

# ECONOMIC & MARKET INSIGHTS

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## An Executive Summary for May 2022

Headline market returns were modestly positive, however, May brought another volatile month for investors, adding to an already tumultuous 2022. Macroeconomic risks remained abundant with the war continuing in Ukraine, several notable central banks transitioning to restrictive monetary policy, and the pandemic still having a material impact on select areas of the world (most notably China). The world economy appears to be within a significant regime change which brings a variety of uncertainties to investors. Large-scale macroeconomic shifts usually lead to choppy markets, but can create new opportunities on the other hand.

Inflation was still top of mind for investors. The headline consumer price index (CPI) fell slightly from 8.5% to 8.3% (year-over-year change) in April but is still well above target levels. Strong employment and a firm economic footing have supported the Federal Reserve (Fed) in implementing its second rate hike of 2022 in May and its first 50 basis points (0.50%) increase since 2000. The Fed's recent actions were in-line with expectations and consequently caused minimal movement in yields. Moving forward, futures markets are expecting two additional 50 basis point rate hikes in June and July with further, but potentially smaller magnitude, rate increases from there. Ultimately, the Fed is seeking to bring policy rates back or slightly above neutral levels in hopes of quelling inflation.

Small gains in major equity market indexes disguised significant intra-month volatility. Both cyclical (energy, financials) and defensive (utilities, healthcare) portions of the market were relative outperformers while consumer names lagged. A similar trend is also mostly representative of year-to-date results, and value stocks have far outpaced growth stocks – defying a theme that persisted for much of the last decade. Non-U.S. equities demonstrated outperformance in May, as year-to-date returns are now ahead of domestic counterparts in U.S. dollar terms. Valuations for equities outside of the U.S. remain more compelling, although they come with their own set of risks. That said, negative performance across the board this year has brought valuations much closer to historical averages. The last cycle could be characterized by ample liquidity and tame inflation which translated to record valuations and profit margins for many investment assets, particularly equities. These tailwinds have since converted into headwinds, likely leading to lower forward returns for equities.

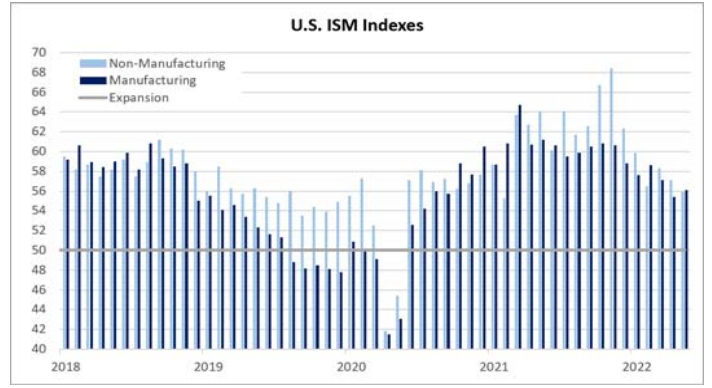
Fixed-income assets generated positive returns over the month, modestly offsetting losses from earlier in the year. After a swift rise, yields fell slightly while moves in spreads were mixed, but muted. Corporate spreads were slightly wider while municipal spreads were tighter – contributing to a strong result for the asset class. Asset flows have turned around for municipals as valuations relative to Treasuries reached their most compelling level since the depths of the COVID-19 Crisis. The municipal market should also be supported by favorable supply/demand factors heading into the summer months following large reinvestment demand paired with muted issuance. The rapid rise in rates throughout 2022 has been damaging to fixed income returns year-to-date, but could provide some support going forward as rates are likely to stabilize and yields have reset to higher levels – providing greater future income. Wider credit spreads could also compress if recession/credit concerns turn out to be overblown.

The alternative asset market continues to grow as investors seek to add further diversification and return generation to traditional balanced portfolios. Hedge funds as a group have offered some protection against market volatility, although performance is highly varied across different strategies. Global Macro funds have been able to profit from volatility and generate positive returns while more directional strategies, such as long/short equity, have again struggled to demonstrate their value-add. Private equity and real estate funds have so far weathered the storm better than public market equivalents and sit on historic levels of dry powder ready to capitalize on further distress.

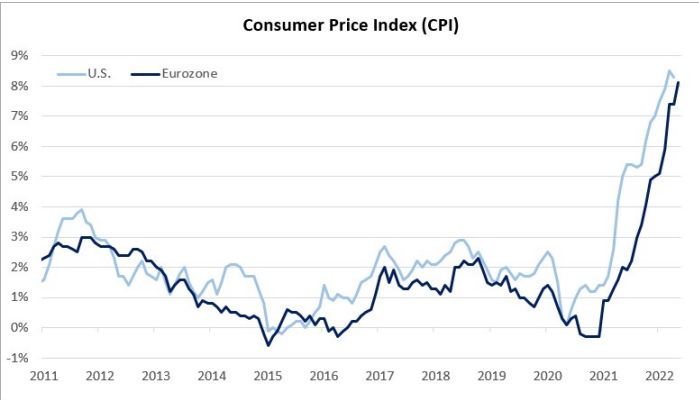
As an investor, the current environment remains complicated. Certain areas of the economy, such as employment, still seem to be on solid footing, although they might be at an inflection point. On the other hand, historic inflation and monetary tightening are rapidly reining in areas of excess in other sectors. During times like these, it's essential to ensure that your portfolio is at or near personal target levels and that desired liquidity is available, to prevent drawing on investment assets during periods of heightened volatility.



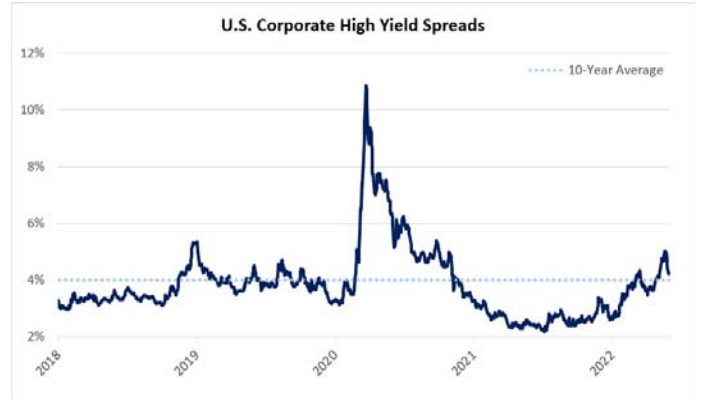
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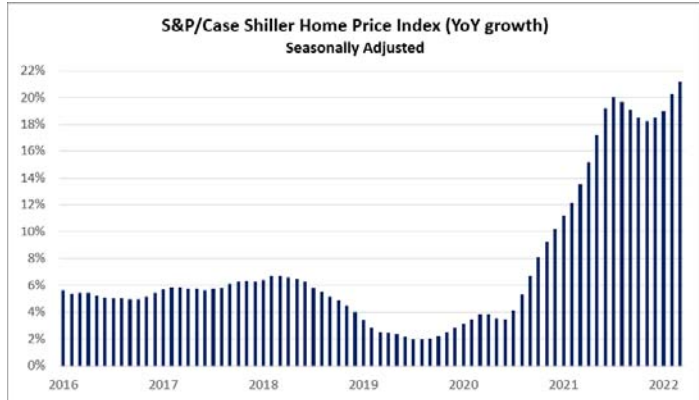
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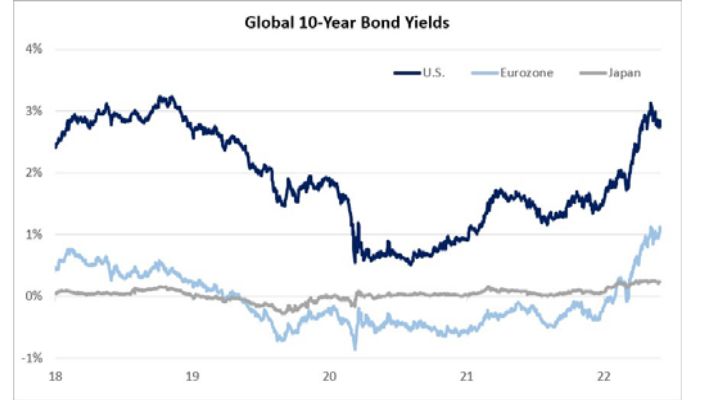
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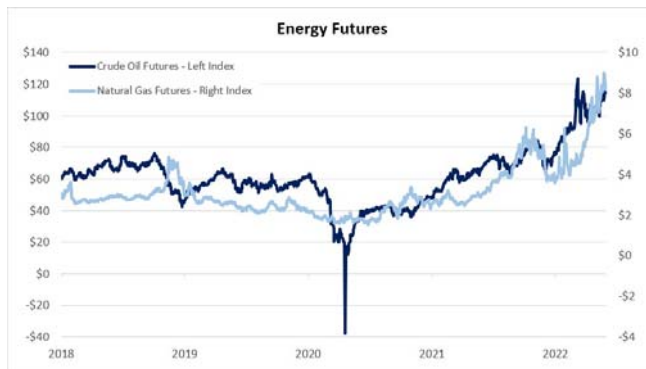
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