Ostrum
ASSET MANAGEMENT

PRESS RELEASE

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OUTLOOK: Inflation will still influence markets in 2022

After a difficult year in 2020 and in the wake of the 2021 economic crisis, Ostrum Asset Management (Ostrum AM), an affiliate of Natixis Investment Managers, anticipates a return to the pre-crisis trend in 2022. However, markets are still expected to be affected by many risk factors and uncertainties. With inflation expectations on the rise, Philippe Waechter, Head of the Economic Research department, Stéphane Déo, Head of Market Strategy and Ibrahima Kobar, Chief Investment Officer at Ostrum AM present their views on the different sectors and asset classes.

Inflation reached record levels but should only be transitory

According to Philippe Waechter**, most developed economies have rapidly converged to their pre-crisis level**, largely due to the management of the macroeconomy by government economic policy. In Europe, the governments acted preventively, with economic policy alleviating the shock as it occurred and absorbing the risk so that there would be no direct impact on households and businesses. In the United States, the shock occurred during the lockdown period and the authorities therefore had to act curatively to correct its impact and magnitude with measures to support demand.

Overall, **employment has improved rapidly in line with the recovery, thereby legitimizing the policy strategies implemented.**

The disruptions observed in the markets since the spring of 2021 emanate from three key factors: the rise in Chinese imports until the summer, the impact of the incentives put in place by Presidents Trump and Biden between December and March, and finally the diminishing uncertainty with vaccination and the lifting of sanitary restrictions. **The excess demand caught companies by surprise** as demand was mostly for goods and companies had low inventories. This led to an imbalance that resulted in shortages, port congestion, higher freight prices… and a rise in inflation. Once this excess is eliminated, the situation should evolve towards a more stable trajectory.

Inflation has reached levels rarely observed in the last 25 to 30 years. Despite this, there has been no upheaval in the price indices for goods and services in the Eurozone. If we analyze the patterns in the United States, the price of services has hardly been affected and **the volatility in the markets comes exclusively from the price of goods.**

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As for the end of the crisis, we can learn from past events, for Philippe Waechter explains *"After each recession, the growth rate of the new cycle is a little lower than that of the previous one. We should therefore not expect a sudden and lasting increase in growth"*.

What are the risks for the coming year?

According to Philippe Waechter, we will face several types of risks in 2022.

Returning to a normal cycle should cause inflation to slow down. The impact on long-term interest rates should then be reduced. If inflation were to be more persistent through a sustained rise in wages, an inflation premium would be built into long-term interest rates. This would penalize indebted economic actors and the hierarchy in financial investments.

The second risk factor is **the rise in commodity prices, particularly agricultural commodities**, which prices are increasing at worrying levels, with consequences that could be perilous for emerging countries.

The **economic situation in China**, where the country is facing a slowdown in activity (particularly in real estate) and the fragility of local governments, represents a third risk factor.

Finally, **the necessary adaptation to climate change** could lead to upheavals in the months to come.

Tightened monetary policies; persistent inflation still impacting markets

For **Stéphane Déo, Head of Market Strategy** at Ostrum AM, three main themes will be at the center of the markets' attention in 2022: **central banks' decisions, the robustness of fundamentals which will continue to impact credit yields, and inflation which should remain a major issue.**

In mid-December, three major central banks will have to make important decisions. The U.S. Federal Reserve is expected to reverse its tapering, the European Central Bank (ECB) should unveil on December 16 the program that will replace the PEPP [1] and the Bank of England should announce a rate hike, despite the surprise it created this month by keeping its rates unchanged, reneging and certainly reflecting its concerns concerning Brexit. Central banks are therefore facing a global turnaround accompanied by a tightening of monetary policies, suggesting a lot of uncertainty…

The solidity of the fundamentals will continue to impact credit rates, given the very low default rate, which tends to compress the risk premium, and the continued strong presence of the ECB through quantitative easing, absorbing more than the equivalent of the net supply of investment grade credit. On the other hand, risk is very low because interest rates remain very low, which creates favorable borrowing capacities even though companies have restored their margins and cash flows to pre-crisis levels. Finally, the balance sheet situation, and particularly the liquidity position, is very solid.

Markets are changing their minds about inflation. It seems that their opinion has changed quite distinctly since this summer, continuing the trend of the past year.

"The outlook is quite similar in the United States and in Europe: the markets expect inflation to be well above 2% in the immediate future, followed by a rapid decline that would eventually stabilize at a level close to 2%. Inflation is therefore not a transitory phenomenon for the markets", says Stéphane Déo.

2022: where to find value

According to **Ibrahima Kobar, Chief Investment Officer** at Ostrum AM, sovereign bonds could offer opportunities in 2022. Despite exposure to inflation risks, the market seems overly optimistic about European inflation. Sustainable bonds represent a great investment opportunity: nearly €900 billion have been issued in 2021, and investors could benefit from the evolution of the "greenium" and continue to support sovereign issuers in their energy and social transition. For emerging markets, conditions should be more favorable in 2022 and the asset class offers an attractive carry with improved risk resilience.

On the credit market front, fundamentals continue to improve, and Ostrum AM's experts anticipate more "rising stars" than "falling angels" in the coming year. Notwithstanding, interest rate risk management will be an important source of performance, and the teams suggest seeking yield by taking credit risk, by investing in High Yield for example, rather than by increasing the maturity of investments.

Finally, equities should benefit from economic growth. ***"Some sectors such as financials, media, technology, or travel & leisure have interesting growth prospects,"*** according to Ibrahima Kobar. Other sectors such as healthcare, energy and basic resources, and luxury seem to be the most resilient to rising inflation and the impact it may have on margins.

1 PEPP: ECB Pandemic emergency purchase programme

About Ostrum Asset Management

Ostrum Asset Management draws on its investment expertise to enhance the impact of its clients' commitments as they act together to support European citizens' life plans, health, and retirement.

A European institutional investment management leader[1], Ostrum Asset Management supports its clients in their liability-driven investments, offering both asset management solutions on the back of its long-standing fixed-income and insurance-related management expertise (equity and fixed income), and investment services via its innovative technological platform.

Ostrum Asset Management is a well-established responsible investment advocate[2] and manages €440 billion[3] in assets for large institutional clients – insurers, pension funds, health insurers, corporations – as well as €575 billion[3] in assets under administration for professional investors worldwide across all asset classes.

Ostrum Asset Management is an affiliate of Natixis Investment Managers.

1. IPE Top 500 Asset Managers 2021 ranked Ostrum AM as the 51th largest asset manager in 2021. Any reference to a ranking, a rating or an award provides no guarantee for future performance.
2. Ostrum AM was one of the first French asset manager signatories to the PRI in 2008. More details; www.unpri.org
3. Source: Ostrum Asset Management, consolidated data at end-March 2021. Administered assets include Ostrum AM's assets. The services provided for a given client may concern certain services only.

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About Natixis Investment Managers

Natixis Investment Managers' multi-affiliate approach connects clients to the independent thinking and focused expertise of more than 20 active managers. Ranked among the world's largest asset managers1 with nearly $1.4 trillion assets under management2 (€1,199.4 billion), Natixis Investment Managers delivers a diverse range of solutions across asset classes, styles, and vehicles, including innovative environmental, social, and governance (ESG) strategies and products dedicated to advancing sustainable finance. The firm partners with clients in order to understand their unique needs and provide insights and investment solutions tailored to their long-term goals. Headquartered in Paris and Boston, Natixis Investment Managers is wholly owned by Natixis. Natixis is a subsidiary of BPCE, the second-largest banking group in France. Natixis Investment Managers' affiliated investment management firms include AEW; Alliance Entreprendre; AlphaSimplex Group; DNCA Investments;3 Dorval Asset Management; Flexstone Partners; Gateway Investment Advisers; Harris Associates; Investors Mutual Limited; Loomis, Sayles & Company; Mirova; MV Credit; Naxicap Partners; Ossiam; Ostrum Asset Management; Seeyond; Seventure Partners; Thematics Asset Management; Vauban Infrastructure Partners; Vaughan Nelson Investment Management; and WCM Investment Management. Additionally, investment solutions are offered through Natixis Investment Managers Solutions and Natixis Advisors, LLC. **Not all offerings are available in all jurisdictions.** For additional information, please visit Natixis Investment Managers' website at im.natixis.com | LinkedIn: linkedin.com/company/natixis-investment-managers. Natixis Investment Managers' distribution and service groups include Natixis Distribution, LLC, a limited purpose broker-dealer and the distributor of various U.S. registered investment companies for which advisory services are provided by affiliated firms of Natixis Investment Managers, Natixis Investment Managers S.A. (Luxembourg), Natixis Investment Managers International (France), and their affiliated distribution and service entities in Europe and Asia.

1 Cerulli Quantitative Update: Global Markets 2021 ranked Natixis Investment Managers as the 15th largest asset manager in the world based on assets under management as of December 31, 2020.
2 Assets under management ("AUM") as of September 30, 2021 are $1,390 billion. AUM, as reported, may include notional assets, assets serviced, gross assets, assets of minority-owned affiliated entities and other types of non-regulatory AUM managed or serviced by firms affiliated with Natixis Investment Managers. Excluding H2O Asset Management.
3 A brand of DNCA Finance.

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