

February  
2022

# XPS Investment News

Bringing you our market round-up and the latest news affecting UK pension scheme investments

## Month in brief

- US equities suffered their worst month since the beginning of the pandemic and many stocks frequently experienced wild intra-day price swings
- UK gilt yields continued to rise sharply
- The Bank of England announced on 2 February that it was increasing interest rates from 0.25% to 0.5%



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Felix's February update

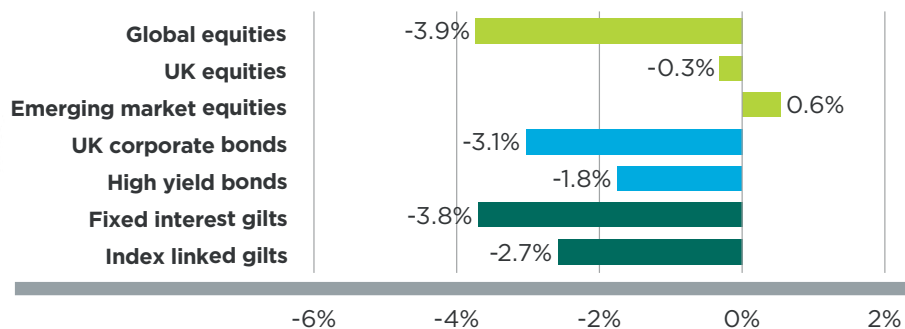
## A turbulent start to 2022 for investment markets

Investment markets saw large, volatile, movements throughout January as investors grew concerned about various challenges global economies and markets face. Snowballing inflation levels have necessitated preparations by central banks to tighten monetary policy at a faster pace than previously thought.

US equities suffered their worst month since the beginning of the pandemic; the S&P 500 and the tech-heavy Nasdaq fell 5.3% and 9%, respectively, which would have been worse if not for a strong equity up-tick during the last couple of days of the month. Many stocks experienced wild intra-day price swings and the sell-off was particularly prominent in technology and growth stocks, where valuations have long been considered stretched, although broader sectors were not immune. Companies such as Netflix, Spotify and Tesla all experienced double-digit price falls over the month. UK equities, where valuations have been significantly lower, generally fared better.

Investors have seen a marked shift in tone from the US Federal Reserve ('the Fed'), which has become increasingly hawkish on inflation. At its January meeting, Jay Powell, chair of the Fed, strongly indicated that it is planning to start the rate rising cycle in March. He also confirmed it will now finish its bond-buying programme in early March. The speed of this bond-buying wind-down and his refusal to rule out a more aggressive string of interest rate rises surprised investors. Markets are now pricing in almost five US interest rate hikes in 2022 compared to three previously. Higher interest rates reduce the value that investors place on future earnings which can affect equities, as well as bond markets.

### Emerging market equities were the strongest performer over the month One Month to 31 January 2022



Source: Refinitiv Datastream



Geopolitical tensions, particularly in Europe, also weighed on market sentiment. The West remains in a stand-off with Russia, who appear to be using the threat of an invasion of Ukraine to achieve a series of 'security guarantees'. The outcome of this situation remains uncertain and could have significant repercussions for the world, both politically and economically.

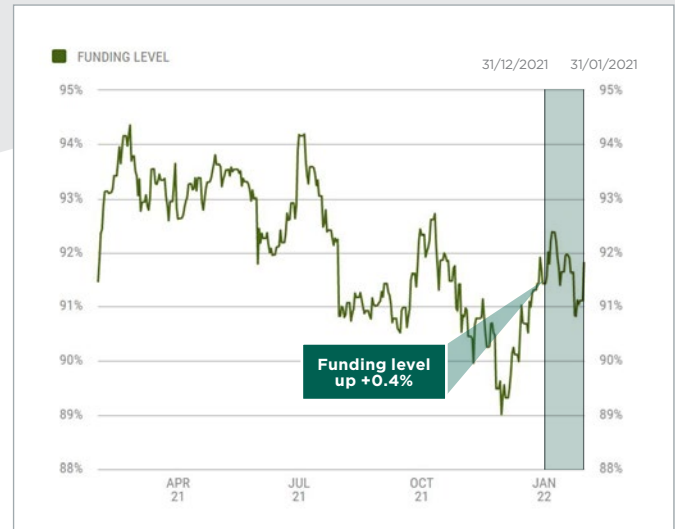
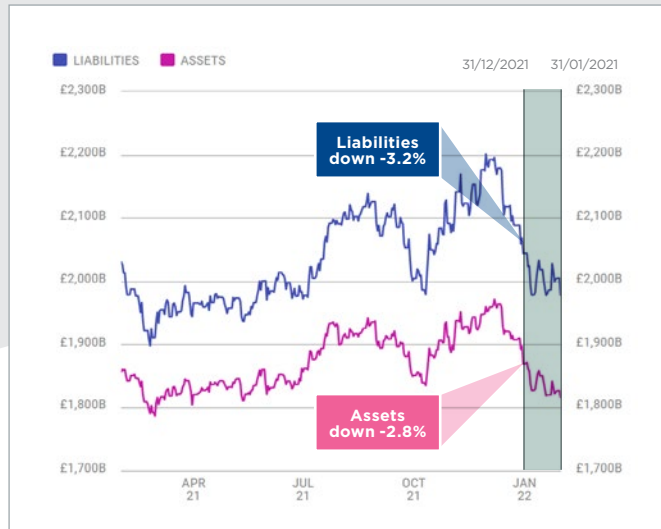
The credit spreads of corporate bonds widened, reflecting a perceived increased risk of default. Coupled with the rise seen in gilt yields, this led to a tough month for investment grade and high yield corporate bonds.

GDP data released in January for the UK showed that the economy surpassed its pre-pandemic level for the first time in November. Whilst growth globally continues to be

strong, there remains signs that it is slowing. The continued spread of Omicron globally is likely to be one of the factors contributing to this slowdown, although the impact will be more limited in countries with high vaccination rates.

UK gilt yields continued a remarkable increase seen since early December as investors shifted their expectations around the policy action required to tackle inflation. The 20-year gilt yield ended the month 0.6%pa higher than it was at its lowest point in December 2021. The Bank of England increased interest rates at its February announcement from 0.25% to 0.5%. CPI hit 5.4% in the UK in December.

The estimated aggregate funding position of UK DB pension schemes, on a long-term basis, whipsawed over January, but ended modestly higher as a result of higher gilt yields.



Source: XPS DB:UK [www.xpsgroup.com/services/xps-pensions/xps-dbuk-funding-watch](http://www.xpsgroup.com/services/xps-pensions/xps-dbuk-funding-watch)

The charts above are based on data from The Pensions Regulator, the PPF 7800 Index and the XPS data pool. The assumptions used in the UK:DB long-term target basis include a discount interest rate of gilt yields plus 0.5%. The assumed asset allocation is 16.9% equities, 20.0% corporate bonds, 6.9% multi-asset, 5.1% property, 3.8% private markets and 47.3% in liability driven investment (LDI) with the LDI overlay providing a 60% hedge on inflation and interest rates.

**To discuss any of the issues covered in this edition, please get in touch with Felix Currell.**



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