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2021- Looking in the Rear-View Mirror

In contrast to previous years, the total returns on global equities and bonds were quite divergent in 2021. While equities returned a strong +21.8%, global bonds nursed losses of 4.7%.

Equity returns were led by the S&P500, which gave a total return of 28.7% including dividends reinvested. The 28.7% annual return was sharply above the long-run average of 11% over an 88-year history, ranking in the top quartile of annual returns. The broader market was pulled higher by particularly strong performances from the energy (+54.4%), real estate (+46.1%) and information technology sectors (+34.5%). Ironically, despite the strong performance of the infotech sector, the tech-heavy Nasdaq index underperformed the S&P500 returning only 22.2%. As we have written before, the Nasdaq's performance has been concentrated in just a few stocks with the majority of the index constituents struggling to give any return for the full year.

With US equities recording another year of strong performance, global portfolio managers who benchmark their portfolios against the MSCI equity index have their tasks cut out. US equities represent well over 60% of the developed markets index. The MSCI World Index clearly has become more concentrated and does not provide the diversification it once did.

Globally equity returns were quite mixed. **European equities get a very poor press at times, but 2021 should be seen as something of a success** with EuroStoxx 50 index returning 23.3% for the year. However, for dollar-based investors the strong local currency returns were offset by a 7% loss of value in the euro against the dollar.

Asia saw some of the weakest performances. Asia ex Japan was down 4.7% in dollar terms. Among major markets gains were rather modest. Japan returned just 6.6% and China 7.0% in dollars. China was a particular disappointment as the index had started the year on a strongly positive note. The CSI 300 index hit a high of 5809 in February, but ended the year at 4916, a drop of 15% from its high. A major shift in government policy on several fronts didn't help.

But Asia did have its winners, too. India and Vietnam were the outright winners. India's Sensex index gave a capital return of 22%. Returns would have been even better but for the fears of the Omicron strain's impact on global growth that saw some profit taking in the fourth quarter with the index dropping 7% from its October high. The Vietnam Ho Chi Minh Index rose over 30% for the year.

The biggest surprise to the bond markets through to the end of the year was the scale and persistence of global inflation. US inflation, which started the year at less than 2% had by November surged past 6%. At the start of the year, economists had expected inflation to peak in the summer months at around 3-4%. By the end of the year, though, even the Federal Reserve had to give up on the transitory narrative that it had so far been staunchly sticking to.

A mix of strong growth, higher inflation and increasing market anticipation of higher US interest rates weighed heavily on global bonds. The global aggregate bond index finished the year with a loss of 4.7%. The market is

increasingly coming round to the view that we could be in the midst of a structural break with a 40-year trend of disinflation in the major western economies.

The global high yield index ended the year with a modest 1.0% return. To date the high yield market has held its nerve with carry and some spread narrowing contributing to aggregate significantly better returns than high grade bonds.

With the lift off in inflation it remains a surprise that the precious metals markets ended the year nursing losses. Physical demand for gold has remained strong, however investors have only had limited interest in paper gold. ETF buying has been subdued. The attractions of cryptocurrencies to investors looking for an inflation hedge explains at least some of the poor performance of precious metals. Ironically, central banks' gold purchases have remained strong on their view that gold is a valid asset for reserve management of inflation risk.

Among other commodities the 50% plus rise in the spot price of oil surprised many, although many years of underinvestment in exploration and production is starting to limit supply growth and persistently push prices higher.

Table 1: Asset Class Total Returns for 2021 (%)

Equity Market	1 year
S&P 500 INDEX	28.7
DOW JONES INDUS	20.9
NASDAQ COMPOSITE	22.2
NIKKEI 225	6.6
EUROSTOXX 50 (EUR)	23.3
FTSE 100 INDEX	18.4
SWISS MARKET INDEX	23.7
MSCI AC ASIA x JAPAN	(4.7)
MSCI TR Net World (\$)	21.8
MSCI EM Equities	(2.5)
Straits Times Index STI	13.6
CSI 300 INDEX	7.0
Bond Markets	
Global Aggregate Index	(4.7)
Global High Yield Index	1.0
US Treasuries Index	(6.6)
Precious Metals	
Gold oz	(3.6)
Silver oz	(11.7)
Platinum	(9.6)
US Crude Oil WTI \$bbl	59.1

Source: Bloomberg

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