THE PRIVATE CLIENT GROUP
BALANCING LIFE & WEALTH

ECONOMIC & MARKET INSIGHTS

An Executive Summary for February 2022

Headlines regarding future Federal Reserve (Fed) policy action and the ensuing path of the pandemic temporarily faded into the background as the escalation of tension in Ukraine quickly stole the world's attention. Russia's decision to invade Ukraine is heartbreaking and represented a dramatic departure from how many experts expected the situation to evolve. Russia's actions and Putin's unpredictability will have long-lasting implications on the balance of power in Europe and the world. Additionally, recent events, paired with the implications of the pandemic, could further shift the world towards fragmentation, interrupting a multi-decade trend of globalization.

In economic terms, the size of both the Russian and Ukrainian economies is relatively small – accounting for around 1% of global GDP. While it's impossible to predict the full implications of Russia's actions, what's perhaps more apparent is the effect on energy and commodity markets. Russia and Ukraine were collectively significant exporters of important commodities including crude oil, natural gas, metals, and wheat. This is especially true for Europe, which imports a significant amount of its energy supplies from Russia. Brent crude oil futures rocketed past $100 per barrel for the first time since 2014 and European natural gas prices rose by double-digits over the month with little signs of stopping. Higher commodity prices present a new challenge in central banks' fight against inflation coming out of the pandemic.

Outside of the Russia/Ukraine conflict, growth has been robust in many developed areas of the world as the economy recovered from an Omicron-induced lull. The labor market remained strong with wages rising for many employees. Strong wage increases have also fueled healthy consumer spending helping support GDP growth. Although elevated consumer spending has been supportive for growth, higher wages and further supply-chain disruptions also had the adverse impact of fueling higher-than-desired inflation. Central banks have been keen on taking action to combat higher prices. While consensus expectations had the Fed raising rates six times by the end of 2022, the ensuing Russian military conflict and its impact on global growth could take some pressure off the Fed and other major central banks to raise rates as quickly as expected.

February proved to be a challenging month for risk assets. At its start, markets started to more aggressively price in multiple rate hikes by global central banks. Around mid-month, the focus quickly shifted to the conflict in Ukraine and a more bearish sentiment took hold. Investors shed risk from their portfolios, resulting in declining equity markets, widening credit spreads, and receding sovereign bond yields. Within equities, higher earnings, paired with negative price performance, have brought down valuations – although this reflects the current geopolitical environment. Lower starting valuations could present a higher upside case were the current crisis to de-escalate, while also providing central banks more latitude to normalize rates to fend off inflation. Most bond markets generated modest losses but still offered diversified portfolios some stability, relative to equities. Municipal yields rose for much of the month but then retraced after news of the Russian invasion broke. After a record period of fund inflows, municipals have had several consecutive weeks of redemptions. Despite recent outflows, the fundamental landscape for municipals remains supportive and the asset class should continue to offer investors stability during the current bout of volatility.

The swift recovery of risk assets since the start of the pandemic has made markets susceptible to a wide variety of risk factors. Although the catalyst is rarely what's anticipated, we again find ourselves in a period of elevated volatility. Higher levels of uncertainty in the near term should perpetuate volatility, but ultimately, a new equilibrium will be reached. As the Ukraine Crisis unfolds and valuations adjust, there will likely be opportunities to take advantage of others' fear. As a result, we encourage investors to maintain a focus on long-term goals while attempting to selectively take advantage of compelling investment opportunities as they arise.

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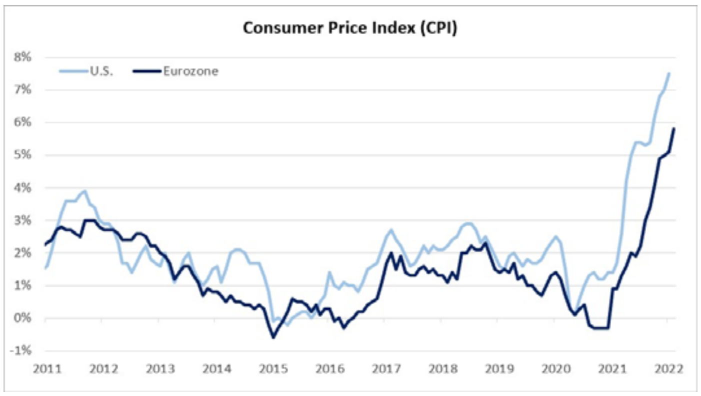

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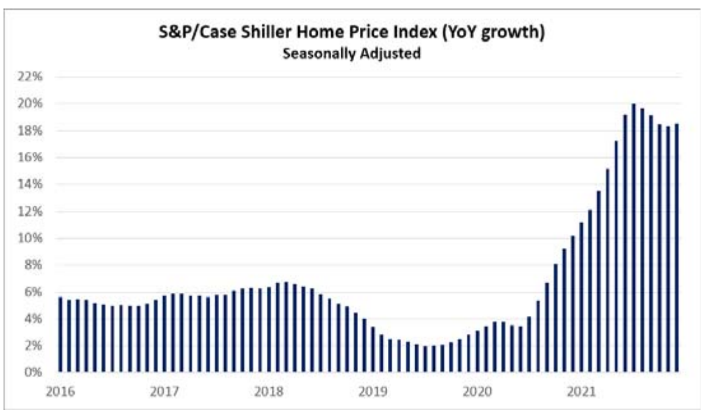

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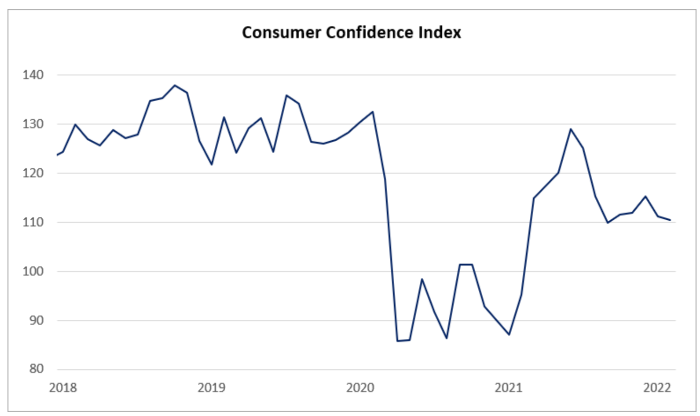

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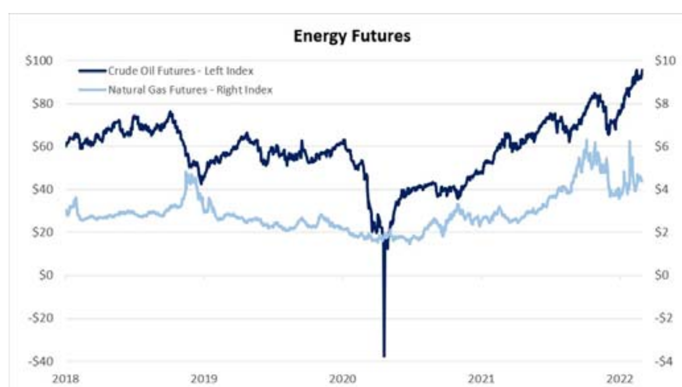

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