About Investing

Understanding market sentiment

Sentiment can be a powerful force, leading markets to behave in sometimes unexpected ways. How might investor instinct and emotion influence financial markets in 2022?

When the COVID-19 pandemic began in early 2020, many investors braced themselves for a market downturn amid a huge and sustained sell-off. In fact- it didn't quite work out like that. While 2020 was volatile, global stock markets had by the end of the year more than recovered the losses of February and March, with a record-breaking month in November.[1] It was an emphatic reminder that investment markets reflect much more than broad economic movements.

Sentiment defined

In simple terms, sentiment is how investors feel about a particular market, company or sector and where they think prices will move in future. If more investors think a stock is worth selling rather than buying, that stock is likely to go down in price and vice versa.

Data can play a role but is often second to emotion

Investor sentiment can be influenced by investment fundamentals, a company's financial measures which demonstrate its position compared to its peers. Economic factors including inflation, prevailing interest rates and supply versus demand can also feature. However, it's more broadly about what investors believe will happen and isn't necessarily justified by the evidence available. In other words, market movements and investment returns can be heavily influenced by investor emotions, especially over shorter time frames.

The language of market sentiment

Sentiment indicators and surveys can provide a clue as to the prevailing investment mood. One of the best known is the Chicago Board Options Exchange Volatility Index (VIX), which measures expected price movements in the S&P 500 Index. When the VIX is going up, it suggests professional investors such as fund managers are feeling more pessimistic about the market outlook (they're 'bearish'), while falls in the index indicate confidence is rising (investors are 'bullish').

When sentiment takes over

In early October 2021, the US S&P 500 Index was close to a record high. Yet it had just recorded its biggest monthly loss since the start of the pandemic, with investors increasingly worried about factors such as rising inflation and the possibility of a US debt default.[2]

There was a similar dynamic in May, when investor concerns over the US inflation outlook prompted a sell-off in both the US and Europe.[3] Inflation worries contributed to a FTSE 100 dip in September too,[4] due largely to rising energy prices, while the July falls in global markets reflected investor doubts over the economic outlook in China and concerns about a potential removal of some of the central bank stimulus put in place during the pandemic.[5] Even as economies reopened and recovered from the worst effects of the pandemic, markets were impacted by the way investors anticipated developments and interpreted signals.

The end of 2021 was dominated by the Omicron variant and inflation

The emergence of the Omicron variant of COVID-19 in November saw global markets tumble on fears of a dangerous new phase in the pandemic.[6]

Other factors also made investors less hopeful, most notably inflation which will likely remain a prominent theme in 2022 and beyond. According to the Consumer Price Index UK Inflation reached 5.4%[7] in December, the highest rate in 30 years, prompting the Bank of England to increase rates from 0.15% to 0.25%, with more rate rises expected to help bring down inflation over time to their target rate of 2%. They expect inflation to remain at around 5% for the next few months, peaking at around 6% in April as household energy bills are pushed up by wholesale gas prices. While price pressures will remain, inflation is predicted to fall back to some extent in the second half of the year,[8] but still average 4%.[9]

Higher inflation in the US and elsewhere also points to interest rate increases over the coming period, during which central banks may continue to reduce the financial support launched early in the pandemic.[10] While the US central bank, the Federal Reserve, did not raise interest rates at its last meeting of 2021 it expects to do so three times in 2022.[11]

Key investment themes for 2022 will include sustainability and infrastructure

Short-term sentiment aside, demand for sustainable investing strategies is set to grow rapidly as governments and companies strive to meet their net zero targets and policymakers focus increasingly on the energy transition.[12] The increased flow of both public and private investment into sectors and companies engaged in tackling the climate crisis may create opportunities in areas including electric vehicle manufacturing, hydrogen production and carbon capture, as well as the financial sector.[13]

Keeping your balance in a changing investment landscape

While 2022 will have unique challenges, an ever present risk remains - losing sight of long-term goals and getting caught up in short-term market sentiment, which could lead to poor outcomes.

There are several ways you can manage your risks. One is to have a diversified portfolio, invested across a range of different sectors, regions and asset classes. This can help to make sure you're not over-exposed in the event of a downturn in one or two areas.

One way to achieve this is by investing in one or more multi-asset funds, which can invest across different assets, sectors and fund types, with the manager reviewing and rebalancing the portfolio over time to help keep it on track as market conditions change. Another option is a managed portfolio service, where a professional fund manager invests your money in a portfolio, which can include multi-asset funds.

A professional financial adviser can also play an important part. They can help you to manage emotions, keep focused on long-term goals through times of uncertainty and make sure your portfolio remains a good fit for meeting those goals.

Learn more

Stay up-to-date with our latest **Markets and Insights** at **santanderassetmanagement.co.uk**.

[1] Reuters – Global stock markets slide at end of record November, 30/11/20
[2] USA Today – Is the stock market primed for an October swoon? Why investors shouldn't fear the frightful month, 1/10/21
[3] Market Watch – Stocks fall across Europe and Nasdaq slips as inflation concerns and selloff sentiment spread, 11/5/21
[4] Market Report – FTSE 100 closes in the red as markets fall globally on broad investor sell-off, 28/9/21
[5] Sky News – FTSE 100 slips below 7,000-mark as economic jitters spark global sell-off, 8/7/21
[6] BBC – Global markets fall after Moderna Omicron warning, 30/11/21
[7] Guardian – UK inflation jumps to 30-year high of 5.4% as cost of living crisis deepens, 15/12/21
[8] Bank of England – Bank Rate increased to 0.25% - December 2021, 19/01/22
[9] Santander Asset Management UK – State of Play, 9/12/21
[10] Santander Asset Management UK – State of Play, 9/12/21
[11] FT.com – Fed officials expect three rate rises next year in hawkish pivot on inflation, 15/12/21
[12] Santander Asset Management – Market Outlook 2022, 14/12/21
[13] HM Government - Net Zero Strategy: Build Back Greener, 7/10/21

Asset Management

Let's be clear!

Investment terms explained

Asset class: A group of investments with similar traits. shares, bonds, property, cash and alternatives are all examples of asset classes.

Bear: A bear market is often defined as having seen falls of at least 15-20% over at least two months. An investor who is 'bearish' is one who feels pessimistic about the outlook.

Bull: A bull market is often defined as having seen or expecting to see rises over a sustained period. An investor who is 'bullish' is one who feels optimistic about the future.

Diversification: Spreading your money across different investments to help manage risk.

Index: A way of tracking the overall performance of a basket of individual investments of a similar type. For example, the FTSE 100 index tracks the performance of Shares in the 100 largest companies by market value on the London Stock Exchange.

Inflation: Measures the increase in price of selected goods and services in an economy over a period of time.

Multi-asset fund: A fund that offers a diversified, mixed asset portfolio.

Portfolio: A group of investments that are managed together to meet a particular objective.

Volatility: The extent to which the value of an investment fluctuates over time.