Monthly market review – August highlights

To 31 August 2022

For Professional Investors only – Not For Use by Retail Investors.

August highlights

- Most equity markets fell in August as macroeconomic concerns once again spooked investors
- Commodities fell but gas prices rose as Europe experienced shortages
- The Bank of England (BoE) raised rates as US Federal Reserve (Fed) officials signalled more hikes to come

Equities

Equities initially rose, then dropped back, in August, during a continued volatile period for stock markets. Selling was again motivated by high inflation figures and fears over central banks' intentions. There were falls in European, US and UK shares; however, emerging market stocks and Japanese indices rose. The MSCI World Index returned -4.14% in August (total return in US dollars).

August was a month of two halves for equity investors. Stocks gained early in the month as July's positive sentiment carried through. US stocks rose, with the NASDAQ Composite Index reaching its highest level since April. Investors took optimism from lower-than-expected inflation figures, suggesting that central bank action had had the desired effect. However, this positivity was short-lived. Markets fell as central bankers at the annual Jackson Hole summit reiterated their hawkish intentions. The S&P 500 Index finished the month below 4,000.

European stocks underperformed the global average, given growing fears about a potential recession. Southern European markets, including Spain and Italy, held up better than Germany, France and Switzerland. The UK market also dropped, with the blue-chip FTSE 100 Index faring better than the mid and small-cap FTSE 250 Index. Energy and utilities stocks notably struggled. However, Japanese companies bucked the trend, with the Topix Index closing the month higher. Among developed-market currencies, both sterling and the yen weakened considerably over the month. Meanwhile, emerging market shares rose in general, with strength in India and Brazil, though Chinese onshore-listed A-shares fell.

Commodity prices dropped back over the period. Precious and industrial metals weakened slightly, while agricultural commodities rose. However, energy prices showed some of the biggest moves. Oil fell sharply, with West Texas Intermediate dropping more than 10% to close the month below US$90 per barrel. European natural gas prices rose sharply, with Russia again halting supplies through the Nord Stream 1 pipeline at the end of the month. The UK announced its domestic energy price cap would rise by 80% in October.

Bonds and economics

Yields rose in August, as central bankers' comments prompted a wave of selling. The BoE increased its base rate by 0.5%, while the Fed reiterated its commitment to controlling high inflation. Corporate and sovereign bond prices fell.

Bond yields soared throughout August, pushing prices lower. The BoE was the only major central bank to meet in August. A 0.5% rate hike early in the period was the largest in 27 years, bringing the base rate to 1.75%. The UK's consumer price index rose 10.1% year on year in July, slightly above economists' estimates, driven by rising food prices. The BoE estimates rising fuel prices could push annual inflation above 13% in October, triggering a recession which could last until the end of 2023.

Bond investors' fears intensified as Jay Powell spoke in Jackson Hole. July's US consumer price index was slightly below estimates, with annual inflation of 8.5%, However, the Fed chair was markedly hawkish, committing to control inflation even if the labour market weakens, while acknowledging that rate hikes could bring pain for households and businesses. The US employment picture has been mixed, with weekly initial jobless claims rising then falling during the month. In Europe, sovereign bond yields moved sharply higher in anticipation of rate hikes – perhaps as much as 0.75% – from the European Central Bank in September. High energy and food costs pushed Eurozone annual inflation to a record 9.1% in August, according to a flash estimate. While corporate bonds and emerging market sovereign bonds also fell over the period, riskier bonds generally outperformed.

Real Estate

According to the MSCI Monthly Index, total returns for July (the latest data available) were -0.6%, down from June's 0.7%. The residential and hotel sectors drove performance over the month, returning 0.6% and 0.5%, respectively, while the industrial sector lagged at -1.6%.

Sales of London offices have dropped sharply and values are being revised lower as rising interest rates and fears of a recession trigger the largest market “reset” since the financial crisis, according to BNP Paribas. Investors poured £8.1 billion into London offices in the first six months of this year, the highest half-year total since 2007, with most of the deals coming during the first quarter. However, the increase in the Base Rate from 0.1% to 1.25% over the past eight months has pressurised the sector, threatening the value of offices owned by major institutions such as pension funds. The last “reset” was during the Global Financial Crisis when the London office investment market collapsed and capital values fell more than 25%.

According to Knight Frank’s Retail Investment report, investment in UK shopping centres increased by 170% year on year to £1.24 billion in the first half of 2022 as domestic and overseas investors capitalised on the attractive pricing of assets, coupled with the anticipation of a return to pre-Covid-19 shopping habits.