Monthly Market Commentary
May 2022

Markets resurface after taking a dive.

- Global equities were slightly down in aggregate for May as a decline through the first half of the month was masked by a powerful recovery rally toward the end of the period.
- The bond rout eased a bit in May as most domestic fixed-income markets were only down modestly.
- Volatile environments provide an opportunity for active managers to review exposures in an effort to weed out likely losers from winners.

Economic Backdrop

Global equities were slightly down in aggregate for May as a decline through the first half of the month was masked by a powerful recovery rally toward the end of the period. Emerging-market shares performed in line with developed markets, but a top-down perspective fails to capture the wide range of regional performances.

Latin American equities generally had the greatest concentration of strong gains in May, with Chile, Colombia, Brazil, and Mexico delivering the top-four country-level performances. The broader Middle East was well-represented among May's poorest performers: the United Arab Emirates, Egypt, Saudi Arabia, Turkey, and Qatar earned five of the month's seven largest losses (Pakistan and Hungary had the first and second steepest drops, respectively).

Among major markets, Hong Kong shares led with a strong gain, and U.K. and Japanese equities also performed quite well. Mainland Chinese shares generated a healthy positive return, while European shares were modestly positive and U.S. shares were moderately negative.

The bond rout eased a bit in May as most domestic fixed-income markets were only down modestly.

Commodity prices continued to climb in May. West-Texas Intermediate and Brent crude oil prices gained 9.5% and 7.9%, respectively, and natural gas prices increased by 10.7%. The EU prepared to impose additional sanctions on Russian oil imports as May concluded, and planned to ban insurance providers from covering tanker ships transporting Russian oil to anywhere in the world.

Russia's aggression against Ukraine has also resulted in sanctions on Russian wheat; this, along with Russia's blockade of Ukrainian ports pushed importers of the food staple further into crisis as the two nations accounted for nearly 30% of global wheat exports in recent years.

Wheat prices advanced by 3% for the full month, but temporarily climbed by more than 20% in mid-May after India—the world's second largest wheat producer—compounded the supply shortage by imposing a wheat export ban as a heatwave threatened output.

United Nations efforts to broker a compromise between Russia and Western powers—which would allow critical Russian fertilizer exports if Russia gives way on Ukrainian ports—received a cool reception by Moscow in late May as it pushed for broader relief from sanctions.

The U.K. signed formal declarations of mutual defense with Finland and Sweden in early May. Shortly thereafter, both Scandinavian countries applied for NATO membership. Their applications—which require unanimous approval by current members—were met with resistance by Turkey; the NATO member demanded that Finland and Sweden both cease support for the Kurdistan Workers Party (PKK) and resume arms exports to Turkey.

Central Banks

- The Bank of Canada (BoC) raised the policy interest rate by 0.50% to 1.5%. This was the second consecutive 0.50% increase and the move was largely expected. Demand and economic growth have both been strong while inflation has been running higher than the BoC target of about 2.0%. Further rate hikes are expected.

- At its early May meeting, the Federal Open Market Committee (FOMC) increased the federal-funds rate by 0.50%—the first hike of its size since 2000—to a 0.75%-to-1% range. The FOMC also announced plans to reduce its balance sheet in June, allowing Treasurys and mortgages to run off (that is, mature without being replaced) at maximum respective paces of $60 billion and $35 billion per month.

- The Bank of England's (BoE) Monetary Policy Committee (MPC) voted to increase the bank rate by 0.25% for the fourth consecutive time at its May meeting, pushing the benchmark rate to 1.0%, its highest level in 13 years. It also began to reduce its balance sheet by ceasing to reinvest proceeds from its asset-purchase program and commencing corporate bond sales.

- The European Central Bank (ECB) did not hold a monetary policy meeting in May. Following its mid-April meeting, the central bank restated its commitment to winding down its Asset Purchase Programme—set to conclude in the third quarter following monthly net purchases of €40 billion (euro) in April, €30 billion in May, and €20 billion in June.

- The Bank of Japan (BOJ) did not hold a monetary policy meeting in May after redoubling its commitment to loose policy at its late-April meeting. Its short-term interest rate remained at -0.1%, and the 10-year Japanese government-bond (JGB) yield target held near 0%. The central bank offered unlimited purchases of 10-year JGBs at 0.25% in order to keep its yield within the BOJ's acceptable range.

Economic Data (unless otherwise noted, data sourced to Bloomberg)

- According to Statistics Canada, the rate of inflation increased (as measured by the change in the Consumer Price Index (CPI)) by 0.6% for April, and 6.8% for the one-year period—both figures remained well above the BoC's preferred range. Inflation was broad-based, led by transportation and fuel costs. Producer price increases eased some, but were still elevated. The Industrial Product Price Index (IPPI) was up 0.8% in April, while the Raw Materials Price Index (RMPI) slipped 2.0%. On a year-over-year basis, the IPPI climbed 16.4% and the RMPI jumped 38.4%. Prices for energy and petroleum products remained strong, while costs for lumber moderated. The labour market remained strong as it added 40,000 jobs in May. Unemployment ticked down 0.1% to 5.1%, while wages grew at a 3.9% clip over the past 12 months.

- The U.S. labour market added 390,000 jobs in May, while average hourly earnings increased by 0.3% for the month and 5.2% over the prior year. The unemployment rate held at 3.6%, just above a 50-year low. The U.S. consumer-price index increased by 8.3% in the year through April, just below the multi-decade high of 8.5% recorded in March. Manufacturing activity in the U.S. was mixed in May, with healthy new-order growth, stagnant employment conditions, and high price pressures. U.S. services growth continued to slow in May after accelerating sharply from the beginning of the year. The overall U.S. economy contracted during the first quarter by an annualized 1.5%, the first decline since the second quarter of 2020.

- Consumer prices in the U.K. jumped by 9.0% in the 12 months to April compared to a 7.0% 12-month climb in March, and the highest level since 1989. UK's claimant count (which calculates the number of people claiming Jobseeker's Allowance) declined in May for the fifteenth consecutive month—by about 57,000, with total claimants representing 4.1% of the population in April compared to 4.2% in March. U.K. manufacturing growth continued to cool slightly in May from a January peak, but remained at healthy levels. Growth in the U.K. services sector dropped sharply during May from elevated April levels and red-hot growth in March. The U.K. economy expanded by 0.8% during the first quarter and 8.7% year over year, slowing from rates of 1.3% and 9.5%, respectively, in the fourth quarter of 2021.

- The eurozone unemployment rate held at 6.8% in April—the lowest level since Eurostat began tracking the dataset in 1998. Consumer prices in the eurozone increased during May by 0.8% for the month and 8.1% for the 12-month period, compared to relatively slower respective rates of 0.6% and 7.5% in April. Eurozone manufacturing activity remained healthy but eased in May compared to the uptick that held through March and April. Expansion in eurozone services maintained a solid pace in May, but below April's peak. The eurozone economy grew by 0.3% during the first quarter and 5.1% year over year, compared to 0.3% and 4.7%, respectively, in the fourth quarter of 2021.

Market Impact (Referenced Index Returns are in CAD)

Global equity markets staged a relief rally in late May, which significantly trimmed earlier losses. Notable developed markets with modest gains included the U.K., Japan and Canada. Domestic gains were mostly attributable to the energy sector, which continued to benefit from significantly higher prices for crude oil. Meanwhile, the U.S. suffered a slight loss and Europe declined in aggregate. Emerging markets were also down, with India declining while Brazil was up, and China had an insignificant gain. Volatility eased, but remained elevated.

Persistent inflation and rate hikes—with the expectation of more to come—remained headwinds for fixed-income markets. After several months of significant declines, most fixed-income markets were essentially flat. Corporate and government bonds fell slightly, while short-term bonds including Treasuries were modestly positive. Real-return bonds and residential mortgages were the worst domestic performers. U.S. high-yield bonds, which are risky and more correlated to equity markets than most fixed-income assets, were positive on a currency-hedged basis but down on an unhedged basis.

Index Data (May 2022)

- The S&P/TSX Composite Index was nearly flat, gaining just 0.06%.
- The FTSE Canada Universe Bond Index was also nearly flat and returned -0.07%.
- The S&P 500 Index, which measures U.S. equities, declined 0.85%.
- The MSCI ACWI (Net) Index, used to gauge global equity performance, dropped 0.92%.
- The ICE BofA U.S. High Yield Constrained Index, representing U.S. high-yield bond markets, returned 0.24% (currency hedged) and -0.80% (unhedged).
- The Chicago Board Options Exchange Volatility Index—a measure of implied volatility in the S&P 500 Index that is also known as the "fear index"—eased from 33.40 to 26.19.
- WTI Cushing crude oil prices—a key indicator of movements in the oil market—moved higher from US$104.69 to US$114.67 a barrel to end May.
- The Canadian dollar strengthened to C$1.26 per U.S. dollar. The U.S. dollar was slightly weaker versus the world's other major currencies; it ended May at US$1.07 versus the euro, US$1.26 against sterling and at 128.65 yen.

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