



CIO OFFICE MORNING MARKET WRAP – 6th July, 2022.

Fears of an economic downturn fuelled risk aversion this Tuesday on global markets, with an extreme volatility. Oil prices collapsed, with the Brent crude oil approaching the \$100 mark during the session and closing at \$102.7, a -9.5% drop. Global stocks fell -0.8% on average in developed markets, and it could have been worse: US indices recovered from their session lows to close on a +0.3% gain, but losses in Europe were significant at -2.1% for the Euro area and -2.8% in the UK. The latter was not helped by the resignation of two senior members of the government: both the Chancellor of the Exchequer and the health secretary quit the cabinet, saying they lost their confidence in Boris Johnson. Stocks in Japan closed +1% higher but emerging markets as a whole slipped -0.8%. Growth scare pushed interest rates lower in a bull flattening pattern. It was even an inversion as the 10-year Treasury yield, which lost -7 basis points to 2.81%, ended the day slightly below the level of the 2-year at 2.84% while the 5-year ended at 2.82%. The longest 30-year maturity decreased by -6 basis points but remained slightly above 3%, at 3.04%. In a flight to safety, the US dollar continued to climb, adding +0.2% versus its trade-weighted counterparts and approaching a 20-year record for the broad DXY dollar index. The gauge is up 11% so far in 2022.

A series of PMI data was released yesterday. Starting with our region, the advanced indicators were buoyant for Saudi Arabia at 57 and very strong, although decelerating, for the UAE at 54.8. PMI for Services in the Eurozone came out slightly above expectations at 53 and it was a larger beat in the UK at 54.3, almost 1 point better than the median forecast. A comparable

measure for India came out at a high 59.2. Yes, the global economy is decelerating, but so far it is impressively resilient. The risk of recession is material but our current scenario is more for a significant downturn than for an outright global contraction. Inflation and its consequences on central banks' action is obviously the major concern, and to that extent, numbers continued to print higher than expected in Turkey, Vietnam and Thailand. So far, exceptions are China and Japan where the pressure remains contained. In other news, according to a report from Bloomberg, the US is putting pressure on the Netherlands to ban ASML from supplying certain semiconductor technology to China. ASML is a global leader in chip manufacturing equipment and intellectual property, and the US wants to counter China's ambitions to become a champion in the field. This proves that the removal of tariffs from the Biden administration is guided by internal goals rather than the result of a material improvement in the relations between the two superpowers. There is also some irony to see the US, advocate of free markets, pressuring another country to restrict the business of an independent company with China. This also highlights the strategic importance of semiconductors – and thus of Taiwan.

This is the transition to Asian markets were unsurprisingly, risk aversion is palpable as we write. All stock markets are in the red, around -1% for Japan, Hong-Kong, Korea and China's onshore indices. US Treasury yields are marginally higher at 2.83% for the 10-year, and so are oil prices, as the barrel of Brent currently trades at \$103.5. Cryptocurrencies continue to suffer: bitcoin is back below \$20k and ether is down to \$1120.

We held our monthly tactical asset allocation committee this Tuesday and decided to adjust some of our exposures, mostly within fixed income. We cut our allocation to the riskiest segments, namely High Yield and EM Debt, to a clear underweight, while adding to DM government bonds. We consider that the risks are simply not adequately compensated by expected returns, especially as growth scare will continue to move markets. We however kept our overweight in stocks from emerging markets, due to their fundamental upside potential. We also continue to favor alternatives, especially through hedge funds. The level of risk of our tactical asset allocation is very close to our strategic reference, as we keep on expecting extreme volatility for the months to come: concerns are very serious, but pessimism is also at record levels, so unpredictability is our only conviction for the short term. Our medium-term view remains reasonably constructive, with a base scenario where global growth is seriously dented but not totally derailed, which should, as soon as inflation convincingly abates, unlock some upside potential.

The US ISM Services will be released today, and the consensus expects it to moderate to 54 from May's 55.9 level. We would intuitively say that services activity could have been stronger than forecast, but more important will be the details of the June FOMC meeting, also released later today, and of course the monthly US job report on Friday. We will also look at retail sales in the Euro Area and follow the developments of the current political turbulence in the UK.

Stay safe.

Chief Investment Office
Wealth Management,
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