Confidence must be earned

Amundi ASSET MANAGEMENT

Weekly Market Review

The latest news from financial markets

for the exclusive attention of professionals

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The week at a glance

- **Markets:** The euro reached parity vs the U.S. dollar for the first time in 20 years.
- **United States:** The June U.S. Consumer Price Index (CPI) came out stronger than expected.
- **Eurozone:** The German ZEW survey saw the expectations reading for the economy fall to its lowest level since the sovereign debt crisis.

KEY FIGURE

9.1%

U.S. June Consumer Price Index

Focus

The European Commission lowers its growth forecasts

The European Commission has just lowered its 2022 GDP growth forecast to 2.6% (from 2.7% previously) and, even more important, its 2023 forecast to 1.4% (from 2.3% previously). It raised its inflation forecasts to 7.6% for 2022 and to 4% for 2023. These revisions are due mostly to fallout from the war in Ukraine (e.g. higher energy and food prices and the negative impact on confidence), to supply-chain disruptions owing mainly to draconian lockdowns in China and to higher interest rates. The Commission did not rule out the possibility of further reductions in its forecasts in the event of a total shutoff of Russian gas.

KEY DATES

21 July	26 July	28 July	29 July
European Central Bank (ECB) Committee	U.S. Federal Reserve's monetary policy meeting (FOMC meeting)	U.S. second quarter GDP	Eurozone second quarter GDP

Source: Amundi Institute.

Our weekly analysis

Latin America's Exposure to the Perfect Storm

Latin America is once again finding itself between a rock and a hard place. The dollar's strength is due to the perfect storm of three factors: i) the U.S. Federal Reserve's (Fed's) crusade against inflation; ii) a global slowdown in economic activity; and iii) scrutiny of domestic imbalances such as inflation. All this has exposed Latin America on many fronts and in different ways. All three are blowing up at the same time, magnifying the headwinds and creating a vicious cycle of sorts.

The triple storm and Latin America's starting points are a bit different this time around. Regional central banks, the Central Bank of Brazil (BCB) in particular, famously front-ran the Fed – at least during the first leg of its catching-up phase. The global economy is slowing in an unsynchronised way, with China heading in the other direction. Supply factors, too, will keep commodity prices more elevated than they otherwise would be. Finally, domestic imbalances and inflation specifically are not just Latin America's problem this time around.

The Achilles heel: politics and related policy. The Bank for International Settlements' recent paper on fiscal vs monetary dominance, found an impact on inflation up to five times greater under fiscal dominance. This is more damaging to price formation and a timely reminder that potential regime changes in Latin America will have real consequences across the economy. And while the political cycles have been playing out, elevated uncertainty has kept capital expenditure on the side-lines, to the detriment of foreign direct investment, mining output and domestic demand, which is being constrained by design.

Unevenly exposed. The region looks split into three groups across the three axes of exposure and the political angle: a) Mexico is exposed to a lesser degree; b) Brazil and Peru are exposed but are less vulnerable; and c) Columbia and Chili are both exposed and vulnerable.

Andean contagion? Emerging market-wide contagion is less likely, given that the emerging universe heavyweights are somehow better positioned. But there are still some regional hot spots such as the Andeans and parts of Central and Eastern Europe. Accordingly, the Central Bank of Chile (BCCh) and Central Bank of Columbia (BanRep) might also have no choice but to hike rates in an emergency fashion, as Hungary's central bank (MNB) has been doing in recent days.

Indice	Performance			
Equity markets	15/07/22	1 W	1 M	YTD
S&P 500	3831	-1.8%	1.1%	-19.6%
Eurostoxx 50	3446	-1.7%	-2.4%	-19.8%
CAC 40	5979	-0.9%	-0.8%	-16.4%
Dax 30	12762	-1.9%	-5.4%	-19.7%
Nikkei 225	26788	1.0%	1.8%	-7.0%
SMI	10891	-1.1%	1.0%	-15.4%
SPI	14053	-1.1%	1.3%	-14.5%
MSCI Emerging Markets (close -1D)	965	-3.4%	-5.4%	-21.6%
Commodities - Volatility	15/07/22	1 W	1 M	YTD
Crude Oil (Brent, $/barrel)	101	-5.6%	-14.7%	29.9%
Gold ($/ounce)	1703	-2.3%	-7.1%	-6.9%
VIX	25	0.8	-4.2	8.2
FX markets	15/07/22	1 W	1 M	YTD
EUR/USD	1.004	-1.4%	-3.8%	-11.7%
USD/JPY	139	2.0%	3.7%	20.7%
EUR/GBP	0.85	0.4%	-0.9%	1.0%
EUR/CHF	0.98	0.5%	-1.3%	7.6%
USD/CHF	0.99	-0.9%	-5.1%	-5.0%

Source: Bloomberg, Amundi Institute – 15/07/2021 – 15:00 pm

Indice	Performance			
Credit markets	15/07/22	1 W	1 M	YTD
Itraxx Main	+124 bp	+7 bp	+18 bp	+76 bp
Itraxx Crossover	+614 bp	+38 bp	+85 bp	+372 bp
Itraxx Financials Senior	+136 bp	+8 bp	+18 bp	+81 bp
Fixed Income markets	15/07/22	1 W	1 M	YTD
ESTER OIS	98.43	-1 bp	-5 bp	-31 bp
EONIA	-0.51	-	-	-
Euribor 3M	0.07	+16 bp	+25 bp	+64 bp
Libor USD 3M	2.51	+9 bp	+48 bp	+230 bp
2Y yield (Germany)	0.49	-4 bp	-60 bp	+111 bp
10Y yield (Germany)	1.16	-19 bp	-49 bp	+134 bp
2Y yield (US)	3.16	+5 bp	-4 bp	+242 bp
10Y yield (US)	2.95	-13 bp	-33 bp	+144 bp
Eurozone Sovereigns 10Y spreads vs Germany	15/07/22	1 W	1 M	YTD
France	+61 bp	+8 bp	+3 bp	+24 bp
Austria	+58 bp	-	-2 bp	+31 bp
Netherlands	+33 bp	-1 bp	-2 bp	+18 bp
Finland	+53 bp	-1 bp	-7 bp	+25 bp
Belgium	+64 bp	--	-3 bp	+27 bp
Ireland	+61 bp	+1 bp	-7 bp	+18 bp
Portugal	+116 bp	+8 bp	-5 bp	+52 bp
Spain	+115 bp	+8 bp	-10 bp	+41 bp
Italy	+212 bp	+18 bp	-5 bp	+77 bp

Asset Class

	MARKET	AMUNDI ANALYSIS
Equity	Equity markets deliver negative returns as inflation once again surprises on the upside. The MSCI World is down almost -2.2% at the time of writing. The main drivers are the U.S. and Emerging Markets with the S&P 500 down almost -2.5% and the Nasdaq down almost -3.3%. In emerging markets, the MSCI emerging market is down almost -2.9% and the Chinese CSI 300 almost -2.4% week to date. European stocks were somewhat more resilient with the Stoxx 600 index down almost -1%. Japanese stocks are the only spot of blue in a sea of red at the time of writing, up almost +0.3% this week.	The U.S. Consumer Price Index (CPI) print this week came in at 9.1%, above consensus expectations of 8.8%, putting further pressure on the performance of long duration stocks and Growth stocks. This is reflected in the weak performance of the Nasdaq and on the performance Growth stocks, which marginally underperformed Value so far this week despite recession concerns intensifying which normally should favor Growth.
Fixed Income	U.S. Treasury yields rose at the front-end of the curve on the back of another shockingly-strong Consumer Price Index (CPI) report. Front-end yields rose sharply on increased expectations of a 100bp hike at the July U.S. Federal Reserve's monetary policy meeting (FOMC meeting), but unwound part of the rise after Governor Waller indicated he would support a 75bp hike and Bullard made similar comments. The long-end of the curve declined on recession concerns. U.S. and German yields are down over the week.	The European Central Bank (ECB) is in a difficult position, caught between high inflation, the need to avoid financial fragmentation across the euro area and growth concerns. A recession should diminish core inflationary pressures, but it would likely be caused by the energy crisis, which would push headline inflation further up. On top of growth and inflation, financial fragmentation concerns could also weigh on the ECB's response, as a further energy shock would only increase divergence across countries. We expect that the ECB will nevertheless start its hiking cycle next week as the priority remains inflation. It should also give more detail about its anti-fragmentation tool.
Credit	Credit markets recovered ground following the sharp widening in spreads suffered in June. U.S. speculative grade led the tightening among global high yield bonds, while euro investment grade outperformed U.S. high grade, as spreads in Europe were back close to 200bp from their 213bp early July peak. On the other hand, while cash bonds recovered ground, credit default swaps were still feeling the pain of higher equity volatility.	Technicals remain challenging for credit markets, as market positioning has not been reduced to the same extent as in other asset classes, despite last months' outflows, while primary market activity remains muted in euro high yield, and quite limited by historical standards in U.S. speculative grade. As valuations remain attractive, the markets' focus is likely to turn to the upcoming second quarter earnings season over the next few weeks.
Foreign Exchange	The euro reached parity vs the U.S. dollar for the first time in 20 years. The dollar was supported by higher-than-expected U.S. inflation that raised prospects of further rate hikes from the U.S. Fed. The Japanese yen was the worst-performing G10 currency vs the U.S. dollar, against which it hit a 24-year low. The only emerging currency positive vs U.S. dollar this week was the Russian rouble.	We have hit parity, the target we had in mind for U.S. dollar/euro for 2022. Some more appreciation in U.S. dollar/euro is possible in the near term, due to the current complex context. The euro will regain some ground in late 2022 and 2023. We are still cautious on emerging market currencies, Eastern European currencies in particular. We are sticking to a marginal positive stance on some commodity exporters far from the conflicts, like the South African rand and Malaysian ringgit.
Commodities	Commodities fell by 1.9% this week on recession fears. West Texas Intermediate (WTI) and Brent nosedived to \$96 and \$99, respectively. Agriculture plummeted by 5.7%. Gold fell to \$1703, while base metals moved down by 3.6%.	We maintain our positive view on commodities, despite fears of global demand and U.S. Fed liquidity drain. Supply shortages should last for some specific base metals, due to geopolitical tensions and world electrification. Central banks and nominal (real) rates are still the key movers for the gold price, pending U.S. Fed actions at its upcoming committee meetings. Oil will be driven by OPEC decisions and a cooling in demand in the coming quarters.

Economic Indicators

	MARKET	AMUNDI ANALYSIS
United States	The June U.S. Consumer Price Index (CPI) came out stronger than expected. The year-on-year figure was at +9.1% (vs a consensus of +8.8%), the highest since 1981, and the month-on-month at +1.3% (vs a consensus of +1.1%), the highest monthly reading since September 2005. The core CPI came in at its highest in a year, at +0.7% (versus +0.5% expected).	The acceleration in headline inflation largely reflects higher prices of gasoline (+11.2% month-on-month), food (+1.0% month-on-month) and shelter (+0.6% month-on-month). However, besides the volatile components of the CPI report, inflationary pressures remain elevated across the board. June inflation numbers were of particular interest to markets, as they led to speculations that the U.S. Fed could hike by 100bps at its 27 July meeting.
Eurozone	The German ZEW survey saw the expectations reading fall to its lowest level since the sovereign debt crisis, at -53.8 (versus -40.5 expected), whilst the current situation reading fell to -45.8 (versus -34.5 expected).	The disappointment in the German economic sentiment index is weighing on an already concerning economic juncture for the country (and the continent's other major economies), as European natural gas prices continue to spike higher amidst risks of Russian gas supply cut-offs. The closure of Nord Stream 1 until 21 July (for its usual annual maintenance) is of concern this time round as to what might happen at the end of this period.
Japan	Two days after the assassination of former Prime Minister Shinzo Abe, Japan held its upper house election on 10 July, with 125 out of the 248 seats being contested. The ruling Liberal Democratic Party (LDP)-Komeito coalition won 70 seats in this election, successfully expanding its presence to 146 seats in the upper house.	The upper house election confirmed that the Kishida government would remain in place until 2025. Former PM Abe was an influential figure in the ruling party, chairing its biggest faction. A potential breakup of this faction creates room for Kishida to pursue his own political agenda, including a less hawkish fiscal policy.
Emerging Market	In an inter-meeting decision, the Central Bank of Philippines (BSP) hiked its policy rate by 75bps, to 3.25%. The decision was driven by signs of sustained and broadening price pressures, whilst growth is strongly rebounding. The urgency should better suit the anchoring of inflation expectations and limit the risk of a further spiking in prices.	The BSP decision was surprising in its timing, as well as in its extent, considering the gradual approach to policy normalisation advocated so far. The latest inflation figures have triggered un upward revision of inflation path for 2022, prompting larger-than-expected front-loading by the BSP. We raised the terminal rate to 4.25% from 3.5%, to be attained in the second part of this year.