



CIO OFFICE MORNING MARKET WRAP – 7th July, 2022.

Extreme volatility continues to rule markets, which should not come as a surprise. Typically, Wednesday was the exact opposite of Tuesday on global markets. Global stocks were up in the West, with Europe outperforming, but down in Asia, while interest rates were on the rise. The US 10-year Treasury yield increased +12 basis points to 2.93% while the 2-year gained +18 basis points at 3%, confirming the current inversion. In between, the 5-year closed at 2.98%. The price of Brent crude oil continued to fall, losing -2% to \$100.7. The dollar followed interest rates and was stronger on average by +0.9% against trade-weighted counterparts.

There was one positive economic data behind firmer interest rates. The US ISM Services came out higher than expectations -which was our guess in our previous daily notes- at a solid 55.3, only marginally lower than May's 55.9 and well above the median forecast of 54. Economists may sometimes be too quick to extrapolate market trends, which by nature anticipate, to the current economic situation which continues to show impressive strength, as illustrated by the sharp rise in the business activity component. The job market should thus remain tight and we would be surprised to see a weak monthly job report this Friday. The minutes of the Fed's June FOMC meeting were also published yesterday. Unsurprisingly given the outcome of last month, they were hawkish with inflation being their one and only priority. Officials noted downside risks to the growth outlook but saw it as a natural feature of their policy rather than as an undesirable outcome to be avoided. One of the key concerns expressed by the minutes was not about recession, but about the credibility of the Fed itself

in its mission against inflation. Fact is that so far no data, apart from market implied readings, suggests an imminent recession in the US, which is why we keep on expecting aggressive tightening in the near-term. If anything, oil prices have moderated in the recent weeks which could support US consumers. The situation is obviously more challenging in Europe which faces the major risk of not getting enough natural gas to run its economies. But apart from that, activity remains resilient: Euro area retail sales and German industrial data were both decent. Bottom-line, Western economies are decelerating but they're not falling. Switching to the political arena, UK prime minister is facing significant pressure to resign with five additional ministers quitting his cabinet yesterday, and another one being fired by Boris Johnson, apparently for not being loyal enough. Meanwhile, the war keeps on raging in Ukraine. The US and its allies keep on discussing the idea of a cap to prices on Russian oil – it looks a bit unrealistic, and prices of natural gas in Europe resumed their rally. Talking about European energy, France's prime minister said yesterday that its leading utility company EDF will be nationalized to help it face the crisis and invest in new nuclear plants. While this is good news for bondholders, it could be seen as an outrage by shareholders who bought those shares at 32EUR from the very same French state, which is now considering a nationalization at EUR9. In the meantime, the French government imposed a cap on electricity prices which obviously had consequences on the company's financials. Finally, there is a topic we don't comment much anymore which is Covid. Cases are on the rise globally, especially in Europe, but also in China which reported 54 new infections in Shanghai, a 5-week high. While infections are rising everywhere, the important point is that intensive-care admissions and deaths are not surging.

As we write this morning, markets are overall well oriented in Asia. Stocks are down -0.6% in Hong-Kong but up +2% in Korea after Samsung's results. Japan gains +1.4% and China's domestic markets +0.6%. Interest rates are marginally lower and so is the dollar, while oil stabilizes a bit higher with the Brent trading at \$101.4. Major crypto currencies are modestly up, around \$20,400 for bitcoin and \$1,170 for ether.

There is no crucial economic data being released today but tomorrow will be all about the US monthly job report at 4.30PM Dubai time. The median forecast for the change in nonfarm payrolls is for +268k jobs being created, after a spectacular +390k in May. Our best guess is that the actual number could be marginally better than expected. With the Fed being focus on inflation and markets weighing recession risk, we are in a delicate situation. A much stronger number would raise the probability of an even more aggressive tightening, while a much weaker one would confirm growth scare. Good could be bad but bad could be bad as well. This is the kind of paradox which explains why volatility should remain significant in the coming months – the short-term is simply unpredictable. Ahead of a longer week-end in the UAE, we wish you and your family Eid Adha Mubarak. Our daily investment notes will resume next Tuesday.

Stay safe.

Chief Investment Office
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