MULTI ASSET
DYNAMIC
PORTFOLIO

MARCH 2022

Monthly Update

As Russian troops started bombing Ukrainian cities, tremors were felt across the global financial markets. The markets were already weak due to the roll-back of the unprecedented liquidity pumped into the economy by the Fed and expected rate hikes. But the geopolitical tensions escalated investors' fears and heightened volatility in the markets. During the month, Nifty 50 corrected by 3.1%, while, broader markets fell sharply with midcaps and smallcaps seeing correction to the tune of 6.9% and 9.4%. The US benchmark index S&P 500 extended its January losses of 5.3% and further fell by 3.1% and Nasdaq 100 dipped another 4.6% over the month. Gold yielded return of 7.5% serving as the safe haven during war times.

Russia – Ukraine War and its impact on the markets:

This is not the first time Russia has waged a war on its neighboring countries to arm twist them to accept Russia's demands. The two such recent episodes have been Russia attack on Georgia in 2008 and Russia's annexation of Crimea in 2014. The performance of equity markets during these 2 events is starkly different as seen in the following table:

	Start Date		Nifty 50 (in INR)	S&P 500 (in USD)	MSCI DM	MSCI EM
Russia - Georgia War	1-Aug-08	1M	-1.2%	2.7%	-0.5%	-7.1%
		3M	-38.9%	-22.4%	-29.6%	-45.5%
		6M	-34.9%	-33.9%	-38.0%	-48.6%
		1Y	5.1%	-19.7%	-22.7%	-18.0%
Russia annexation of Crimea	22-Feb-14	1M	7.0%	1.0%	-0.8%	-0.6%
		3M	19.7%	2.9%	2.3%	8.7%
		6M	28.6%	8.1%	4.6%	12.9%
		1Y	43.5%	14.2%	6.5%	2.6%

The above table shows that the timing of the crisis matters more than the nature of crisis itself in the financial markets.

During Annexation of Crimea, the Russian RTS index dropped from 1350 in Jan 2014, to a little over 600 by December 2014. However, the equity markets outside of Russia had a relatively short term and mild impact of the war. The US S&P 500 corrected 5.8%, yet markets quickly recovered their initial losses closing the year higher by 18.2% from the low it made in Feb 2014. Nifty 50 made a low of 6000 as on 13th Feb 2014, a drawdown of 4.8% from the start of the year and closed the year at 8283, a mouth-watering gain of 38% from the low.

On the other hand, the S&P 500 index fell by a more dramatic 43% after the Russian invasion of Georgia in 2008, but that had more to do extremely poor sentiment with the US sub-prime mortgage crisis than Russian invasion. While, the financial markets tend to recover quickly from geopolitical events, it's the timing and the sentiment prevailing during the crisis that matters more.

The current Russia-Ukraine tension is a low earnings risk for U.S. corporates but an energy price shock as a result of disruption or sanctions amid an aggressive central bank pivot focused on inflation is a bad outcome for financial markets. The twin troubles of looming conflict and soaring prices has led to plunge in investor sentiment further putting more downward pressure on equity markets globally. The sanctions put up by US and EU on Russia this time are much more stringent and include ban on the import of Russian oil by the US than those in 2014, which were limited to only financial transactions and did not include sanctions on energy sharing. The equity markets hate uncertainty and a war with no resolution in sight by definition creates uncertainty. While India does not import much crude from Russia, higher crude prices in international markets will inflate input costs for corporates leading to lower profitability and subsequent earning downgrades. An increase in power and freight costs and logistic disturbances could further flare up supply side issues. Strong inflation across the board and slowing global economy growth pose risk for equities as an asset class and Indian equities in particular, being crude dependent.

Having said that, today equity markets have priced a mixture of rising interest rates, war and the highest rate of inflation since 1980s. The S&P 500 entered a correction phase and Nasdaq 100 corrected by more than 20% since its recent peak. Nifty 50 too has seen a drawdown of 15.7% from a top of 18,600 to a recent low of 15683 with smallcaps correcting by almost 20% from the top. However, the uncertainty around the war still remains. This month is crucial as Fed is expected to raise Fed fund rate in its March 15-16 FOMC meeting.

Our Portfolio positioning:

With the rising volatility across the globe, our meters indicated a risk off scenario during February. At the start of the month, we were 70% into equities including US equities. However, our quant meters indicated a sharp cut in equities supported by deteriorating sentiment, waning momentum, weakening technicals, and lesser risk appetite. Our Macrometer indicated a higher probability of stagflation (slow growth and higher inflation) in the global economy. Based on these factors, we reduced our equity exposure to 53% at portfolio level. Historically, gold has yielded impressive returns during times of external shocks such as a war or a global crisis. Our model indicated increasing allocation to Gold from 11% to 15%. We also raised our cash positions from 2% to 12% in the portfolio to navigate the volatile times in a smoother manner. While the valuations look reasonable after the recent correction in equities, we are still in wait and watch mode and closely following our meters to indicate any shuffling in the portfolio in terms of change in allocations. The following table shows how MADP has navigated the turbulent times over the past one month:

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Period	Nifty 50	Nifty 100	Nifty Midcap 150	Nifty Small Cap 250	Nifty 500	MADP
1 M	-7.26%	-7.19%	-9.20%	-10.44%	-7.74%	-1.74%

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