



## **CIO OFFICE MORNING MARKET WRAP – Wednesday February 16, 2022. ALSO AVAILABLE ON ALEXA**

After a Kremlin declaration affirming that diplomacy is always possible, Russia's defense ministry signaled yesterday the withdrawal of some of the troops. This was a clear relief for markets, reviving some appetite for risk, pushing equities and interest rates higher. Global stocks rose +1.2% on average on Tuesday, led by the US closing +1.8% higher. The US 10-year treasury yield added 6 basis points and crossed an important mark to settle at 2.04%. We wrote it yesterday, this is the level at which we have decided to start reducing our large underweight in govies. The 5 and 30-year maturities added respectively 3 basis points to 1.94% and 7 basis points to 2.36%. The geopolitical relief obviously impacted oil, with the price of Brent crude falling -3.2% to \$93.4.

Interestingly, it didn't take long for Joe Biden to call for vigilance, as he considers that an invasion remains possible, and said that the US hasn't verified the withdrawal of troops. Meanwhile, Vladimir Putin said Russia is ready to continue supplying Europe with natural gas via Ukraine after the current contract expires in 2024. The topics are obviously linked as the US hates the Nord Stream 2 pipeline project, but factually, Europe needs energy which is both reasonably cheap and green, and there is little alternative. Higher energy prices are a clear issue at a time when demand is elevated, and should remain so: the omicron wave keeps on abating everywhere except in a couple of Asian countries, and yesterday's labor market reports for the UK and the Euro area confirmed a clear improvement. Q4 GDP reports were also broadly positive, from Japan to Europe at respectively +5.4% and +4.6% annualized. In the US, the January PPI surprised to the upside with a 1% increase versus December, and +9.7% year on year.

Talking about inflation, and in line with the expectations we expressed yesterday, the pressure remains reasonable in China, especially for consumers. The January numbers, just released this morning, indicate a very modest +0.9% year on year increase on the CPI, and a return to single digit appreciation for the PPI, at +9.1% year on year which compares to +10.3% in December – and is now lower than in the US. This confirms that China is in the quite unique situation of having some room of maneuver to stimulate the economy, and that's just what PBOC Governor Yi Gang just said minutes ago: the central bank will keep policy appropriate (saying the opposite would have been surprising) and supportive, especially for the “weak links in the economy”. He also said that China growth should return to its potential level in 2022. No doubt, stimulus in on the table.

No surprise then that risk appetite is back on Asian markets this morning. Stock indices are in the green everywhere, from +2% in Japan to +0.7% in onshore China, while Korea and Hong-Kong are in between, gaining +1.5% as we write. Future contracts on Western stock indices and oil prices are broadly stable, while interest rates are marginally lower.

Talking about interest rates: as we had repeatedly said, the 2% mark on the US 10-year treasury yield is for us the threshold to start reducing our underweight in DM government bonds, which we will implement today in our Cautious and Moderate profiles. With a +2% increase in our allocations, mostly funded from cash and hedge funds, our underweight will stand around -3.5% relative to our SAA. This underweight position, initiated more than a year ago, is obviously successful. We are not outright bullish on safe bonds and on duration -in which case we would be overweight- but the risk/reward has improved, justifying a reduction in our underweight. In line with our theme of low visibility ahead, 2022 is a year for tactical adjustments, and we also have

internally approved levels at which we would buy back the stocks from developed markets that we sold at the beginning of the year.

Today, the minutes from the Fed's FOMC meeting of late January will be released at 11pm Dubai time and they may give more details about the raging debates between doves and hawks, which will hopefully help us get a less blurred picture about the trajectory of the various layers of tightening, or at least more clarity on the key triggers. We will get inflation numbers from the UK as well as the weekly US crude oil inventories. NATO defense ministers will start a 2-day meeting – yes, Russia's timing was probably well thought out. The earnings season continues with Cisco or Carrefour, among others, releasing their numbers. Stay safe.

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