RICHMOND HOUSE
INVESTMENT MANAGEMENT

Investment commentary

May 2022

Market overview

Global equities were broadly flat in May although there was a wide divergence in the fortunes of different sectors of the market. Growth stocks declined by 2%, weighed down by continuing concerns over rising inflation, potentially more aggressive monetary policy tightening from central banks and the impact of the conflict in Ukraine. As has been the case through this year so far, value stocks have been less impacted by these concerns and in fact rallied by 2.2% over the month. Value stocks have now outperformed their growth counterparts by over 18% so far this year. Commodity-related stocks were once again strong as Ukraine related supply concerns continued to send prices higher.

The sector makeup and inherent 'value' nature of UK and Japanese markets meant that they were the most resilient over the month, while more cyclical regions such as continental Europe lagged. Some loosening of covid restrictions in China and a slightly weaker US dollar led emerging market equities to outperform.

There was no set pattern to bond returns as a fair degree of the pro-interest rate hike rhetoric has seemingly already been priced in. In the UK, the 10-year gilt yield rose from 1.9% to 2.1% as UK 1-year CPI reached 9%, a level not seen since the 1980s. As expected, the Bank of England raised rates from 0.75% to 1%. In contrast, some weaker economic data and support for dollar assets meant that US treasury yields fell. The 50bps rise in US rates during the month was widely expected and did not impact yields – two further 50bps hikes in June and July have now also been priced in by markets. High yield bonds underperformed as spreads widened but investment grade bond returns also diverged, with positive returns in the US and negative returns from most other developed markets.

The conflict in Ukraine continues to create supply side issues and uncertainties on an array of commodities, which is fuelling inflationary pressures. Increasingly tight labour markets are also beginning to drive wage growth, albeit not in real terms given current levels of inflation, and central banks have an unenviable task of trying to dampen inflation without stifling economic recovery.

Strategy positioning

We have recently reduced exposure to continental European equities in favour of more defensive infrastructure related equities. This was in part a reflection of our view that Europe remains most vulnerable to the impact of the crisis in Ukraine. We are monitoring markets very closely and will continue to make changes across all asset classes as the environment and relative valuations change. There is considerable uncertainty at present, but we believe that our approach of actively managing the asset allocation of investment strategies and ensuring broad diversification at the stock and issuer level is well placed to navigate such a period, as it has done very successfully in the past.

Equities have historically provided effective protection against heightened inflation, and we think it is right to maintain stockmarket positions at their current levels, with the strategies remaining at the upper end of their corresponding Dynamic Planner risk profiles. This positioning is further supported by relatively undemanding valuations and the current outlook of a continued and reasonably healthy profit recovery.

We are very mindful of the potential risks to bond markets; however we are also open to opportunities as markets potentially overreact to news flow and sentiment. The alternatives exposure is also proving valuable as a place where we can identify strategies designed to produce absolute returns, regardless of overall market direction.

Risk warnings