Current Focus

March 2022

A monthly market comment from Rivers Capital Management. Views expressed here are subject to change and for professional advisors only

RIVERS CAPITAL MANAGEMENT

INTELLIGENT INTUITIVE INVESTING

Rivers Capital Management

+44 (0)20 3383 0180

www.riverscm.com

Summary

- The invasion of Ukraine has changed international relations irreversibly
- The Russian Ruble has collapsed with Russia isolated on the world stage
- Energy and Agricultural prices spiked higher and are expected to remain high for some time
- The war increases existing inflationary pressures making interest rate rises more likely
- The need to slow inflation while avoiding a recession is made more difficult by the invasion
- Volatility is expected to continue offering tactical opportunities to reallocate

Contacts

Richard Bonnor-Moris
rbm@riverscm.com

Eduardo Tomacelli
etomacelli@riverscm.com

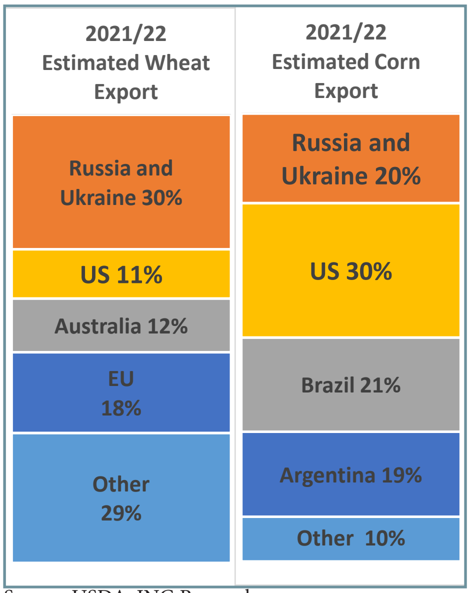
Najib El-Rayyes
ner@riverscm.com

Market Comment

On February 24th the Russian invasion of Ukraine changed European and Global politics significantly. Russia's position in the world order has been altered materially and, for as long as Putin remains President, this change seems unlikely to be reversed. Whatever the objectives of Putin's invasion were, they appear to have stalled as his army gets bogged down. Ukraine's defence and the unified response from almost every country, especially NATO and the EU, must have surprised Putin. Even China is preferring to stay neutral. In the last three weeks Putin has put his country in an unwinnable situation. He has subjected his country to a series of sanctions that may not bankrupt Russia, but will isolate them in ways not experienced since the 1980s. From an investment perspective, the Russian Ruble is at all-time lows and the risk of default on Russian bonds the highest since the 1998 crisis. The impact on global energy prices has been huge, with Europe urgently seeking alternative sources of gas and oil. It is unclear how the war proceeds and whether Putin continues to double down or if some settlement can be reached. The latter seems less likely by the day and the former will subject the Ukrainians to months of the type of carnage already seen in Mariupol.

Just as the Covid-19 crisis seemed to be abating, this action by Russia, of invading another sovereign state, has created a crisis likely to dominate the news for months to come. Not only a humanitarian disaster but a crisis for world trade, global growth and potentially world peace. We do not know how this crisis will be resolved. As Gideon Rachman wrote in the FT this week "... there are three options: a prolonged war; a peace settlement; or a coup in Russia. Expect the first, work for the second and hope for the third." In this month's Focus we will look at the heightened inflationary impact of a prolonged war, its likely investment implications and how the Rivers Portfolios may be adjusted, tactically, from the cautious, underweight risk position they have held for some time.

The UK, like the US, and unlike many countries in Europe, is not particularly reliant on Russian oil and gas supplies, but will be affected by the rising energy cost this war has already caused. Less obvious, but possibly more inflationary, is the loss of Russian and Ukrainian wheat and corn



Source: USDA, ING Research

exports. Together they make up nearly 30% of global wheat exports and 20% of global corn. Russia is also the world's biggest exporter of synthetic fertilizer which has already led to farmers, concerned about shortages, pushing fertiliser prices to record highs. All of this is inflationary. With inflation in the UK already running at 5.5% and in the US at 7.9% there is no wonder that Bank of England Governor Bailley and Federal Reserve Chairman Powell are now having to play catch up. We have been saying for some time that rock bottom interest rates were not justified given strong economic growth and rising inflation. With both economies now close to full employment the pressure on wages to meet the rising cost of living is clear. It is difficult to see how Central Banks, using the blunt tool of interest rate rises, can slow down economic growth sufficiently to dampen inflation, while also avoiding a recession. The crisis in Ukraine makes this already challenging task extremely difficult. If interest rates rise too slowly, an inflationary spiral remains possible, while if they are raised too quickly, then a recession becomes increasingly likely.

Alternative sources of oil, gas and agricultural produce will be found but prices are likely to rise further at least in the short run. The poor levels of investment in oil and gas production over the last ten years have increased dependency on Russian exports, particularly in Europe, but the motivation to reduce, or remove this dependency has never been higher. As a Saudi oil minister said in 2008, (the last time a barrel of oil cost more than $120) 'The Stone Age didn't end because we ran out of stones.' While the crisis certainly offers opportunity in the unfavoured hydrocarbon sector the medium to longer term solution still lies in alternative energy sources.

We already know that inflation not seen since the 1980s seems almost certain. The question remains how long inflation stays that elevated. Commodity prices will not rise forever and provided wages remain controlled, inflation will eventually slow as forecast by the Central Banks. This could take years though, and is definitely not 'transitory'. Even before the Russian invasion the Federal Reserve forecast for inflation was above the 2% target for 3-5 years. The recent, more hawkish comments by Chairman Powell are not surprising.

The Rivers portfolios have no direct exposure to Russia, but the effects of high inflation and rising interest rates will impact all investment assets. The technology sector, and in particular the enormous tech companies in the US seem vulnerable to interest rate rises but other sectors could benefit. The portfolios have been underweight risk for many months as valuations appeared, to us, to be extended. Some still are but others are already much more attractively priced. As long term investors we would rather not hold an asset than own an asset we think is overvalued. Volatility is very likely to remain high, in this environment, but this will provide opportunities to realign the portfolios, adding funds which provide long term positive real returns. With inflation high, and rising, the risk of not being invested is high but not as high as the risk of being invested in assets with unsustainably high valuations, however good the underlying corporations may be.

Market Returns (£) - 28th Feb 2022	1 Month	3 Month	1 Year	3 Year	5 Year	S/I*
Anchors						30/06/2016*
Cash + 1%	0.0%	0.1%	0.9%	4.0%	7.3%	8.3%
Inflation Linked UK Bonds	-0.3%	-8.5%	9.6%	19.7%	20.5%	30.8%
Gilts	-1.5%	-8.1%	-3.2%	4.4%	5.8%	5.8%
Global Government Bonds (hedged)	-1.0%	-3.1%	-1.9%	5.1%	8.0%	4.7%
Enhancers						
Global Corporate Bonds (hedged)	-2.1%	-4.8%	-3.5%	9.7%	12.5%	13.2%
Global High Yield (hedged)	-2.4%	-3.2%	-2.6%	7.1%	12.4%	22.5%
Emerging Market Bonds (hedged)	-2.4%	-2.1%	1.2%	3.4%	4.1%	14.2%
FTSE 100 TR Index	0.3%	6.3%	19.2%	17.6%	24.3%	42.3%
FTSE UK All-Small Cap	-3.7%	-3.6%	9.2%	37.4%	50.2%	81.4%
Global Equity (MSCI)	-2.5%	-5.1%	15.4%	48.6%	63.8%	97.9%
European Equity (MSCI)	-4.1%	-4.0%	9.8%	24.4%	32.7%	54.9%
US Equity (S&P)	-3.0%	-5.3%	20.8%	61.4%	82.9%	123.5%
Japan Equity (Topix)	-0.4%	-4.7%	-0.7%	19.3%	21.8%	49.2%
Pacific Ex Japan Equity (MSCI)	-2.1%	-5.8%	-14.6%	16.6%	33.0%	62.8%
Emerging Market Equity (MSCI)	-3.0%	-4.4%	-6.9%	18.2%	30.0%	58.7%
Chinese Equity (Hang Sang)	-4.8%	-4.8%	-16.8%	-13.5%	3.7%	29.0%
Indian Equity (Nifty)	-4.0%	-3.2%	21.2%	50.1%	60.4%	85.6%
Diversifiers						
Commodity Index	6.9%	18.0%	40.1%	42.6%	27.9%	36.0%
Gold	5.8%	5.4%	13.8%	37.1%	32.7%	34.3%
Silver	8.6%	5.1%	-4.7%	46.5%	13.5%	19.3%
Brent Oil	6.9%	18.0%	40.1%	42.6%	27.9%	36.0%
UK Property	0.9%	5.0%	14.9%	14.8%	26.8%	29.4%
Global Property Shares	-3.2%	-3.1%	19.5%	18.9%	27.1%	36.6%
Rivers Model Portfolios						
Rivers Preservation Portfolio	*-0.3%*	*-2.3%*	*0.5%*	*7.3%*	*9.3%*	16.5%
Rivers Cautious Portfolio	*-0.7%*	*-2.8%*	*2.3%*	*15.8%*	*20.8%*	33.8%
Rivers Balanced Portfolio	*-0.7%*	*-3.4%*	*2.9%*	*20.4%*	*27.8%*	44.7%
Rivers Adventurous Portfolio	*-1.1%*	*-4.4%*	*3.0%*	*24.6%*	*32.5%*	52.6%
Rivers Aggressive Portfolio	*-1.6%*	*-5.5%*	*3.3%*	*26.9%*	*36.1%*	60.9%
Rivers Cautious Income Portfolio	*-1.5%*	*-3.0%*	*1.8%*	*8.5%*	*10.5%*	17.5%
Rivers Balanced Income Portfolio	*-1.3%*	*-2.4%*	*2.9%*	*12.4%*	*16.3%*	28.2%

Source: Financial Express in GBP (unhedged unless stated) as at 28th February 2022. *Rivers Portfolios since launch June 30th 2016
Model Performance is indicative only and is net of Rivers Capital Management Charge and Underlying Fund charge but not advisor or platform costs.