"A riddle, wrapped in a mystery, inside an enigma" -Winston Churchill on Russia.

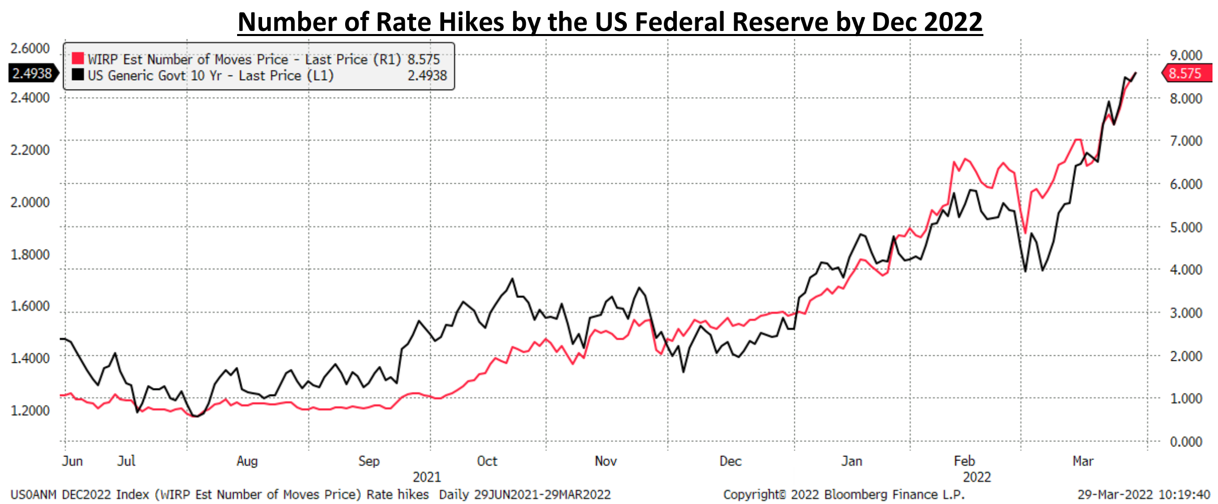
It is easy to become pessimistic when faced with the horrors of war in Ukraine being played out in the news daily, rising prices for everything from food to fuel and fertiliser, and, for UK voters, an unwelcome increase in National Insurance contributions to boot. Economic optimism has dropped sharply in most developed regions, the chart below shows the UK registering optimism worse than at the height of the pandemic, and only matched by the Great Financial Crisis and the late 1970s.

UK optimism for the next 12 months

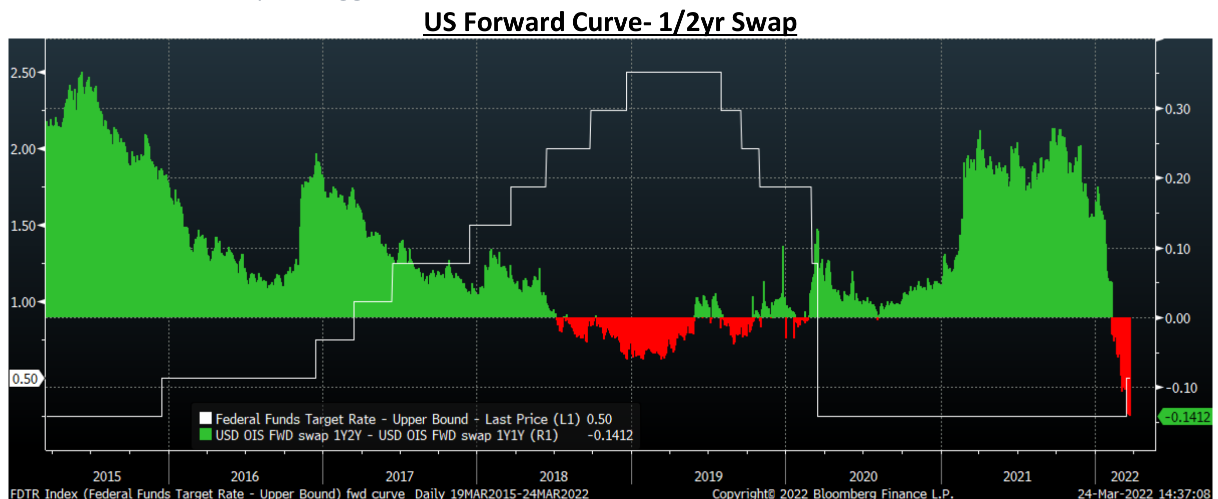
Source: TIM/ IPSOS

Peak fear is hard to time but has usually proved to be a good moment to invest, even though heuristic tendencies tell investors to do otherwise; to sell around peak fear risks causing permanent capital loss at a time when the cost of living is increasing. Even though it is difficult to predict what the full ramifications of Russia's horrific campaign in Ukraine will finally look like, and the attacks and counterattacks may last for months, markets are likely to react ahead of any significant increase in general optimism.

The hawkish commentary after the Federal Reserve announcement of the start of a new interest rate cycle this month has resulted in significant moves in bond yields. Jerome Powell has sought to assuage investor concerns that his policy of raising rates into an already slowing economy risks stopping the economy in its tracks and thereby causing the second recession in little over two years; it is a tight path he seeks to follow, and the risks of a policy error are large. Inflation has hit levels not experienced for 40 years, but that was after peaking at 14.8%, which we do not expect to see in this cycle, especially given the base annualising effects that are about to come into play from next month, however the members of the FOMC are determined to 'do whatever it takes' to bring inflation back under control, despite many of the factors being outside their control. The expectations for number of increases in interest rates put through by the Fed have increased with the 10-year yield over the month to between eight and nine times (from 5 prior to the meeting), but this is significantly below the 12 hikes proposed by the President of the St. Louis Federal Reserve.



Bond markets remain unconvinced by the ability of the Federal Reserve to walk this narrow path without slipping up, and thus the yield curve has inverted with 5-year yields being higher than 10-year ones (and briefly the 30-year yield too), showing that that they expect that the Federal Reserve will have to cut interest rates next year to re-energise the economy, which is the polar opposite of what the latest FOMC dot plot suggests.



One of the major changes brought about by the pandemic and recent ongoings in Ukraine has been an end to the trend towards globalisation and just-in-time manufacturing. Governments and Companies have come to realise that energy security and inventory management can not be taken for granted in times of crisis.

The outsourcing of work and manufacturing to lower cost countries has driven prosperity to the emerging world but has left the developed markets reliant on good relationships and low tariffs (and no embargoes or sanctions) between nations; China's refusal to disavow Russia recently has served to accentuate concerns over security of supply from one of the key beneficiaries of the past 20 years. There has been a realisation that perhaps the risk/reward balance has swung too far and conceivably some jobs and manufacturing will have to return onshore to ensure supply in times of crisis; many companies will not accept running into the problems of being unable to meet demand again.

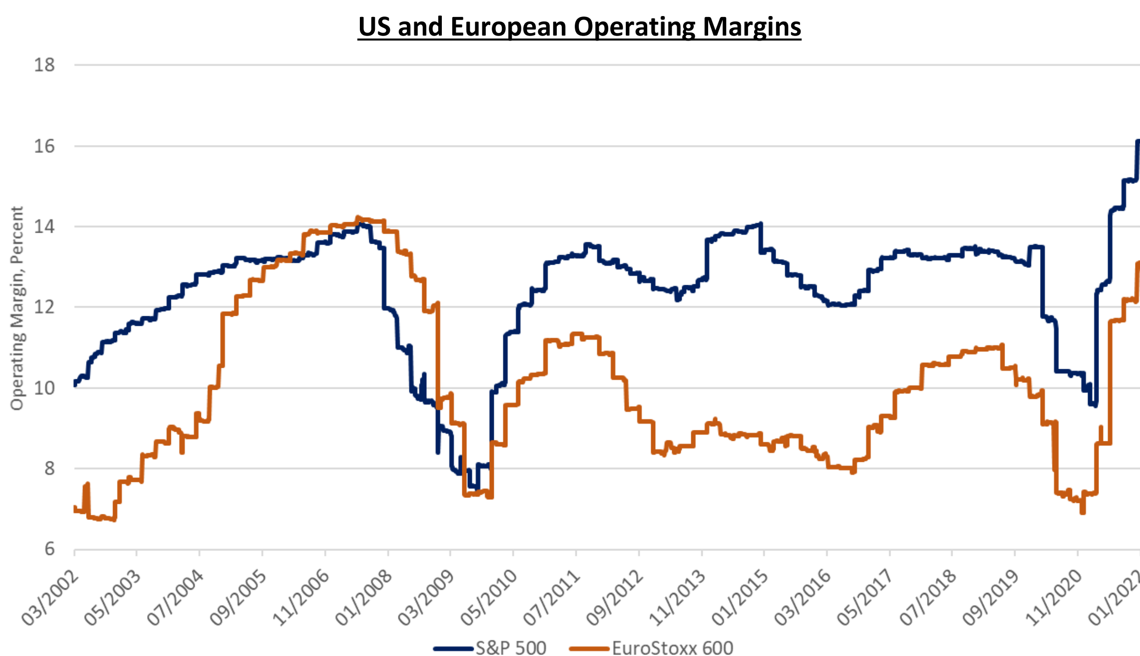
This will likely have an impact on margins for those companies who are unable to pass through the added costs of salaries and raw materials to end consumers. Those with higher gross margins and uniqueness of product are likely to be more insulated, but innovation and investment in research and development will need to remain high to maintain competitive moats wide enough to fend off competition. In the short-term, however, companies still have robust backlogs from orders that they

Value of investments can fall as well as rise and you may not get back the amount you have invested

were not able to fulfil in 2021 and one comment in particular from the Fed's latest Beige Book shows the significance of this: *"Firms reported an increased ability to pass on prices to consumers; in most cases, demand has remained strong despite price increases. Firms reported that they expect additional price increases over the next several months as they continue to pass on input price increases."*

With operating margins above pre-pandemic levels despite the raw material and transportation cost inflation in 2021, the question remains as to how sustainable these margins are in a time when global growth appears to be slowing and capex and inventory restocking are increasing. One of the more notable comments on inventory restocking came from the CFO of Apple, who told us on a call that many companies are double or triple ordering their semiconductor requirements in order to ensure that they do not have to contend with lack of supply again, which has served to increase delivery times at certain nodes.

US and European Operating Margins



Source: TIM/Bloomberg

The VT Tyndall Global Select Fund rebounded well from hitting a 12-month low, ending the month up 4.35%. As a result, the VT Tyndall Global Select Fund B Acc (GBP) returns for 2022 thus far are -7.90%.

Fund Activity and News

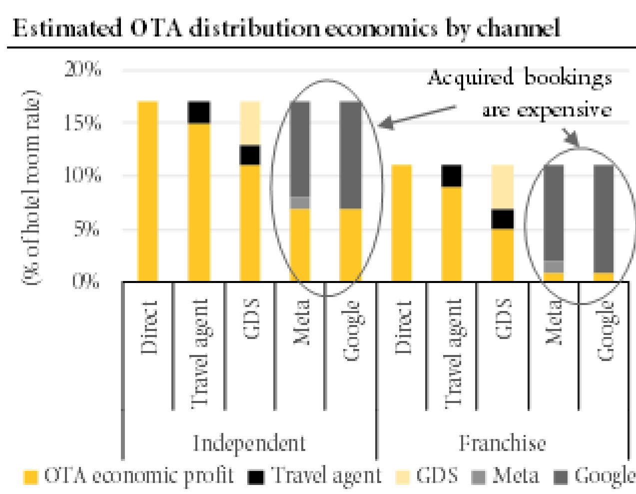
This month we have been more active than normal as we took advantage of the increased volatility in equity markets to increase the size of several of our holdings within the Fund as we believe that once the dust finally settles these investments will prove to be timely and add value for investors.

One of these positions is Booking Holdings, which has been particularly volatile as the war in Ukraine has weighed on people's willingness to travel, and, for obvious reasons, severely impacted its business in Ukraine, simultaneously the company took the decision to cut its listings in Russia and Belarus; Ukraine and the surrounding countries represent around 4% of bookings, while Ukraine and Russia amount to less than 2% of bookings. Against these headwinds also came the news that Google is shutting down its 'Book on Google' offering as it believes that *"people prefer to book directly on partner websites, whether through the hotel itself or with an OTA."*

The fact that even the behemoth Google, openly admits that it cannot replicate the offering that the OTAs such as Expedia, Airbnb and Booking.com do so effectively, removes one of the most perceived

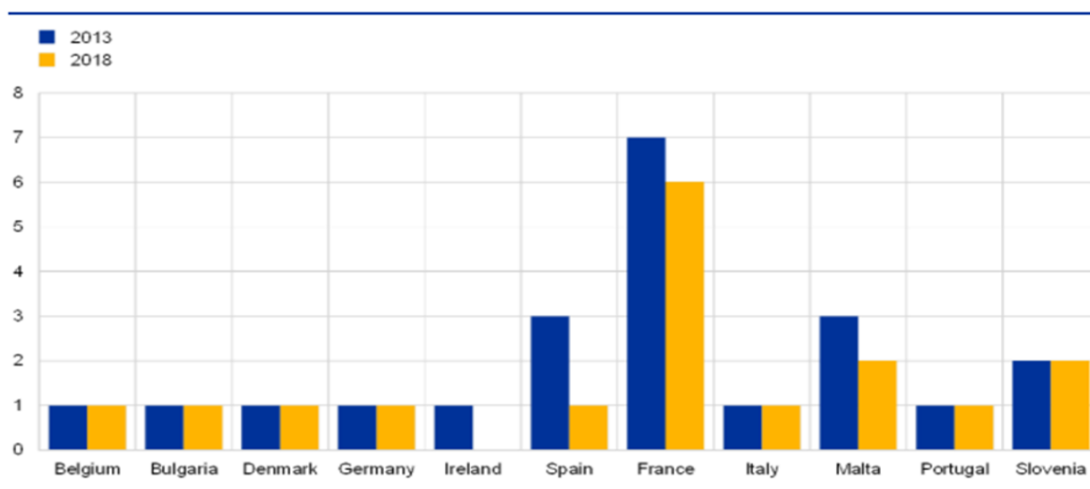
threats to their investment proposition, and suggests that TripAdvisor and Trivago will be facing similar problems to Google in competing.

Google still derives a significant amount of revenue from the OTAs as it monetises traffic diverted to the OTAs by taking as much as 10% of the booking value; prior to COVID, Google earned almost $10 billion of revenues in this manner, however both Booking.com and Expedia have succeeded in increasing their percentage of bookings placed directly through their websites, effectively bypassing Google in the past four years. Booking.com's direct bookings have increased from 40% in 2016 to almost 60% today which substantially increases its profitability when volumes return.



Source: Redburn, company

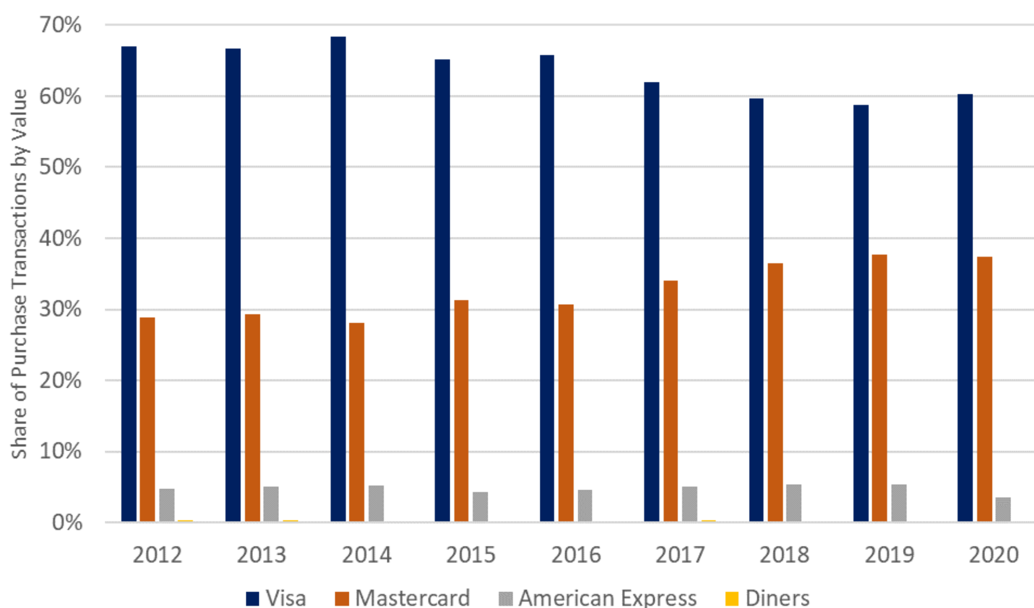
In a similar vein, Finextra reported that the European Payment Initiative (EPI) had abandoned its plans to set up an alternative payment system to the Visa and Mastercard ecosystems, after 20 banks pulled out of the consortium. The scheme was due to be operational this year, but the failure of the project at the first fence, reinforces how strong the competitive moats that both Visa and Mastercard enjoy are. The EPI was set up with the backing of the ECB to stem the tide of domestic card schemes losing share to Visa and Mastercard. The 13, mainly French, remaining shareholders are likely to shift their focus towards the digital wallet instead, where they will have to compete with the likes of PayPal and Square.



Source:ECB

While digital wallets are growing in significance with the growth of ecommerce, on a physical card basis it is easy to see why the ECB wanted to break the duopoly of Visa and Mastercard, but any hope that they will not compete aggressively in Digital wallets too may be optimistic. With both companies investing in Buy-Now-Pay-Later offerings (Visa & Mastercard Installments) to capture the growth emerging in this part of the digital wallet spectrum, the idea that digital start ups will displace the incumbents seems unlikely, and it is more realistic to categorise Visa and Mastercard as enablers for the fintech industry.

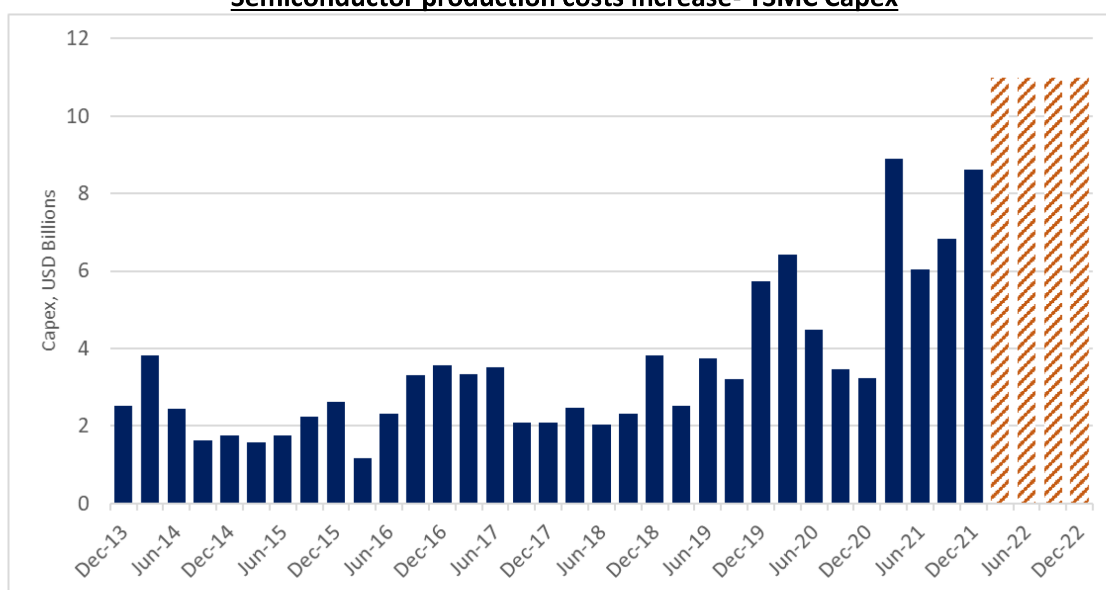
European Card Issuer Share of the Market



Source: TIM/Nilson

During the month we sold our remaining holding in the global leading semiconductor manufacturer, TSMC, which had risen to be the largest company in Asia by market capitalisation, as demand soared for their products over the past few years. The semiconductor field is seeing significant expansion, not only from TSMC, whose capital expansion plans amount to $44 billion in 2022, but also from its peers such as Intel and Samsung.

Semiconductor production costs increase- TSMC Capex



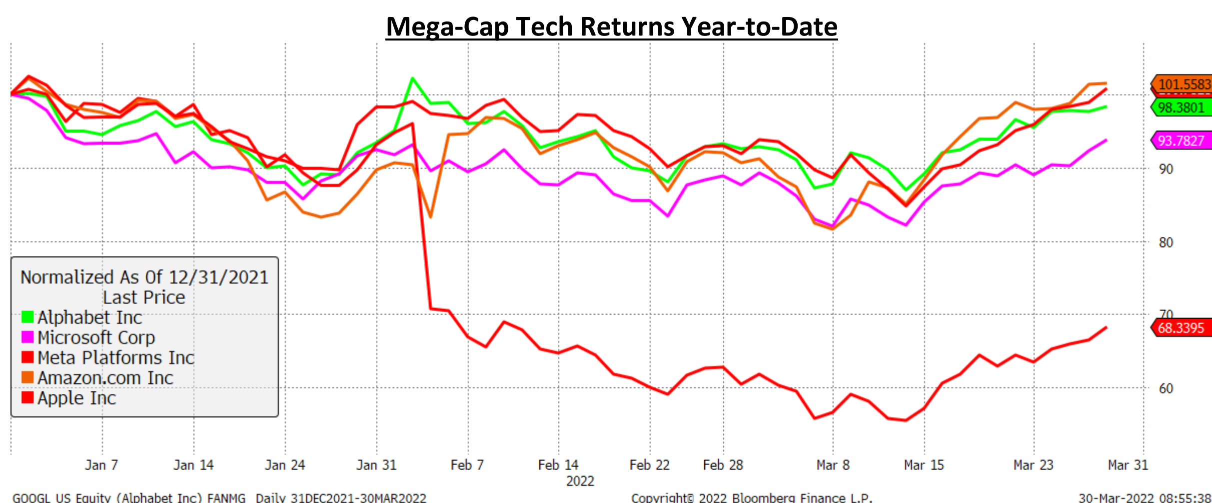
Source: TIM/Company Reports

As mentioned earlier, national security of supply has risen up the agenda, and both Europe and the US are giving large subsidies to companies who build manufacturing within their borders (TSMC is building a plant in Arizona but, as yet is not eligible for any of these grants) as they highlight concerns about being reliant on demand from China and Taiwan, who dominate the market. This is particularly acute owing to the ongoing tensions between China and Taiwan over the ownership of TSMC's parent island. Although the international reaction to, and the troubles that Russia is encountering in Ukraine may temper China's ambitions, the prospect of a Chinese occupation of the island remains a significant threat.

The zero-COVID policy in China puts at risk TSMC's prediction of 20% growth in sales for 2022, as entire cities go into lockdown. We have already seen Apple, their largest customer, run into supply issues as one of Foxconn's major plants had to pause production due to the outbreak in Shenzhen province, the technology hub of China. If the Chinese lockdowns spread further there is a risk to the economic recovery and demand may be softer than the company expects; so far, the company isn't revising its forecasts, as emphasized by its chairman is a recent meeting in Hsinchu, Taiwan. The Fund remains exposed to the long-term growth in semiconductors though its holding in ASML, the world's leading producer of lithography systems which are critical to the production of microchips.

The power of mega-cap companies came under scrutiny this month from both sides of the Atlantic. In the US the Department of Justice said that it would support legislation that would prevent large technology companies from favouring their own services over those of competitors. In Europe the European Union went one step further with their Digital Markets Act, which is due to come into force in October. The aim of the bill is to prevent large technology firms (over €75bn by market capitalisation, and annual revenues in the EU of over €7.5bn and at least 45m monthly users or 10,000 business users in the EU) from using their market position to harm smaller rivals. This is a particularly pointed piece of legislation as many US companies fall under its remit, but in Europe only SAP qualifies. The EU intends to fine violators up to 10% of global revenues and 20% for repeat offenders, but we question how enforceable it will be in practice, and any fines will probably be tied up in legal battles for years to come. Despite being directly targeted by these bills, Amazon and Apple's returns turned positive year-to-date during the month; Alphabet came close too.

Mega-Cap Tech Returns Year-to-Date



Richard Scrope, Fund Manager, VT Global Select Fund, 31st March 2022
Data source (unless otherwise stated): Bloomberg.

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