



## **CIO OFFICE MORNING MARKET WRAP – Sunday November 14, 2021. ALSO AVAILABLE ON ALEXA**

The MSCI World Index put in a lacklustre performance for the week, yet much less so at a country level, with US equities mildly negative and underperforming on the highest inflation reading in three decades, Europe barely positive and EM stocks led higher by China on expectations of looser regulation. All of the three main US benchmarks, S&P 500, Nasdaq and Russel 2000, hit a new record high, a sign of strength soon to be put to the test as retailers, most exposed to rising materials and labor costs, are slated to report next. Global government bonds fared much worse, recording new 52-week lows, as investors pulled forward bets that central banks would be tightening policy next year on soaring inflation breakevens. The yield on the 10-year Treasury note rose by 11bps, while the yield curve continued to flatten at the very long end, steepening only at the shorter maturities, an indication that investors are either discounting a worsening growth-inflation tradeoff, or the Fed falling behind the curve eventually forced into a steep tightening mode. Market-implied concerns

about future growth cropped up in the increasingly diverging performance of crude oil, at the highest levels since 2018, and long-dated Treasury yields, far out of line with the oil's rally. Animal spirits dominated the gold market for the first time this year, with the yellow metal breaking out of a four-month range, while the dollar advanced for the third consecutive week, and Brent crude traded marginally weaker.

China and the United States released stand-out inflation reports. In China the producer-consumer inflation gap was the widest in three decades, as the October PPI ran at 13.5% versus the CPI at 1.5%, driven by supply-demand imbalances and shortages in commodity markets. These price gains are anyway considered to be unlikely to deter the PBoC or the government from stepping up measures to cushion the protracted slowdown phase, and consensus is actually growing that a bottom of the Chinese credit impulse should not be far away. In the United States the CPI growth sped up to 6.2%, a level last reached in 1990, while the core measure ran at 4.6%. A broadening of gains to more price categories in the US economy suggests more uncertainty about when inflation pressures could subside, although Fed officials remain unfazed and in particular Janet Yellen, who said that the Fed would intervene if needed to prevent a rerun of the '70s. And rightly so, since today's level of the real Fed Fund rate, an abysmal -6%, was last seen, you may have guessed it, in the '70s indeed.

The Fed in its twice-yearly Financial Stability Report highlighted a plethora of different risks, with top concerns ranging from persistent inflation, more insidious Covid variants, US-China relations alongside Beijing's relentless regulatory measures, cryptocurrencies and soaring asset prices. As for asset bubbles, it is not often the case that who lights up the fire also gives the impression to be feeling the urge to fight fires. On inflation, renowned investor Mohammed El Erian once more highlighted that, the slower the tightening response of the Fed, the greater the threat of contractionary forces for the economy, a viewpoint to be nicely contrasted with the above-mentioned unfazed stance of ex Fed chair Janet Yellen. Stablecoins, cryptocurrencies pegged to existing currencies, were deemed to be a threat as susceptible to bank runs, an issue exacerbated by lack of standards on the assets backing them, hence the need for more bank capital requirements and supervision. Such foundedness of viewpoints was blithely ignored by the crypto-market, with bitcoin and ethereum recording new all-time highs. The Fed also saw the Chinese real estate market and its regulator focus on leveraged companies as a risk potentially extending globally via tighter financial conditions and deteriorating investor sentiment.

Last week saw the conclusion of the 19th Communist Party of China Central Committee, a party plenum held yearly which passed its first "historical resolution" in 40 years, paving the way for president Xi Jinping to stay in office for a third consecutive

mandate until 2028. The plenum cemented Xi as China's most important leader since Mao Zedong and Deng Xiaoping. This has important implications, making president Xi an even more formidable adversary, now that he has made himself politically untouchable. The United States will be confronted with a superpower whose aim is to become globally even more powerful, under an unflinching leadership set to last in the medium term. A China expert mentioned that the party is ready to embark on the construction of a 'socialist modern country', with strong emphasis on 'socialist'. As a matter of fact, both politics and economics will be shifting to the left in China, with the latest push towards self-reliance and redistribution of wealth via constraints on the private sector already pointing in that direction. Also, China is now offering a new model, which seems to be so far working, as an alternative to the Western democratic one.

Joe Biden and Xi Jinping will hold a virtual meeting on Monday, trying to smooth relations between the countries. At the same time, President Biden will be trying to forget President Xi's political narrative about the decline of the West and the rise of the East.

In the week ahead, the release of US retail sales on Tuesday will be highlight event, with consumer demand expected to remain resilient. On Monday China will release key indicators for October, on Wednesday investors will focus on the CPI prints in Europe as well as some major countries, on Thursday the Conference Board Leading Index is published. Stay safe.

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