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A Month in the Markets

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In this latest edition our Head of Multi-Asset Solutions UK, Stefano Amato, looks at how key themes impacted markets in December: inflation concerns, supply chain issues, and new restrictions due to the Omicron variant.

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Market Overview

As 2021 drew to a close, most of the world's major stock markets generated positive returns for investors. Despite some turbulence at the start of December, the so-called Santa Claus rally emerged once again. This helped lift global markets across the board, especially in the US.[1]

When the month began, concerns about inflation and the pandemic dominated the news. Travel and leisure stocks were again impacted by the emergence of the Omicron variant of COVID-19. Governments around the world strengthened travel restrictions – albeit briefly in some cases – in an effort to slow the spread.

Approaching Christmas and New Year, encouraging data on hospitalisations linked to Omicron helped most stock markets recover lost ground. Improved government preparation and vaccine uptake mean we do not think Omicron will affect markets as much as previous variants have.

Against this backdrop, most of the world's major stock markets delivered solid single-digit positive returns (in local currency terms). The US led the way, followed by Europe, the UK and Japan.[2] China was notable however, for delivering negative returns over the month.[3]

[1] Market Watch - Santa Claus rally is off to best start in 20 years, 27/12/21
[2] The Guardian - FTSE 100 bounces back despite Covid to finish 14.3% up in 2021, 31/12/21
[3] Schroders - Monthly markets review - November 2021, 3/12/21

UK and Europe

In the UK, the economy was in a generally good condition. Manufacturing output was on the rise,[4] but tighter restrictions blunted business activity and caused retail sales to fall.[5] Economic growth in the third quarter was revised down from 1.3% to 1.1%, with overall output still 1.5% less than at the end of 2019.[6] Meanwhile, inflation reached 5.1%, the highest for 10 years.[7] This prompted the Bank of England to increase its benchmark interest rate to 0.25%.[8]

In Europe, businesses and consumers began the month facing many of the same issues linked to the pandemic. This included snarled supply chains, rising inflation and staff shortages, though there were signs this supply chain crisis was easing in December. [9] The shortage of materials, and low demand meant Europe's manufacturing was unchanged from November.[10] Inflation increased to 4.9% in November, the highest recorded in the trading bloc.[11]

US

The US continued to be in a solid economic position over the month. While there was slightly slower growth in the manufacturing sector,[12] consumer confidence was on the rise.[13] The overall unemployment rate fell to 4.2% in November, the lowest since the pandemic began.[14] Furthermore, initial claims for unemployment benefits finished the year close to pre-pandemic levels.[15]

Despite the Bank of England raising rates during the month, the Federal Reserve (the Fed) held off hiking rates despite rising inflation. The Fed instead announced that it will accelerate an end to the central bank's pandemic-era support of the economy. It also signalled the potential for three interest rate hikes in 2022.[16]

Asia and emerging markets

The world's second-largest economy, China, continued to struggle over the month with jitters in its property sector and rising levels of debt. Property developer China Evergrande was put in default by S&P after failing to make bond payments.[17] There were some small positives, though. After six months of falling activity, China's manufacturing activity returned to growth in December.[18]

China's central bank, known as the People's Bank of China, also cut its one-year loan rate from 3.85% to 3.8%. This bid to encourage growth comes as the economy grew by 4.9% in the third quarter, the lowest increase in a year.[19]

Outlook

We continue to look ahead with a cautiously optimistic view of the global economy and stock markets. As the pandemic continues, governments and health agencies are better equipped to fight the virus. For individuals, vaccines are doing their part in reducing serious illness and central banks continue to support financial markets. This is a positive for investors.

With that view in mind, we favour shares over bonds. We believe that higher inflation and rising interest rates create a negative environment for fixed income investors. Within shares, we continue to favour European over US shares for the value opportunities that we see. Nevertheless, we still believe there are strong growth stories among American companies. Although supply chain issues and concerns over the impact of the Omicron variant of COVID-19 remain, it appears that much of the disruption is behind us. It is therefore unlikely in our opinion that we will see the same degree of restrictive measures that were put in place early in the pandemic.

Asset Management

Portfolio Management for our multi-asset fund of funds

Over the month, we reduced the overweight position in shares across some portfolios in December. This reflected our concerns about inflation, the Omicron variant and the potential for stock market volatility. This entailed reducing our weighting towards developed market shares and re-investing the proceeds from this reduction into investment-grade bonds. Our weighting towards emerging market shares remained neutral.

Santander Atlas Income Portfolio update

The **Santander Atlas Income Portfolio's** long-term investment objective is to provide a target annual income of 4% (not guaranteed) with the potential for capital growth over 5+ years, whilst operating within a defined volatility range. It aims to pay a monthly smoothed income throughout the fund year (which runs from 1 August to 31 July) over 11 months with a final balancing payment being paid on the 12th month to help meet the income needs of investors.

Due to market conditions, for the accounting year which started on 1 August 2021, we projected an annual income of 3.30% (not guaranteed) which translates to a PPU of 0.60, for the II share class.

Given the current market conditions have not improved materially since the PPU was set for the fund year, we can confirm that the smoothed PPU payment remains the same for the current month. If the payments need to be adjusted up or down throughout the year as a result of receiving more or less income than expected, we will communicate with you within these monthly updates, or with a separate income update if required. If you have any concerns or require additional information please do not hesitate to email us at IFAEnquiries@santanderam.com.

All data as at 31 December 2021.

[4] Markit Economics - Manufacturing upturn continues at end of 2021, 4/1/22
[5] Markit Economics - Sharp slowdown in UK private sector growth in December as Omicron variant hits spending on consumer services, 16/12/21
[6] ONS - Gross Domestic Product (GDP), 22/12/21
[7] ONS - Consumer price inflation, UK: November 2021, 15/12/21
[8] The Guardian - Bank of England raises interest rates to 0.25%,16/12/21
[9] The Wall Street Journal - Supply-Chain Problems Show Signs of Easing, 21/11/21
[10] Markit Economics - Stocks of purchases rise at survey-record rate as supply chain pressures ease , 3/1/22
[11] Eurostat - Euro area annual inflation up to 4.9%, 30/11/21
[12] Trading Economics - United States Manufacturing PMI, 2/12/21
[13] The Conference Board - Consumer Confidence Improved Again in December, 22/12/21
[14] Trading Economics - United States Unemployment Rate, 4/1/22
[15] CNBC - Unemployment claims end 2021 near pre-pandemic levels, 30/12/21
[16] The Guardian - US Federal Reserve speeds up taper and signals three rate hikes in 2022, 16/12/21
[17] Reuters - S&P dumps Chinese property giant Evergrande into default, 17/12/21
[18] Reuters - China Dec factory activity edges up ahead of economic headwinds, 31/12/21
[19] CNBC - China's central bank cuts a benchmark rate for the first time since the pandemic, 19/12/21

Important Information