Global Matters Weekly
22 March 2021

Bailey, Powell and Lagarde; the new eco-warriors?

– **Robert White, CFA**

For all the column inches dedicated to central bank meetings this month, one potentially seismic change to monetary policy has slipped under the radar over the last few weeks. In the most recent UK budget, chancellor Rishi Sunak announced that the Bank of England should reflect the "importance of environmental sustainability"[1] in policy decisions, which includes asset purchases. The prospect of central banks determining which assets to support based on environmental credentials points to a significant increase in the importance of environmental, social and governance (ESG) factors for investors, and also raises questions about the appropriate role of central banks going forward.

Rishi Sunak's announcement has certainly not emerged from a vacuum; the Bank of England conducted a review of climate risks to the insurance sector in 2015, expanding this to the banking sector in 2018. Outside of the UK, Christine Lagarde has sought to make climate policy a key part of the ECB's strategic review and has already introduced new climate stress tests for Eurozone banks. Even the Fed is now flagging the dangers that climate change poses to financial stability in the US, although it remains a politically contentious issue in Congress.

Before the financial crisis, this sort of ambition from central bankers was near unthinkable; governors were expected to be independent of politics and predominantly focussed on controlling inflation. The rationale behind this remains sound; politicians are required to retain office every few years through elections, and so may have ulterior economic motives which are incompatible with long term price stability.

After two historic global recessions, the role of central bankers is now much broader. Not only have large quantitative easing programs become the norm, but so has buying direct corporate bonds and equity ETFs (the Bank of Japan is now the largest owner of Japanese stocks). Even the notion of political impartiality has been stretched, with the likes of Janet Yellen and Mario Draghi moving into high profile political roles shortly after their tenure as leaders of the two most important banks in the world came to an end.

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Of course, the widening remit of central banks can rightly be justified by their mandate for ensuring financial stability. Increased flooding, droughts and storms are just some of the potential damaging effects of climate change, and it is difficult to argue that these will not create problems for the financial sector. Furthermore, the risk of delaying climate action now could create problems associated with a rushed, disorderly transition to a low carbon economy later. To some however, there is a question as to how much power should be in the hands of unelected technocrats. Are central bankers best placed to determine which companies are the worst polluters? Such decisions are not trivial, and there is plenty of nuance when you delve into the weeds.

Here at Momentum, we believe that you need much broader participation from a range of institutions to tackle environmental issues meaningfully. The change in mindset from central bankers is certainly welcome, but individual companies and investors also need to think in ESG terms. Active managers are particularly well placed in this regard as they have more involvement, knowledge, and influence over the companies in their portfolios. At Momentum, our business was among the first to sign the UN Principles for Responsible Investment back in 2006. We acknowledge that we are in a privileged position to act as fiduciary to our clients and stakeholders, and we take our ESG responsibilities seriously. With the most important global financial institutions now changing policy, it could be costly for investors to ignore.

[1] https://www.ft.com/content/f436d69b-2bf0-48cd-bb34-644856fba17f

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The **Marketplace**

- Global equities fell -0.4% last week
- Government bond yields continued to rise around the world
- Brent crude fell -6.8% to $64.5 a barrel as demand flags in key markets
- Gold rose by 1% to 1745.2 per ounce

Market **Focus**

US

- US equities fell -0.8% last week despite the major index hitting an all-time high last Wednesday before falling back. Energy stocks were the biggest losers
- The composite PMI for February rose to 59.5, it's highest reading in seven years
- The 10-year treasury yield rose for a seventh consecutive week ending Friday at 1.7%. The 2y10y curve steepened to 456.8bps, its highest level since July 2015
- Weekly jobless claims rose to 770K, above market expectations of 700K
- Industrial production fell 2.3% in February
- A dovish policy statement from the Federal Reserve last Wednesday indicated that policy makers are not anticipating any rate hike until 2023 and said they are going to maintain the pace of their asset-purchasing program

Europe

- Continental European equities rose +0.3% last week
- The German 10-year Bund yield rose +1.2bps to -0.29%
- Germany's exports rose 1.4% month-on-month in January, higher than the previous increase
- European car sales slump continued in February with new registrations plunging by 20% to 850K - the lowest total for a month since 2013
- France has imposed a third lockdown in the Paris area
- The EU is seeking to reset its vaccination drive after reversing its Oxford/AstraZeneca ban

UK

- UK equities fell -0.7% last week
- The 10-year Gilt yield rose 1.6bps to 0.8%
- The Bank of England's policymakers voted unanimously to keep the benchmark interest rate at an all-time low of 0.1% and its bond-purchasing program at £895bn
- Britain and the EU are poised to strike a limited deal on post-Brexit financial services co-operation after months of fraught talks
- European Commission President Ursula von der Leyen threatened to introduce emergency controls on vaccine production and distribution and to stop vaccine exports to the UK

Asia/Rest of The World

- The benchmark Global Emerging Markets index fell -0.8% last week
- Japanese equities had a strong week, returning +3.1% by the close on Friday
- Japan's exports fell by a faster-than-expected 4.5% year on year in February,
- Chinese equities fell -0.4% last week - the losses came after an acrimonious meeting between President Xi Jinping and US President Joe Biden earlier in the week
- Chinese retail sales in the combined January–February period rose 33.8% year on year, according to the National Bureau of Statistics
- Brazil's central bank implemented its first rate hike since 2015, and its largest interest rate increase in more than a decade – rates increased from 2.0% to 2.75%
- Turkey's central bank increased its key lending rate from 17% to 19% to address growing inflation risks

Past performance is not indicative of future returns.

Source: Bloomberg. Returns in local currency unless otherwise stated.

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Asset Class/Region	Currency	Currency returns			
		Week ending 19 March 2021	Month to date	YTD 2021	12 months
Developed Market Equities					
United States	USD	-0.8%	2.7%	4.4%	64.4%
United Kingdom	GBP	-0.7%	3.8%	4.9%	31.4%
Continental Europe	EUR	0.3%	4.8%	5.9%	50.6%
Japan	JPY	3.1%	7.9%	11.6%	60.6%
Asia Pacific (ex Japan)	USD	-0.8%	-0.6%	4.3%	79.2%
Australia	AUD	-0.9%	1.2%	3.0%	44.1%
Global	USD	-0.4%	2.7%	4.2%	67.6%
Emerging markets equities					
Emerging Europe	USD	-2.6%	3.6%	2.5%	55.3%
Emerging Asia	USD	-1.0%	-1.2%	4.0%	82.5%
Emerging Latin America	USD	1.8%	6.6%	-3.6%	61.5%
BRICs	USD	-0.4%	-0.5%	3.0%	66.9%
China	USD	-0.4%	-2.6%	3.5%	64.2%
MENA countries	USD	-0.3%	3.0%	8.0%	42.2%
South Africa	USD	-0.4%	5.1%	11.1%	101.9%
India	USD	-1.6%	3.5%	6.5%	86.7%
Global emerging markets	USD	-0.8%	-0.1%	3.8%	78.1%
Bonds					
US Treasuries	USD	-0.3%	-1.3%	-4.7%	-2.3%
US Treasuries (inflation protected)	USD	-0.1%	-0.8%	-2.3%	13.5%
US Corporate (investment grade)	USD	-0.2%	-2.4%	-5.3%	15.7%
US High Yield	USD	-0.5%	-0.7%	0.0%	29.9%
UK Gilts	GBP	-0.1%	-0.1%	-7.3%	0.5%
UK Corporate (investment grade)	GBP	-0.3%	-0.3%	-4.8%	15.2%
Euro Government Bonds	EUR	-0.2%	0.1%	-2.4%	3.7%
Euro Corporate (investment grade)	EUR	0.0%	0.1%	-0.8%	9.8%
Euro High Yield	EUR	-0.1%	0.2%	1.3%	27.8%
Japanese Government	JPY	0.0%	0.6%	-0.7%	-0.8%
Australian Government	AUD	-0.5%	0.8%	-4.3%	-1.1%
Global Government Bonds	USD	-0.3%	-1.4%	-5.1%	4.9%
Global Bonds	USD	-0.3%	-1.4%	-4.2%	9.0%
Global Convertible Bonds	USD	-0.9%	-2.2%	0.7%	43.4%
Emerging Market Bonds	USD	0.5%	-0.8%	-6.1%	20.2%

Source: Bloomberg. Past performance is not indicative of future returns

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Asset Class/Region	Currency	Currency returns			
		Week ending 19 March 2021	Month to date	YTD 2021	12 months
Property					
US Property Securities	USD	-2.0%	2.9%	7.1%	51.1%
Australian Property Securities	AUD	1.3%	3.8%	-3.7%	53.2%
Asia Property Securities	USD	2.4%	1.8%	8.7%	42.2%
Global Property Securities	USD	-0.1%	2.5%	5.0%	54.1%
Currencies					
Euro	USD	-0.3%	-1.4%	-2.6%	11.5%
UK Pound Sterling	USD	-0.3%	-0.5%	1.7%	20.1%
Japanese Yen	USD	0.2%	-2.0%	-5.1%	1.4%
Australian Dollar	USD	-0.2%	0.3%	0.7%	33.4%
South African Rand	USD	1.4%	3.0%	-0.4%	18.6%
Swiss Franc	USD	0.0%	-2.1%	-4.8%	6.1%
Chinese Yuan	USD	0.0%	-0.5%	0.3%	9.2%
Commodities & Alternatives					
Commodities	USD	-2.4%	-0.7%	13.0%	50.7%
Agricultural Commodities	USD	-0.8%	-1.1%	8.3%	46.9%
Oil	USD	-6.8%	-2.4%	24.6%	126.7%
Gold	USD	1.0%	0.6%	-7.9%	18.5%
Hedge funds	USD	0.0%	0.3%	1.9%	19.4%

Source: Bloomberg. Past performance is not indicative of future returns

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