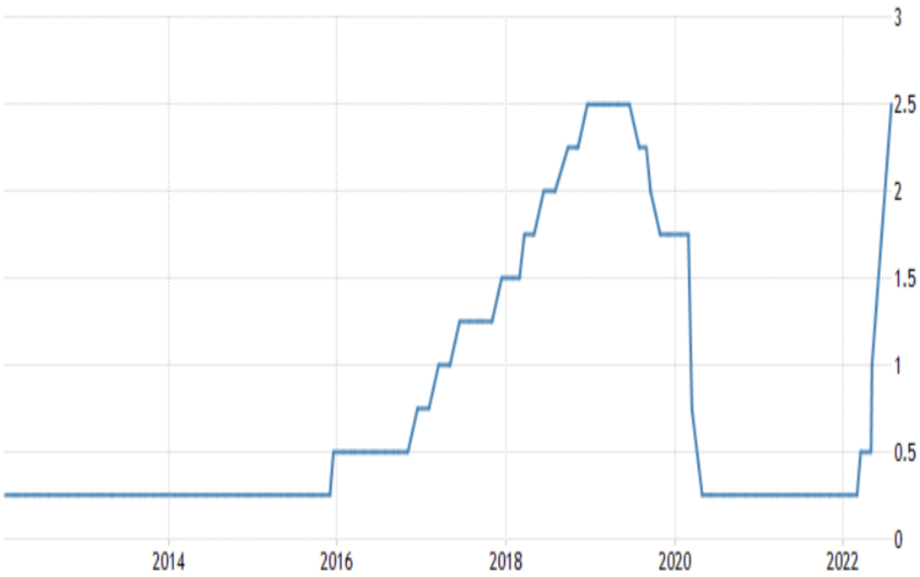
VERNY CAPITAL

Global Markets Updates: US Federal Reserve Rate Hike

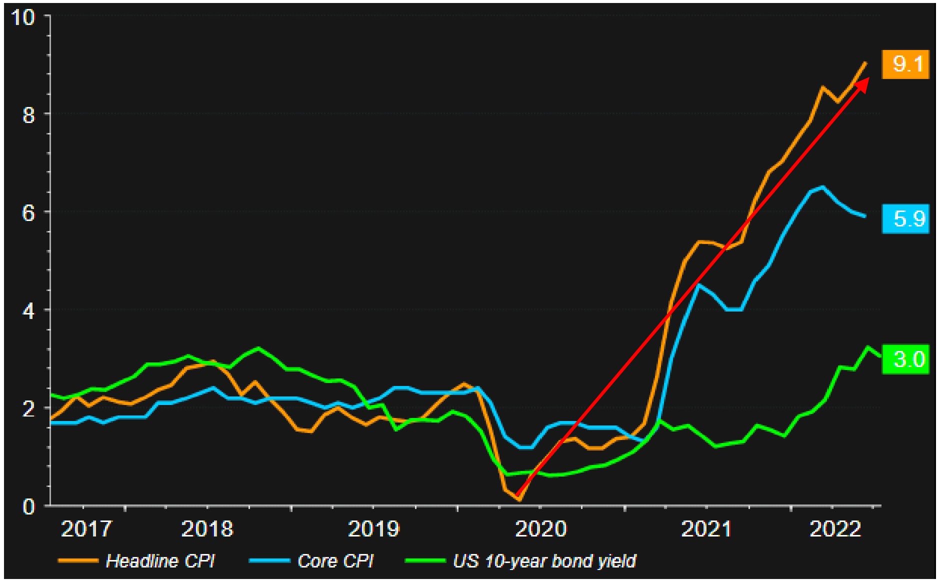
28th July 2022

US Fed Reserve raised interest rate by 75bps to 2.25%-2.5%, reinforced commitment to contain inflation

US' Fed Fund Target Rate, %



US' Inflation, Core Inflation, 10-Year Bond Yield, %



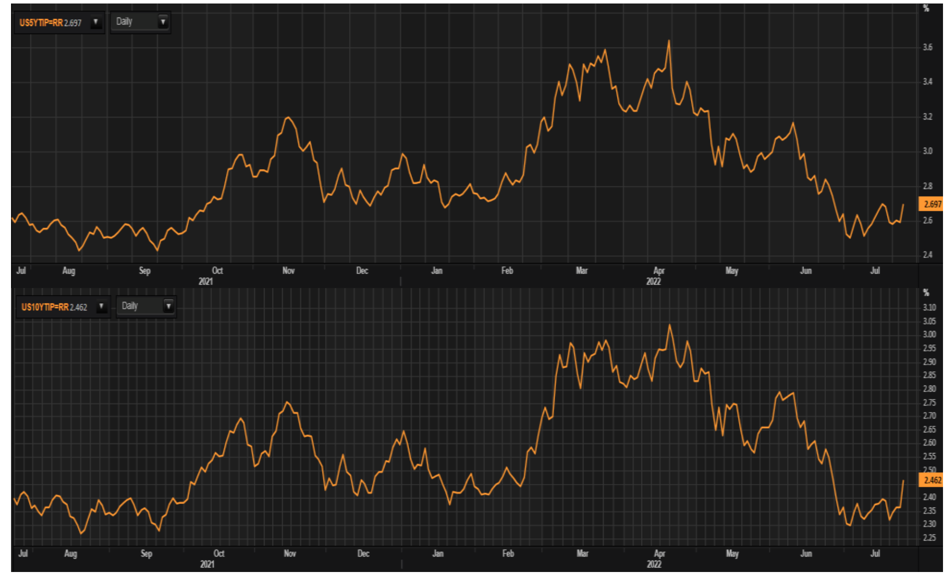
- ✓ As expected, the **US Fed Reserve raised its key interest rate a second consecutive time by 75bps to 2.25%-2.5%**, the highest since 2019, and **reinforced its commitment to contain inflation**.
- ✓ The *US Fed Chair acknowledged that the economy was slowing and would likely need to slow more for the Fed to brake the pace of price increases*.
- ✓ The policy rate is now at the level most Fed officials feel has a neutral economic impact. The policy rate also matches the high point of the central bank's previous tightening cycle from late-2015 to late-2018, a level reached this year in the span of just four months.
- ✓ Monetary policy decisions will be data-dependent. **Investors expect the Fed to raise its policy rate by at least 50bps at its 20-21 September meeting**.

Source: Reuters, Trading Economics

US Treasury yields eased, driven by flight to safety following concerns of US and Europe economic slowdown

2 and 10-Year Treasury Yield Spread, 1-Year Trend, as at 27th July

5 and 10-Year Treasury Inflation Protected Securities Breakeven Rate, %, as at 27th July



- ✓ US Treasury yields trended lower this week, driven by a flight to safety, on rising concerns about a US economic slowdown and the latest cuts in gas supply to Europe heightened concerns on energy supply volatility.
- ✓ The 2-year yield moved lower to 2.9776%, while the 10-year yield edged up to 2.7867%, post the interest rate hike.
- ✓ **The yield spread between 2- and 10-year Treasury notes has been inverted for more than two weeks and widened a bit further at -25.7bps, before easing to -19.1bps**. An inverted yield curve is seen as a recession signal when the short-end yield is higher than the long-end.
- ✓ The breakeven rate on five-year US Treasury Inflation-Protected Securities (TIPS) was at 2.679%. Meanwhile, the 10-year TIPS breakeven rate was at 2.444%. These indicate the market sees inflation averaging about 2.7% and 2.4% in the next 5 and 10 years respectively.

Source: Reuters, VC

US stocks gained as investors speculate the US Fed would slow the pace of interest rate hikes

S&P 500 Index, 1-Year Trend, 27th July

Dow Jones Industrial Average Index, 1-Year Trend, 27th July

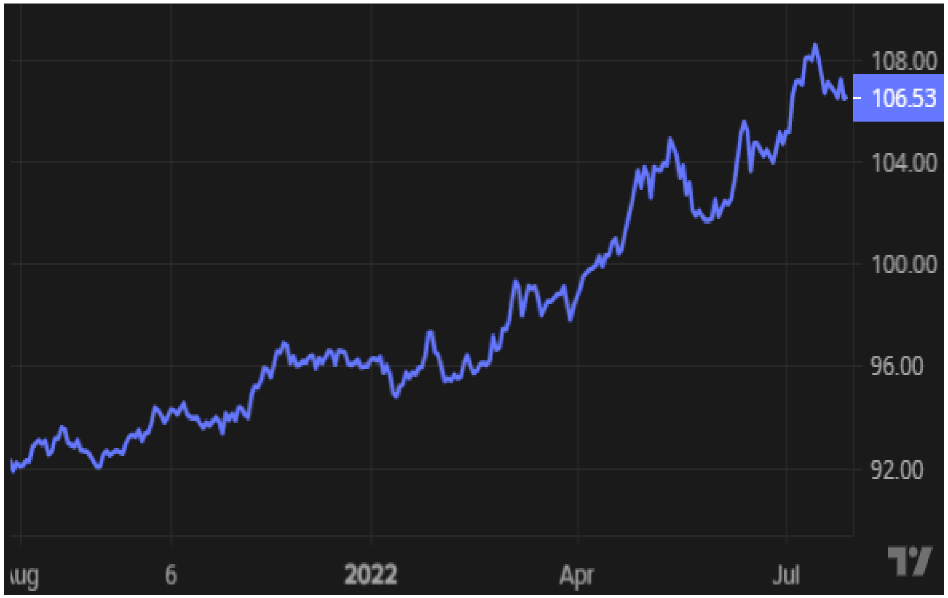
Nasdaq Composite Index, 1-Year Trend, 27th July

- ✓ US equities rose as investors speculate the US Fed would slow the pace of interest rate hikes for the rest of 2022.
- ✓ The S&P 500 gained 2.62% or 102.56 points to 4,023.61, while the Dow Jones Industrial Average rose 1.37% or 436.05 points to 32,197.59 and the Nasdaq Composite added 4.06% or 469.85 points to 12,032.42.
- ✓ The market was also boosted on Wednesday by quarterly updates from Microsoft Corp and Alphabet Inc that helped spark a relief rally in technology and growth shares as they boosted investor confidence in Big Tech's ability to navigate a recession.

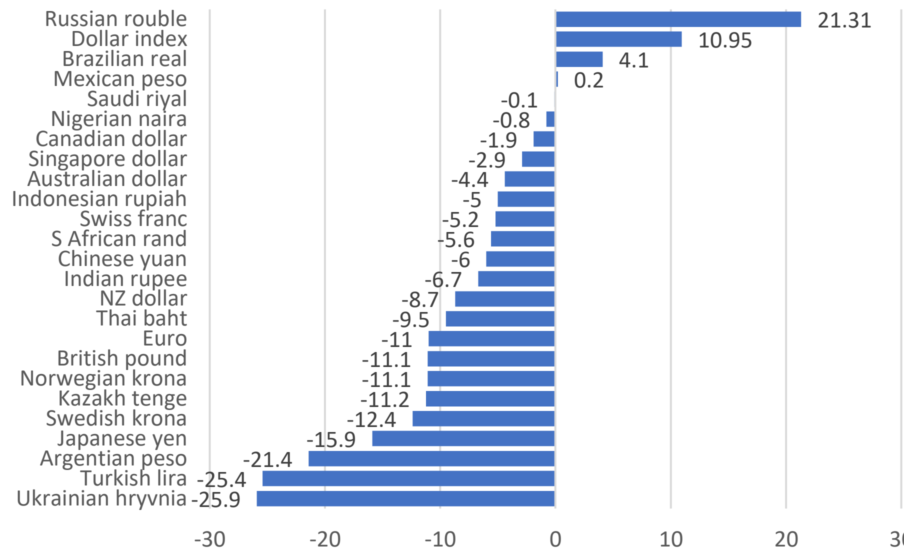
Source: Reuters

The dollar index has gained 10.95% YTD on US interest rate hikes, weak growth outlook in Europe and China and safe-haven flows

DXY (Dollar) Index, 1-Year Trend, as at 27th July



Global FX Performance YTD, as at 27th July

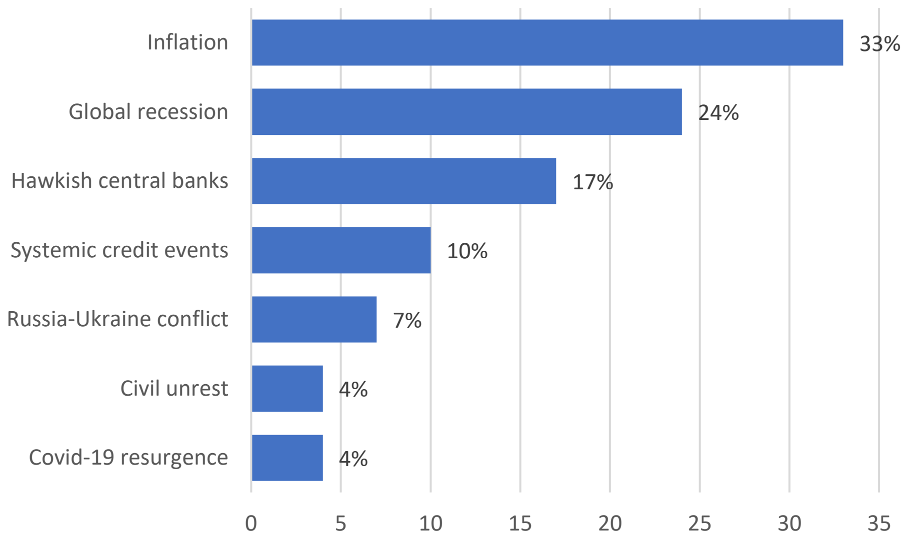


- ✓ The US dollar weakened 0.625% against a basket of major trading partners' currencies.
- ✓ The euro was up 0.79% to $1.0194. The Japanese yen strengthened 0.26% to 136.58/USD, while the British pound was up 1.06% to $1.2153/USD.
- ✓ The US dollar has strengthened his year due to a combination of rising US interest rates and weak growth outlook in Europe and China. The dollar pushed above parity on the euro for the first time in almost 20 years in mid-July, before easing back.
- ✓ **The US dollar bull run may not be over yet - the US Fed Reserve is expected to lift the its key rate by 50bps during September meeting, global growth is slowing and the downside risks are intensifying**.

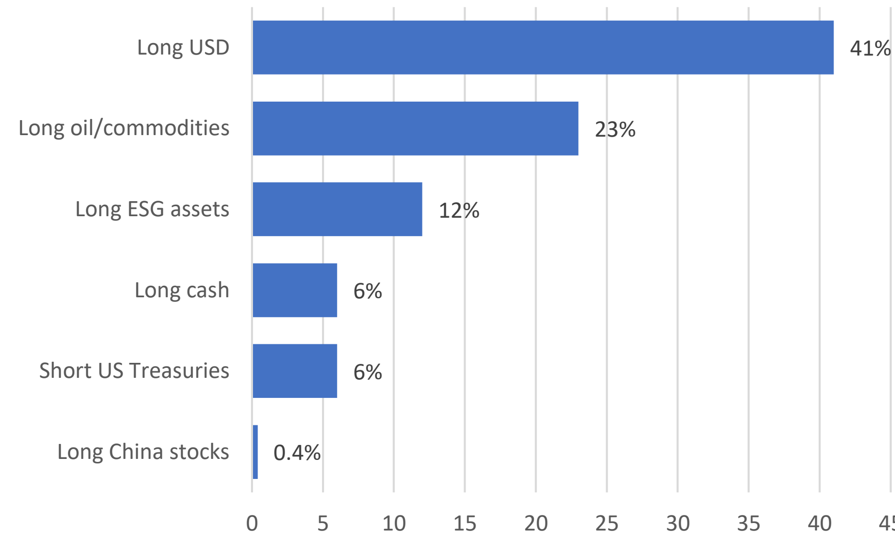
Source: Reuters, VC

BofA study: Investor sentiment in doldrums, growth optimism hits record low in July

What do you consider the biggest "tail risk"?



What do you consider the most crowded trade?



✓ The latest Bank of America monthly global fund manager survey shows *(i) investors have scaled back allocation to equities as pessimism reached alarming levels due to subdued economic outlook; (ii) while inflation was seen easing, investors' sentiment was still stagflationary, while recession expectations are at the highest since May 2020; (iii) expectations for global growth and profits are at all-time lows and cash levels are at the highest since the 9/11 attacks*.

✓ Fund managers view that **corporates should consider shoring up balance sheets and not increase capex or buybacks** as buffer against a downturn.

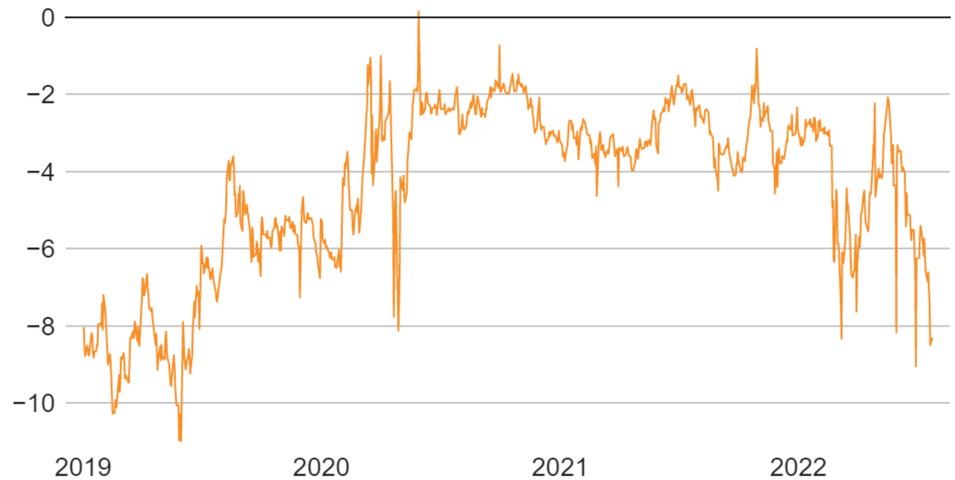
✓ Investors are taking lower than normal risk, with risk appetite below the level seen since the global financial crisis. **The most taken positions currently is to "long USD", followed by "long oil and commodities"**. Both trades have yielded good results YTD as USD strengthened against global currencies, while oil prices are high due to geopolitics.

Source: Bank of America's July global fund manager survey of 300 fund managers with combined AuM of USD800bln

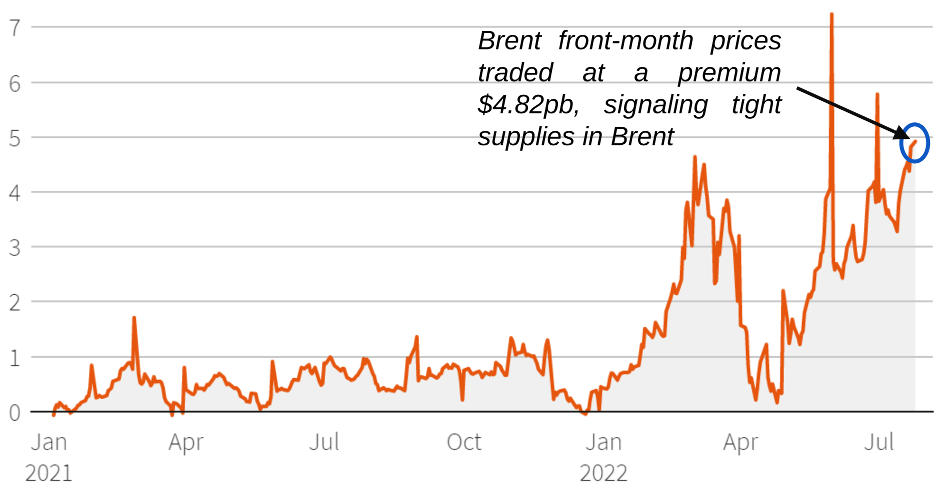
Global oil prices inched higher on Wednesday on US oil inventory drop

Brent Oil Price, YTD, as at 27th July

WTI Discount to Brent, in USD



Brent Crude Intermonth Spread, in USD

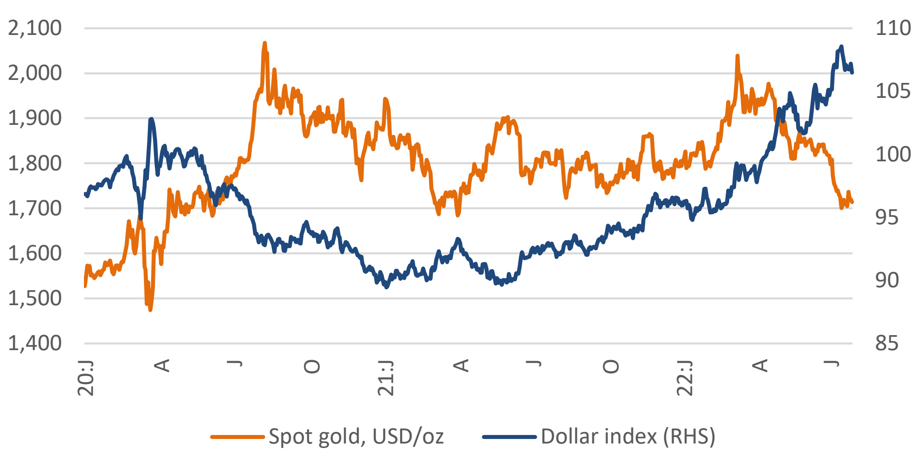


- ✓ Brent crude rose 2.1% of $2.22 to $106.62pb, while WTI gained 2.4% or $2.28 to $97.26pb.
- ✓ Brent and WTI spread widened further to $9.36, the widest since June 2019, as easing demand for gasoline weighs on US oil prices while supply concerns and Asia buying supported Brent prices.
- ✓ The US will release an additional 20mln barrels of oil from the Strategic Petroleum Reserve as part of an earlier plan to tap the SPR facility to stabilize global oil prices.

Source: Reuters

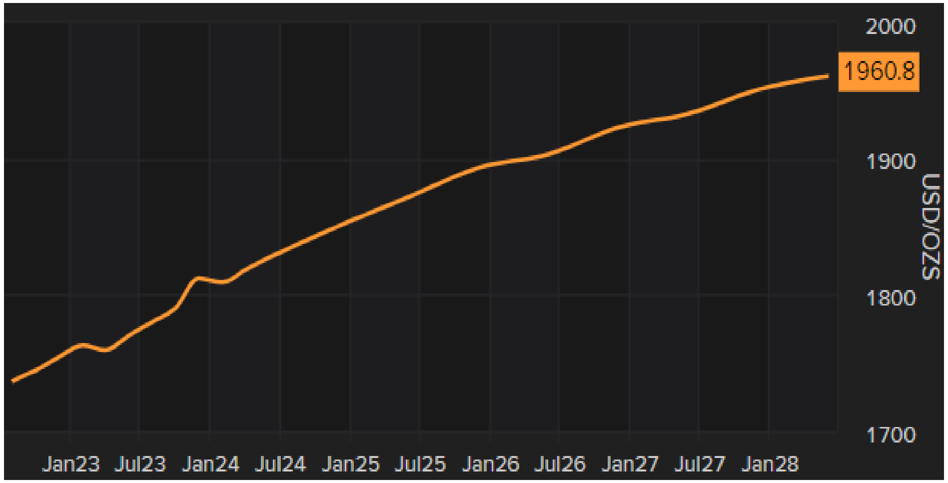
Spot gold rises as dollar and Treasury yields slip after the US Fed rate hike

Spot Gold vs. USD Index, as at 27th July



US Gold Futures, as at 27th July

Gold Price Forward Curve, as at 27th July

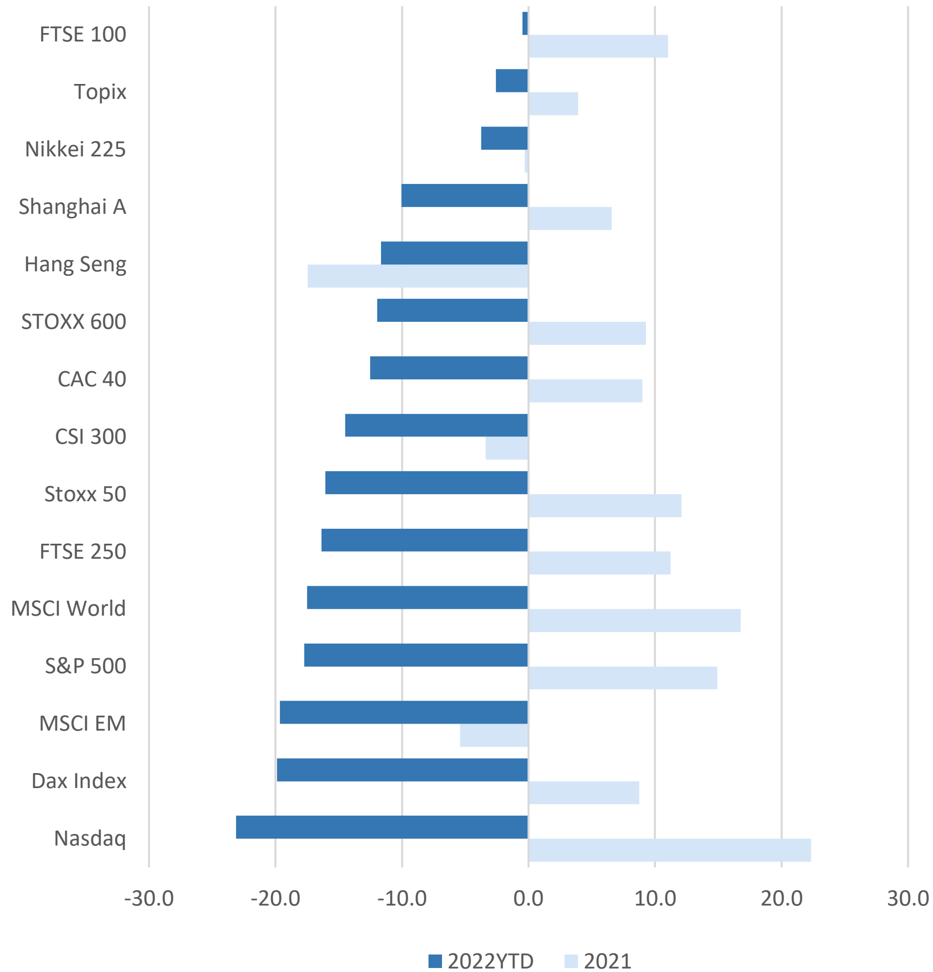


- ✓ Spot gold gained more than 1% as the USD and US Treasury yields retreated after the interest rate hike.
- ✓ Spot gold added 1.0% to $1,734.49 per ounce, while US gold futures were 0.1% higher at $1,719.1.
- ✓ Downside risk to gold price as the market continues to take its cue from the USD strength amidst a seasonally low demand period for gold as the market prices in rate hike expectations for September.
- ✓ Although gold is seen as an inflation hedge, higher US interest rates and bond yields hurt the appeal of bullion (it is a non-interest bearing asset).

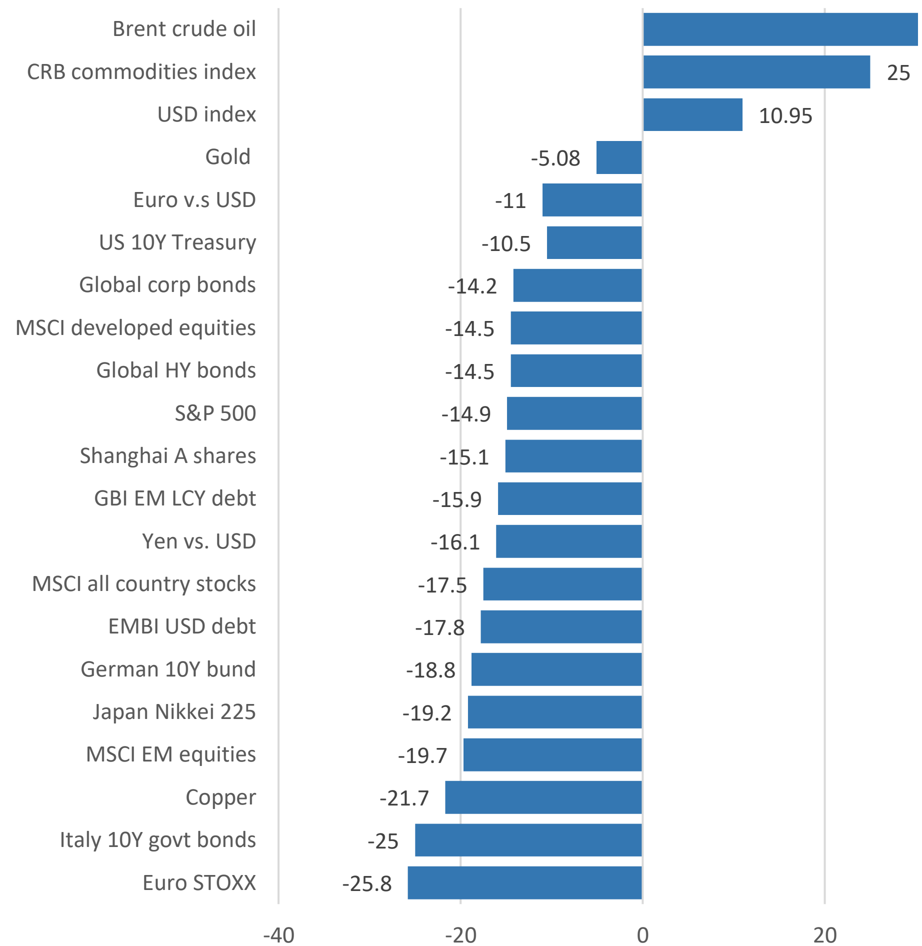
Source: Reuters, LBMA PM spot gold database, VC

Asian equities made cautious gains on Thursday as investors scented a possible slowdown in the pace of US rate hikes, easing USD and bond yields

Global Equities Performance, YTD % change, as at 27th July



Global Assets Performance, YTD % Change, as at 27th July



Source: Reuters, VC

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