

A Hawkish FED Increased Recession Concerns

As of May 31, 2022

After closing the worst first half of the year, US equity markets rebounded in July to close their best month since November 2020¹. It was a busy month, in which we saw mixed corporate earnings, the highest inflation number in decades, a 75bps rate increase in the Fed's target rate and the result for the 2nd Q GDP growth that showed that the US economy contracted for a second straight quarter. Investors interpreted this data with optimism hoping that the drawdown is priced in and that the Fed could pivot its hawkish path. The Fed recovered some credibility of its ability to tame inflation sending yields down, specially in the long part of the curve, supporting fixed income markets. Positive performance was present across almost all traditional assets classes and regions.

US Equity	Jul-22	YTD	Last 12m
S&P 500	9.2%	-12.6%	-4.6%
Russell 1000	9.3%	-13.6%	-6.9%
Russell 1000 Value	6.6%	-7.1%	-1.4%
Russell 1000 Growth	12.0%	-19.4%	-11.9%
Russell 2000	10.4%	-15.4%	-14.3%
Russell 2000 Value	9.7%	-9.3%	-4.8%
Russell 2000 Growth	11.2%	-21.6%	-23.2%
International Equity			
MSCI All-Country World ex-US	3.4%	-15.6%	-15.3%
MSCI EAFE	5.0%	-15.6%	-14.3%
MSCI Europe	4.9%	-16.9%	-15.1%
MSCI Japan	5.7%	-15.7%	-14.3%
MSCI Emerging Markets	-0.2%	-17.8%	-20.1%
Fixed Income			
U.S. Intermediate Treasuries	1.3%	-4.5%	-5.8%
U.S. Long Treasuries	2.7%	-19.2%	-19.2%
U.S. TIPS	4.4%	-5.0%	-3.6%
Corporate IG Bond	3.2%	-11.6%	-12.6%
High-Yield Bonds	5.9%	-9.1%	-8.0%
Tax-Exempt Bonds	3.3%	-7.7%	-7.7%
International Bonds	2.1%	-12.1%	-14.6%
Emerging Market Bonds	2.1%	-15.4%	-16.4%
Currencies			
Us Dollar	1.2%	10.7%	14.9%
Euro	-2.5%	-10.1%	-13.9%
Yen	-1.8%	15.8%	21.5%
Emerging Markets	-0.3%	-4.2%	-4.0%
Real Assets			
Commodities	4.3%	23.5%	27.2%
Energy	9.6%	41.6%	60.5%
Industrial Metals	0.4%	-11.9%	-7.8%
Gold	-2.3%	-3.5%	-2.7%
Master Limited Partnerships	12.5%	23.8%	25.3%
Real Estate Investment Trust	9.1%	-13.0%	-2.5%
Alternative Investments*			
Equity Hedge	0.9%	-5.7%	-5.4%
Equity Market Neutral	0.4%	-0.1%	0.7%
Event Driven	0.7%	-4.1%	-2.8%
Relative Value Arbitrage	1.2%	-4.7%	-5.3%
Macro	0.4%	-1.1%	-0.3%

Source: Bloomberg data
*AI Source: HFRI Hedge Fund Indices

US Equity

The S&P 500 closed the month with a +9.2% positive performance. Hopes that inflation has peaked, and that the FED could pivot from its hawkish path were important tailwinds for US equity markets that also benefited from better-than-expected corporate earnings of most companies. Growth factor had the highest performance as technology and consumer discretionary companies benefited from corporate earnings, lower rates, and risk-on sentiment. Value factor lagged due to mixed results from banks and underperformance of value defensive sectors as consumer staples and utilities. Small caps outperformed large caps as they enjoyed the risk-on sentiment that drove up stocks with cyclical characteristics.

International Equity

Non-US equities had mixed results as developed regions finished the month in the green but emerging markets were negative. European equities were positive as investors supported the ECB rate hike and the GDP growth reading for the second quarter was 0.7%, surpassing expectations of 0.2%². Nevertheless, the region was lower than the US since the Nord Stream 1 gas pipeline, that sends gas from Russia to Europe, has reduced its capacity and has even been closed, exacerbating the energy crisis in Europe. Emerging markets was dragged down by China, that faces increasing Covid-19 cases, soft economic data and its real estate crisis diminished sentiment for the region. The MSCI Emerging Markets ex China was up +4.64%³ as risk on sentiment benefited most countries.

Alternative Investments

The month dynamics created divergence across the different strategies of hedge funds. Equity hedge strategies were positive for the month thanks to their natural long exposure to equities. Equity market neutral were also positive as the environment was beneficial for stock selection. Event driven strategies faced headwinds from M&A activity and macro hedge funds struggled with the dollar strength and shifts in commodities⁴.

Fixed Income

Yields were lower during the month as investor continue to fear that the Fed's efforts to tame inflation could lead to a recession. These fears were present in the yield curve that was inverted for most part of the month, due to investors flight to quality, pushing the 10-year yield curve from 2.97% to 2.64%. The 2-year treasury yield went from 2.84% to 2.89% in July, widening the spread between these yields. Fixed income assets with larger duration benefited the most as yields drop. TIPS outperformed since inflation continue to be the highest in decades. Corporate bonds had an excellent month as low default rates and risk on sentiment were important tailwinds for the segment, especially for high yield bonds.

Liquid Real Assets

Commodities had positive performance during the month, benefited from energy outperformance. Oil price decreased during the month due to demand fears as global economic growth decreases and production increase commitments from the OPEC. Nevertheless, the energy sector is still enjoying high prices and natural gas surged as Europe's imports continue to decrease. High yields and a stronger dollar continue to weigh on gold and real estate gained from lower rates.

Sources:

1. July 2022. Greycourt. Capital Market Flash Report. A summary of global market activity in July. [Link](#)
2. Euro Area GDP Growth Rate. Trading Economics. [Link](#)
3. Bloomberg data.
4. July 2022. Greycourt. Capital Market Flash Report. A summary of global market activity in July. [Link](#)

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