



## CIO OFFICE MORNING MARKET WRAP – 3rd March, 2022. ALSO AVAILABLE ON ALEXA.

The war in Ukraine is intensifying and commodity prices continue to skyrocket. However, risk-appetite came back to financial markets on Wednesday. Global stocks added +0.5% on average across regions, with an impressive +1.9% gain at the close in the US. Interest rates sharply rose: the US 10-year Treasury yield added +15 basis points yesterday alone to reach 1.88%. The 5-year added +16 basis points to 1.76%, and the 30-year +14 basis points to 2.25%. The dollar benefitted, with a trade-weighted average +0.4% gain. Those are spectacular numbers, but oil was even more: the price of Brent crude oil gained almost 10% to close just below \$115.

The reason for such a pro-cyclical day is to be found in Fed chair Powell's testimony to the US Congress yesterday. Market participants took comfort from his speech: while a rate hike in March is definitely on the cards, Mr Powell would personally prefer not to start with 50 basis points. The Fed will be vigilant on inflation but its chairman reiterated that the US economy is strong enough to stomach disruptions from the global context as well as higher interest rates. Bottom-line, the Fed will tighten its policy, keep an eye on the war and its implications, and is confident that economic growth won't be derailed. Factually, nothing revolutionary was said there, but as always markets appreciate any bit of visibility they can find and the key take-away is that the Fed appears to be measured.

Meanwhile, the war is only intensifying. Russian forces are slowed in the North around Kyiv, but are gaining traction in the South, especially on the Black Sea coast, with the city of Odesa now under fire and Kherson probably under Russian control. Talks between officials from both countries will resume tomorrow, which is a day later than initially planned. This delay could be seen as a positive, and hope is rising for a mediation from China. Should it happen and deliver, the diplomatic capital of China would considerably surge on the global scene: what is more powerful than being able to stop a war? This may be the plan, which would be both geopolitically smart and very welcome for the world. At this stage, it's just a hope. At the same time, the ostracism of Russia continues in the West: Toyota and Honda are the latest companies to stop making business with the country, and MSCI is simply eliminating Russian equities from its emerging-markets index, which will be mimicked by FTSE Russell. Russia's credit rating was cut by multiple notches below investment grade by both Fitch and Moody's as the severity of sanctions could threaten debt service. Sanctions are indeed extreme and can be seen as outright economic war, which will sadly have a devastating impact on ordinary people first, like every war. Of course, the primary objective is to inflict a maximum pressure on the Kremlin to end the invasion, but the opposite consequence, an outright escalation, cannot be ruled out. The key signal for an escalation would be the suspension of energy supply to Europe – the economic equivalent of a bomb on Western economies. Paradoxically, or not that much, the White House could be playing with fire there. Joe Biden said that he considers restricting imports of energy and natural gas related technology. No doubt that he is not unhappy to see that the Nord Stream 2 project is factually dead, which should lead to a write-off in billions for parties involved.

As we write this morning, Asian markets are overall well oriented. Stocks are up in Japan, Korea and Hong-Kong and marginally lower in China's onshore markets, following a tepid print of the Caixin PMI Services. Interest rates are giving back a fraction of yesterday's gains with the US 10-year currently trading at 1.8%. Oil prices continue to be firmer, with Brent futures above \$116, while gold is stable and major cryptocurrencies are slightly down.

Today we will have a look at the PMI Services for the Eurozone as well as on its US ISM equivalent. Of course, geopolitical developments are the dominant driver for markets, which are exposed to radically versatile sentiment as well. Volatility will remain extreme everywhere: seeing interest rates intraday swings of 15 basis points is certainly not business as usual. Any short-term speculation is dangerous, and so is excessive leverage which can tie your hands at the worst possible time.

Stay safe.

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