



CIO OFFICE MORNING MARKET WRAP – 22nd September, 2021. ALSO AVAILABLE ON ALEXA.

Most Asian stocks are leaning weaker and US futures are mixed this morning after Evergrande, the cash-strapped Chinese property developer, negotiated an interest payment with some bondholders and the PBOC made cash injections in the system. Trading resumed in China following a holiday and equities were lower but avoided a bigger sell-off, while the commodity-linked Australian and New Zealand dollar pushed higher, pointing to improving risk sentiment.

Mixed US equities yesterday suggest that not much dip-buying occurred following the slump on Monday to eight-week lows for the S&P 500 Index. Energy and real estate stocks led gains, while industrials underperformed the most, pointing to a lingering risk-off mode at a sector level as well. Economic bellwether Fedex cut its earnings forecast, causing futures to extend declines in after-hours trading. Treasury yields and the US dollar were little changed, crude oil rebounded and gold advanced following two weeks of losses. Bitcoin dropped to retrace 50% of the gains made in the rebound off the June lows, and this begs the question whether we are witnessing a temporary drying up of the market liquidity portending further losses. Usually a relevant stock market bottom would see the inversion of the futures curve of the implied volatility, meaning that the one-month futures contract on the VIX Index would be trading

higher than the three month on heightened risk aversion. This has not yet happened, so we may have to brace ourselves for further uncertainty.

Investors are closely watching Evergrande, after the overly-leveraged Chinese property developer missed interest rate payments due Monday to at least two banks. Everybody considers the restructuring of the company inevitable, though it is not so much important the 'if', as the 'how' of the process. How will we get there? The largely shared assumption is that the Chinese authorities will do their best to put in place an orderly restructuring in order to avoid contagion effects. Ray Dalio said that Evergrande's debt crisis "is all manageable", though "investors will be stung". Citi analysts wrote in a research note that the company's potential systemic risk is not shaping up as "China's Lehman moment". The liquidity injections made by the PBOC today provide some comfort, signalling a plan to reduce systemic stress.

Investors are undoubtedly looking forward to today's Fed policy meeting that began yesterday, when the central bank is expected to prepare markets for a November taper announcement. At the July meeting "progress" was mentioned on unemployment and inflation and NY Fed Williams last week said that the August soft jobs report isn't a game-changer, suggesting the intention to start the stimulus-reduction process. There is a chance that the so-called dot plot, showing projections for the federal funds rate, will point to a median forecast pulling forward the start of the tightening cycle to 2022.

Whatever the details of the Fed's message, a forthcoming implementation of the tapering implies that the direction of travel for longer-dated nominal yields is up, and since market-implied inflation is already at the top-end of the historical range, real yields would have to rise. That is not bullish for gold, which we would expect to be leaning weaker into the tapering announcement expected for November.

Stay safe.

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