



## CIO OFFICE MORNING MARKET WRAP – Monday October 19th, 2020. ALSO AVAILABLE ON ALEXA.

About a week ago Mohamed El-Erian, former CEO of PIMCO, said that “right now, this market wants to go higher”. Explanations for such buoyancy range from a Democratic sweep, to the swiftness of the rebound from September lows, to a fiscal package coming after the elections. Will the cycle start again via fiscal stimulus under Democratic leadership? Investors seem to be betting on something of the sort. Cyclical bellwethers like the Dow Jones Transportation Average and the Philadelphia Semiconductor Index, usually leading the broader equity market, currently sit at all-time highs. One could come to similar conclusions looking into much less visible recesses of the financial arena. Consider Eurodollar futures, tied to the LIBOR interest rate, hence allowing investors to take a wager on the expected direction of the Federal Reserve’s policy rates.

Bloomberg reported yesterday that recently a very large position via options on Eurodollar futures was built, implying the expectation that US policy rates will rise sooner than currently discounted. In short, someone with big pockets is of the view that future fiscal stimulus will pull forward the start of the next tightening cycle in the US. As a matter of fact, positions were ramped up as polls suggested a growing chance of a Democratic sweep. So, never mind today’s mini fiscal cliff due to a split Congress, investors are looking through this little drama and expecting much larger public outlays by 2021. In case, while the owners of equity portfolios would be happy down the line, it would be much less so for the ones owning high-quality bonds with a duration factor not playing in their favour at all. This scenario ties in with a fixed-income report recently sent to our clients, where it was recommended to selectively increase exposure to high-yielding bonds as the outlook brightens and yields could edge higher.

For a longer term view, readers who would rather pour cold water on enthusiastic short-termism, should mind Carmen Reinhart's words, pronounced during a Bloomberg interview four days ago. The World Bank economist known for her work on the last financial crisis, said that the current crisis could morph into a major economic one, "with very serious financial consequences" and in relation to most central banks making asset purchases she remarked that "the scenario we are in is not a sustainable one". For sure it is not a sustainable one for the dollar, indeed in relation to the Quantitative Easing operations regularly carried out by the Fed, capping yields and reducing the appeal of the US currency. Low policy rates and growing twin deficits in the United States will ultimately translate into a long-term down cycle for the dollar.

The easing of financial conditions coming with it could prove to be a boon for several countries, though, in particular in our region. In the GCC countries the hospitality and real estate sectors would be boosted by a weakening of the currencies pegged to the dollar, once the negative impact from the pandemic softens. "We want our country back" was a slogan initially brandished by Brexiteers obsessed with severing ties with EU. It is not of particular good omen that they got it back with a credit rating lowered by one notch. Moody's cut Britain's credit score justifying the decision also with the UK's inability to reach a trade deal "that meaningfully replicates the benefits of EU membership". Mr Boris Johnson must have radically different views on the benefits stemming from that membership.

Stay safe.

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