



**Singer**  
Capital Markets

# Global Equity Markets Report

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Written by  
Jamie Constable,  
Market Strategist at  
Singer Capital Markets







# AN INTRODUCTION

"Déjà vu" is a much used phrase, but as we come to the end of 2021, it has to be the first phrase written in this annual report!

Again, we start the report writing about Covid-19. Think back a year and the UK moved from Christmas being "normal" to lockdown over a matter of days. Travel was cancelled and shopping trips were hastily made to make sure households were able to put a Christmas meal on the table. Roll forward a year and Christmas 2021 seems to be attempting to replay the same drama – if the politicians and scientists are to be believed. What is the saying from Mark Twain? "History never repeats itself but it (often) rhymes" !

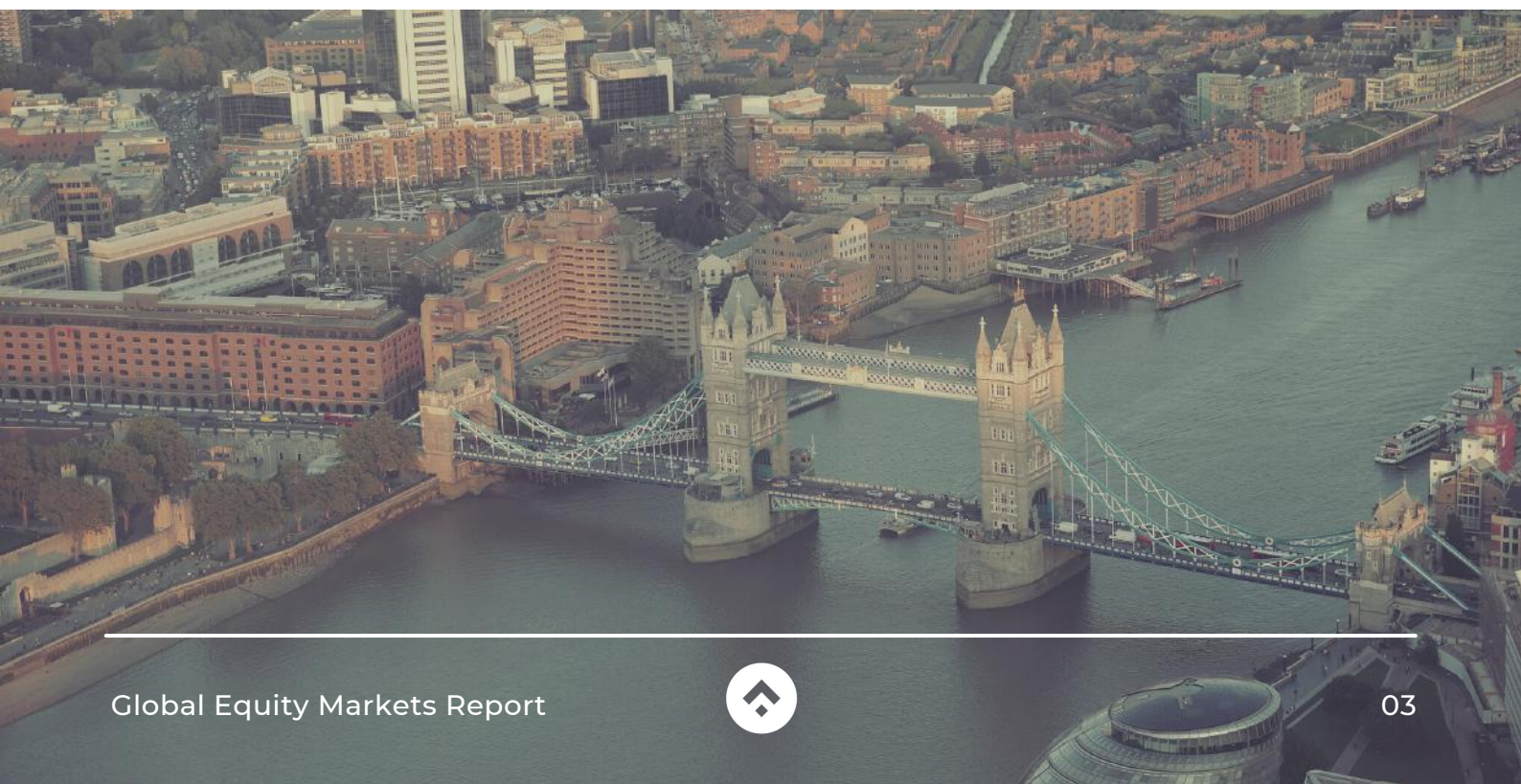
If we look back at the 2021 Half Year Report, the Covid variant strain, Delta, was making all the headlines. Now we have jumped forward to Omicron. It's early days with Omicron, so without a crystal ball, it's very difficult to see how this development will play out. To date there are no horror stories coming out of South Africa and many there are saying that cases are proving to be mild. What does appear to be clear, though, is that it is a lot more transmissible. The risk then is that if cases ramp up rapidly, even if only a small number require hospitalisation, then a country's health services could become overwhelmed. If that were looking likely to happen then governments



may have to reintroduce lockdowns to create a “fire-break” in the rate of infection. We have already see Denmark introduce a soft lockdown and the Netherlands lockdown completely.

The problem with lockdowns is that they will have an immediate impact on the economic recovery and growth, which may require the government to reintroduce direct support / loans for industrial sectors and companies – and maybe even a reintroduction of furlough schemes. What we have seen, though, is that each subsequent lockdown in a country has had less of an impact on growth, as the economy and its actors have learnt to continue activity in differing ways. That is not to say that some of those actors suffer a lot more than others, though. For an example of that, look at the pubs and restaurants in the UK this Christmas where their December trade has been severely compromised.

Equity markets around the world have generally been relatively relaxed over the Omicron variant as measured by the headline indices. “Why?” you may ask – partly that is because economies have seen the impact of each subsequent lockdown lessen as outlined above. Secondly, following the very successful rapid development of vaccines, investors see any likely hit from a variant to be time-limited as the vaccines can be tailored to work against a variant. The challenge to that would be if the frequency of new variants increases to the extent







that it impinges on the time to produce new vaccines.

Boosters are the chosen policy tool against variants in the developed world and, importantly, we are now seeing the developing world receiving plenty of vaccines. The limiting factor is how fast their infrastructure can roll them out. As we wrote in the half year report, investors are now concentrating on how well a country is managing its vaccination programme and the speed of that programme.

Enough of Covid! Since the half year report, inflation forecasts have moved significantly higher across the world. In our 2020 report we talked of the Fed seeing inflation moving above their 2% target for a short time. The last reading for CPI was 6.8% and for their preferred measure the PCE deflator 5%. In the UK CPI has hit 5.1% and is heading higher. More of this later. At least the “transitional” phrase beloved of the central bankers is being retired!

Geopolitics remains in the headlights. China is still threatening Taiwan, but of more note is the continued strained relationship with the US. If anything, it has got worse under the Democrats. Russia has troops massed on the Ukraine border as Putin plays his usual trick of wanting (or is it having to appear?) to be strong at home.

It's the latter, as that is what Russian history is all about. Iran continues to rumble with the nuclear talks said to be starting again in early 2022.

As is traditional, let's go on a trip around the world now, before ending with some concluding thoughts.



**Jamie Constable**

Market Strategist at Singer Capital Markets







# Asia-Pacific





China is, of course, the focus here for more than one reason, and especially as it has been the engine for global growth since the Financial Crisis. The much heralded property sector crisis appears to be finally coming home to roost. Evergrande, once the poster child of the sector, has now defaulted on overseas denominated debt, and it appears only a matter of time before bankruptcy and a wholesale restructuring (with the banks taking pain, too) is negotiated through. Of slight worry is that there is some evidence of contagion into other property companies, something that the Chinese authorities need to allay.

Talking about those authorities, a new Chinese feature for 2022 has been the attacks, and even destruction, of certain sub-sectors led (it appears) by Premier Xi. We have the home tutoring sector told to go non-profit, destroying the market capitalisation of a number of companies. Similar attacks have been made on the video game industry and the mega tech companies. Of course, this is a lot easier in a centrally controlled (or is it dictator-led?) economy, as Xi sets himself up to be leader for life.

The effect of the above has been to significantly slow the rate of GDP growth in China. In effect they appear to be attempting to deflate



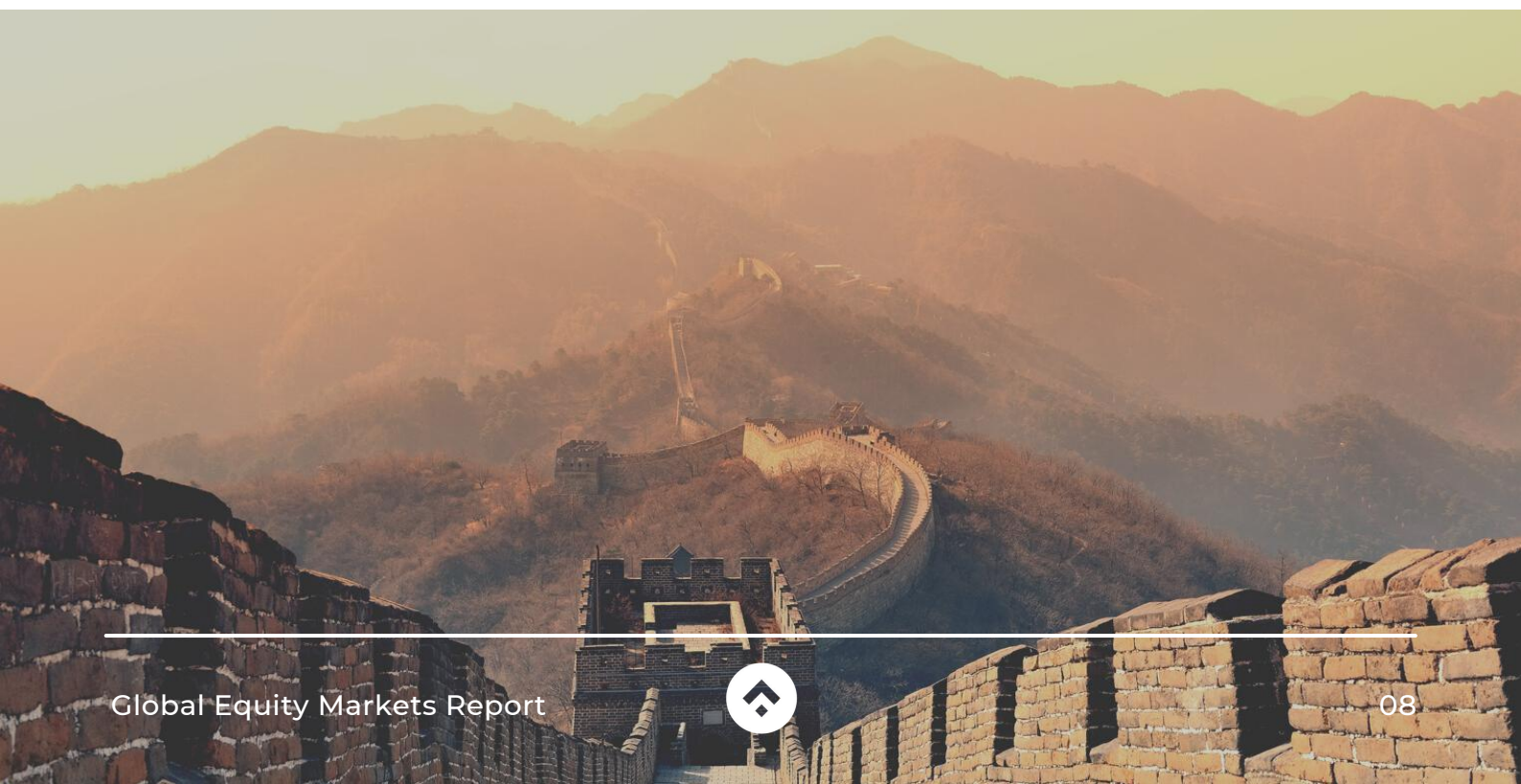
bubbles “gently” without them causing too much damage. All of this couched in Xi’s mantra of “common prosperity” which, for the new wealth titans, means paying a lot more tax and / or a substantial cut in that wealth – or even ending up incarcerated!

The result of the above looks like being that, whilst the rest of the world is tightening monetary policy, it looks like China may be loosening, with one ‘RRR’ cut already. That is likely to have some sectoral impact globally, not least with its impact on commodity prices and thus inflation (i.e. metal prices and their impact on inflation is likely to remain elevated).

The Chinese equity market has substantially lagged other global markets as growth has slowed being down some 6.5% for 2021 at the time of writing, with the Hong Kong Hang Seng down 16.5%, which has been heavily hit due to the attacks on technology companies.

After GDP growth of 8% for 2021, China are exiting for Q4 at around 3.2% annualised, so a significant slowdown after they put the policy brakes on mid-year. 2022 GDP growth is forecast to be just north of 5%.

On geopolitics the disputes with the US remain, at least, as fractious as under Trump as we expected in last year’s note.







In Japan we have had a change of Prime Minister. Is there likely to be any change in policy or outlook? There may be tweaks, but any substantial change is unlikely – although the Bank of Japan have signalled they are ready to start tapering QE. Japan GDP is forecast to grow by 2.9% in 2022 after 1.8% in 2021.

To date, there has been little evidence of the Omicron variant in Asia. If it were to hit, and it seems difficult to see how it will not, then that has implications for supply chains and product shortages and, consequently, inflation. A lag on when the variant hits Europe / North America could make matters even worse, with demand coming back as Asia locks down!



# Europe







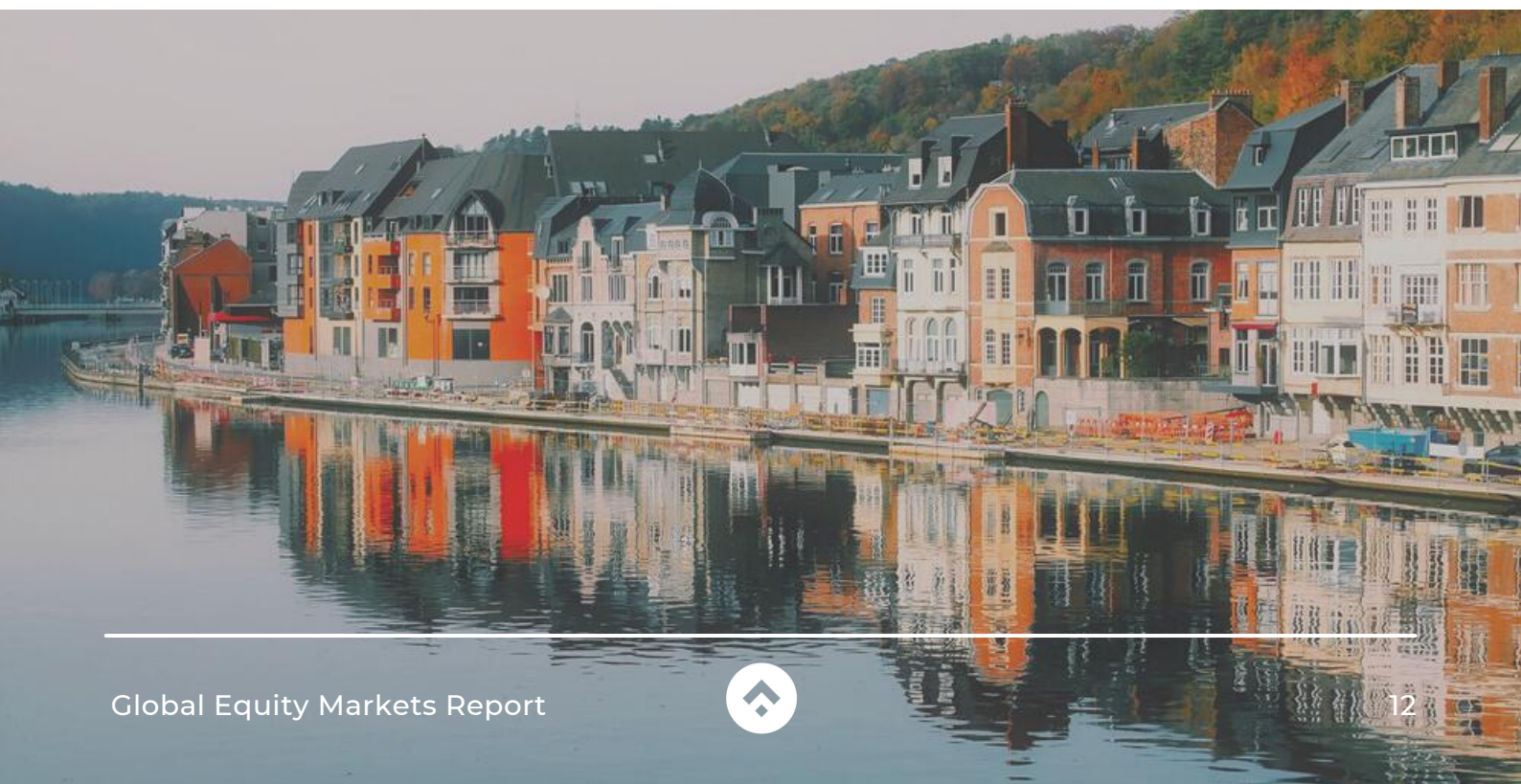
The European Central Bank ('ECB') has defiantly stood against any tapering of QE, but even they are now relenting in the face of inflation being elevated like the rest of western world. They are effectively one of the few, if the only one, hanging onto the transitory mantra around inflation, despite CPI rising to 4.9% with PPI at 21.9%. How long will the Bundesbank be happy with German CPI at 5.2%? Importantly looking into 2022, forecasts are not signalling a fall back anywhere near the 2% target in the short to medium term.

The substantial EU Covid recovery funds will be handed out into 2022 – maybe not to Poland and Hungary, where the disputes with the EC Parliament over national policies continue to rage. The key is how well these are spent by governments and how much actually goes into productive investment in their economies.

Germany has seen the end of an era with Merkel stepping down; the question now being “will there be any significant change in direction?” It’s too early to tell yet. In France we get a Presidential election in April 2022, with Macron still not confirming whether he will stand or not. Expect lots of stories around the renaissance, or otherwise, of the Right – especially if we see more lockdowns.

European equity markets have been some of the best performing in 2021, with mid to high teens and above percentage gains for the indices common, despite them giving up some of those gains into the end of the year on Omicron. Looking into 2022, that leaves equities on relatively high ratings globally.

EU 2021 GDP growth looks like being c.5.4% and the 2022 forecast is for 4.3%, so slowing year-on-year after the bounce back in 2021. The delta (i.e. the rate of change, not the variant), which we have been talking about though the Autumn – in the UK in particular with respect to the RMI (Repair, Maintenance and Improve) construction led stocks and online – is not likely to be the markets' friend, especially with Covid likely to depress Q1 growth.







# USA





The year started with the new President Biden and the Democrats looking at a key 12 months to get his campaign policies into law. It started well with the \$1.2 trillion Infrastructure Bill signed into law in November, following on from the \$1.9 trillion Coronavirus relief package that Biden signed into law in March.

The US economy has had a cracking year. Powell was re-nominated as Fed Governor and has had to retire the term “transitory” with regard to inflation, and the Fed now sees the US as getting close to full employment. There are a record 11 million job vacancies and c.7.5 million claiming unemployment. In a term coined the “Great Resignation” people are changing jobs, often to get pay rises, and wage growth is coming through – especially for the lower paid. All this without having to vote through an increase in the minimum wage.

Despite all of that, Biden is down in the approval ratings and the reason appears to be that theme running through this report, namely inflation, as the populace see their disposable income squeezed with CPI at 6.8%. Importantly as we look forward, their inflation expectations are also rising. 2022 sees the mid-term elections, with Trump still hovering in the shadows. There is a real possibility that the Democrats could lose their Senate “majority”, which is there courtesy



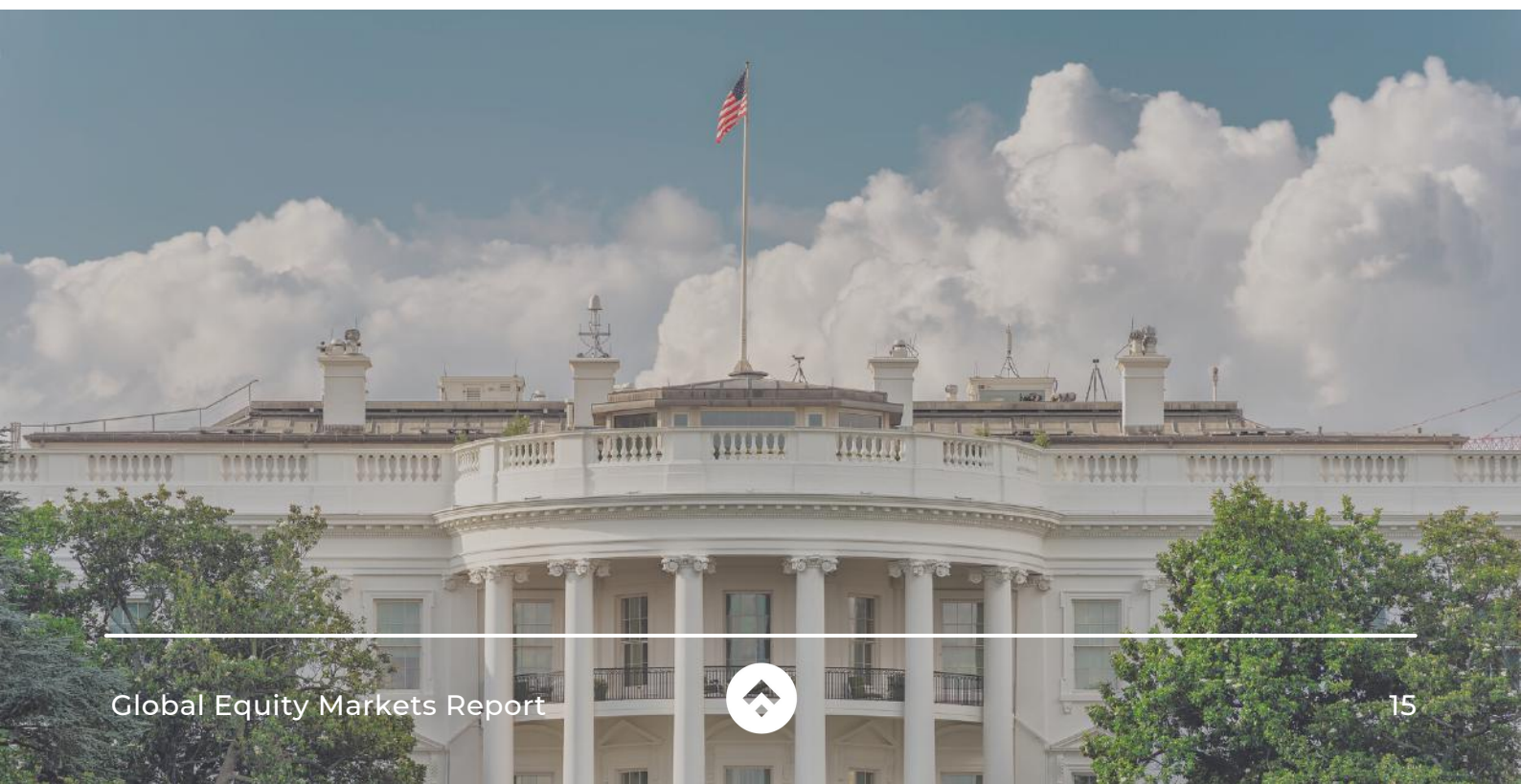


of the Vice President's vote (otherwise tied 50-50). We are seeing the very real issues that this can cause with the problems they are now hitting in voting through the c.\$2 trillion “Build Back Better” bill. One Senator has changed his mind, and they could be back to the drawing board! The likelihood of Biden being a hamstrung President in the second half of his term is, currently, high. To be fair, we thought in last year’s piece that that could be the case in the first two years, but the Georgia election result changed all of that.

Returning to inflation, the markets switched their view on US interest rates in the Autumn, but it took a couple of months more for Powell and the Fed to see what was going on! Powell stood up and finally retired the “transitional” mantra they had been chanting through the year. They had already announced tapering QE, and have most recently doubled it, so bond buying will end on that trajectory by the end of March 2022.

We have started to see 2022 GDP growth forecasts being cut with forecasts now below 4% and some close to 3% from 5.6% in 2021. Like in Europe, the delta is unlikely to be the markets’ friend. With inflation rising, the Fed have a tricky path to navigate.

Despite this, US equity markets have, or maybe because of the above, gone through 2021 continuing to hit new highs and lead global





indices rankings. Technology has stalled a little of late, as the prospect of interest rate rises has risen.

If the Fed follows through on its current agenda, are we seeing a seminal change in the US with “free money” coming to an end for the first time since the Financial Crisis? A world unknown for many of those investors who are new to markets during that period. The consumer has been the driver of the US economy for a long time now.

With inflation high and rising, and free money seemingly coming to an end, it will be a challenge for the rest of the economy to take up the mantle. As mentioned above, wages are rising as are the costs for businesses, with the resultant potential pressure on margins – unless they raise prices. That is the wage-inflation feedback loop that the Fed is tasked to prevent occurring.





UK





Finally then, the UK, and it is difficult to know where to start. An economy that has topped the G7 GDP growth charts with 6.9% growth, but a government that appears to stumble from crisis to crisis! Topping the growth charts was, of course, pretty much the result of being at the bottom of them in 2020 as the pandemic hit!

The UK economy did bounce back then as we expected, but at a much faster rate (i.e earlier in the year). The consumer showed that, when released, they were very capable of spending. Much of those lockdown “enforced savings” remain unspent though, with consumer balance sheets continuing to look healthy. The feel-good factor for property owners was enhanced by a record year for the housing market, going all the way back to 2008. 2022 looks likely to be much quieter with Halifax saying 1% house price growth which, for a body where growth is their mantra, could mean falls.

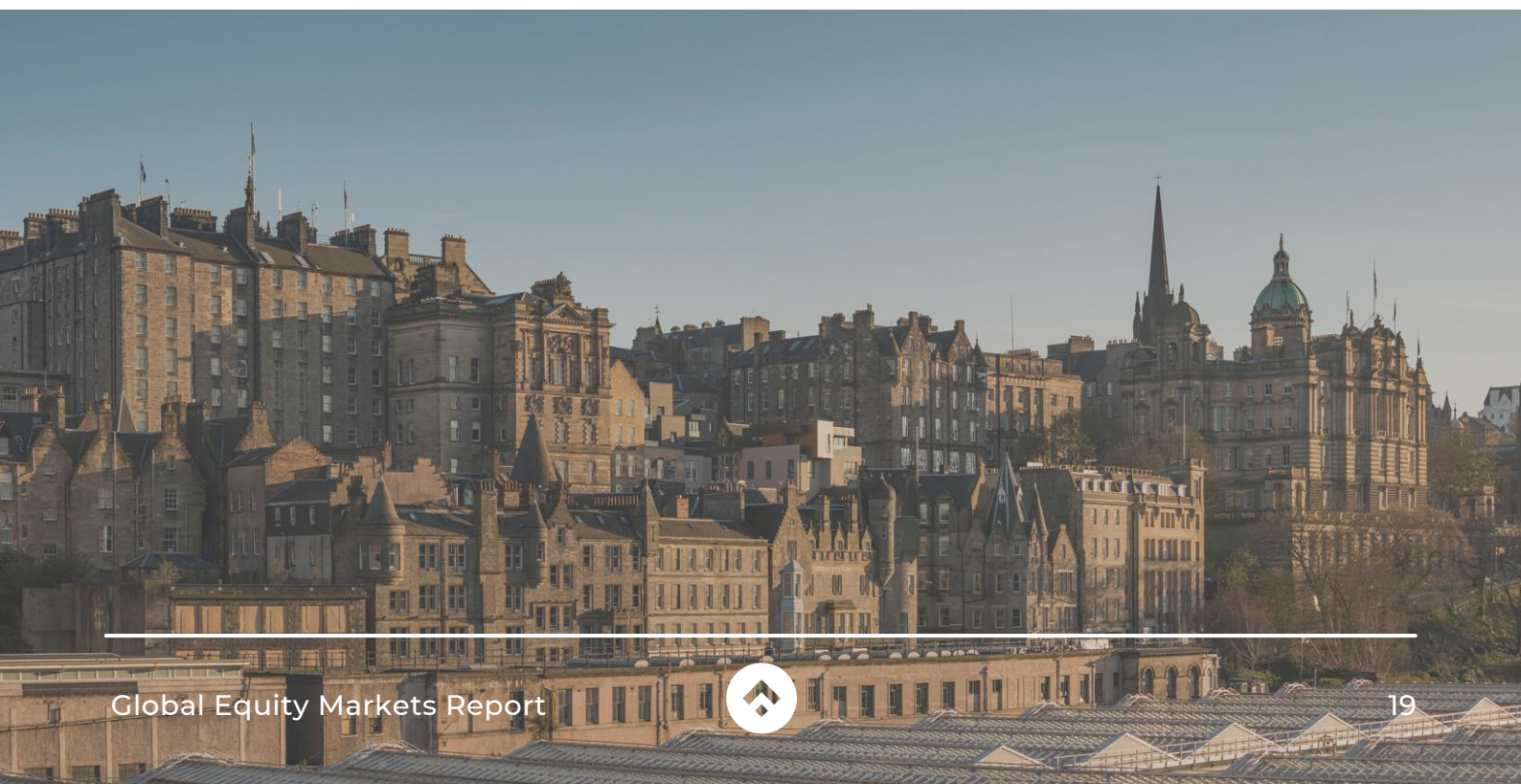
A lot happened in and to markets in the Autumn. Fixed interest futures markets switched their view on UK interest rates to expecting three rate rises in 2022 – coincidentally that is what US markets are forecasting for the Fed rate, too, as CPI continued to ramp ahead of forecasts. The Bank of England lost their way during the year and arguably “forgot” their mandate. It looked like they were back on the





straight and narrow come November as they signalled a 15bps rate rise, but then “wimped out” at the final moment, earning the new Governor the same nickname as Carney, namely the “Unfaithful Boyfriend.” Then, come December, they found themselves in a very awkward situation as there was no rise in unemployment as furlough ended – their most recent mark in the sand – but the Omicron variant had started to rage. With UK CPI at 5.1% against their 2% target and in their new forecasts heading to 6%, they had no choice but to act and raise the UK base rate by 15bps to 0.25%. The futures markets still have three interest rate rises pencilled in for 2022, which would take rates to 1%.

Is the UK close to full employment, then, like in the US? The UK, too, has a record number of job vacancies at some 1.2 million. The official unemployment rate has fallen faster than expected and, for example, the leisure industry was talking of hundreds of thousands of job vacancies they could not fill with similar challenges in logistics, butchery and so on – that all before December got cancelled, of course! On another measure, the number of people in work is back above the level the UK was at pre-pandemic. So, is this buoyancy starting to translate into wage rises? It does appear to be doing so, if evidence and employer surveys are to be believed. For example, we are seeing signing on bonuses for logistics workers and seasonal workers, a 5% backdated rise for Tesco workers and so on. As in the US,





there are some early signs that the balance of power between employer and employee may have moved back the other way somewhat.

The Autumn also saw a few tax and spend bombshells. Employer and employee National Insurance rates are to rise by 1.25% for both parties. Corporation tax is rising from 19% to 25% at the end of the 2022/23 tax year, and the impact of that on companies' earnings forecasts will be right in investors headlights come H1 2022. Following Sunak's Autumn Budget, the UK tax take is projected to be at the highest level since the 1950's, which was when we were rebuilding after World War II – and all under a Conservative government!

Looking back at inflation again, the government's finances are not going to be helped by RPI – generally the measure used for index linked government payments – at 7.1% in November. Already they have limited annual rail fare rises to an over 3% rise rather than a higher figure calculated using their formula. April 2022 will see the next electricity and gas price review with prices expected to rise strongly, again. Do you expect local authorities to put through sizeable percent increases in council tax, too? Their costs are only going one way!



Like the rest of the developed world, UK GDP growth will be lower than 2021 as it cannot be higher, given 2021 was the bounce back year from a disastrous 2020. The delta is, as we have said before, often very important in financial markets. Omicron is starting to drive some 2022 GDP downgrades with Q4 and Q1 growth likely to be impacted. Forecast are now for GDP growth in 2021 of 6.9% and for 2022 4.7%. That is still a very respectable reading given pre-pandemic the UK's trend growth rate was seen to be closer to 2%. Growth was expected to slow through the year, but given the winter slowdown, it could well now be more balanced.

Don't despair then, you could be in bonds – and that helps explain why the outlook for equities remains solid. The UK 10 year gilt yield is currently 0.77% and 2 year 0.52%. If UK interest rates rise to 1% over the next year, how can they maintain these low levels? Something has to give. The metrics to watch are inflation and growth to see whether equities or bonds win out. Our money is on equities as we sit today, with flows into them from bonds. That is not to say that it could be a bit more of a volatile journey as we move through 2022.

Finally, we seem to write this every year (déjà vu again, anyone?) – the UK equity market trading on a 40% discount to global peers on PE's and 45% on price to book. In 2021 M&A was a huge feature – see below – and on those metrics it looks like 2022 will bring more of the same





with private equity having record amounts in their coffers. That lack of inflows into UK equities, in fact outflows, continued for a sixth year after a head fake in Q1 2021 as Brexit was finally confirmed.







# In Summary





To conclude, let's look into 2022 from where we sit today.

**(1). If investors are concerned about one thing it appears to be inflation, not Covid.**

As illustrated by the indices, they have remained pretty sanguine as the latest variant, "Omicron", has spread. Yes, some sectors have risen and others fallen but overall this is nothing like what we saw when the pandemic first hit when equity markets saw dramatic falls. We would explain this through the rapid development of vaccines that can be "tweaked" against variants, looking forward together with economies learning how to function under the "new normal".

The move up in inflation forecasts in the western world through the second half of 2021 has thus seen the interest rate cycle turn, a potential seminal moment for markets. Interestingly, inflation is, so far, not such an issue in Asia. It is in emerging markets, though. Whilst the UK has been the first to raise interest rates in the G7, others have started tapering with the Fed doubling its speed of tapering and three rate rises pencilled in for both countries in 2022. The interest rate rises in some developing countries have already been rapid. Examples in 2021 include four rises in Brazil to 9.25%, five rises in Mexico to 5.5%,



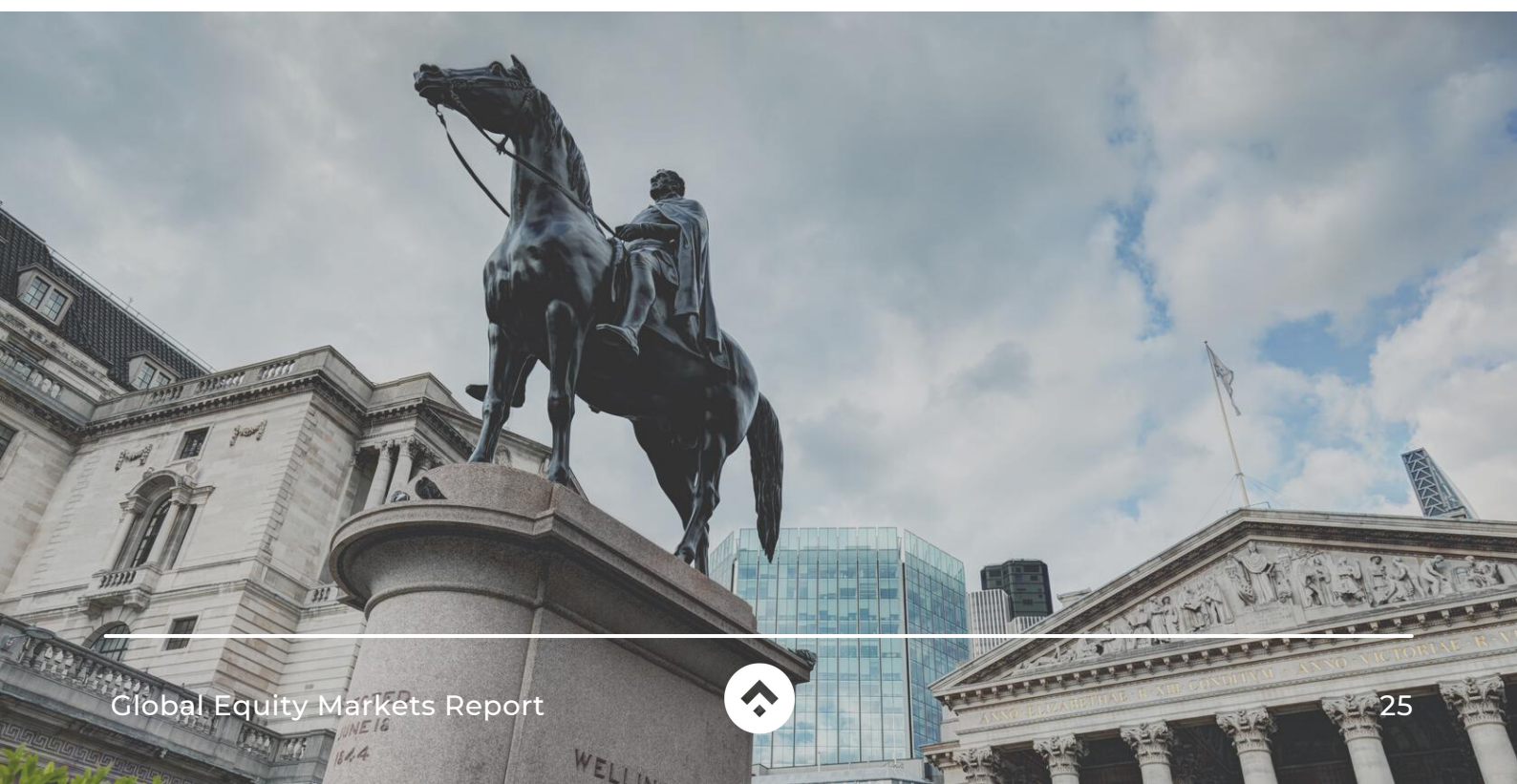


seven rises in Russia to 8.5% and in Poland three rises to 1.75%. Turkey is going the other way, but the less said about their monetary policy, the better!

Money has been effectively “free” for a long time now. Is that tap now going to be turned down, or even off? There may be a lot of repositioning to be done in financial markets if that cycle has really turned. Bonds certainly look exposed under that scenario, especially if inflation continues to ramp. We continue to call for bond yields to rise as they have done in 2021, but not to the extent that we expected.

2022 is arguably one of the most difficult calls we have ever had to make, given all the moving parts at present. Covid and variants – Covid itself and the pandemic with lockdowns – has proven to be inflationary; inflation in prices and wages, supply chain constraints, labour constraints, pressures on governments’ finances and so on. Markets are likely to see the central banks as walking a tightrope of tightening too fast and killing growth or, alternatively, being seen as behind the curve against inflation. The risk of policy error going into 2022 has to be seen as significantly raised.

With all that inflation, as discussed at length, we question which way company margins are going? Pricing power remains a crucial determinant of quality of earnings for many investors.





The scenario we do not want to see emerging for markets is that of stagflation – i.e. inflation remains elevated but growth peters out.

## **(2). COP26 and the drive of ESG investing...**

...into pretty much every investor's process means that this has become mainstream. All corporates need to have up-to-date policies as investors are only going to expect more and more. The move up in oil price as the global economy bounced back in 2021 has illustrated that the move to carbon neutral and to reduce emissions is, at least in the short term, likely to add to those inflationary pressures in the global economy. Just look at how the gas price is moving, not only in Europe as we enter the 2021/22 winter season. It continues to hit new highs with warnings of brown outs as we move to new sources of energy.

## **(3). Supply chains could well be the phrase of the year!**

Did you ever imagine you would be looking at the queues of ships outside Ningbo-Zhoushan, Los Angeles or Felixtowe to determine the outlook for your business? That has been one end of the 2021 supply chain puzzle. At the other – are there enough drivers to collect your



container and deliver it you? Oh, and don't forget, did the factory have enough healthy workers to produce the goods that you ordered in the first place? All of this and the huge increases in freight rates have driven other catch words. "Onshoring", "nearshoring", "reshoring" are some of those words and all of these activities are likely to continue apace through 2022 as companies look to shorten those supply chains and gain more control looking forward.

#### **(4). Capital investment has been low since the Financial Crisis.**

That has arguably amplified the impact of the world attempting to turn itself back on through 2021. One theory is that the continuation of support for "zombie companies" has accentuated this – they run for cash and lower the returns for all. Governments such as the UK are looking to drive up capital investment – the UK to be fair ahead of the corporation tax rise – which would be good for the global economy in 2022. We are certainly likely to see that capital devoted to reducing carbon emissions expand dramatically.

#### **(5). If there is one thing that the pandemic has accelerated for everyone, it is digitisation.**

Valuations on some stocks in fast-growing, new industries may have gone to extreme levels – look at the US in particular here – but this





secular trend is not going to end.

#### **(6). M&A continues to be rampant.**

It has been a record year across Europe, including the UK, going all the way back to 2007 with some \$18 trillion of transactions. The UK was a record 32% of it. With the UK equity market valued as it is – see above – expect more in 2022.

#### **(7). Finally, we have to finish on Omicron.**

If it is as transmissible as they say it is, then we should know very quickly if it is serious (i.e. health systems can't cope) or not. The simple progression of a doubling of cases every two days means that we should know the seriousness of it in the UK at least by the end of the year, probably at the latest. For investors, the recovery of H1 has been followed by a very tricky H2 of 2021 for UK equities. The upside looking into 2022 is that Omicron is very transmissible, but causes mild illness and becomes the dominant variant. That would be a nice Christmas present for us all.

Wishing you all a very Happy Christmas and a prosperous 2022.







**Singer**  
Capital Markets

## Head office

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1 Bartholomew Lane,  
London EC2N 2AX

**+44 (0)20 7496 3000**

**[enquiries@singercm.com](mailto:enquiries@singercm.com)**