May 2022 | Fund review

Omnis Multi-Asset Income Fund

For the six-month period ending 31 March 2022

We explain how the global economy and financial markets have evolved over the past six months, with a comment about fund performance from the manager responsible for the strategy

View from the Omnis investment team

Robert Jeffree,
Chief Investment Officer

Over the past six months, we have navigated an ever-changing macroeconomic and market environment. Following a pickup in economic growth in Spring 2021, as vaccines paved the way for economic reopening, we saw inflation pick up sharply due largely to supply chain disruptions. Central banks were initially confident that inflation would be transitory, though in reality it has been more prolonged than they expected. Over the review period the Bank of England and the US Federal Reserve began raising interest rates to combat inflation. We also began to see economic growth slow down to more normal pre-pandemic levels.

At the start of the review period, in September 2021, global financial markets were rocked by the news that Chinese property developer Evergrande would likely default on its interest payments to bond holders. In the US the S&P 500 dropped more than 4% in the month; the worst drop in over a year. In the UK the economic rebound slowed as attention turned to the impact of Brexit on the economy.

Volatility in markets continued in October as a global shortage of natural gas supplies impacted energy and fuel price across the world. October also saw the Bank of England warning that the global rise in inflation could slow the UK's economic recovery.

Markets rallied for most of November despite inflation remaining high and the economic recovery slowing down. However, this rally was short-lived as towards the end of the month, Omicron, a new variant of the coronavirus spooked markets across the world. The Omicron variant caused markets to experience a period of volatility, which lasted well into December, but despite this, most global markets ended 2021 with solid gains. The UK's inflation rate surged prompting the Bank of England to raise interest rates in December for the first time since November 2017 and the US Federal Reserve decided to accelerate the tapering of its bond-buying programme sooner than expected; both moves to dampen inflationary pressure.

Markets gave back gains in 2022 due to concerns that the US Federal Reserve would increase interest rates more aggressively to control inflation in 2022; investors began to worry that an aggressive interest rate hike cycle could harm global growth.

2022 has so far been dominated by Russia's invasion of Ukraine on 24 February and the ongoing war. From a social and political perspective, the impact will be hug. Investment sentiment has been rocked causing a marked increase in volatility that we expect will last for some time. There has already been an impact on energy prices, which will prove to be yet another headwind for economic growth around the world and further fuel to inflationary pressures. This may temper the desire of Central Banks to continue raising interest rates.

Ahead of the invasion, Omnis had become concerned about the prospect of sanctions and capital controls on Russia, which could limit our investment managers' ability to sell holdings in the region if necessary. We had exposure to a small number of Russian and Ukrainian holdings in our funds. Omnis Investments, as Authorised Corporate Director (ACD) of its funds, reviewed this exposure to Russia and Ukraine and decided to take action to ensure investors were not exposed to the risk of sanctions or capital controls. Omnis instructed its investment managers to sell their Russian and Ukrainian holdings immediately, and all holdings were sold before the invasion and any sanctions were imposed. We currently have no direct exposure to Russia or Ukraine and an embargo on investing in the region will remain in place further notice.

Stock markets were volatile in March, and oil and gas prices continued to soar with Brent crude reaching $139 a barrel. The International Monetary Fund and World Bank warned that increasing commodity prices are likely to fuel inflation for some time. Concerns that the world economy could suffer a period of stagflation – surging consumer prices combined with weak economic growth – also became more prevalent. The war in Ukraine has and will continue to affect financial markets, as investors weigh up Russian actions the economic implications of sanctions imposed. After an initial fall, share prices recovered some of their lost ground over the second

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half of March. The price of commodities like oil, gas and wheat eased following an initial spike higher, and reaction to the European Union's economic response to the war improved investor sentiment.

While events in Ukraine and concerns over the economic outlook might ordinarily be expected to boost the appeal of 'safe-haven' assets, including high quality bonds issued by the likes of the US and UK governments, the threat of inflation has outweighed such considerations. As a result, bonds have suffered significant losses so far in 2022.

To combat rising inflation, the Bank of England raised interest rates once again in March and, for the first time since 2018, so did the US Federal Reserve signalling that there are likely to be further rises this year. Inflation rates in the US, UK and Europe have now reached multi-decade highs, paving the way for further interest rate hikes for the remainder of this year.

Elsewhere, China's new regulations and restrictions on its tech industry caused another sell-off in its stock markets. China's top economic official responded by saying that the government would take measures to support the economy and financial markets. Following this statement, markets initially performed strongly, but have since levelled off as we are yet to see those words translate into action. Stocks in China also dropped towards the end of the period due to a surge in cases of Covid-19 in parts of the country. This could have global implications as China's zero-Covid policy means strict lockdowns are in place in many parts of the country impacting global supply chains.

Investment outlook

Despite ongoing uncertainty caused by the war in Ukraine, a degree of stability has returned to stock markets as investors perceive that some of the worst-case scenarios have become less likely. However, the unpredictability of the situation means we can still expect to see some volatility in markets for some time.

Russia's invasion of Ukraine, and China's zero-Covid policy continue to cause inflationary pressures. The invasion has elevated energy and commodity prices, whilst the localised lockdowns in China are disrupting supply chains. Both factors contribute to rising prices but there are signs that a peak in inflation is not far off. In the US, key components of inflation such as second-hand car prices are set to fall sharply. In Europe, cuts in fuel duties have been announced.

Central banks are now raising interest rates to combat high inflation after keeping rates very low during the pandemic to help boost growth. The increases are designed to limit inflation by encouraging people and firms to borrow and spend less, and to save more. Continued rate rises are signalled by the central banks in the US, EU, and UK. Should these happen, it is likely that economic growth will slow. Most central banks are mandated to control inflation, but overly aggressive rate rises could trigger a recession. In the short term, market sentiment is likely to remain extremely sensitive to events in Ukraine and the risk of recession remains elevated.

Whilst we are likely to experience further challenging periods in the short term as economic growth slows and central banks navigate the current inflationary environment, it is important to separate out the economic environment from the investment opportunities. Our funds are actively managed by our specialist investment managers who continue to search for quality investments regardless of the more challenging economic environment.

Fund review

The Omnis Multi-Asset Income Fund benefited benefited from a positive contribution from alternative assets over the period, with particularly strong performance from renewable-energy holdings. There was also a broad-based positive contribution from equities, in particular from the energy, health care, consumer staples and industrial sectors. This was partially offset by a negative contribution from holdings in the financial and technology sectors.

Given the rising interest rate environment over the period, bonds were a negative contributor to performance on a currency-hedged basis.

Within equities, we initiated a position in German electric utility company RWE. The company is seeking to transform itself into a leading global renewables business and already boasts an impressive portfolio across offshore and onshore wind, as well as solar energy. We took advantage of share-price weakness caused by a volatile (but now stabilised) political environment to initiate a position in Credicorp, which is a financial-services holding company in Peru, with a presence in Bolivia, Chile, Colombia, and Panama.

Credicorp has a strong track record of value creation, and the group has significant growth opportunities, given low banking penetration in Peru. We sold our holdings in Thailand's Kasikorn bank and PT Bank Rakyat Indonesia. We took advantage of share-price strength to take some profits in Albemarle; the lithium miner retains its appeal as a vital part of the electric-vehicle supply chain.

The holding in Novartis was sold to fund the addition of AstraZeneca; we believe the switch gives the Fund better growth prospects for an acceptably higher valuation multiple. We bought Universal Music Group (UMG), a leading global record label, to add to the Fund's exposure to the growth in music streaming, alongside the existing holding in Hipgnosis.

We also added Taiwanese company MediaTek, a global leader in smartphone silicon processors. The company has a net cash position on its balance sheet, has consistently generated strong free cash flow and appears to have good visibility on its cash dividends. We also added US financial company State Street as a pure play on rising interest rates and because of its oligopoly position in custodial services.

Within alternatives, we sold Atrato Onsite Energy. While the management team is high quality, we felt the valuation looked quite full and it will take a long time for the company to build out its solar capacity. We also sold Home REIT – we continue to like the fundamentals, but the valuation was also no longer as attractive as it previously was.

Within fixed income, we increased the weighting to government bonds from around 1% to 7%, index-linked bonds from 3% to 7%, investment-grade bonds from 1% to 6% and sub-investment grade bonds from 6% to 8%. This resulted in an increase in fund duration from 0.8 years to 2.2 years.

For more information, please speak to your financial adviser, or visit the Multi-Asset Income Fund page on the Omnis website.