Watson Moore
INDEPENDENT FINANCIAL ADVISERS LIMITED

Monthly Investment Update
March 2022

Contents:

Performance Update

The FTSE 100 actually rose in February by 0.31%, but most stock markets suffered falls. The FTSE 250, S&P500, Japan and Europe fell 3.74%, 3.00%, 1.80% and 3.90% respectively. Our portfolios fell between 0.54% and 2.31%. The FTSE 100 advanced as it comprises a lot of oil/gas and mining companies, which benefitted from increases in commodity prices.

We are all shocked and deeply saddened by the Russian invasion and our hearts go out to the millions of people affected. From the news headlines we would have expected stock markets to be significantly lower, but stock markets have no feelings especially in the horrible days of wartime like today and ghastly to say, wars can be good for stock markets in the long run. The S&P 500 was significantly higher in the few years after the Gulf War started.

The biggest economic impact of the invasion will be on the commodity supply chain and prices. February saw Oil, Wheat and Gas up 8.25%, 11.92% and 31.52% respectively. Global energy prices had already been rising significantly and we are all braced for the forthcoming rise in our bills. It is likely that Putin believed that European governments were less willing to retaliate with firm sanctions or otherwise, due to the threat of interrupting energy supplies and thus compounding our inflationary problems. It is no coincidence in the timing. However, Putin has underestimated the economic sanctions imposed and military assistance by the West.

Bonds also suffered losses for their third consecutive month, with the price of UK corporate bonds falling by 2.65% and UK Gilts by 2.24%. Normally safe havens like bonds rally in times of uncertainty but they are more concerned that inflation will move even higher due to higher energy and food costs.

Our lower risk portfolios have completed a further de-risking, increasing their cash position significantly. This is now the third monthly rebalance that has seen cash positions increase for them. The positions held in gold and commodities are performing very well and offsetting some of the equity losses. There is also now very little held in Bonds, further protecting the portfolios.

Some good news is that the global economy continues to re-open following milder symptoms from omicron.

The performance of the portfolios over the last month, 6 months and 1 year is shown below:

Portfolio	Performance % 1 month	Performance % 6 months	Performance % 1 year
Foundation	-0.60	-2.44	5.74
Cautious	-0.54	-3.25	5.26
Balanced	-0.56	-3.19	6.38
Adventurous	-1.51	-4.71	6.67
Dynamic Equity	-2.31	-5.89	8.29
Income Generating	-2.18	-2.00	8.71
Fourth Industrial Revolution	-2.21	-14.47	-3.74
Retirement Investment Solution 1	-0.81	-3.75	6.42
Retirement Investment Solution 2	-1.06	-4.17	6.63
Retirement Investment Solution 3	-1.28	-4.55	6.81

Please note that these figures do not include the platform or Watson Moore's fees.*All figures are sourced from Financial Express to 28.02.2022.

Trend Following Signals

The table below shows whether the asset class is in a positive trend (✓) or a negative trend (x). The portfolios will have more exposure to those asset classes in a positive trend and less (if any) to those in a negative trend. These are the main asset classes we monitor:

Asset Class	Trend Signal		Trend Signal
Global Equity	x	Emerging Market Equity	x
UK Equity	✓	Commodities	✓
Europe ex UK Equity	x	UK Corporate Bonds	x
US Equity	x	UK Corporate Bonds (Short dated)	x
Japan Equity	x	UK Index-Linked Bonds	x
Pacific Equity	x	Global Bonds	x
Gold	✓	UK Gilts	x
Global Property	✓	Emerging Market Bonds	x
Global Infrastructure	✓	Overseas Corporate Bonds	x

Most equity markets are now below trend, including the US. All bond markets are now below trend.

Cautious, Balanced and Adventurous portfolios

These portfolios are now much more defensive, having a higher weighting in cash. They have reduced risk on the first day of each month in 2022 and exposure to US and global stock markets was reduced this month, as well as technology stocks as they moved below trend. Inflation-linked UK bonds were also sold, meaning that there is now no bond exposure in the portfolios.

Dynamic Equity portfolio

The Dynamic Equity portfolio will be highly correlated to global stock markets and will thus experience falls in line with them. However, the momentum philosophy that forms the core of this portfolio has made the portfolio more defensive over the last few months, selling out of smaller companies and increasing the weighting to stock markets such as the FTSE 100 which is actually benefitting from rising oil prices and interest rates. This will hopefully assist the portfolio going forward. In addition, when global stock markets do recover, then the momentum philosophy will hopefully identify those asset classes that are rising the fastest and thus we could experience strong returns at this stage. We are therefore confident that the underlying investment philosophy within the portfolio will produce good long term returns despite suffering significant losses from time to time.

Foundation portfolio

Exposure to equities and bonds fell further this month, in line with the reversal of many markets from positive to negative trends. This portfolio will always have a much more diversified approach and will not negate exposure to an asset class entirely. In this way we can attempt to achieve steadier returns. Cash positions are now similar to the height of the COVID crash in 2020.

Income Generating portfolio

The Income Generating portfolio has a history of falling less than other similar risk portfolios during difficult times. By investing in income producing assets, the portfolio is better equipped when we are faced with a downturn in the stock market. This is because, as stock markets fall, the income that is generated from the underlying companies increases as a percentage of their value. Eventually this income yield becomes very attractive and buyers step in, thus cushioning the falls. This does not work every time and during the COVID-19 related crash in March 2020, dividend paying companies were hit the hardest as they were forced to cut dividends.

Fourth Industrial Revolution portfolio

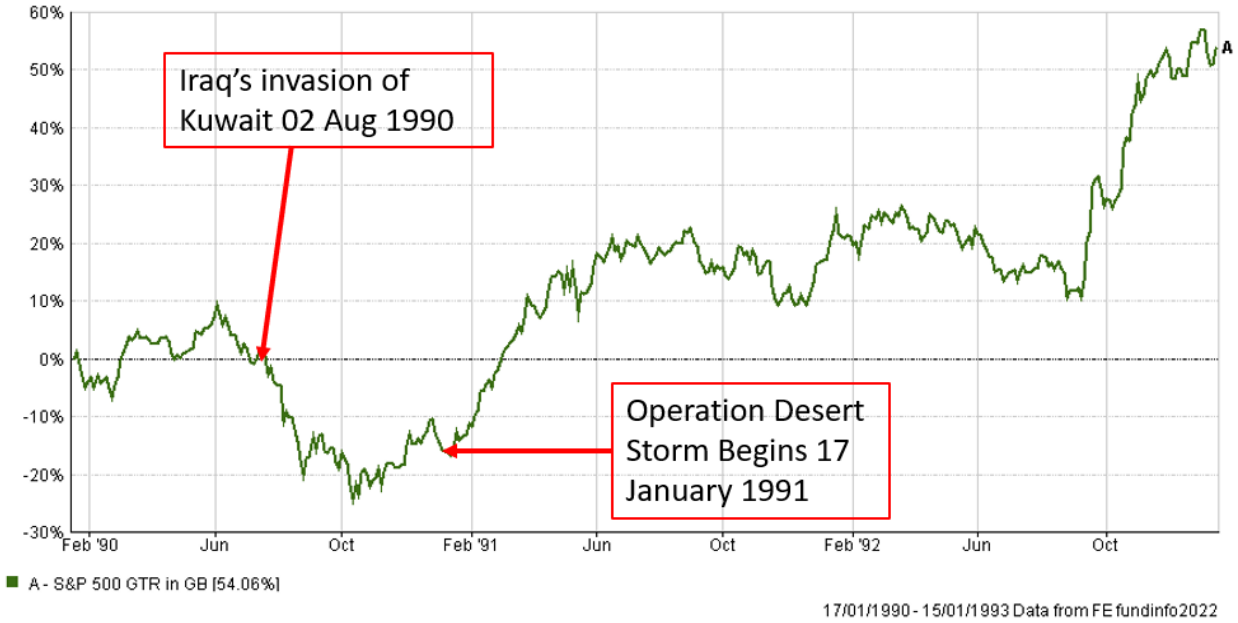
The fear of rising interest rates has hurt the portfolio over the last year. However, we are beginning to see part of the portfolio rebound after experiencing significant falls. The underlying companies within this portfolio are trying to solve the worlds problems and, due to this, we believe will produce excellent long-term returns. Last month the clean energy fund grew by 11.62% as the world looks at how we can become less dependant on Russian gas and oil much sooner. The cyber security fund also grew by 2.01% as these companies are now vital in protecting the West from an escalation of cyber security warfare from Russia. This may now be a good time to invest in this portfolio.

Retirement Investment Solutions

The Solutions have continued to become much more defensive this month as exposure to bonds and equities has reduced. The cash levels are nearly at the same level as they were at the height of the COVID crash in 2020. We should thus experience much lower volatility over the next few months.

Summary of Portfolios

Russia's unprovoked aggression in invading Ukraine dominated markets in the closing days of February, further aggravating falls in equity markets that had already begun from inflation and short-term interest rate concerns. History tell us that geopolitical tensions tend to cause stock markets to fall initially due to the uncertainty, but they often rise at the most difficult times. The chart below shows how the S&P 500 fell after the Gulf War started, but was significantly higher after it finished and the rebuilding started (will a similar pattern happen this time?):



Perhaps the biggest economic uncertainty is how inflation will be impacted over the next few months as energy prices have advanced even though supplies from Russia have not yet been cut. The expectation was that the US would increase interest rates by 0.5% this month in order to combat inflation, but now that expectation is for just 0.25%. This is due to the economic uncertainty that the war is having on the economy. Lower rate rises has helped support equity markets as well as bond markets and the fallout so far from the Russia invasion has been a lot milder than anticipated.

In the meantime, our trend following, and lower risk portfolios, have been increasing their cash holdings and thus reducing their risk during 2022 so that their cash levels are close to the levels we experienced at the height of the COVID crash.

Asset Class Review

This section will give you an insight into our current thinking and we have included some charts that we believe look interesting. This month we focus on how the invasion has affected certain asset classes.

Further losses in Europe, Japan and US; FTSE 100 continues to hold up

The FTSE 100 has benefitted from its exposure to miners, but other global stock markets continued to fall. The falls in February were much less than those in January, with the end of month rebound helping.

Food prices go up

Since the summer of 2020, and after many years of price falls, the price of a basket of agricultural commodities have increased significantly. Ukraine is a big producer of many commodities (see later) and therefore any disruption in their supply from the conflict will lead to higher prices. You can see how agricultural commodities have surged higher this year, and this is feeding into higher inflation, particularly for poorer countries in which food represents a higher proportion of people's costs.

UK Bond Yields rise but then pull back

Bond yields rose again in February on concerns that higher inflation will lead to higher-than-expected rises in interest rates. However, the economic uncertainty surrounding the invasion has led to some discussions that central banks will not raise interest rates as quickly and thus yields fell towards the end of the month.

Gas spikes then falls

Germany generates 40% of its electricity from renewables; primarily wind and solar. Natural gas represents 15% and Russia supplies about a third of that, so the country relies on Russia for 5% of its electricity generating capacity. The initial fear was that gas supplies would be cut, and gas prices spiked, but Russia needs the money from oil and gas, so the opposite occurred with Russian gas exports through Ukraine jumping higher. This has led to the price falling. As warmer weather is approaching, we will need less gas, and this gives time for countries like Germany to ramp up production of other energy producing sources.

In Summary

The impact on financial markets has not been that severe (yet). Stock markets have fallen a bit, food prices have continued to go up, but energy prices have not jumped to levels that we initially thought would happen. We do know that markets will continue to be volatile over the next few months though.

Why Ukraine matters Economically

Ukraine is the second largest country in Europe and is known as the "breadbasket of Europe" for it is a major producer of wheat. Ukraine also has a large industrial concentration due to the many raw materials in the country and is an important tie between Russia and the rest of Europe. Its geography is also vital. Russia supplies about 25% of Europe's gas needs, and half of that is pumped via pipelines running through Ukraine. This is why Russia wants to build the Nordstream 2 gas pipeline which effectively circumvents Ukraine when delivering gas to Europe. The map shows how strategic it is as its ports allow exports via the black sea and an important trading route between Russia and Europe:

The following facts have been circulating around and we have repeated what we believe are the most important ones to show just how important economically Ukraine is as it ranks:

- 1st in Europe in terms of arable land.
- 1st place in the world of exports of sunflower and sunflower oil.
- 2nd place in the world in barley production.
- 4th largest exporter of corn in the world.
- 4th largest producer of potatoes in the world.
- 8th largest producer of wheat in the world.
- 1st in Europe in ammonia production.
- 4th largest natural gas pipeline in the world.
- 3rd largest iron exporter in the world.
- 4th largest exporter of turbines for nuclear power plants.
- 1st in Europe in proven recoverable reserves of Uranium ores.
- 2nd largest iron ore reserves in the world.
- 4th in the world by the total value of natural resources.

Control of the above resources, the gas pipelines and the Ukrainian ports allows Putin to have much more economic power globally and has been summed up by the Daily Telegraph as follows,

"Putin's seizure of Ukraine elevates Russia into a full-spectrum commodity superpower, adding critical market leverage over global grain supply to existing strategic depth in energy and metals."

It is not difficult to understand why Putin wants Ukraine. President Biden has already reacted with a surprise announcement to expand domestic mining in strategic metals (lithium, graphite, rare earths, cobalt, rhodium, nickel, zinc etc). This points to a supply chain challenge where environmental objections now take second place. We should expect our Prime Minster to make announcements on fracking shortly as the West tries to reduce its dependency on Russia.

Final Comment

Just when we had started to come out the other side of the war against COVID, we enter another war that is causing catastrophic destruction and loss of life in Ukraine. Where this will end up is anyone's guess but our relationship with Russia has reverted back to that of the Cold War. It is easy to see why Putin wants Ukraine as it is an economic prize but will the invasion backfire and destroy his rule or will this war rumble on for many years.

Stock markets have reacted mildly so far, albeit in a volatile way. Despite rising commodity prices which will feed through to higher inflation, the expectation is that interest rates will now not rise as quickly due to the war. This has helped support stock markets. In addition, mining and oil companies have risen significantly as has the clean energy sector. We are expecting much more volatility over the coming months and our lower risk portfolios have become much more defensive this year.

Watson Moore Independent Financial Advisers Limited
54 Station Road
Upminster
Essex
RM14 2TU

Tel: 01708 250624

Email: chrismoore@watsonmooreifa.com

www.watsonmooreifa.com