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Amundi
ASSET MANAGEMENT

# Weekly Market Review

**The latest news from financial markets**

for the exclusive attention of professionals

**Edition of August 1, 2022** By Amundi Institute

## **The week** at a glance

- **Markets:** US stocks performed quite well the week of the further 75bps Fed rate hike.
- **United States:** Following a rise in new orders of defence aircraft, new durable goods orders increased 1.9% month-on-month in June, well above consensus.
- **Eurozone:** The European Commission’s economic sentiment indicator (ESI) decreased from 103.5 in June (downwardly revised) to 99.0 in July, a 17-month low.

**KEY FIGURE**

**75bps**

Increase (in basis points) in the key interest rates decided by the US Federal Reserve at their July meeting.

**Focus**

The Fed continued to take aggressive steps to cool inflation down. The monetary policy meeting (FOMC meeting) delivered a second consecutive 75bps rate hike at its July meeting, bringing the target range for the federal funds to 2.25-2.5%. According to the Fed, this is the range considered as neutral. The Fed remains hyper-focused on fighting inflation and determined to continue hiking rates to slow the demand. The Fed remains much more concerned about inflation expectations becoming unanchored than on downside risks weighing on growth. Indeed, price pressures are spreading across more and more sectors. Powell continued to defend the scenario of a soft landing. Powell acknowledged that “recent spending and output indicators have softened,” but pointed to the strength of the US labor market. Rate hikes will now be a meeting-by-meeting decision as the policy rate is back to neutral. The lag with which the tightening of monetary policy affects economic activity increases the uncertainty surrounding the economic outlook.

**KEY DATES**

**4th August**
Monetary policy committee of the Bank of England (BoE)

**5th August**
Release of non-farm payrolls in the US in July

*Source: Amundi Institute.*

*Document for the exclusive attention of professional clients, investment services providers and any other professional of the financial industry.*

# Our weekly analysis

**GDP release for the 2nd quarter, the US in technical recession: weakening demand, labour market developments even more pivotal to the outlook.**

US GDP contracted again in the 2nd quarter by 0.9% quarter-on-quarter (after -1.6% in 1st quarter), thus configuring a so-called 'technical recession'. GDP growth decelerated sharply to 1.6% year-on-year in 2nd quarter, which is already below potential, from 3.5%. There was an element of the sort of volatility that we recently have been used to (a huge drag from inventories this time, subtracting approximately 2% from GDP growth), but the deceleration in domestic growth was nevertheless noteworthy:

• There was a visible deceleration in consumption, with signs of a shift from goods to services consumption.

• There was a visible slowdown in non-residential investments (due to a mild contraction in equipment investments and a continued decline in investment structure), whilst intellectual property investments kept expanding at a strong pace.

• Residential investment contracted and its sensitivity to interest rates means it is likely to keep weakening.

In 2nd quarter, GDP growth moved below potential. Crucially, this sharp deceleration can't be fully ascribed to the impact of Fed tightening so far, since policy works with lags. Instead, it is mainly the result of other drags operating on US consumers (e.g., the post-pandemic support fiscal cliff) and the impact of inflation on real incomes. We may have not yet seen a wealth effect taking place. While inflation may have peaked, it will remain well above the Fed's target in the coming quarters. Labour market data still looks resilient, which means consumption should be positive, albeit weak. However, the outlook for domestic demand, and especially investment, will become cloudier as the Fed's rate hikes start to have an effect.

| Indice | Performance | | | |
|---|---|---|---|---|
| Equity markets | 07/29/22 | 1 W | 1 M | YTD |
| S&P 500 | 4072 | 2.8% | 6.6% | -14.6% |
| Eurostoxx 50 | 3697 | 2.8% | 5.2% | -14.0% |
| CAC 40 | 6427 | 3.4% | 6.6% | -10.2% |
| Dax 30 | 13440 | 1.4% | 3.4% | -15.4% |
| Nikkei 225 | 27802 | -0.4% | 3.7% | -3.4% |
| SMI | 11199 | 0.9% | 3.6% | -13.0% |
| SPI | 14503 | 1.1% | 4.2% | -11.8% |
| MSCI Emerging Markets (close -1D) | 998 | 0.7% | -1.5% | -19.0% |
| Commodities - Volatility | 07/29/22 | 1 W | 1 M | YTD |
| Crude Oil (Brent, $/barrel) | 110 | 6.1% | -5.8% | 40.8% |
| Gold ($/ounce) | 1763 | 2.0% | -3.0% | -3.6% |
| VIX | 22 | -1.2 | -6.3 | 4.6 |
| FX markets | 07/29/22 | 1 W | 1 M | YTD |
| EUR/USD | 1.024 | 0.3% | -1.9% | -9.9% |
| USD/JPY | 133 | -2.1% | -2.5% | 15.8% |
| EUR/GBP | 0.84 | -1.2% | -2.4% | -0.1% |
| EUR/CHF | 0.95 | -1.2% | -0.3% | 4.3% |
| USD/CHF | 0.97 | -0.9% | -2.3% | -6.1% |

*Source: Bloomberg, Amundi Institute – 07/29/2022 – 15:00 pm*

| Indice | Performance | | | |
|---|---|---|---|---|
| Credit markets | 07/29/22 | 1 W | 1 M | YTD |
| Itraxx Main | +102 bp | -2 bp | -15 bp | +54 bp |
| Itraxx Crossover | +520 bp | -8 bp | -61 bp | +277 bp |
| Itraxx Financials Senior | +112 bp | -4 bp | -15 bp | +57 bp |
| Fixed Income markets | 07/29/22 | 1 W | 1 M | YTD |
| ESTER OIS | 98.41 | -1 bp | -4 bp | -33 bp |
| EONIA | -0.51 | - | - | - |
| Euribor 3M | 0.23 | +3 bp | +42 bp | +80 bp |
| Libor USD 3M | 2.81 | +4 bp | +53 bp | +260 bp |
| 2Y yield (Germany) | 0.31 | -14 bp | -53 bp | +93 bp |
| 10Y yield (Germany) | 0.89 | -14 bp | -63 bp | +107 bp |
| 2Y yield (US) | 2.87 | -10 bp | -17 bp | +214 bp |
| 10Y yield (US) | 2.70 | -5 bp | -39 bp | +119 bp |
| Eurozone Sovereigns 10Y spreads vs Germany | 07/29/22 | 1 W | 1 M | YTD |
| France | +57 bp | -2 bp | +2 bp | +19 bp |
| Austria | +54 bp | -1 bp | -2 bp | +28 bp |
| Netherlands | +31 bp | -2 bp | -4 bp | +16 bp |
| Finland | +52 bp | -2 bp | -5 bp | +24 bp |
| Belgium | +61 bp | -2 bp | -4 bp | +24 bp |
| Ireland | +65 bp | +2 bp | +2 bp | +22 bp |
| Portugal | +108 bp | -8 bp | +2 bp | +44 bp |
| Spain | +115 bp | -8 bp | +8 bp | +41 bp |
| Italy | +233 bp | +4 bp | +44 bp | +98 bp |

## Asset class

| | MARKET | AMUNDI ANALYSIS |
|---|---|---|
| **Equity** | **US stocks performed quite well** the week of the further 75bps Fed rate hike and of the US GDP release for the 2nd quarter, which showed that the American economy shrank for a second consecutive quarter. Investors are now betting on the Fed to end its aggressive hiking campaign. | We keep our preference for the US versus the Economic and Monetary Union. We remain cautious on emerging markets overall, as they are perceived as riskier by the market due to Chinese deceleration. We prefer to remain selective in the region, playing commodity exporters far from the region of the Ukraine-Russia conflict, like Latin America, South Africa and Indonesia. |
| **Fixed Income** | **US yields fell by 5bps across the curve** as investors pared expectations for how much policy tightening the Fed will do based on a weak initial estimate of the US economy's performance in the second quarter. Moreover, as Powell indicated that now that policy rates are back to neutral level and as the stance of monetary policy tightens further, the pace of rate increase will slow. Investors now expect the Fed funds rate to peak around 3.25% before the end of this year, less than a percentage point above its current level. As Europe's economic growth is already suffering under the weight of record inflation and the increasing likelihood of a Russian energy cutoff, 10-year German yields continued their decline, falling by 12bps over the week to less than 0.9%. | The FOMC delivered a second consecutive 75bps rate hike at its July meeting, bringing the target range for the Fed funds to 2.25-2.5%. According to the Fed, this is the range considered as neutral. As the stance of monetary policy tightens further, the pace of rate increase will slow. That decision will be based most importantly on progress on the inflation front, but will also include other factors: where policy is relative to the Fed's estimate of neutral, evidence that growth is slowing sufficiently and the labor market is coming into better balance, and whether financial conditions are broadly calibrated to meet the Fed's objectives. |
| **Credit** | **Credit markets have remained relatively stable this week** after the severe contraction recorded since the beginning of July. Spreads widened slightly this week for the US credit bond market (+2bps for Investment Grade and High Yield). They only slightly tightened on the euro Investment Grade (-1bp) and remained stable on the euro High Yield. To date, 50% of US Investment Grade issuers have reported second quarter results, with 60% positive earnings surprises. | Following the Fed meeting, Investment Grade spreads benefited from a steeper Treasury yield curve and lower interest rate risks. On the Eurozone side, the European Central Bank ended quantitative easing, forward guidance and raised these rates this month, leaving euro credit markets in a state of extreme volatility. In the euro zone, the beta decompression dynamic should continue, as the "upgrades" of the ratings of Investment Grades issuers are increasingly visible. Valuations have started to look less attractive following the publication of Purchasing Managers' Index figures below 50 in the United States this week. |
| **Foreign Exchange** | **The Fed delivered the second 75bps hike in July,** yet its growing attention to growth (at the expenses of inflation) has been taken as a dovish shift on most markets. Within emerging markets, Latin American currencies rebounded strongly, whilst the Russian ruble and the Polish zloty lagged behind. The same dynamics were seen in G10, where the euro and the Swedish krona lagged behind the rebound in cyclicals. On the other hand, the Japanese yen got a strong boost on Thursday, as the GDP release for the 2nd quarter in the US made the recession live. | Correlation with monetary policy decisions dropped significantly in the latest quarter, with hawkish central banks' repricing failing to push up currencies. Whenever global growth is at stake, the Fed is the only central bank able to invert investor sentiment. We think it is still too early to call for the end of the normalisation process and still like to be exposed to the US dollar in the short run. |
| **Commodities** | **Commodities drifted higher by 1% this week,** rebounding after the recent sell-off. The price of WTI and Brent rose to $99 and $107 a barrel, respectively. Agriculture rebounded by 7%. Gold moved above $1,750/ounce, while base metals were up by 0.6%. | We maintain our positive view on commodities despite greater concerns on growth going forward after recent US data and central bank hikes. Supply shortages should last for some specific base metals, due to geopolitical tensions and the green transition. |

## Economic indicators

| | MARKET | AMUNDI ANALYSIS |
|---|---|---|
| United States | **Following a jump in new orders of defence aircraft,** new durable goods orders jumped 1.9% month-on-month in June, well above consensus. When excluding the volatile component of defence, new durable goods orders still moved up by 0.4% month-on-month on the month. Core capital goods orders rose by 0.5% month-on-month. | Incoming data on new durable goods orders and the goods trade balance would imply business equipment investment is posed to slow over the next few quarters, yet not to collapse in the near future, remaining on a stronger footing than a full-blown recession would imply. At the same time, data released suggest the restocking cycle is losing momentum as inventory accumulation slows. |
| Eurozone | **The European Commission's economic sentiment indicator (ESI) decreased** from 103.5 in June (downwardly revised) to 99.0 in July, a 17-month low. The decline was broad-based, with all sectors experiencing a deterioration in sentiment. | Supply-chain shortages persist, although there are signs of easing on softer demand, while the survey indicates that labour market is getting tighter too. This implies that price pressures will likely remain intense for a while, even if demand will be cooling. Indeed, selling price expectations for industry, services and retail remained at very high levels in the survey. |
| Japan | **Japan continues to see record high daily increases in Covid-19 cases.** Its weekly increase of about 1 million infections was the highest in the world. The sharp increase is caused by the highly contagious BA.5 variant. Despite an increasingly strained medical system, the government says there is no need to put in restrictions. | Although no domestic restrictions will be imposed, this new and contagious Covid outbreak will delay the timeline of a full opening of Japan's borders. It now caps the number of daily visitors at 20,000, one-seventh of the level of 2019, and allows tourists to enter only on guided tours. It will take longer time for its tourism sector to recover. |
| Emerging Markets | **Unravelling the foreign exchange situation led to a political reshuffle in Argentina** and the naming of Sergio Massa as a 'Super Minister' of sorts. He will head the ministry of the economy, production and agriculture and will talk to the International Monetary Fund. Massa is a former chief of staff, and until now lower house speaker, but, most importantly, he is considered one of the most market-friendly politicians within the ruling coalition. | The highly unbalanced economy desperately needs an orthodox policy response and Massa appears to have the credibility and support of the coalition to deliver some of it. His appointment is a much needed confidence boost that should also lead to an improvement in governability and a reduction in political uncertainty. He is rumoured to favour a dual foreign exchange 'mechanism' for exporters and arguably also a currency devaluation. |