CIO OFFICE MORNING MARKET WRAP – Monday February 14, 2022. ALSO AVAILABLE ON ALEXA

Last week was another highly volatile one, with risk-aversion culminating after the US CPI hit the screens on Thursday, with the geopolitical standoff around Ukraine as a backdrop. January headline inflation in the US rose to +7.5% year-on-year, which was higher than both the median forecast at 7.2% and the December print of +7%. This was the latest addition to a number of recent regional reports, from all of Europe and Canada to some Asian countries. The tension is serious, and broad based. We keep on thinking that some of its drivers, typically supply-chain bottlenecks and energy prices, will normalize. However, numbers are here, with significant breadth, and the consequence is of course a sharper than expected adjustment of central bank policies, importantly not only in the US. There are of course some exceptions: China continues to go the opposite way, easing monetary policy and preparing for more fiscal stimulation, with a CPI yearly gain below 2%. India also has a clear patient stance, with the RBI staying on hold again, and guiding markets towards a first hike only in June.

Japan also doesn't seem to be willing to leave interest rates climbing, as the BoJ announced fresh moves to defend the upper band of their target for long-term rates. But the norm, especially in the West, is rising inflation, tightening job markets, and an accelerated normalization of monetary policies.

Markets obviously didn't like it. Most of asset classes were in the red last week, especially in developed markets where almost all asset classes were down -0.6%. Stocks did better in emerging markets, up +1.6% over the week, with the key caveat that the largest ones were closed when Wall Street's losses accelerated on Friday, to close almost -2% down. Gold was surprisingly sought after, with a +2.8% weekly return which put the precious metal in positive YTD territory, which can be explained by heightened geopolitical tensions. The price of Brent crude oil saw another sharp appreciation, adding +2.3% over the week to close just below the $95 mark. The behavior of interest rates was interesting: on one hand, of course, they are directly sensitive to inflation and hawkish central banks. But on the other, safe bonds are a haven in times of risk aversion. This is why rates fell across maturities on Friday. The US 10-year Treasury yield is at 1.94%, while the 5 and 30-year maturities are respectively at 1.85% and 2.24%. They are all up over the week, but lost 8 to 10 basis points on Friday alone.

The week was not just about inflation and rhetorical escalation on Ukraine. The earnings season continued, and it is unambiguously good. With more than two thirds of major US companies having reported, almost 80% of them delivered better than expected earnings and 75% are beating revenue estimates. The bar was not low with an average +28% rise in earnings per shares, propelled by an impressive +17% rise in sales. In Europe, Q4 EPS growth averages +44% with 67% of companies exceeding forecast. The same measure is at 55% in Japan, where topline growth is also running at a double digit pace, which doesn't happen often there. It's arithmetic: rising earnings and falling prices mean that valuation multiples are falling, which is of course a positive for future returns. Earnings are not the only good news: the Omicron wave is fading. Global new cases seem to have peaked in the West as well as in India and in China, according to official numbers. Singapore, Korea and Japan are still struggling but it looks like global mobility is set to move higher, which is also good news for growth.

One of the crucial questions of the "Year of Low Visibility", the title of our 2022 Global Outlook, is of course whether growth is good for markets, at a time when all eyes are on inflation and central banks. We can't help staying -reasonably- optimistic. Medium term inflation expectations remain anchored: between participation rate in the US and reduced working weeks in Europe, there is some additional capacity in the employment market, and supply chains will not struggle for ever. Central banks themselves have demonstrated many times in history that they care about market volatility – "financial conditions". While there is no doubt that they have to withdraw their emergency support simply because there is no economic emergency anymore, they also don't want to become the major problem themselves. There are reasons to hope that they won't go too far and will also be careful not to destabilize bond markets given the enormous amounts of debt in the system. The recent predictions for 6,7 or 8 rate hikes this year in the US look excessive to us. The idea of positive interest rates in Eurozone this year is even questionable, given the fiscal situation of most countries there. This is why our positioning is close to neutrality, with the clear intention to put more cash at work on a more severe correction in risk assets or when safe yields will become irresistible. Having said that, when we write "low visibility", we mean it, and it includes a lower level of confidence in our own forecast.

As we write this morning, stocks are falling across Asian markets, reacting to Wall Street selloff and of course to the situation in Ukraine. It's a sea of red from Japan, down -2.6%, to China, down -0.6% onshore and -1% in Hong-Kong, and including Korea down -1.5%. Havens are only moderately down: the US 10-year treasury yield is marginally up 2 basis points to 1.96%, while gold is not far from flat. Bonds in Australia and New Zealand even rise, in a typical "flight to quality" pattern. Of course, tensions over Russia's military buildup and the heightened rhetoric from the West are pushing oil prices even higher. The Brent crude oil trades close to $96. Russia has constantly denied any intention to invade Ukraine – and there are reasons to believe them. However, the situation is volatile, especially as many Western leaders face low approval rates in an election year. Should the situation deteriorate into open conflict, flight to safety would be the name of the game, with another level of complexity being added on the inflation front: while Russia is a key supplier of energy, Ukraine is a major exporter of wheat and corn.

We are not there and in the absence of clarity, acting emotionally is usually a mistake, Our asset allocation is built to stomach shocks as it typically did when the coronavirus broke out 2 years ago. Our last word today is to thank you for the record attendance and considerable engagement during our Global Investment Outlook webinar last week. We had simply never received so many questions, which only confirms our forecast of low visibility – we unfortunately do not have all the answers, but are positioned accordingly, with caution and humility. Stay safe.

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