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May Day or ‘mayday’?

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“We know what we are, but know not what we may be” - William Shakespeare

Welcome to the month of May, which always seems to be a pivotal month for investors and this year feels no different. It certainly starts off with a difference. Here in the UK, May Day is a celebration of the summer to come and a perfect excuse to put on your Morris bells, worship a Green Man and crown a May Queen. Meanwhile, in much of the rest of the world it is International Workers Day where you may want to swap your Morris bells for a red flag.

And then of course there are the financial markets. At face value, April was a good month to be an equity investor with a strong bounce in the UK stock market - only outpaced during the month by the rampant energy indices - and a sufficient gain in the broader pan-European benchmark to push the latter into positive territory for 2018. Meanwhile, bond yields globally gave a more muted performance, including the influential 10 year Treasury briefly breaching the psychologically important 3% yield level.

Dig a bit more deeply and April was more of a mixed up month than the headline statistics would suggest. Whilst the headlines were captured by some geopolitical successes in the Korean peninsula and no material further deepening of global trade angst, the big underlying trend was the rise of the US Dollar.

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If there is one investment theme which has underpinned many of the general financial market movements in the last couple of years, it is the fall of the US Dollar back towards levels suggested by fundamental exchange rate models. A lower Dollar has boosted emerging markets, commodity prices and encouraged much needed economic reforms in Europe by not allowing the Euro to remain very weak. It has even - whisper it quietly - improved the terms of trade for the United States and lessened the need for aggressive trade actions.

However, something changed in April and the US Dollar recovered to levels not seen since mid-January this year. Maybe it was the reduced likelihood of any imminent interest rate increases in the Eurozone, Japan or the UK in comparison to the United States. Maybe it was even the betting polling performance of the US President following the aforementioned diplomatic successes. Or maybe it was just that the US Dollar was due a bounce after a while in the doldrums. Either way, a higher Dollar did cause an impact during April, with many leading emerging market currencies coming under particular pressure.

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Now this is where May Day can become 'mayday'. We all know the positive structural story around the emerging markets and are increasingly aware of the importance of this collection of economies in terms of their contribution to global growth. However, despite typically lower levels of debt than we see among the more developed economies, a good chunk of their borrowings are Dollar denominated - the burden of which goes up with a rising US Dollar. Combine this with the sensitivity of many western economies - including the US and the UK - to higher interest rates or higher bond yields and you can see why the big picture may be more finely poised than many think right at the moment.

However - as I have said before - it is not a time to get too downhearted, as long as government policy makers continue to make efforts to improve general levels of economic dynamism via policies of reform and change. I remain excited at the initiatives apparent in places such as China and France, note the continued 'soft, transitional Brexit' tone here in the UK and remain of the view that fears about trade wars remain overstated. And my best guess on the US Dollar? It will end the year clearly lower against currencies such as the Euro and the Pound.

On balance, stick with the Morris bells and not the red flags this May Day and - to paraphrase another familiar market saying often pulled out at this time of year - I would not be selling in May and going away. There is far too much of interest going on at both the big picture and individual company level to be doing this.

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