LGIM

Countdown to 2022: starter for 10

2021 was another year full of twists and turns, so what will 2022 bring? As we hastily forge our new year's resolutions, our attention has turned to what's next. Here are 10 themes our Asset Allocation team will be mulling over before welcoming in the new year.

Biden's **10** month report card

US President Biden's tenure started promisingly after he completed his goal of vaccinating 100 million people within his first 100 days and passed another round of hugely popular stimulus cheques. However, since then, the US Commander-in-Chief has struggled to pass two spending bills which are considered key to his mandate, against a backdrop of rising and broadening inflation amid supply shortages and a low labour participation rate. These issues, and others (e.g. the Afghanistan exit, vaccine mandates, border crisis) have damaged his polling numbers with only a 42.9% approval rating at the end of November 2021, down from 54.4% at the end of March 2021.[1] The Democrats will be seeking to improve this going into next year's midterms.

9 in 10 Americans have heard about cryptocurrencies

The asset class has surged in popularity in 2021 with the price of a bitcoin increasing from $18,114.41 at the end of November 2020 to $57,834.36 at the end of November 2021, a 219% increase.[2] 16% of Americans say they have invested in, traded or used cryptocurrency,[3] but what is our view?

We see cryptocurrencies as a speculative investment at present. While returns have been impressive, we believe they are too volatile and not established enough for us to consider them in our portfolios. We recognise, however, that the asset class is increasing in popularity and as such, we will continue to monitor its progress to see if the tide changes sufficiently for it to become a viable investment in our strategies.

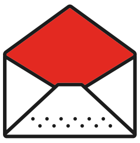
8bn doses of COVID-19 vaccines

So far in 2021 we have seen a huge effort to get people vaccinated globally. However, doses have not necessarily been administered equitably with the World Health Organisation chief stating in August that 75% of jabs have gone to just 12 countries. This has led to somewhat of a two-speed recovery, with developed market countries able to reopen their economies to a greater extent than emerging markets (EM) countries which tend to rely more on the tourism economy. This perhaps goes some way to explaining the fact that spreads in emerging market debt remain attractive compared to their developed market counterparts. We currently prefer emerging market debt in our portfolios to high yield and investment grade bonds.

7 to 1

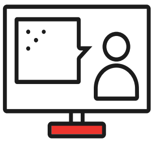
The current odds for the England men's football team to win the 2022 World Cup in Qatar are around 7 to 1. But it's not just England's football team that's on the up; its interest rates are, too. At the time of writing, we anticipate four rate rises by the Bank of England up to 0.75% by the end of 2022, as the bank seeks to defend against rising inflation which we forecast will peak at 5%. What impact will higher interest rates have on house prices in the UK by the time football (hopefully) comes home?

1. Project Thirty Five Eight, December 2021
2. Statistica, November 2021
3. Pew Research Center, November 2021



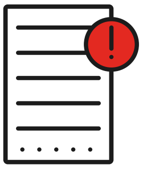
6 emerging market elections

There are six EM countries with elections in 2022. Although there are fewer pivotal elections than we expect to see in 2023, if coronavirus anxieties recede in EMs, we expect upcoming electoral contests to play a larger role in our investment strategy. In 2022, we are likely to have some continuity, with the incumbent party consolidating in Poland and Viktor Orban to remain in power in Hungary. But we also anticipate key changes such as controversial Brazilian president Bolsonaro being replaced as the country lurches to the left along with Colombia. If we do see market turbulence due to surprise election results or polls, we believe such volatility can often be overdone and could provide attractive investment opportunities.



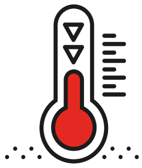
1 in 4 thinking about changing jobs

One of the economic phenomena of the COVID-19 crisis is that wages didn't really drop as they normally would through a recession. This was partly because of fiscal policies and also the initially perceived temporary nature of the crisis. As the global economy reopened, more job vacancies became available and workers became increasingly discerning about their current employment. This now means a record level of people are either quitting their jobs, or thinking about it. If you're lucky, this may mean you are in for a pay rise as companies seek to retain staff, but on the other hand, such wage pressures can contribute to an inflationary spiral like we saw in the 1970s. The recovery and reshaping labour market is one to watch for 2022.



5 Chinese growth headwinds

Chinese economic growth is facing a series of headwinds in 2022, and our expectation for growth of around 4% is slowly becoming consensus amongst economists and investors.[4] We see this as a potential line in the sand for the government. Those headwinds include the totemic zero-COVID strategy, the regulatory crackdown on technology, education and gaming, and the property sector. China's high-yield bond market, especially property developers' bonds, has been under incredible strain in recent months, with prices tumbling by nearly 40% since May.[5] We think this could be a significant opportunity to pick up an uncorrelated distressed asset. Although we must admit it always feels scary to buy 'deep value', we think high-yield Chinese property bonds could be a top asset pick for 2022.



3°C makes a world of difference

As endurance swimmer Lewis Pugh commented after his recent swim in partnership with LGIM across a Greenland Icefjord – "we were expecting 3C water temperature today, but got 0C. Only a few degrees colder but the difference between life and death."

Small but critical differences in temperature were the focus of the COP26 conference on climate change in November 2021. There was some progress made, but unfortunately not enough. Under current global policies the world is on track for almost 3°C warming (2.7°C) and even with new carbon reduction pledges from the conference the world will emit roughly twice as much in 2030 as required for an acceptable 1.5°C scenario.[6]

LGIM has been very active in widening the application of coal divestment policies, setting decarbonisation goals for our business and for some funds where appropriate, providing ESG reporting for our funds, and of course engaging with companies on climate change as part of our Climate Impact Pledge.

4. Macrobond and LGIM, 30 November 2021
5. Bloomberg, 30 November 2021
6. Climate Action Tracker, November 2021

2 Superpowers

How the power dynamics between China and the US are resolved is the geo political question of our age. One risk is a Thucydides trap, where the rising power and ruling power fall into armed conflict; another outcome is termed the "Churchill trap" of prolonged cold war-style confrontation. Alternatively, the two powers could co-operate and co-rule in different spheres of influence.

Under Biden, there is still a cool relationship between the superpowers; the US has been raising human rights abuse concerns, there are tensions over Taiwan and threats of boycotting the Beijing Winter Olympics, and latent wariness about technology transfer. But there are also tentative signs of co-operation; an online leaders' summit stressed the importance of competition not turning into conflict, and a surprise announcement at COP26 declared that the two countries would boost co-operation on climate. As Churchill once said, "to jaw-jaw is always better than to war-war".

1 Hundred years since the start of the roaring twenties

The 1920s started with a post-war and post-Spanish Flu economic slump. The party didn't really get started till 1922. While the decade was notable in terms of cultural and technological change, the stock market also had a wild ride. Many similarities have been drawn between the 1920s and today, not least a post-pandemic recovery, but also huge technological change.

So, are we in for another roaring '20s or is it more likely to be the snoring '20s? Our scenarios suggest that the upside potential is there, and if supply disruptions are resolved and consumers continue to spend, we could see a boom. It's a nice thought for the final countdown into the new year…maybe…but unfortunately, it's just one of the 6 main scenarios we see ahead of us.

Contact us

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