CIO OFFICE MORNING MARKET WRAP – Thursday March 17, 2022. ALSO AVAILABLE ON ALEXA

Wednesday was Fed day: the central bank hiked 25 basis points as expected, and delivered an overall hawkish message which combined realism on inflation with confidence in growth. This combined with indications of progress in the negotiations between Ukraine and Russia to trigger a sharp rise in risk appetite on financial markets. Global stocks added +2.4% on average, while interest rates flattened further, a step closer to inversion: the US 5-year Treasury yield added 8 basis points to reach 2.18%, which is also the level of the 10-year after a 4 basis points increase, while the 30-year actually decreased 3 basis points to 2.45%. Gold was marginally lower, just below $1930, while the price of Brent crude oil moved down -1.9% to $98.

More details on the Fed. The rate decision itself was not a surprise with the first quarter point increase since 2018. Every other formal output from the FOMC was slightly more hawkish than expected, starting with the "dot plot" which reflects individual forecast from the voting members. The median dot now implies a total of 7 rate hikes in 2022, including yesterday's, then another 3 to 4 in 2023 which would raise the funds rate to 2.75% by then. There was no new indication about the balance-sheet runoff, except for the fact that it could commence "at a coming meeting" – a bit ridiculous, but it could mean May. Most importantly, the Fed expressed realism and confidence. Realism: less growth and more inflation are now expected this year, with respectively +2.8% for real GDP and 4.1% for core PCE inflation. The Fed's preferred measure of inflation is expected to decrease to 2.6% in 2023 and 2.3% in 2024, while economic growth for the next two years should remain robust at respectively 2.2% and 2%. That's the important message of confidence: the Fed chairman highlighted the strength of the US economy, especially its employment market, and is confident that the expected hikes will achieve disinflation without damaging the economic outlook. This is indeed the goal and an opposite statement would have been surprising, however it was convincing and Chair Powell also pledged that the Fed would be nimble, citing the risks from Ukraine's invasion by Russia in particular. Bottom-line, we just started a full cycle of interest rates hikes, backed by a robust economic backdrop, which should lead to a mildly restrictive policy stance by the second half of next year, if everything goes according to plan.

Of course, the future is as unpredictable as ever and things usually don't go according to plan. However, the message was well calibrated and while details on the balance-sheet action remain unknown, the intended trajectory for interest rates is now clear, and can be seen as a "maximum", which could be smoothed if needed. It is the most aggressive policy change in decades, but market participants had had months to get prepared to it, and the delivery was well received. It was even more so positive for equities as the FT reported significant progress between Ukraine and Russia on a tentative 15-point peace plan. Both parties didn't confirm, and even played it down, but in essence the future military neutrality of Ukraine, with its own army but outside of NATO, appears increasingly likely, and this could be exactly what Russia meant by its objective to "de militarize" Ukraine. The other key objective from President Putin's initial speech of February could relate to the independence of the two eastern regions. Nothing is signed yet and the war keeps on intensifying on the battlefield, with also heightened geopolitical rhetoric: the US officially called Russia "war criminal" and accused Moscow to commit "atrocities", while warning against using chemical or biological weapons, in a statement which reminds President Obama's "red line" in Syria. Russia also warned the US against providing weapons to Ukraine which could be considered by them as taking part in the conflict. The US however is said to send an expanded arsenal to Ukraine, including the armed Switchblade drone which was used in Afghanistan.

Turning to the economic war and its potential financial repercussions, reports indicate that no payment was posted yesterday with regards to coupons from two US dollar-denominated Russian sovereign bonds which became due for an amount of $117 million. Russia's finance minister said that payment could be made in rubles, which would be categorized as default after a grace period of 30 days. With regards to economic data, February US retail sales were disappointingly weak, but January numbers were revised up, which depicted a very strong consumer spending for the first two months. Of course, the impact of higher energy prices will start hitting in March.

Switching to Asia, another very important news which broke out yesterday was an official statement from China's Vice Premier Liu expressing their willingness to stabilize financial markets, potentially ease the regulatory crackdown, stimulate the economy and importantly support property and technology companies. The country should "actively introduce policies that benefit markets", and the least we can say is that markets took note. After the late session rebound of yesterday (which happened after we released our daily notes, we wake up too early), today is also extremely positive in Asia. Stock markets are up everywhere, led by Hong-Kong which adds a spectacular +5% after +9% yesterday. China's onshore markets follow with +3%. Overnight, an index of US listed Chinese stocks jumped +33%. Stocks are up +1.8% in Korea, and +2.8% in Japan despite a strong earthquake which shook the northern part of the country near Fukushima with a small tsunami but overall probably limited economic consequences. Interest rates on the dollar are down by an average 5 basis points, a counterintuitive but actually usual reaction after a Fed hike: the US 10-year Treasury yield stands at 2.13% as we write in Tokyo. Oil prices are modestly up, with the Brent future trading just below the $100 mark.

It's a long update, with many events happening overnight. Today should be calmer in terms of news. The Bank of England will meet and probably raise interest rates by a quarter point and ECB's Lagarde will deliver a speech. We will have a look at the February CPI for the Euro area and at US industrial production.

Stay safe.

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