energy and land-use system, 2019, %



Source: McKinsey Center for Future Mobility Electrification Model (2020); McKinsey Hydrogen Insights; McKinsey Power Solutions; McKinsey–Mission Possible Partnership collaboration; McKinsey Sustainability Insights; McKinsey Agriculture Practice; McKinsey Nature Analytics; McKinsey Global Institute analysis

# Ukraine conflict impacts growth but recession risk still low

## *Favour alternatives – neutral equities - cautious bonds*



Global strategy update – April 2022

<b>Bonds</b>	<p><b>Strong underweight</b></p> <ul style="list-style-type: none"> <li>• Strong UW Government Bonds – global inflationary pressures remain elevated</li> <li>• UW Investment Grade Credit – yield spreads too narrow – UK charity &amp; infrastructure issues offer social impact benefits</li> </ul>
<b>Equities</b>	<p><b>Neutral</b></p> <ul style="list-style-type: none"> <li>• Global Neutral – earnings slow but value attractive outside of the US</li> <li>• UK Neutral - dividend support and valuation attractive – M&amp;A likely</li> <li>• EM Neutral – rising Dollar and tighter rates a challenge – China policy support significant</li> </ul>
<b>Alternatives</b>	<p><b>Strong Overweight</b></p> <ul style="list-style-type: none"> <li>• OW Other Alternatives– infrastructure and renewables beneficiaries of fiscal spend – inflation linked returns attractive</li> <li>• OW Uncorrelated Alternatives – gold effective hedge against policy error</li> </ul>
<b>Cash</b>	<p><b>Strong Overweight</b></p> <ul style="list-style-type: none"> <li>• No currency preference</li> <li>• Consider opportunistic portfolio insurance</li> </ul>
<b>Risks</b>	<p><b>Current:</b> Valuations stretched, bond market risk as policy tightens, inflation higher for longer on energy shock</p> <p><b>Longer-term:</b> Central bank policy error, China/Taiwan, real bond yields normalise, climate transition risks</p> <p><b>Ukraine:</b> Russia ceases European gas exports, NATO dragged into border war, further nuclear warnings</p>

Source: Sarasin & Partners, April 2022

# Important information

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