

# Investment letter

***Monthly review of global  
financial markets***



SWISS  
CAPITAL<sup>IB</sup>

JUNE 2022

# MACROECONOMICS

The inflation outlook continues to dominate financial markets' narrative. Tentative signs of peaking demand and inflation in the US helped volatility fall across a number of asset classes in May as market participants pondered whether peak Fed hawkishness was in sight.

However, the global energy supply picture remains particularly tight, with refined products at very low inventory levels for this time of year. Prospects for more successful diplomatic efforts to end the war in Ukraine continue to look remote, keeping short term uncertainty high on the path for headline inflation. The process of demand destruction will eventually feed into lower core inflation, but this is unlikely to emerge before a few months.

China started to ease sanitary restrictions which, if sustained, should lead to less acute supply chain disturbances, eventually helping goods inflation retrace, especially as goods demand starts to fade rapidly, as evidenced by recent comments from retail companies.

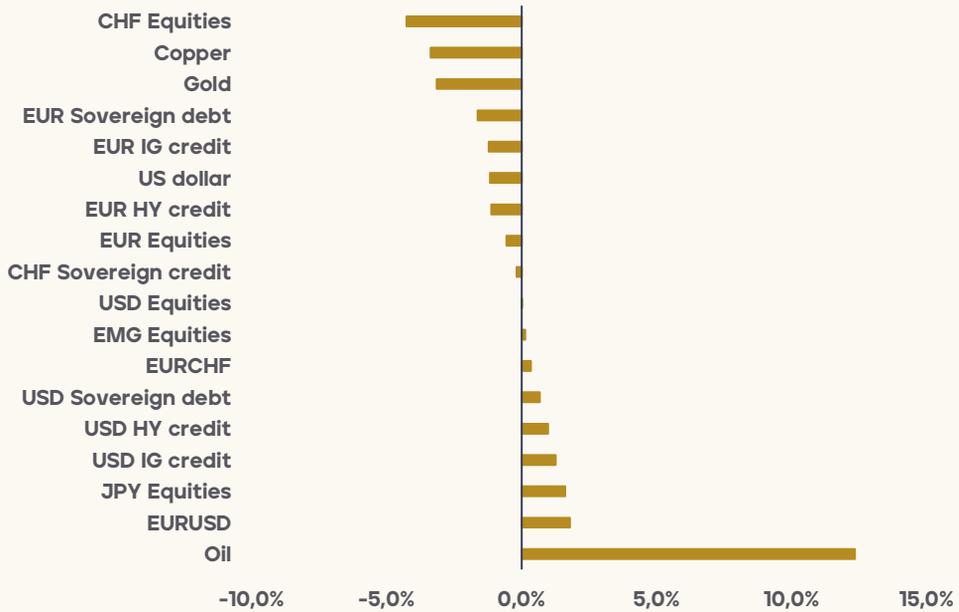
"inflation now,  
recession tomorrow"

Despite elevated spot inflation numbers, inflation breakeven rates have edged down relatively materially since late April, as the medium term nominal growth outlook is revised lower and outflows from TIPS funds accelerated.

As we progress through 2022, the growth outlook faces increasing headwinds from an energy supply led inflation rise, weakening consumer demand and a rapid tightening in global monetary conditions. The consequences of the shrinking availability and rapid rise in the cost of capital are already visible in the more speculative ends of credit markets, in emerging markets and in housing. HY and EM default rates are likely to rise to higher levels in 2023 than the average levels have seen post the Global Financial Crisis.

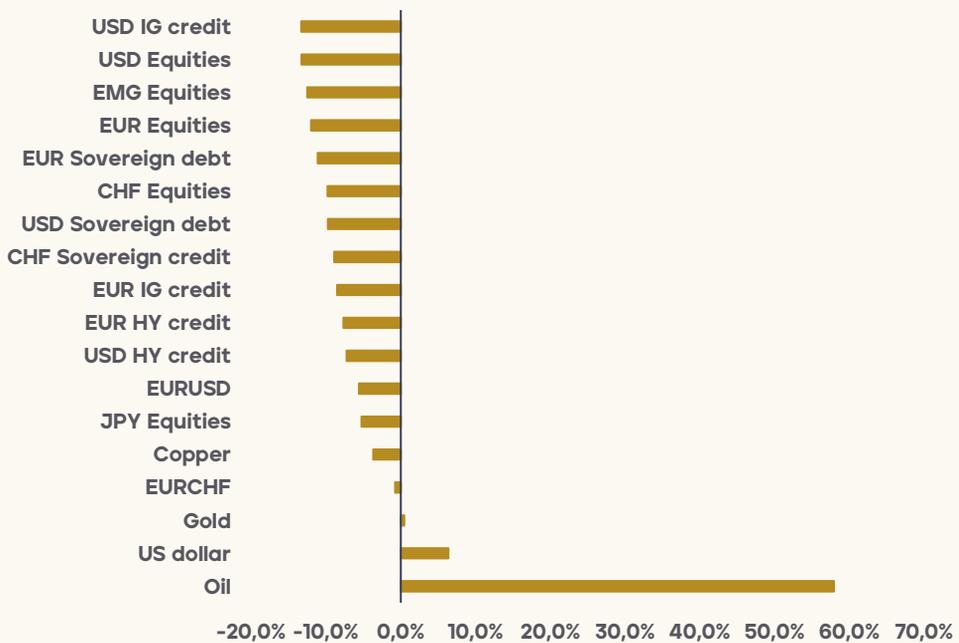
# OVERVIEW

## MAIN ASSET CLASSES MONTHLY PERFORMANCE



Source: Bloomberg, 31/05/2022

## MAIN ASSET CLASSES PERFORMANCE YEAR-TO-DATE



Source: Bloomberg, 31/05/2022

# MACROECONOMICS (continued)

As volatility subsided and risk premia decreased moderately during the second half of May, the financial conditions index eased somewhat. As long as hard inflation numbers remain elevated, this is unlikely to please central banks. Despite rising economic tail risk, it is increasingly likely that Central Banks will hike rates rapidly above neutral, with more Developed Market Central Banks joining the Fed.

The combination of rapid tightening in monetary policy and sharp rise in energy prices has always led to a recession. It is unlikely that this time will prove different.



Soft landing  
unlikely

## EQUITY MARKETS



Retail  
underperformance

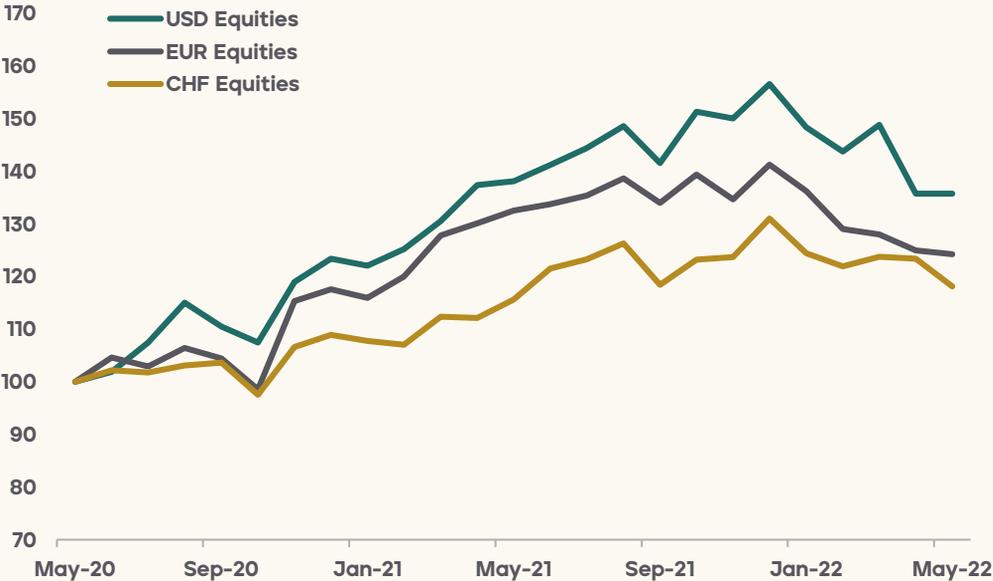
Equity markets staged a sizeable comeback in the second half of the month amidst relatively low liquidity and falling implied volatility levels. The most underperforming and shorted segments of the markets (tech and small cap) outperformed, suggesting that the medium term trend remains weak.

US non-luxury retailers were the most significant underperformers after both Target and Walmart cut guidance as inventory levels rise rapidly, consumer demand weakens and margins are pressured by rising costs.

EM equities performed in line with DM equities, closing about unchanged on the month after a strong end to the month, helped by a weaker USD and UST consolidation.

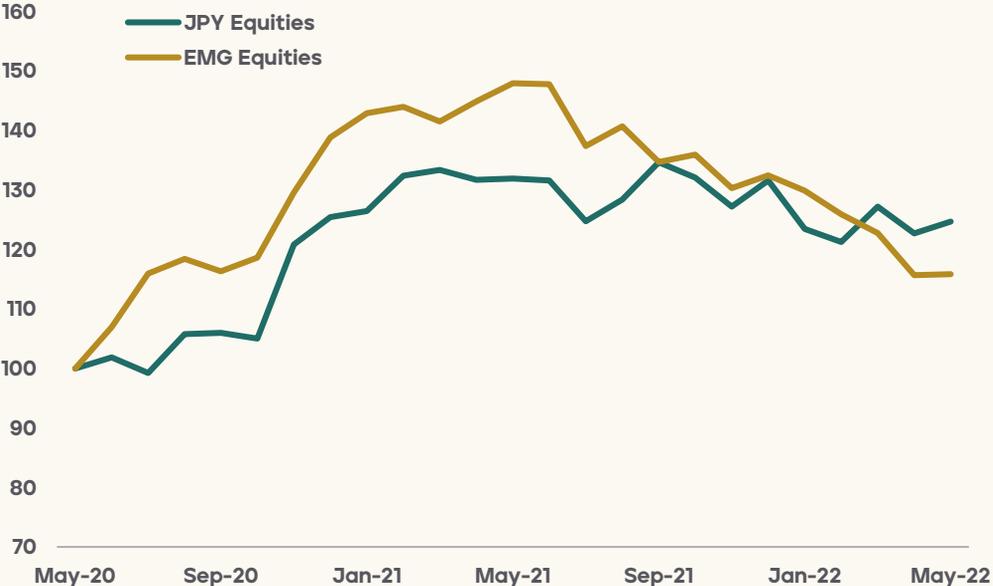
# EQUITY MARKETS

## EQUITY MARKETS EUR USD CHF PERFORMANCE OVER 2 YEARS



Source: Bloomberg, 31/05/2022

## EQUITY MARKETS JAPAN - EMERGING MARKETS PERFORMANCE OVER 2 YEARS



Source: Bloomberg, 31/05/2022

# BOND MARKETS

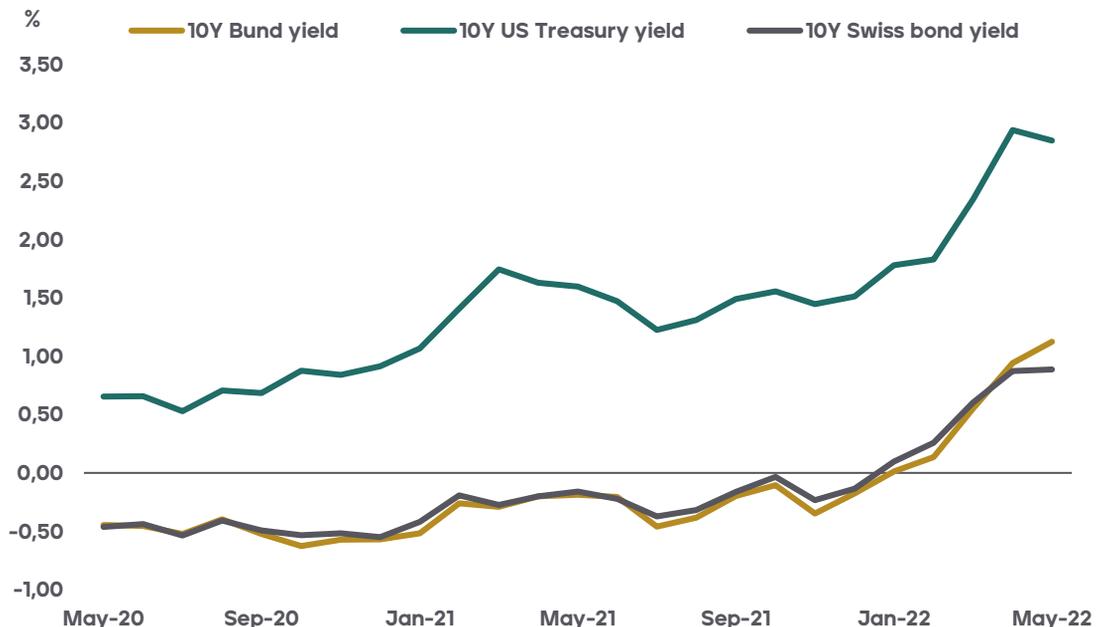
European government bonds underperformed US Treasuries as hard inflation numbers continue to print at elevated in Europe and market participants price a more hawkish ECB behavior. BTPs continued to underperform as technical support is seen weakening rapidly in the coming months. US Treasuries consolidated and closed the month close to unchanged.

Credit spreads tightened after some early month widening pressure and as implied volatilities fell across markets. However, this prompted an increase in issuance from IG corporates, financial institutions and HY borrowers. This capped the potential for further gains and with spreads moving back to 400bps in USD HY, the risk/reward has deteriorated materially and favors an underweight positioning as recession risk spikes.

Financial credit consolidated in line with wider markets, but the higher quality parts underperformed on higher rates sensitivity. This leaves capital structure at fairly compressed levels and favors an overweight in senior and T2 vs an underweight in AT1s.

## “short term relief EBG underperformance of USTs”

### 10Y SOVEREIGN BOND YIELDS EVOLUTION OVER 2 YEARS



Source: Bloomberg, 31/05/2022

# CURRENCIES

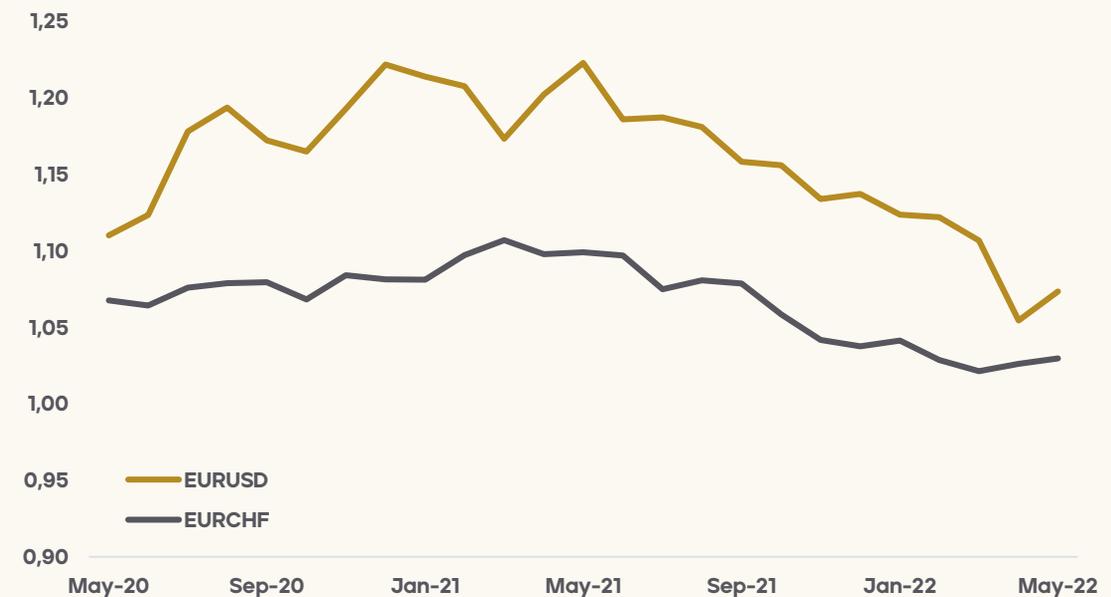
The US dollar consolidated, in line with USTs. The EURUSD traded close to 1.08 from an intra-month low of 1.038 as FX volatility remains high. The British pound was relatively stable despite increasing political noise.

The yuan made new lows despite the easing of sanitary restrictions and as the inflation and economic outlook differ from other regions.

In emerging markets, the Turkish Lira weakened considerably despite the softer USD tone. Monetary policy remains at odds with domestic inflation pressure and global macroeconomic context. This raises the prospects of adverse debt outcomes, as evidenced by the Turkish sovereign CDS widening pressure.

## USD & CHF

### EVOLUTION OVER 2 YEARS AGAINST THE EUR



Source: Bloomberg, 31/05/2022

# COMMODITIES

## OIL

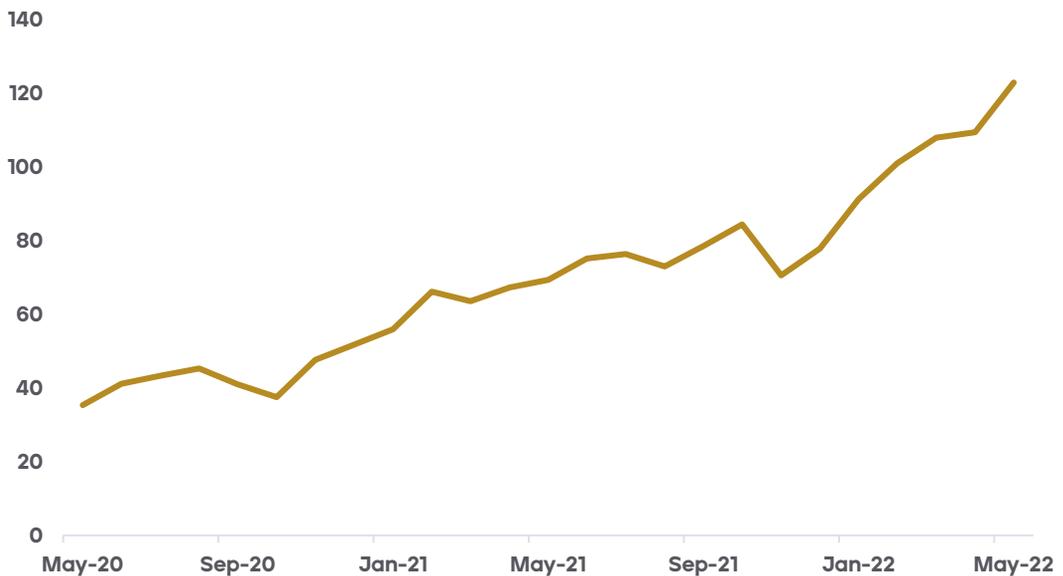
Oil and gas prices remained steady in May as the supply situation remains particularly tight. Refining margins are reaching extremely high levels, leaving gasoline prices at very steep levels. The medium-term demand outlook should be seen as lower, however, for now, supply is likely to dominate the short-term price action.

As expected, the European Union agreed to a partial embargo of Russian oil and gas with a progressive phasing out. Floating LNG facilities and inventories are being built to offset Russian supply.



Oil on the boil

### OIL EVOLUTION OF BRENT PRICES OVER 2 YEARS



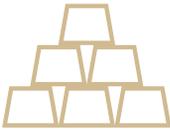
Source: Bloomberg, 31/05/2022

# COMMODITIES

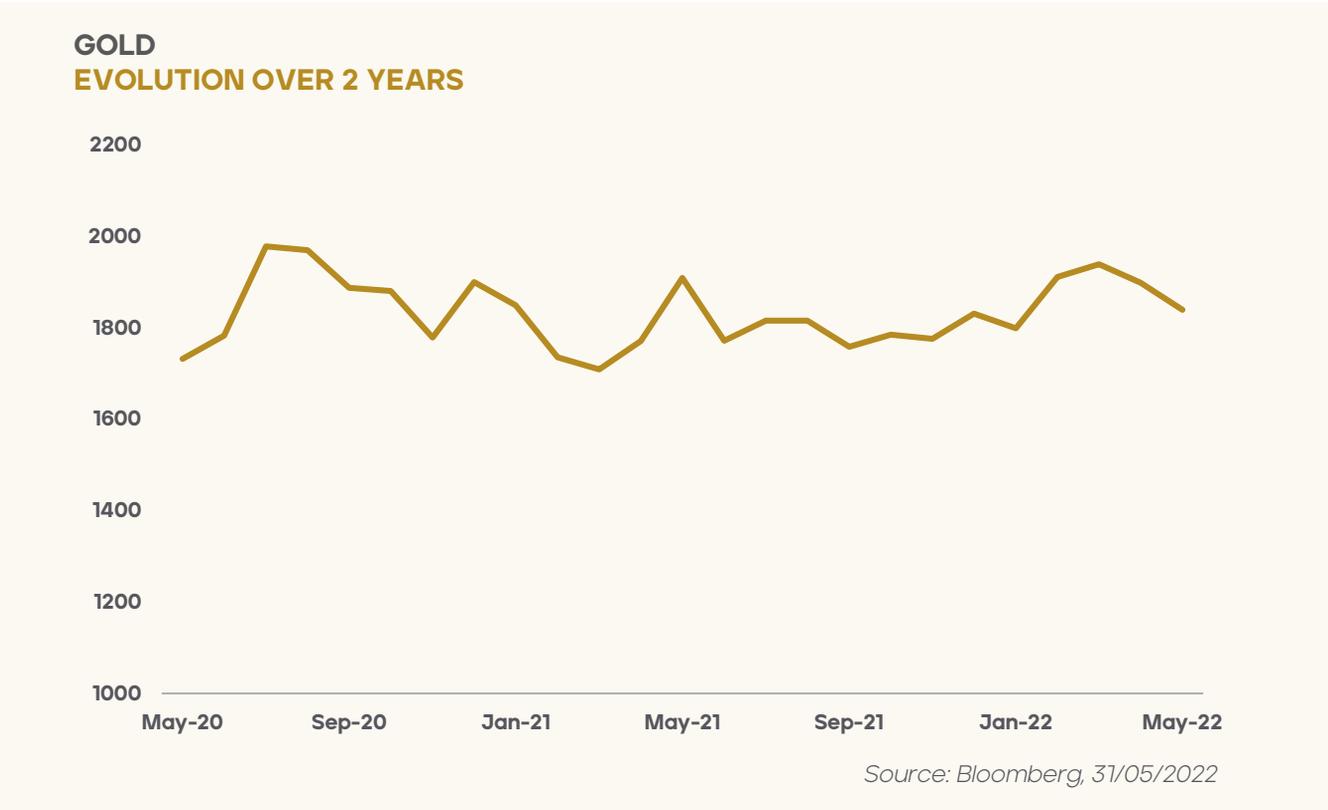
## GOLD

Gold traded marginally lower again last month, despite the softer USD and still elevated geopolitical tensions.

The yellow metal continues to screen as expensive against the price action in the USD and real rates.

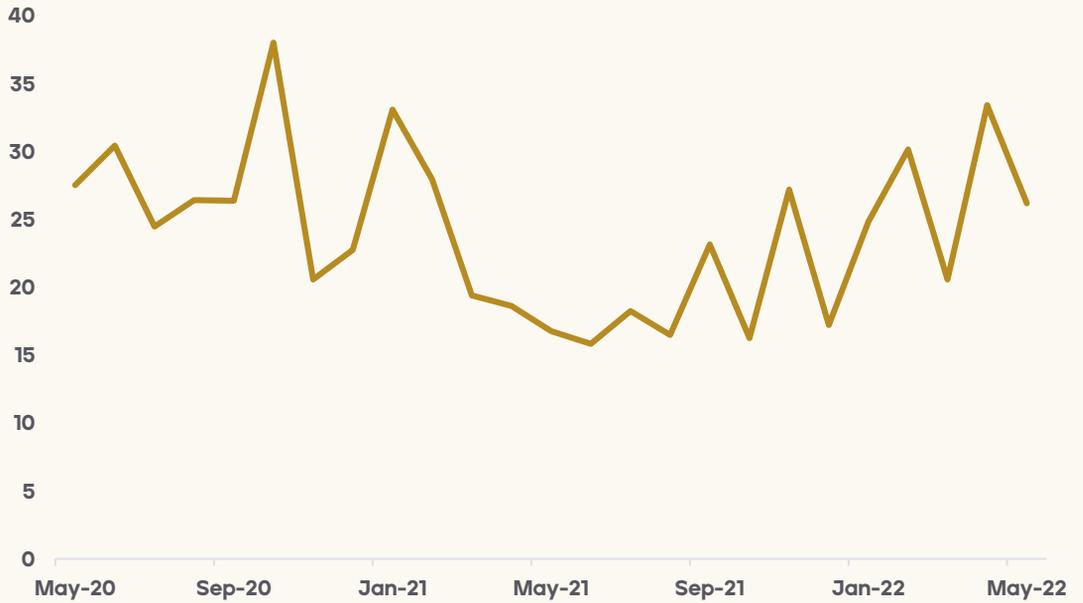


Weak RV



# VOLATILITY

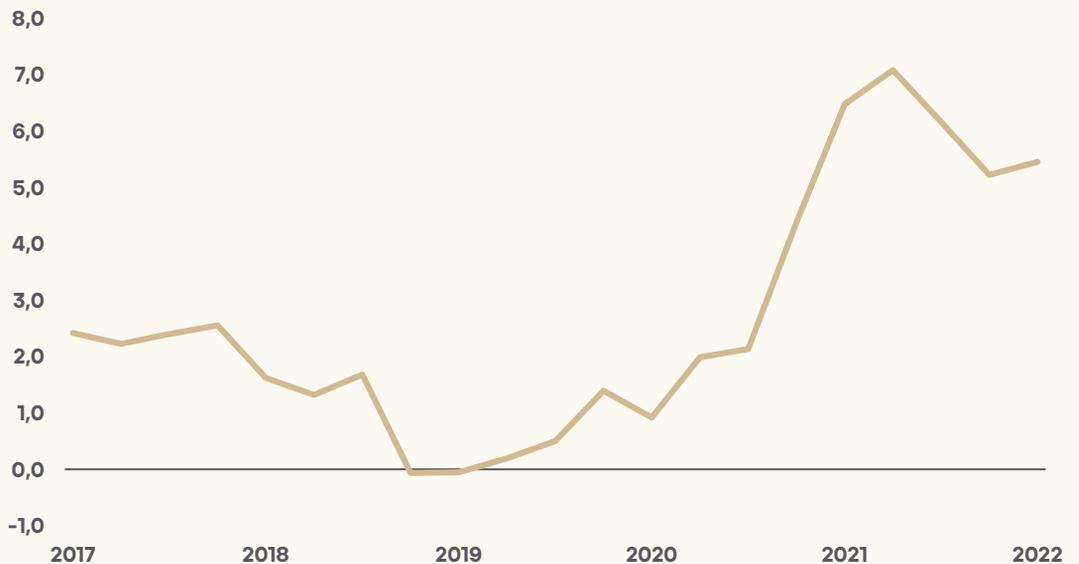
## VOLATILITY - VIX INDEX EVOLUTION OVER 2 YEARS



Source: Bloomberg, 31/05/2022

# REAL ESTATE

## SWISS RESIDENTIAL REAL ESTATE ANNUAL PRICE CHANGE



Source: Bloomberg, 31/05/2022

# CALENDAR

Date	Country	Economic Data	Period	Previous
09 June	Eurozone	ECB Interest Rate (%)	Jul-22	-0,5
10 June	US	Consumer Confidence	Jun-22	58,4
	US	Inflation (YoY)	May-22	8,3
	China	Inflation (YoY)	May-22	2,1
14 June	UK	Unemployment Rate (%)	Apr-22	3,7
	Japan	Industrial Production (MoM)	May-22	-1,3
15 June	US	Federal Reserve Interest Rate (%)	Jun-22	1,0
	China	Retail Sales (YoY)	May-22	-11,1
	China	Industrial production (YoY)	May-22	4,0
	Eurozone	Industrial Production (MoM)	Apr-22	-1,8
16 June	US	Philadelphia Fed Business Survey	Jun-22	2,6
	UK	Bank of England Interest Rate (%)	Jul-22	1,0
	Switzerland	Swiss National Bank Interest Rate (%)	Apr-22	-0,8
17 June	US	Industrial Production (MoM)	May-22	1,1
	Japan	Bank of Japan Interest Rate (%)	May-22	-0,1
22 June	UK	Inflation (YoY)	May-22	9,0
23 June	Eurozone	Markit Manufacturing PMI	Jun-22	54,6
	Eurozone	Markit Services PMI	Jun-22	56,1
	UK	Markit Manufacturing PMI	Jun-22	54,6
	UK	Markit Services PMI	Jun-22	53,4
	Japan	Nikkei Manufacturing PMI	Jun-22	53,3
24 June	Germany	Ifo Business Climate	Jun-22	93,0
29 June	US	Real GDP (QoQ)	Jun-22	-1,5
	Eurozone	Unemployment Rate (%)	May-22	6,8
	UK	Real GDP (QoQ)	Jun-22	0,8
	Switzerland	KOF Leading Indicator	Jun-22	96,8

# *Let's talk about it.*

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