MARKET COMMENTARY

Executive Summary

The horrific events unfolding in Ukraine due to the Russian invasion at the end of February has triggered a unanimous response from Western nations in the form of sanctions against Russia and the effect is being felt around the globe.

Amanda Tovey

Investment Director

Whitechurch Response

Tuesday's announcement by the US Government that is it banning Russian oil imports demonstrates how far countries are willing to go from an economic perspective and there will be more to come to increase pressure on Russia. The global economy was already feeling the effects of increasing inflation moving through 2021 as it recovered from the COVID-19 pandemic with supply shortages coupled with increased demand leading to rising input costs in commodities, with oil particularly affected. Central Banks had in response started to raise rates and this contributed to a market rotation at the end of 2021 as growth stocks, which had fared so well during the pandemic sold off in favour of value orientated stocks. This negatively affected many stocks in the sustainable investment sphere which tend to have more of a quality growth tilt by nature or are more technology focused which feature heavily in these types of funds (think industrial tech providing solutions to environmental issues rather than FANG stocks).

As January progressed into February, geopolitical tensions increased as Russian troops amassed at the Ukraine border and fears started to escalate of a Russian invasion. This pushed already buoyant energy and commodity prices higher and as Russian troops started their assault inevitably global markets fell.

Whilst there are many theories on how the war in Ukraine may end no one can know for certain how long this will last or how it will be resolved. We can however be certain of some of the economic effects in both the near and longer term.

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Risk Aversion and Safe Haven Assets

As is always the case in times of severe market uncertainty there has been a move away from equities towards perceived 'safe haven' assets, mainly gold, currencies such as the Yen and US Dollar and Government Bonds. Our portfolios don't invest directly in currencies and within the Ethical range of portfolios we do not have exposure to Gold and very limited exposure to Government Bonds, so the portfolios have suffered in this regard.

Inflation

Whilst last year many commentators were talking about inflationary pressures being 'transitory' we believe this idea is firmly off the table at this point due to the negative supply shock to energy and agricultural commodities. There have been numerous headlines in recent weeks about the squeeze on the consumer and this will now be amplified as energy and food prices rise and will have a knock-on effect across many sectors as people and businesses cut back and re-evaluate spending.

Global Food Supply

Russia and Ukraine were expected to contribute around 25%-30% of the world's exported wheat supply in 2021-2022 and around 20% of the world's corn supply as well as other agricultural commodities. Disruptions in the supply due to the war has already led to soaring prices for these grains and this disruption will be felt for a minimum of 2-3 years as planting and harvests are disrupted and much longer if the war continues for a protracted period.

Global fertiliser supplies will also be impacted as 10% of nitrogen (a key raw material in the manufacture of ammonium fertilisers) production and phosphate exports come from Russia and around 40% of global potash capacity is in Belarus and Russia. Rising fertiliser prices affect global crop yields and will again impact on global food prices.

Food security was already in a precarious position due to climate change and is an area considered by numerous Sustainable Impact funds, with many investing in companies looking to provide solutions in these areas. Whilst stocks are likely to be affected in the near term in the long term the theme will remain relevant and an area for investment and growth.

Energy and the Energy Transition

At the current time the oil price continues to move upwards, supply was already tight post the pandemic and many OPEC countries are already running at near peak utilisation meaning increasing supply is difficult. Climate change, the pressure of the transition to a low carbon economy and a depressed oil price in recent years has also meant there has been less investment in exploration and production. Supply is likely to remain tight for some time meaning the oil price is likely to remain high. Russia is also a key provider of oil and gas particularly for Europe so energy prices which were already high are likely to move higher. However, Tuesday's announcements by Western governments clearly signal a move away from dependence on Russian energy supplies, in Europe and the UK in particular, this will provide a boost to renewables as this area is seen as the way forward. Renewable energy funds have held up particularly well in recent weeks and are back in positive territory as renewables become more attractive. It should be noted that these are long-term investments and will take time to fully come online, but an already attractive long term investment thesis has just received a significant boost.

Caring Capitalism?

Alongside the raft of economic sanctions imposed by governments over the past week we have also seen many global companies announcing they are either suspending activities or pulling out of the Russian market. When you think of companies' involvement in Russia, thoughts first go to oil majors such as BP and Shell who quickly announced they were exiting their joint ventures with Russian companies even before bans on Russian oil imports were announced. Other global brands quickly followed suit, with companies including Apple, Netflix and Unilever all wanting to be seen to be doing the right thing. McDonalds finally announced they were suspending activities in the country after global calls for a boycott of the company if they kept going. Shell wildly misjudged the mood and were forced to issue a public apology after buying cheap oil from Russia at the end of last week, in order to maintain supplies. Consumer pressure to be more responsible is being felt widely and we expect this trend to continue in the long term which will again provide a tailwind for ESG and Responsible portfolios.

In the short term the Ethical and Responsible portfolios will not be able to avoid the inevitable market volatility still to come but in the long term we are seeing strong drivers to support the key themes in the portfolio. We see particular support moving forward for the energy transition/ renewable energy theme, sustainable food and water themes and general support for the idea that companies need to prioritise people and planet - those which do will benefit from consumer support in turn helping their profits.

Please Note: Oil majors and many of the companies mentioned above are not held within the Ethical portfolios and are only used as notable examples of recent company behaviour.

| Whitechurch Investment Team | March 2022 |