



## **CIO OFFICE MORNING MARKET WRAP – Monday 15th March 2021. ALSO AVAILABLE ON ALEXA.**

In spite of US long-dated yields being at the highs of the year, markets are having a positive start to the week, with US futures and equities in Japan, South Korea and Australia advancing.

Investors must be looking forward to the FOMC meeting to be held on March 17 -18, when chair Powell is expected to communicate the implications of new economic forecasts and of a possibly revised dot-plot, which traces out the progress of policy rates as per each committee member view. Fed projections would allow to gauge how Fed officials see economic growth and inflation evolve and draw conclusions about when accommodative measures could start to be lifted. In spite of the relevance of the quarterly forecasts, it is hard to see how information potentially contradicting the unequivocal ultra-reflationary longer-term stance of the committee could be provided. Bottom line: we are in full Average Inflation Targeting regime and quarterly figures could just be leaning in that direction to accommodate the stance.

One problem with the new regime is that the Fed will now want to see sustainable price pressures before tightening policy, becoming more reactive versus its former proactive self, risking to fall behind the curve and allow undesirable overshoots as the recovery proceeds faster than envisaged. Janet Yellen said that the risk to inflation is “small” and “manageable”.

A market which is going to rebalance at a quicker pace, alongside the economy, is the crude market, where demand should reach pre-pandemic levels in H1 2022 as per latest projections. The current deficit is maintained only because of production curbs enforced by OPEC, amidst excess capacity and high inventories to be worked down not before 2022 as just mentioned. The oil futures curve, with the spot price above longer-dated futures, in backwardation for the sake of being more technical, suggests tight conditions as well, with backwardation now reaching the highest level in the last 18 months.

The fly in the ointment is the possibility that US shale oil drillers reaccelerate production, now that most companies are profitable following the crude rally. This has not yet occurred due to the 2020 oversupply shock, which culminated in WTI briefly plunging into negative territory, and forced some discipline on producers. Since then the discipline has been maintained, with companies paying down debt and returning cash, and investors punishing the ones announcing production boosts. At which price level will shale companies go back to the old habits?.

Stay safe.

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