



## CIO OFFICE MORNING MARKET WRAP – Wednesday 29<sup>th</sup> June, 2022.

Asian stocks are trading lower this morning, following yesterday's rout on Wall Street led by technology. Australia and Korea are down more than 1% as of the time of writing, while the Chinese indices are mixed. Euro Stoxx 50 and FTSE 100 contracts are negative, while US futures are slightly in the green. Yesterday global stocks lost more than 1%, but US equities dropped by 2%, as an early rally driven by the easing of quarantine rules in China reversed on negative consumer sentiment data in America. Crude oil advanced alongside the dollar, while treasuries and gold were little changed.

Investors remain skeptical that central banks will be able to avoid an economic downturn amidst sharp interest rate hikes. So far surveys for the month of June have painted a worse picture than lagging hard data would suggest. The Conference Board consumer confidence index weakened more than expected, with the drop largely accounted for by the future expectations component, which declined further below its historical average. "Expectations have now fallen well below a reading of 80, suggesting weaker growth in the second half," said a Conference Board representative. This should be no surprise, though, given that the other survey, where inflation plays a larger role, run by the University of Michigan, saw consumer sentiment plunge to all-time lows a week earlier. US regional surveys also pointed

to a material loss of momentum in June. Mary Daly, the San Francisco Fed President, while acknowledging that the pace of US growth could slow below 2% as the Fed tightens, said “it won't actually pivot down into negative territory for a long period of time”.

If the Federal Reserve can convince investors that tightening can proceed while avoiding a hard landing, there could be further room for real yields to rise, whose advance has halted since the mid-June 75bps hike. Real yields currently face the headwind of higher policy rates and declining growth expectations. Their rise has hurt non-yielding assets like bitcoin and gold, as well as risk assets like EM currencies and bonds. If a US recession remains more likely only following the end of the tightening cycle as per historical patterns, then there may be some modest upside. With the 10-year real treasury yield currently at +70bps, consensus sees a level of 1%, combined with the less accommodative conditions induced by Quantitative Tightening, the most the US economy could take without cracking.

On a more positive note, China cut in half the length of time inbound travelers must spend in quarantine. This would make it easier for citizens to return and foreign companies to tend to business. Although this could be a first step towards ending isolation, officials stressed that the measures are compatible with a Covid-zero policy.

On the concluding day of the G7 summit the commitment was reaffirmed to “phase out our dependency on Russian energy”, exploring “further measures to prevent Russia from profiting from its war of aggression”. The leaders of the richest countries must be confident that pushing harder is the only way to go. Easier said than done. Europe’s resolve will meet reality this coming winter, as the German economy could face an over 12% slump if Russia fully stops gas supplies. According to an industrial group 5.6ml jobs would be at risk, hardly a way to prop up popularity for the harsh measures Washington has been advocating, and actually a recipe for political instability. Also, the communique was short on concrete measures. But the G7 aimed for even more, seeking ways to punish Russia while taking on China. China should “abstain from threats, coercion, intimidation”, in the aspirational world painted by the communique. At the same time, NATO seems set to become bigger, with Finland and Sweden progressing on their way to NATO membership, after Turkish President Recep Tayyip Erdogan dropped his opposition to their bids. Ukraine also continues to press for membership. Stay safe.

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