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BONHÔTE

Cold snap

Overview

In September, all market sectors except oil & gas (for obvious reasons) were down sharply as higher inflation plus expectations that the Fed plans to scale back asset purchases as early as November together weighed on sentiment. Signs of slower economic growth in China and political ructions in Washington did nothing to help matters.

The stalemate in Congress over federal government funding, with different sides disagreeing over the increased debt ceiling and the size of the infrastructure plan, has lit a fire under long-term yields. The sheer speed of the upswing shows that, among investors, the pendulum has swung from capital appreciation to protecting gains. This is illustrated by latest surveys, which show the level of bullish viewpoints plunging to 23 while bearish opinions have soared to a score of 40. A scenario of persistent inflation is gaining ground, which is sparking volatility in the prices of financial assets, themselves seemingly at the mercy of the slightest uptick or downtick in bond prices. As we head into October, the profit outlook for the fourth quarter – just as the nine-month earnings season is kicking off – as well as employment perspectives are adding to the chill in the air. US job creation for September, out this Friday, is expected at 470,000. After the upset in August, this figure will be key to determining the Fed's next move, considering that part of its mandate is also to achieve full employment.

Scenario of persistent inflation is gaining ground

A critical question right now is whether the cascade of price increases that we are seeing is a one-off occurrence, stoked by pent-up demand, in which case the damage could be limited by adopting less accommodating monetary policies. But if the inflation is more ingrained, that would be out of the question. Higher input costs are unsettling investors, aware that this also makes central banks more jittery and consumers more hesitant. Supply chains most likely need to be strengthened to limit disruptions, which will require capital expenditure. But only so much can be done to meet the brisk demand, both now and in the longer term.

A critical question is whether the inflation spike is merely the result of economies reopening

In China, the world's manufacturing heartland, rising energy prices (as it curtails the use of coal to reduce emissions) and power cuts have forced factories to curb production output. In September, the manufacturing PMI slipped below the 50-spot marking the start of expansion territory. By contrast, the services PMI recovered after some Covid-related restrictions had been lifted. Last week the authorities asked banks to support the housing market by facilitating mortgages, signalling that they are concerned about the woes experienced by Evergrande – which has defaulted on some interest payments – spreading to other entities. Fears that Beijing could allow GDP growth to slow down even more as it overhauls the structure of its economy are making investors all the more nervous.

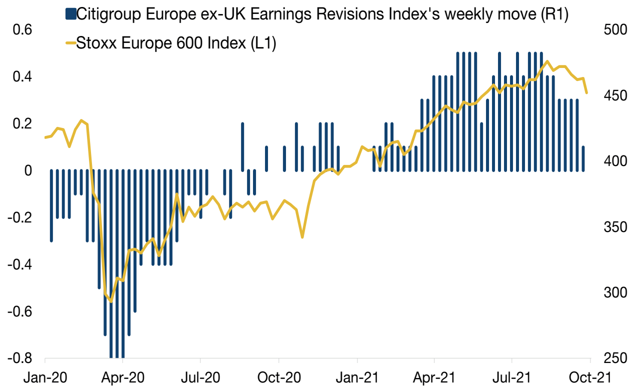
In the US, the manufacturing PMI rose to 61.1, driven by a high backlog of orders. However, delivery times are becoming significantly longer.

Key data

	USD/CHF	EUR/CHF	SMI	EURO STOXX 50	DAX 30	CAC 40	FTSE 100	S&P 500	NASDAQ	NIKKEI	MSCI Emerging Markets
Latest	0.93	1.08	11'575.37	4'035.30	15'156.44	6'517.69	7'027.07	4'357.04	14'566.70	28'771.07	1'246.60
Trend	→	→	↓	↓	↓	↓	→	↓	↓	↓	↓
YTD	5.13%	-0.23%	8.15%	13.59%	10.48%	17.41%	8.77%	16.00%	13.02%	4.83%	-3.46%

(values from the Friday preceding publication)

Earnings momentum falters



September brought the curtain down on the stockmarket's meteoric rise. Moreover, earnings forecasts are falling sharply for the first time since February, stoking uncertainty in the market and undermining the main driver behind the equities rally.

Since July, upward earnings revisions have become less frequent due to fears of slower economic growth and runaway inflation. Meanwhile volatility in the equity market has been rising, zigzagging in line with interest rate prospects. Today, most analysts are predicting a correction, or at least a slower pace of appreciation, as reflected in the massive sell-off of shares by mutual funds in recent weeks. Those outflows were mainly triggered by the disbursement of US dividends and a more neutral positioning by fund managers ahead of the next quarter, on which forecasts are more half-hearted.

Market sentiment is therefore cautious. But since the fourth quarter has historically been good for equities, there is still reason for hope, especially as strategic reallocations have now been implemented and the uncertainty factored into earnings estimates.

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