May monthly commentary

June 10, 2022

Towards the end of May, global equity indices broke their multi-week losing streak. There were recoveries across the board. Technical factors played their part, though identifying when shares are oversold is an art rather than a science. More importantly, the benchmark US 10-year bond rallied, with yields all but unchanged over the month but moving down materially from an intra-month high of 3.1%.

This fall in yields was important because US bonds provide risk free rates, off which many investors price other financial assets. It also suggested that people were less fearful of inflation. Against this, yields may also have come down because the chances of an economic slowdown seemed to be growing. One of the key market themes is the tightrope central banks are walking as they try to manage inflation and growth.

After April's worst monthly performance since 2008, the US tech heavy Nasdaq index was still down another 2.1%. The S&P500, the broad US index, did marginally better ending flat for the month. European stock markets were mixed with the Stoxx 600 down 1.6%. The UK's FTSE 100 was up 0.8% the French CAC down 1.0% and German DAX up 2.1%. An easing of China's Covid regulations saw the Shanghai Composite up 4.6%, whilst Japan's Nikkei 225 was up 1.6%.

The outstanding global sector performer was Energy, up 12.7%. This mainly reflected an almost 10% increase in the price of WTI crude oil. The strength in fossil fuel prices is a serious problem. Whilst getting to grips with an over-reliance on Russian oil and gas is part of the story, years of under-investment mean there is no quick fix. Oil majors are in the eye of ESG and political storms. The UK Government's imposition of windfall taxes on integrated oil companies to help finance fuel subsidies added complexity to an already multi-layered investment proposition.

Consumer Discretionary and Consumer Staples were the weakest sectors, both down around 4% with heavyweights Walmart and Target badly missing earnings. These sorts of events are rarely about just one thing, but both provided evidence that customers are becoming more careful with their money given the pressure inflation is exerting on disposable income.

As stated the yields on 10-yr US treasuries moved a lot through May but were little changed over it, closing at 2.84%. Despite the strength in oil, the Bloomberg Commodities Index was up only 0.4%. After an almost 6% fall in April, the AUD managed to recover 1.6% against the USD in May. The VIX fell materially from 33 to 26.2 but this, of course, is still high.

In a relatively quiet month, dispersion between positive and negative contributors to the fund was narrow. The three best performers were Total Energies, Bayer and McKesson, while the portfolio detractors were Secom, Wheaton Precious Metals and Asahi.

May saw what looked like a bear market rally. This is an inexact term for a short sharp recovery in equities in the midst of a longer run downturn. These are useful opportunities for investors to rebalance their portfolios if they are not positioned for what may continue to be difficult times.