



## CIO OFFICE MORNING MARKET WRAP – Wednesday 22<sup>nd</sup> June, 2022.

As we wrote yesterday, the summer solstice brought some warmth to risk assets. Global stocks rose +1.1% on average, led by the US closing +2.3% higher. Europe was flat, Japan gained 1.8% and emerging markets +0.5% on average. Interest rates were modestly firmer – well, modestly compared to recent volatility standards. The US 10-year Treasury yield added +5 basis points to 3.27% while the 5-year increased +2 basis points to 3.36%. The price of Brent crude oil was supported, gaining +0.7% to just below \$115. The dollar was weaker, receding -0.5% versus trade-weighted counterparts, but cryptocurrencies rebounded to \$21,000 for bitcoin and \$1,120 for ether.

The relief however may be short-lived, as there is no quick answer to the current structural question: inflation and central banks. The supply side may gradually improve for goods as China reopens, and base effects have started to play, but the war in Ukraine continues to support global prices of energy and food. There are also specific situations, starting with the tightness of the US labor market: this explains and in a way justifies the radical stance of the Fed. The next potential concern is obviously to see the housing market being pressured by higher interest rates. In Europe, the ECB faces another specific yet structural issue: having very different countries sharing a currency and a yield curve. Hiking rates could push

sovereign spreads between the most and least indebted into dangerous territory. This “fragmentation” could be worse than inflation in itself, especially as most of the Eurozone’s inflation issue is linked to energy, which is factually out of control of the ECB. This is not improving, with Russia gradually reducing supplies to Europe, which they had warned about. The result is that Germany is generating electricity with coal – climate change can wait, and that instead of buying refined products in Euros from Russia, Europe imports them from India in dollars – transformed from Russian crude of course, but apparently European leaders feel better this way. This looks quite absurd and doesn’t help on inflation. Monetary policies in emerging economies are obviously not immune: Mexico, Colombia, Czechia, Hungary are all set to raise rates imminently. Macro topics will keep on moving markets in the coming months with extreme volatility and very low predictability. Good economic news could be bad for markets as they postpone the end of monetary restrictions, but bad economic news would raise growth concerns and the stagflation scare. Unless positioning is so bearish that markets brutally rebound from time to time without an obvious reason. This is why the only key catalyst is undoubtedly to see a credible inflexion in inflation, but the good news is that most assets provide some level of fundamental upside potential over the medium term once it happens. This is why our positioning is modestly pro cyclical, combing expectation for high volatility in the short-term with a probably constructive outcome later.

As we write this morning, risk aversion dominates in Asia. Stocks are down -2% in Korea, -1% in Hong-Kong, -0.5% in China and flat in Japan. Interest rates are marginally lower, and the price of Brent crude oil is down -3% to \$111, indicating that today is about growth scare. Future contracts on Western stock markets are also in the red. Goldman Sachs, SocGen, StanChart or Morgan Stanley issued warnings about the economy and markets which are probably part of this rise in risk aversion. It’s good however to remember that due to the very nature of their business, making money on flows, these sell-side houses can, and do, radically change their mind quite often. On our side, we always have a look at our year-end fair values at mid-year, and we will do so at our July tactical asset allocation committee in a couple of weeks.

Today we will look at inflation numbers in the UK and at consumer confidence in the Eurozone. Stay safe.

Chief Investment Office  
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