

# Recessionary fears and cost of living concerns to the fore

## Monthly Commentary

For wholesale or professional investors only

Recession fears continued this month as investors grapple with the effects of aggressive monetary tightening into a slowing global economy, hampered by war in Europe and lockdown in China. Starting with the US, the resilience of the consumer in the face of falling real incomes has been a positive surprise over the last year. Average weekly earnings, adjusted for inflation, have fallen for 13 consecutive months and are more than 6% off the highs reached in April 2020. It is the roughly \$2.5 trillion in excess savings built up during the pandemic that has kept the spending party going, whilst also fueling the highest rate of inflation since the 1980's. In April, real US personal consumption expenditures continued to grow at a healthy clip of 0.65% over the last month. However, the party appears to be coming to an end. The personal savings rate, which reached an all-time high of 33% at the height of the pandemic, has now fallen to its lowest level since August 2008 at just 4.4%. Earnings for major US retailers are often seen as a bellwether of the strength of the consumer and thus the state of the US economy. Many were therefore taken aback this month when the likes of Target, Walmart and Kohls issued profit warnings on the back of both rising costs as well as a slowdown in consumer spending.

The recessionary fears have been accompanied by growing calls of a 'peak' rate in inflation. Indeed, the latest year-on-year US CPI data showed prices grew by 8.3% in April versus 8.5% in March. However, the lower CPI number offered little relief to investors or the Fed as core inflation measures (ex-food and energy) continued to accelerate. Shelter CPI, which includes rental prices and makes up roughly 30% of the CPI basket, has grown at a faster rate for 15 consecutive months. The latest data show growth of 5.1% in April 2022. In the Euro Area and the UK, 'peak' inflation is likely to occur much later than in the US. The UK reported inflation of 9% in April, versus 7% in March. German HICP grew by 8.7% in May versus 7.8% in April. The overall Euro Area HICP grew by 8.1% in May. The faster inflation of Germany and Britain relative to the US is of course due to a much larger energy shock. Energy prices have contributed roughly 4 percentage points to inflation in Europe versus 2 percentage points in the US.

In the UK, Chancellor Rishi Sunak has responded to growing pressure to deal with the cost-of-living crisis which has become a reality for many low-income households. Jonathan Brearley, the head of Ofgem (UK's energy regulator) warned that the number of Britons facing fuel poverty could double from 6.5 million to 12 million after revealing a further 42% increase in the energy price cap this October. Sunak's £15bn package involves £9bn of direct spending to low-income households and pensioners. The chancellor also announced a 25% windfall tax on 'extraordinary profits' of oil and gas companies, with the hope of raising £5bn over the next year.

### Export bans exacerbating food costs

Sadly, whilst developed countries face a 'cost-of-living crisis', much of the developing world risks famine and starvation. The war in Ukraine has disrupted exports from two agricultural exporting powerhouses. According to UN Comtrade, from 2016 to 2020, Russia and Ukraine accounted for 24% of global wheat exports, 57% of sunflower seed oil exports and 14% of corn. Since the war broke out, prices for several agricultural commodities have surged. The UN's FAO food index is at an all-time high, up 15% from the start of this year. Several countries have announced export bans to prioritize domestic needs. This month, India announced an export ban on wheat, following a heat wave which reduced output. Wheat futures increased 6% after the announcement. According to the International Food Policy Research Institute (IFPRI), India is among 20 other countries that have imposed some form of export restrictions since the war began, with those restricted exports making up roughly 10% of calories on the global market. The experience from the 2008 food crisis shows that export bans end up exacerbating the problem and lead to acute shortages particularly for commodity importing nations.

In China, the worst is likely over. A sharp fall in Covid cases has allowed Shanghai to exit lockdown and roll back several restrictions. As expected, the economic data show the brutal impact of the lockdowns. Retail sales plunged by -11.1% in April following a -3.5% drop in March. Industrial

production also fell -2.9% over the previous 12 months, with car production down -31.8%. China's premier Li Keqiang warned this month that the economy may struggle to grow in the second quarter. He highlighted the worrying unemployment picture, with a record 18.2% of people aged 16-24 out of a job. The policy stance has remained expansionary. The most recent measure taken at the end of this month was a drop in the 5-year prime loan rate from 4.6% to 4.45%.

### Late month rally a triumph of the optimists?

Following a dismal April which rolled into early May, markets have recovered strongly over the last week to finish the month flat (based on the MSCI World Index). Looking at the different investment styles, value stocks continued to outperform having not been caught up in the initial selloff to the same extent as growth stocks.

The improvement in market sentiment was supported by positive economic data on the strength of the consumer, Shanghai beginning to reopen and inflation expectations easing. Is this enough to mark a continued improvement in sentiment? The potential for an easing of supply chain pressures to rebalance the demand and supply dynamics is clearly a positive, but energy inflation, food inflation and the broader tightening of financial conditions remains a concern. Indeed, record high German inflation driven by energy and food costs, added further pressure on the ECB to act and raise rates.

Inflation expectations remain key to engineering a soft landing and avoiding a recession. In the US, the 5-year, 5-year forward bond posted its biggest drop in May having hit a record of 3% last month. Whilst inflation expectations are coming off extremely high levels, it does suggest the market has some confidence in the Fed's ability to manage inflation. The US 10-year bond tightened over the month finishing at 2.82%, 12 basis points lower. The UK 10-year and the German 10-year bond both widened by around 12 basis points.

### Pyrford International

31 May 2022

Pyrford International Ltd is a wholly-owned subsidiary of Columbia Threadneedle Investments UK International Limited, whose direct parent is Ameriprise Inc., a company incorporated in the United States.

### Risk disclosure

*This document is a marketing publication and a financial promotion and has not been prepared in accordance with legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research.*

*The investments and investment strategies discussed are not suitable for, or applicable to, every individual. All investments involve risk, including the possible loss of principal and a positive return is not guaranteed over any period. Past performance is not a guarantee of future results. Performance data shown in the document may not be in the local currency of the country where an investor is based. Actual returns may increase or decrease as a result of currency fluctuations. Dividends are not guaranteed and are subject to change or elimination.*

*The material contained in this document is for general information only and is not intended to serve as a complete analysis of every material fact regarding any company, industry or security. The opinions expressed here reflect our judgment at this date and are subject to change. Information has been obtained from sources we consider to be reliable, but we cannot guarantee the accuracy. The material may contain forward-looking statements and investors are cautioned not to place undue reliance on such statements, as actual results could differ materially due to various risks and uncertainties.*

*This material does not constitute investment advice and is not intended as an endorsement of any specific investment. It does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may receive this report. Investors should seek advice regarding the appropriateness of investing in any securities or investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not realise. Market conditions and trends will fluctuate. The value of an investment as well as income associated with investments may rise or fall. Accordingly, investors may receive back less than originally invested. Foreign investing involves special risks due to factors such as increased volatility, currency fluctuation and political uncertainties.*

### Regulatory disclosure

*Financial promotions are issued for marketing and information purposes; in the United Kingdom by Pyrford International Ltd, which is authorised and regulated by the Financial Conduct Authority; in the USA by Pyrford International Ltd, registered by the Securities and Exchange Commission as an Investment Adviser, in Canada by Pyrford International Ltd, where it is registered in Ontario, Alberta, British Columbia, Manitoba and Quebec as a portfolio manager; in the EU by BMO Asset Management Netherlands B.V., which is regulated by the Dutch Authority for the Financial Markets (AFM); and in Switzerland by BMO Global Asset Management (Swiss) GmbH, acting as representative office of BMO Asset Management Limited.*

*In Australia, this document is made available to wholesale clients by LGM Investments Australia Limited which is exempt from the requirement to hold an Australian financial services license under the Corporations Act in respect of the financial services it provides to wholesale investors. LGM Investments Australia Limited, a foreign company incorporated in its original jurisdiction of the UK as LGM Investments Limited is authorised and regulated by the FCA under UK laws, which differ from Australian laws. This document is accordingly directed at and is available only to those persons in Australia who are wholesale persons (including financial advisers). It must not be passed on or made available to any person who is a retail client for the purposes of the Corporations Act*

*Pyrford International Ltd is authorised and regulated by the Financial Conduct Authority, entered on the Financial Services Register under number 122137. In the USA Pyrford is registered as an investment adviser with the Securities and Exchange Commission. In Australia Pyrford is exempt from the requirement to hold a financial services license under the Corporations Act in respect of financial services it provides to wholesale investors in Australia. In Canada Pyrford is registered in Alberta, British Columbia, Manitoba, Ontario and Quebec as a Portfolio Manager that conducts business outside Canada.*

### Enquiries:

**Pyrford International Ltd** - 95 Wigmore Street, London, W1U 1FD, United Kingdom  
+44 (0) 20 7495 4641 | [information@pyrford.co.uk](mailto:information@pyrford.co.uk) | [www.pyrford.co.uk](http://www.pyrford.co.uk)

Ref: 2022-195

