
**CIO OFFICE MORNING MARKET WRAP – Monday November 15, 2021. ALSO AVAILABLE ON ALEXA**

Asian shares are mixed this morning, although the PBoC rolled over all of the policy loans falling due this month in a bid to support growth, and Chinese economic data were above forecasts. Treasuries are steady, while the US dollar and gold are slipping. The US retail sales release on Tuesday and the Philadelphia Fed business outlook Thursday will be important to set market direction both for equities and bonds.

Important Chinese indicators released this morning showed that the economy is stabilizing, though this is still far from being a recovery in the making. Output stabilised, while consumption showed stronger momentum. Industrial output growth rebounded to 3.5% year-over-year in October, stronger than the previous month at 3.1%, fixed asset investment slowed to 6.1%, substantially in line with the forecast, while retail sales grew at 4.9%, well above estimates. Home prices fell slightly, recording a larger decline than in the previous month. The National Bureau of Statistics cautioned that the "international environment is still complicated and severe". With headwinds still strong, further policy support will be needed, which should come by year-end with expected cuts in the reserve requirement ratio and measures to address power shortages and speed up fiscal spending.

The 2021 United Nations climate change conference, called COP26, the Conference of Parties, concluded in the week end in Glasgow, with 197 countries agreeing new rules to limit greenhouse emissions. The reduction of the use of coal, the end of inefficient fossil fuel subsidies and the push towards specific climate targets were the major achievements of the summit. In a considerable step forward the framework for the trading of carbon credits was approved. The world should be on a path to reduce the rise in global temperatures to 1.5 degrees from pre-industrial times, considered necessary in order to avoid catastrophic warming. More realistically, it was decided to phase down, rather than phase out coal, in a concession to larger emitters like China and India. Considering the latest energy crisis in Europe which resulted also from a clumsily planned transition to green energy policies, a more realistic approach should not be frowned upon. The economic relevance of the agreement is in the required trillions of dollars of investments in clean energies and the restrictions on the use of fossil fuels. That will in turn resurrect many nooks and crannies of the so-called old economy, as the building of the necessary green infrastructure entails huge consumption of commodities. Will, in the end, more and more concessions to the 'old' way of producing energy be necessary for us to be able to label almost everything as green? And, more to the point, should in the process everything 'ungreen' be frowned upon with zero-tolerance?

The latest University of Michigan consumer sentiment report came in below expectations in large part due to rising inflation. As a matter of fact, one in four consumers mentioned rising price pressures for the reduction in their living standards, a case in point of potential demand destruction, with sentiment at the lowest point in ten years. The crucial question is whether the Fed should intervene to curb excessive price gains, and the answer is not clear-cut at all, pointing to the conundrum developed market central banks currently find themselves in. Central banks indirectly cap demand by raising policy rates which tend to limit borrowing, in turn working only with some lag. The pre-pandemic concern was oversupply, well described by the downward trend in US industrial capacity utilisation since the '70s, producing disinflation. And now supply is only artificially limited due to existing bottlenecks and labor shortages. So, should the Fed start tightening, to avoid that inflation becomes entrenched, or wait until the supply-side normalises and meets demand? If by the time the tightening feeds through the economy the spare supply comes back, the Fed will have caused the demand destruction it wanted to avoid; if it waits for too long and inflationary trends get reinforced, it will have failed to avoid the demand destruction it could have. In our view the Fed might have to embark in some sort of token tightening soon after the tapering to avoid losing credibility, being maybe done with the bare minimum of one hike and then stop. With the US real policy rate now at -6% such a move would be very well tolerated, both by markets and the economy. Stay safe.

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