



## **CIO OFFICE MORNING MARKET WRAP – Thursday November 18, 2021. ALSO AVAILABLE ON ALEXA**

Asian stocks are mixed this morning and Treasuries are steady, as inflation remains at the forefront of trader minds bringing closer the prospect for tighter policy. S&P 500 and Nasdaq futures are little changed, while yesterday US stocks closed mildly weaker, with new construction softer and retailer Target Corp. warning about rising costs impacting margins. The yield on the 10-year note closed below 1.6%, gold appreciated, the dollar saw some profit taking and crude oil sank as Washington and other nations are considering tapping their oil reserves.

Inflation runs high in the major developed countries and industrial metals are flashing a warning of tight supply, since the spot prices of all of the main metals are higher than futures for the first time since 2007, that for now also signifies that demand remains

very strong. Signs are multiplying that price pressures, less transitory than originally thought, point to an overheating US economy. Not only is inflation at multi-decade highs, but it is also broad-based, extending to categories not directly related to reopenings, and for the goods and services which experienced the biggest run-ups price rises are not moderating that much. Wage pressures are heightening, and inflation expectations have retraced all of the post-GFC drop. Former US Treasury Secretary Lawrence Summers went so far as to say that the failure to address the deteriorating purchasing power of consumers could bring about the re-election of former President Donald Trump.

Although most are concerned about a belated and excessive monetary response, the Fed is indeed stealthily doing something about this, by means of a more hawkish rhetoric strengthening the dollar. The Federal reserve not only engineered an unprecedented recovery with a massive liquidity wave, but in the process they also spurred an impressive stock market rally by widening the gap between equity and bond valuations to unrealistic levels. Why, then, crash equities and undo so much work, when they can indirectly boost the value of the global reserve currency, hence tighten monetary conditions without impacting equities? The US dollar has been rising more than 7% year-to-date, markets are pricing in two rate hikes for 2022, as more Fed officials have highlighted the need for being vigilant about inflation. No one has expressed concerns about the rising dollar, and, after all, the success of central bank policy is measured more often than not by the ability of its officials to attain the desired results by persuading with words, rather than by repeatedly stepping into action. Yes, the Fed in the end might have to implement one token rate hike to avoid losing face, but that would be more than well tolerated by markets and the economy.

Calls that energy markets will be less tight in 2022 are multiplying, from OPEC saying that the oil market will be soon oversupplied, to the US energy agency, the Energy Information Administration, pointing to rising supplies and suggesting that “the tide may be turning”. Yet, prominent studies seem to be suggesting otherwise. OPEC+ appears to be comfortable with prices in \$80-\$100 range, with the major GCC countries implicitly eyeing that for still much needed balance-sheet repair. The “oversupplied” narrative is based on the cartel’s member countries producing as per their quotas, which would be unrealistic for some of them due to various constraints, the most relevant being dwindling capacity from under investments in exploration and development. US shale growth continues to remain restrained. US drillers are raking in larger profits now than early in the shale revolution, owing to more stable supply, and continued discipline is enticed by shareholders demanding cash returns, rather than disruptive growth. Also, OPEC has already proven twice to be able to drive prices down to levels more damaging to shale drillers than OPEC member countries.

More newsflow about the so far unabated strength of the US recovery will be coming in today with the release of the Philadelphia Fed Business Outlook and the US Leading Index. Stay safe.

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