Aspect8

Monthly Markets Review

May 2022

A look back at markets in May, when global equities remained largely flat and inflation continued to rise.

The month in summary:

Global shares ended May largely flat in US dollar terms. Markets continued to be dominated by worries over rising inflation and a potentially faster pace of central bank tightening, as well as the ongoing war in Ukraine. The MSCI Value index outperformed its growth counterpart. In fixed income, US Treasury yields fell (meaning prices rose). Higher oil prices helped commodity markets advance.

Please note any past performance mentioned is not a guide to future performance and may not be repeated. The sectors, securities, regions and countries shown are for illustrative purposes only and are not to be considered a recommendation to buy or sell.

US

US equities ended May largely flat overall. The Federal Reserve's (Fed) tone grew increasingly hawkish over the month while growth concerns mounted. Chair Jerome Powell stated said that policymakers will "keep pushing" until inflation falls convincingly, while adding that this may require the central bank to move "more aggressively".

The Fed's stance has shifted in response to inflationary pressures, and in spite of signs of slowing growth. The central bank's preferred measure of inflation (PCE) rose again in April, albeit by a more modest 0.2% month on month, versus the previous 0.9% increase. Industrial activity as measured by the purchasing managers' index (PMI) fell from 56 to 53.8 in May, while GDP was confirmed to have contracted in Q1. Consumer confidence also maintained its downward trend. (The PMI indices are based on survey data from companies in the manufacturing and services sectors. A reading above 50 signals expansion).

The S&P 500 was flat over the month. The energy sector was lifted by strong performance from oil & gas constituents. Utilities and financials also made gains. Consumer-linked sectors – both discretionary and staples - were weaker, with major food and household product retailers declining on concerns over inflation's effect on households.

Eurozone

Eurozone shares registered a modestly positive return in May. The energy sector was among the strongest performers amid ongoing robust demand for oil. The financials sector also saw gains, with banks particularly strong. Certain defensive sectors, including consumer staples and real estate, were among the main laggards. Information technology stocks also underperformed.

Euro area annual inflation is expected to be 8.1% in May 2022, up from 7.4% in April according to a flash estimate from Eurostat. This added to pressure on the European Central Bank to raise interest rates, potentially starting from the meeting on 21 July. The flash eurozone composite PMI for May came in at 54.9, indicating positive growth albeit down from April's 55.8 reading.

As the war in Ukraine continued, EU leaders agreed a partial embargo of Russian oil imports which is due to take effect by the end of this year. Russia's Gazprom said it would halt gas supplies to Shell in Germany after the UK-based oil firm refused to use the Kremlin's rouble payment mechanism.

UK

Large cap equities outperformed over the month led by the energy, financials and basic materials sectors, in line with the trend seen since the beginning of 2022. Small and mid cap equities continued to underperform.

It was confirmed that annual UK inflation based on the consumer price index measure surged to a 40-year high in April, reaching 9% compared to 7% year-on-year in March. The latest jump was primarily due to the rise in the government's energy price cap, which had previously sheltered households from rising wholesale energy prices.

Meanwhile, it was revealed that an easing of coronavirus restrictions resulted in the UK economy growing 0.8% over the first quarter. But this respectable outturn masked a deterioration in the monthly profile for March. After a 0.7% expansion in January, GDP was unchanged in February before going on to contract by 0.1% in March. This was contrary to expectations for economic growth to be steady for the month and raising fears of a recession later in the year. In a bid to tackle a cost of living crisis, chancellor Rishi Sunak unveiled an additional package to help households facing an expected further rise in energy bills this autumn.

The Bank of England (BoE) raised UK base interest rates – the so-called "Bank Rate" – from 0.75% to 1% at the start of May. It simultaneously published its latest forecast for the Bank Rate, which it expected at the beginning of May to be around one percentage point higher over the next three years.

Japan

After initial weakness, the Japanese stock market rose in May to record a total return of 0.8%. The yen briefly reversed some of its recent weakness against the US dollar before losing ground again to end May close to the previous 130 level.

As the human tragedy in Ukraine ground on through another month, equity markets were focused primarily on the US inflation outlook and its impact on interest rates. Japan's equity market largely reflected movements in the US, although domestic sentiment was helped by the corporate results season for the fiscal year that ended in March. Given the current macro background and global uncertainty, it was not surprising to see some companies making overly conservative forecasts for the coming year, but the overall tone of results and guidance was still slightly better than expected.

The debate continues to grow around the likely path for Japanese inflation. Numbers released in May showed core CPI (excluding only fresh food) jumped to 2.1% as the significant reduction in mobile phone charges finally dropped out of the year-on-year numbers.

Some clarity was provided on policy emphasis under Prime Minister Kishida's "New Capitalism". There had been some concerns that Mr Kishida himself might put more emphasis on income redistribution. However, the basic outlines of policy released at the end of May have shifted the focus more clearly to economic growth, which was broadly welcomed by the equity market.

Asia (ex Japan)

Asia ex Japan equities were almost unchanged in May, with modest gains in China and Taiwan helping to offset declines in India and Indonesia. India was the worst-performing index market driven lower amid selling by foreign investors. Financial services and information technology stocks bore the brunt of the selling pressure from foreign investors. Share prices were also weaker in Indonesia, Malaysia and Singapore in May.

Taiwan was the strongest-performing market in the MSCI Asia ex Japan index in May, despite periods of volatility in the month, as investor sentiment towards the country turned increasingly positive. Chinese shares also achieved a positive return in May as authorities in Shanghai, the country's commercial hub, announced plans to ease Covid-19 lockdown restrictions. City officials also unveiled plans to boost the economy, supporting hopes for improved growth and demand from the world's second-largest economy. Hong Kong shares also ended the month in positive territory amid a volatile trading month as lockdowns in China hit corporate earnings. Share prices in South Korea and Thailand were also modestly higher in May.

Emerging markets

Emerging market equities posted a modest gain in May, with US dollar weakness beneficial. Concerns over the impact of more aggressive Fed policy tightening and Covid lockdowns in China eased as the month progressed.

Latin American markets generated robust gains, led higher by Chile which was the best-performing index market. In Chile, the publication of the draft new constitution boosted sentiment, removing some uncertainty, and opinion polls suggest that it will be rejected by a requisite referendum.

China recorded a positive return as lockdown measures in Shanghai began to be lifted, and the government stepped up stimulus. Taiwan, driven by a rally in IT names, South Korea, Thailand and the Philippines also outperformed. By contrast, Hungary posted a negative return and was the weakest index market as Prime Minister Orban announced windfall taxes on banks and other large private companies.

Despite a rise in spot prices, net crude oil exporting emerging markets lagged, with the UAE, Saudi Arabia, Qatar and Kuwait all finishing in negative territory. The EU agreed a embargo on Russian oil, albeit with some exceptions, with implementation expected to cover 90% of imports by year end. However, pressure on OPEC to raise production increased. India also underperformed as the central bank unexpectedly hiked its policy rate by 40bps to 4.4%, in response to accelerating inflation which hit 7.8% in April.

Global bonds

Bond markets diverged over the month. US fixed income markets found support following the fierce rise in yields over recent months. Treasury yields were fairly choppy but ultimately rangebound. Federal Reserve (Fed) rhetoric remained hawkish, but against this risk sentiment soured, benefiting safer assets.

Yields in Europe and the UK rose further, with concerns over inflation and interest rate rises remaining to the fore.

The US 10-year Treasury yield fell from 2.94% to 2.85% and the 2-year from 2.73% to 2.56%. There were pockets of weakness in recent activity data, with a notable fall in housing market indicators relative to expectations.

In Europe, the German 10-year yield rose from 0.94% to 1.13%. European Central Bank President Christine Lagarde again indicated readiness to begin raising interest rates in July. The eurozone consumer price inflation (CPI) index preliminary reading for May was a record 8.1% annualised.

The UK 10-year yield rose from 1.91% to 2.10% though the 2-year yield was down from 1.61% to 1.58%. The UK CPI saw a year-on-year rise of 9% in April, a 40-year high.

Corporate bond markets diverged too. US investment grade (IG) saw a positive total return, ahead of Treasuries, while European IG declined and underperformed government bonds. High yield underperformed government bonds as spreads widened. The US saw a small positive total return but Europe declined. (Investment grade bonds are the highest quality bonds as determined by a credit rating agency; high yield bonds are more speculative, with a credit rating below investment grade).

Emerging market (EM) bond performance was likewise mixed. Local currency denominated bonds performed well as EM currencies rallied, particularly Latin American commodity exporters, with the US dollar broadly weaker.

Among hard currency sovereign bonds, investment grade saw positive returns while high yield fell. EM corporate credit declined.

Although global equities finished the month of May with a slight gain, convertible bonds could not benefit and ended the month with a loss. The Refinitiv Global Focus convertible bond index shed -4.1% in US dollar terms. New issuance of convertible bonds remains lacklustre with a volume of close to US$12 billion since the start of the year. This compares to a volume of more than US$76 billion for the same period last year.

Commodities

The S&P GSCI Index achieved a positive return in May as higher energy prices offset weaker prices for industrial metals and precious metals. Energy was the best performing component of the index during May amid rising demand and supply constraints due to the ongoing conflict in Ukraine.

Within the agriculture component, higher prices for wheat and Kansas wheat offset a decline in the price of corn during May. Sugar and coffee prices rose in the month, while the price of cocoa slipped. In industrial metals, prices for nickel and aluminium were sharply down in the month, while price declines for zinc, lead and copper were less pronounced. In precious metals, gold and silver prices were both lower in May compared to a month earlier.

The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.

Overview

Total returns (net) % – to end May 2022

	1 month			12 months		
Equities	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
MSCI World	0.1	-1.4	-0.3	-4.8	8.6	7.4
MSCI World Value	2.1	0.5	1.7	1.0	15.3	13.9
MSCI World Growth	-2.3	-3.7	-2.6	-11.4	1.1	-0.1
MSCI World Smaller Companies	-0.2	-1.7	-0.6	-13.1	-0.9	-2.0
MSCI Emerging Markets	0.4	-1.1	0.1	-19.8	-8.5	-9.6
MSCI AC Asia ex Japan	0.5	-1.1	0.1	-21.6	-10.5	-11.6
S&P500	0.2	-1.3	-0.2	-0.3	13.8	12.5
MSCI EMU	2.1	0.6	1.7	-16.0	-4.1	-5.2
FTSE Europe ex UK	0.6	-1.0	0.2	-12.6	-0.3	-1.5
FTSE All-Share	1.1	-0.5	0.7	-4.0	9.6	8.3
TOPIX*	1.5	-0.0	1.1	-13.4	-1.2	-2.3

	1 month			12 months		
Government bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
JPM GBI US All Mats	0.2	-1.3	-0.1	-7.1	6.0	4.8
JPM GBI UK All Mats	-2.6	-4.1	-3.0	-21.7	-10.7	-11.7
JPM GBI Japan All Mats**	0.5	-1.0	0.2	-16.7	-5.0	-6.1
JPM GBI Germany All Traded	-0.1	-1.6	-0.5	-20.1	-8.8	-9.8
Corporate bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global Broad Market Corporate	0.4	-1.1	0.0	-13.4	-1.1	-2.3
BofA ML US Corporate Master	0.5	-1.0	0.2	-10.3	2.4	1.2
BofA ML EMU Corporate ex T1 (5–10Y)	-0.3	-1.8	-0.7	-23.1	-12.3	-13.3
BofA ML £ Non-Gilts	-1.0	-2.5	-1.4	-20.0	-8.7	-9.8
Non-investment grade bonds	**USD**	**EUR**	**GBP**	**USD**	**EUR**	**GBP**
BofA ML Global High Yield	-0.0	-1.6	-0.4	-11.0	1.6	0.4
BofA ML Euro High Yield	1.5	0.0	1.2	-12.4	0.0	-1.2

Source: Thomson Reuters DataStream.

Local currency returns in May 2022: *0.8%, **-0.2%.

Past performance is not a guide to future performance and may not be repeated.

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