



CIO OFFICE MORNING MARKET WRAP – Sunday August 16th, 2020. ALSO AVAILABLE ON ALEXA

Financial markets moved on growth and inflation last week, in what looked like a “risk-on” pattern. Defensive assets were in the red, with Gold in particular losing 4.4% to close below 2000, at \$1945. The safest segments of fixed income were also negative, down around 0.8% over the week, due to a rise in interest rates. The US 10-year Treasury yield increased significantly to 0.71%. In front of them, global stocks did better with Developed Markets in particular, led by a fresh new record high in the US, adding 1.2%.

Oil prices and Emerging Market stocks were however steady, as the US Dollar was firmer for the first time in weeks, benefitting from the rise in rates. Clearly, last week was not about quantitative easing lifting all boats, but about better nominal growth including some inflation. PPI and CPI reports confirmed some life in prices.

Of course, base effects more than matters: growth is booming only because it follows the most brutal contraction ever, and the situation is similar in prices, with an unprecedented decline in inflation in the first half of the year. Still, as global retail spending is on track to catch-up to pre-pandemic levels, and as inventories are low everywhere following the lockdown of factories, there are reasons to believe that prices will keep on rising as growth continues to recover.

Investment consequences are mixed: growth is obviously a good news, and stocks in particular are a nominal asset, as their sales and profits include inflation. Having said that, we keep on thinking that equity valuations have already fully discounted a perfect recovery, while interest rates remain priced for a much more conservative outlook. At this stage, the levels of inflation we're talking about should have a limited impact: we are far from the 2% level which could reverse the current action of Central Banks. But higher interest rates would be another headwind for high equity multiples.

Macro data was overall benign last week, but it becomes quite clear that consumer confidence is weaker. From the US Congress's failure to agree on fiscal package to rising COVID cases in Europe this time, the momentum is flattening, and the progression of retail sales is decelerating.

The US Presidential campaign fuels a significant political risk. While the escalation in the US/China conflict is not good for global trade and investment, the domestic meltdown over the \$1 trillion fiscal stimulus is not really priced in by US stocks. The only reason not to turn more defensive than we currently are is that positioning remains light, and sentiment remains bearish, as illustrated by last week's bearish predictions being voiced again by many Wall Street influencers.

Last time it happened was in early May, and markets only went up since then. Closer to us, the historic agreement between Israel and the UAE could be followed by formal ties with Bahrein and Oman. In the week ahead, we will listen to the US Democratic national convention to get a better sense of their program. Japan will publish its GDP growth for Q2, and the Fed will release their minutes.

Stay safe.

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