



CIO OFFICE MORNING MARKET WRAP – 20th June, 2022.

Central bank rate hikes had the Fed not exactly surprising with a 75-bps hike, the BOE by 25bps and the ECB giving direction for a July hike, but still the markets reacted sharply to the inflation and growth narrative. Even though Friday saw some relief, global equities were down 6% last week and have fallen 10% in the first half of June, taking year to date losses to 22%. A broad sell off last week, US equities fell -6%, with tech (usually the laggard this year) performing just a little better. European equities were down -4.6% and Japan -7%. Emerging markets had the UAE, India and China all trading down. Asia equities this morning are trading flat to slightly negative with China announcing new lockdowns, but the fewest cases since February. EM equities have been the better performers as of late, with smaller drawdowns but with still largely negative weekly closes. All global sectors fell last week, with energy which is so far the only sector in the green this year, losing 14% as demand fears and a planned windfall taxation on US oil producers (to provide incentives on fuel purchase to consumers) played on sentiment.

The 10-year US Treasury yield which mid-week touched 3.49%, ended the week at 3.3% with the 10s 2s yield curve flirting with inversion as the 2 year yield hovers close to the 10 year yield. Concerns increase about a possible recession in 2023, amid the hawkish Central Bank monetary policy. Gold was a little higher at \$1,839. The price of Brent crude oil was down to \$113/bbl as demand could be seen cooling off.

The crypto rout continues with Bitcoin down 15% to \$17,599 on Saturday, but has recovered trading closer to \$20,000 today morning. Ether fell 19% to \$881 on Saturday and is back above \$1000 this morning. The two largest crypto currencies are down 70% from all-time highs in early November. A repeating cycle with liquidations driving prices and sentiment lower, which triggers more liquidations and negative sentiment for the broader market. This is in line with the selloff of unprofitable tech and very high valuation stocks. A flight to quality across the equity and fixed income markets.

At what level and when will the fixed income and equity markets settle? High yield bonds have reacted much the same way as have the safer sovereign bonds, in line with equity performance. As the Central bank tightening cycle starts to achieve at least partially its aim to control consumer demand and the supply chain improves as global logistics go back to pre-Covid levels we should see both the major asset classes start to perform better with valuation and growth metrics supportive. Our year end fair values indicate upside from here, but this year it's about continually revising where growth will settle, with many opposing forces still in play. So while we wouldn't rush, in we advocate maintaining a balanced portfolio and adding to quality bonds and equities, keeping in mind that green shoots have begun to emerge on inflation numbers somewhat cooling.

The event of last week, was the US Fed's 75bps hike on Wednesday, a magnitude last seen in 1994. The strong May CPI and the rise in household inflation expectations had Chair Powell indicate that the Committee viewed a 50 or 75bps hike in July as likely. Among FOMC participants, the median forecast was for another 175bps of rate hikes this year. This in a month in which the economic growth has been downgraded by public and private institutions and the hawkish policy stance from the Fed is further tightening financial conditions with the US dollar appreciating, a rise in mortgage rates, and a drop in equity prices. Households have lost \$5 to 8 trillion of wealth this year, with consumer spending likely coming down about 2-3 cents for every dollar lost in wealth as per a JP Morgan report. Mortgage rates have gone up about 280bps so far this year, which will affect residential investment. Consumer data is showing signs of cooling, with retail sales in May disappointing. The more interest-sensitive sectors of the economy, housing and manufacturing, are seeing the effect of higher interest rates with May housing starts and the June homebuilders' survey showing declines, as did the first June manufacturing surveys from the New York and Philadelphia Feds. On the bright side still-strong labor market is supporting wage income and households have only just recently begun to use the "excess saving" from the pandemic stimulus. Chair Powell will give Congressional testimony this week and is expected to maintain the same message. Today we get Germany May PPI, Euro-Area April construction output, ECB's President Lagarde speaks.

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Chief Investment Office
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