TARENO

INTERNATIONAL
ASSET MANAGERS

TARENO VIEW Q2 2022

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MARKET COMMENTARY

Review

The Russian invasion of Ukraine took the world by surprise in late February 2022. In addition to the human tragedies and personal suffering caused by the war, global markets and international price developments are also affected. The entire impact is not entirely foreseeable yet.
The current war plays a decisive role, on the one hand because of Europe's high dependence on Russian imports in the energy sector, and on the other hand due to Ukraine's substantial food exports.
A shift in Western investment preferences, towards military equipment, and the financial sanctions imposed on Russia have unleashed a spillover effect on the entire global economy, which consequences are higher inflation rates and in the worst case scenario numerous famines in developing countries.
The markets reacted with strong markdowns, but were able to stabilise again to some extent towards the end of the quarter; some of the inflation indicators were well above expectations.

Bonds

In line with expectations, the Fed opted for a first 0.25% rate hike, which is also the first increase since December 2018. In response to macroeconomic developments, the Fed announced that further rate hikes can be expected in 2022.
The ECB also hinted at the possibility of a rate hike, but left the current rate at 0% in its last meeting. At the same time, bond purchases are expected to end in Q3 2022.

Inflation forecasts for 2022 have been revised upwards in almost all currency areas, which should lead to a dynamic development of risk premiums.

Equities

Due to both the economic effects of the Ukraine war and the sanctions against Russia, global stock markets fell sharply from mid-February onwards, which they have not yet been able to recover. In particular, the renewed disruption of international value chains led to financial distortions. The immediate announcement by NATO and other European countries to increase their defence budgets particularly benefited military suppliers and their subcontractors. Russian supply companies, which were subject to strict sanctions, were left out in the cold.

Alternative Investments

At the beginning of the Russian invasion, the price of gold rose to USD 2,070 at times. Although the financial environment, which is strongly dominated by fear, has caused the price of gold to fall significantly below this level, it is still very high at USD 1,930. In times of global uncertainty, gold continues to offer a safe haven.
Bitcoin remains a volatile investment, which can be seen in its performance during the first quarter. In early January, it was trading at around USD 45,000, dropped to USD 36,000 in the meantime and is currently at USD 47,000. A continued high volatility remains the most likely scenario.

ECONOMY

The annual inflation rate in the US was 7.9% in February, the highest value since 1982. The annual inflation data from the euro area is also well above the long-term price target of the common currency at 5.1%.

The announced national government transfers and especially the so-called leading indicators underline that considerably higher inflation rates are to be expected in 2022, compared to what we were still forecasting in the last quarter of 2021. In particular producer prices, mainly driven by high energy costs, are over +30% in the EU.

Economies and societies are currently facing the coronavirus and its negative consequences as well as global energy and food shortages. It remains to be seen whether the tighter interest rate policies of the national central banks will lead to a decline in economic growth with falling inflation rates or to stagflation. Both scenarios represent tremendous challenges for us.

OUTLOOK

The war in Ukraine is clearly affecting the sentiment of investors and is causing a persistently high level of uncertainty. It is not advisable to pay too much attention to the media coverage. Instead, we keep an eye on current market developments and try to deduce future developments. That the stock markets have been able to recover in recent weeks shows clearly that markets do not expect a further escalation of the conflict. The recovery of the euro from its lows also indicates that sentiment is calming down. Overall, markets are likely to follow a slight upward trend in the coming quarter while volatility continues to remain at a high level.

The conflict in Ukraine has somewhat overshadowed other disruptive factors, such as persistently high inflation, supply chain distortions and rising interest rates.

High inflation will continue to preoccupy investors and central banks for some months before relief is seen. Even if central banks maintain their restrictive stance, upward pressure on interest rates is likely to ease. This would be a positive sign for equity markets, which is why we continue to favour this asset class.

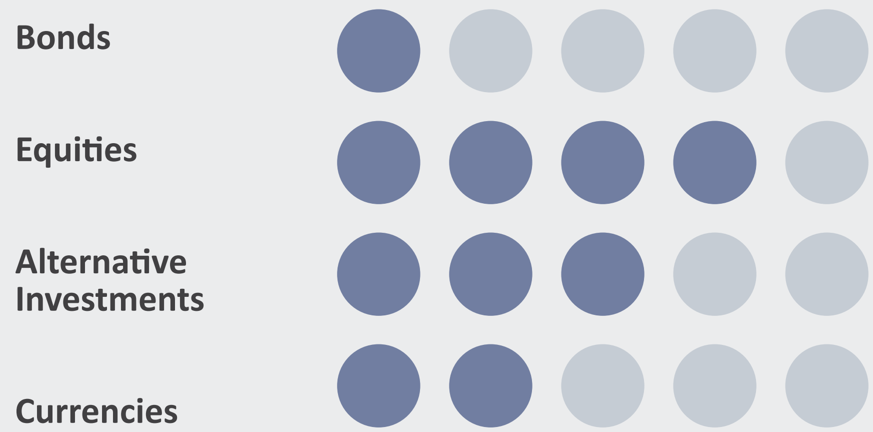
The corporate reports for the first quarter of 2022 will provide information as to which companies are able to survive in this challenging environment. There will certainly be big differences depending on the region, sector and company. For us as active investors, opportunities will arise as a result.
Be assured that we are following geopolitical developments carefully.

INVESTMENT POLICY

Asset allocation

Our assessment of the attractiveness of various asset classes remains largely unchanged. The current environment will remain challenging, especially for bond investors, and will require active management of the bond portfolio. We consider equities more attractive than bonds, as they offer better protection against inflationary depreciation in the current environment. We prefer companies that can adjust their prices and pass on inflation to their customers. We see great diversification potential in alternative investments and have opted for a tactical increase. With regard to currencies, we continue to maintain an active management. We remain largely in the reference currency of the mandates and keep foreign currency exposure low.

Positioning



The chart shows the Tareno PM’s current assessment of its relative attractiveness compared to other asset classes. The more blue dots, the more attractive.

Bonds

Inflation data well above the target range in the United States and the Euro area should prompt the Fed to raise rates by 50 basis points in each of the next two meetings. With these monetary policy measures, we expect yields at the long end of the yield curve to fall over the course of this year. Yield curves are likely to remain partially inverted, especially in the US.

We continue to prefer first-class corporate bonds to government bonds. Due to the generally higher interest rates and the uncertain economic situation, we focus our credit selection on A/AA borrowers, as well as on solid and cash-flow-strong BBB's, since we believe that the risk is best compensated in these categories. Interesting selective investment opportunities are also available in the lower BBB/BB+ range, where we will continue to keep the duration low

Equities

From now on, central banks will have to fight inflation by raising interest rates and reducing their balance sheets, while at the same time managing a soft landing. The excessive inflation will most likely be only temporary, while we have to expect a long-lasting higher inflation regime, unlike the last 10 years.

The stock selection filter should therefore be adjusted to high-margin companies with a certain pricing power, if that has not already been done, as these stocks tend to cope much better with the challenging environment. On the one hand, this is due to the higher purchase prices, which they can partly pass on to customers, and on the other hand, the margin strength provides the companies with an advantageous buffer against competitors. These companies can be found regardless of sector, so it is not explicitly a sector-specific phenomenon.
Careful stock selection is therefore required in order to outperform the market even in this market phase.

Alternative investments

We increased our alternative investments by purchasing a private equity fund from a renowned and globally active provider. Furthermore, we are still invested in gold and bitcoin and have recently increased the weighting in gold.

We see the private equity market as an attractive investment opportunity due to its diversification, the enormous market range and the historically lower volatility compared to the equity market.

On the one hand, we assume that inflation, which has recently risen sharply, will cool down again but remain at a higher level. On the other hand, due to the Fed's limited margin of manoeuvre, we expect real interest rates to remain negative in the short term. For this reason, we already increased our gold position at the beginning of the year.
We are holding on to our bitcoin position due to its disruptive potential. We take the higher volatility of this investment into account with a low weighting of approx. 1%.

Currencies

We maintain an active currency management, in which we keep the weightings in foreign currencies very moderate. The performance volatility which may be triggered by foreign currencies should not be disregarded.

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