



## **CIO OFFICE MORNING MARKET WRAP – Sunday August 8<sup>th</sup>, 2021. ALSO AVAILABLE ON ALEXA**

The past week saw robust gains in global equities, with the MSCI World returning 1% and closing at all-time highs, and losses in longer-duration defensive assets following the strong US jobs report. Financials and materials led US stocks higher, the yield on the 10-year Treasuries note rose by more than 7bps, gold fell 2.7%, Brent crude slumped by almost 8% for the worst weekly decline since last October, and the US dollar advanced.

All eyes were on the US labor report, which came out strong across the board. The economy added more than 940,000 positions in the month of July, the most since last August and way above consensus estimates - the unemployment rate fell to 5.4%. Will the Fed be reassured that the economy is making substantial “further progress” and

finally be more outspoken about pulling back stimulus? Other data-points added fuel to the fire of a solid economy, with factory orders, led by non-durable goods, above consensus and the ISM Services Index topping forecasts to print at record levels. In Europe the final prints of the July PMIs confirmed that growth remains buoyant at the onset of Q3, as Covid-sensitive services catch up from a lower base. This was contrasted with Asian markets marked by a more uneven recovery and China in slowdown mode acting as a drag.

Fed officials did not spare comments on the reduction of bond-buying programs, with the general message being that time is drawing closer for asset purchases to be wound down. The most authoritative voice, that of vice chair Clarida, said that the Fed would make later this year a tapering announcement and that rates would be rising in 2023. His statement was supported by the view of an upbeat outlook and supply-demand imbalances dissipating, hence waning inflationary pressures. Janet Yellen reiterated herself that “inflation will recede to normal levels”. Now, here comes the sore point. It is a bit obvious in and of itself that price pressures due to bottlenecks in the economy will dissipate, being such constraints by nature temporary. The concern is that future inflation is more likely to be driven by other factors, like the lagged effects of rising prices in services, the US economy forecast to cruise at above-trend speed throughout 2022 and the continued net stimulus, in spite of the planned tapering. Market participants have repeated the Fed litany that inflation will be temporary focusing on what the Fed wants investors to focus, the transient bottlenecks. The big boys scratching below the surface, from Blackrock’s Larry Fink, to JPMorgan’s Jamie Dimon and ex Treasury secretary Larry Summers, have begged to differ, in more than one scathing commentary.

The slump in gold is an obvious consequence of the rising real rates, though from historically low levels, as investors realise that expansion rates in the United States are more likely to be elevated for longer than previously projected and the tapering deadline is not to be put back anymore. Yet, until recently, resiliency in gold prices was in general put down to lower yields and the ‘delta variant’, a new kind of tail risk commentators from all walks of life are more and more falling back on. Following the June Fed meeting our fair value on the yellow metal was revised lower to \$1,750 and we stick with that view. Latest Fed officials statements on tapering just reinforce it.

And maybe the time has come for nominal yields to rise again. Our year-end fair value for the yield on the 10-year note is at 1.75%. Either business confidence is set to slump towards the neutral level of 50, separating expansion and contraction, or the current levels for US rates are too low. The 10-year yield last week broke with the sequence of lower lows started from its March peak to settle at 1.3%.

In the week ahead China will be releasing inflation numbers, CPI and PPI YoY, and the US the Job Openings on Monday; the US the Small Firm Business Optimism Index, and Germany the Zew Survey on Tuesday; the US the CPI on Wednesday; the US the PPI, the UK Q2 GDP and Europe euro area Industrial Production on Thursday. At a time yet to be confirmed China will be releasing Total Social Financing numbers. Stay safe.

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