



## CIO OFFICE MORNING MARKET WRAP – Wednesday September 2<sup>nd</sup>, 2020.

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56 was the number of the day: the August ISM Manufacturing survey posted a large increase over the already respectable 54.2 of July and was, as we were hoping for in yesterday's daily notes, clearly above expectations. The similar gauge for the Eurozone from Markit was also in expansion territory at 51.7 and at 55.2 for the UK. The German government revised its GDP forecast for the year from a -6.3% contraction to -5.8%, and Chinese factory data confirmed rising global demand for exports. Details of the US ISM Manufacturing index were interesting, with a jump in production and new orders, both above 63, but no pickup in the employment index. Factories are producing again, but not hiring. No doubt however, economic indicators were good.

As we wrote yesterday, this shouldn't come as a surprise: fiscal stimulus supported a rebound in consumption while production was disrupted. Inventories declined,

manufacturing rebound was set to happen. Should it continue, it will stimulate the most cyclical parts of the economy, from transport to energy and materials. Inventories rebuilding should also reduce part of the inflation in goods prices seen this summer.

Of course, stock markets reacted positively, gaining 0.4% on average but more in the US with a strong close. Emerging Markets added 0.9% with our regional markets up 0.3%. The price of Brent crude oil moved up 1.1%, approaching the \$46 level. OPEC's monthly crude production signal a much disciplined approach to output, as Saudi Arabia pumped below its quota in particular. US crude inventories are also said to be lower, supporting prices. Interestingly, interest rates were actually lower yesterday with the US 10-year Treasury yield losing 4 basis points to 0.67%, which can be linked to various Fed officials confirming a continuous and massive liquidity support.

Growth recovery with very low interest rates looks like a perfect picture, the only question is how much of it is already priced in equity markets. The good news is that earnings expectations from analysts are on the rise again, and that the level of interest rates justify high multiples. And we could add that all the sectors are not as expensive as the index levels suggest. For the time being, the leadership hasn't radically turned.

Technology continued to lead: the Nasdaq prints a new all-time record on a daily basis, and it was no exception yesterday with +1.4%, led by Apple and its stock split and Zoom confirming its post market surge. Tesla plans to issue shares which looks like a very smart move given their current sky-high valuation. The issuance will strengthen their balance-sheet at a ridiculously low cost of capital. Another market friendly news was a report that Dr Fauci said a Covid-19 vaccine may be available earlier than expected as all trials have been fast-tracked.

As we write this morning, the early trading hours in Asia do not show euphoria. The most developed markets such as Japan and Korea are slightly up, and so is Australia despite a disappointing GDP in Q2: the contraction of 7% in annual rate is worse than expected. China domestic exchanges and Hong-Kong are down. The positive US macro data is supporting a firmer Dollar on one hand, which also weigh on Gold, while on the other, there is no relief in sight with regards to US/China tensions.

Typically, the TikTok topic is getting complicated: the White House threatens to shut down the service on September 15th unless the US activities are sold to a US company. There are buyers, but China has issued a "poison pill" regulation to slow the process. Finally Mr Trump demands that the Federal Government to receive a compensation from the sale, which looks as unusual as complicated to implement. On a more sinister tone, the Pentagon says that China has boosted its ability to reunify with Taiwan by

force, and that its nuclear warhead stockpile could double over the next decade. China is said to be soon able to deploy atomic bombs via land, sea and air, joining the US and Russia in this capacity.

Staying in Emerging Asia, India keeps the sad record of the highest number of daily infections in the world, and its banks are dealing with another record among major economies: their non-performing loan ratio could reach 12.5% in the near future, as the Indian economy is set to see a full-year contraction for the first time in decades.

The issue of a fiscal stimulus in the US is still pending. As the US Presidential campaign is getting increasingly aggressive, both parties are sadly but unsurprisingly willing to take credit for any deal, making it of course difficult. We keep on thinking that they should agree on minimal measures and postpone the trillion discussion to November, after the elections. Implied volatility remains at high levels especially at post-election maturity, actually abnormally high given the current positive trend on equities. This can be seen as a signal for future turbulence, but also as a half-full glass: the cost of hedging is high which could mean that many market participants are buying protection. This technically supports the idea that any correction should be temporary, or may even not happen at all.

There is no crucial economic data today: we'll look at EIA weekly crude oil inventories and listen to EU's Barnier speech. The Brexit impasse is actually alarming and it looks like markets don't really care, except for the fact that the UK is one of the worst performing markets so far, which can also be explained by its sector mix: little technology and tons of energy and materials. Tomorrow will see the non-manufacturing leading indicators in the West, especially the ISM Services in the US at 6PM Dubai time. The US monthly job report will be released on Friday.

Stay safe.

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