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BONHÔTE

Fed pours cold water on markets

Overview

The long-awaited Jackson Hole Symposium event last week spooked markets, which summarily handed back part of their summer gains just as the Fed shot down any prospect that it will go easy in its rate-raising cycle. Markets are now pricing in a 0.75-percentage point increase in September.

In a speech lasting only 10 minutes (instead of the usual half hour), the Fed chairman voiced his determination to combat inflation even if this means endangering economic growth. Quoting former Fed chairs Paul Volcker and Alan Greenspan, Powell recalled that a central bank's duty was to ensure price stability. Hence a restrictive long-term monetary policy and consequently a period of low growth – complete with a weaker labour market – are now needed. He forewarned of “some pain” ahead.

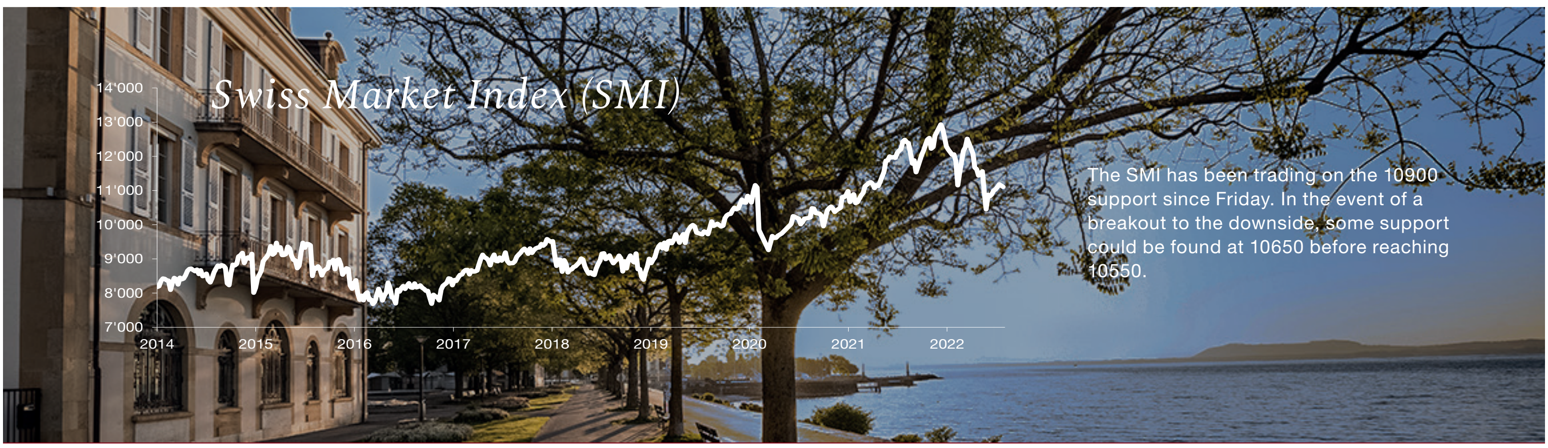
Markets now pricing in a 0.75-percentage point increase by the Fed in September

Since the release of July's inflation figures, which took a hiatus from their uptrend, markets had started anticipating more moderate behaviour from the Fed. This prospect is what led risk assets higher recently. On Friday, however, Powell's words put paid to such hopes. The reaction by markets was not long in coming, as no less than USD 1.25 trillion in market capitalisation went up in smoke – marking the largest daily decline since June. The S&P 500 gave up 3.4% while the tech-heavy Nasdaq, more sensitive to rate expectations, dropped by 3.94% (almost 500 points).

In bond markets, the reaction was much softer. Yields have continued increasing on higher interest rate expectations. The 10-year Treasury has risen more than 8 points to 3.1% but remains below its mid-June peak. Two-year paper is at 3.4%. The yield curve remains visibly inverted with a spread of 36 basis points between the two maturities.

Powell's words put paid to hopes, sending markets down sharply

In Europe, the outlook is slightly gloomier, with the energy crisis weighing heavily on the economic recovery. Several members of the ECB this weekend set out arguments for a steep rise in rates at the September meeting. Despite the hawkish noises, with some favouring 0.75%, the ECB must tread cautiously. Given the fragile state of the European economy, a 0.5% hike seems more realistic.



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	0.97	0.96	10'942.16	3'603.68	12'971.47	6'274.26	7'427.31	4'057.66	12'141.71	28'641.38	1'006.50
Trend	↑	→	↓	↓	↓	↓	→	↓	↓	→	→
YTD	5.91%	-7.20%	-15.02%	-16.16%	-18.34%	-12.29%	0.58%	-14.87%	-22.39%	-0.52%	-18.30%

(values from the Friday preceding publication)

Investment themes for the future

Tomorrow's world will be shaped by progress in areas such as climate science, artificial intelligence and population ageing, to name but a few. And the impact resulting from these themes will depend on how they interlink. Artificial intelligence cannot go mainstream without digitalisation. The climate transition depends on new, less energy-hungry modes of mobility coming to the fore, plus support from artificial intelligence – which will also be called on to make up for the shortage of human capital caused by population ageing. The current economic and geopolitical backdrop should be seen as an opportunity for encouraging investment in these fields.

Renewable energy sources are a perfect example. Until now, these have been cost-ineffective, but rising fossil fuel prices are enhancing their appeal from a financial standpoint. In Germany, if 50% of the building stock were modernised, 200 million tonnes of carbon emissions could be saved on each year, which incidentally represents 58% of Italy's annual emissions. Environmentally responsible buildings have a positive impact on the value of the structure and occupancy rates. The cost of maintenance is reduced and use of resources minimised. Over a 20-year period, savings can amount to 2-3 times the initial outlay.

Climate is not the only sector with attractive prospects. According to a study by PwC, the market for artificial intelligence could be worth more than the combined GDP of India and China by 2030. This market will also play a huge role in environmental transition through its use in climate physics and research aimed at optimising resource efficiency in production chains.

Investing in these themes means first of all seizing the opportunities that will emerge from the next roadblocks we will have to overcome. These funds will also help make our societies more sustainable. It makes sense to invest in a variety of themes to diversify exposure and minimise risk. Key for investors will be selecting those companies making strides ahead. Finding your way through this maze is not easy, which makes getting information and advice from experts all the more essential.

Auteurs et contact

Julien Stähli
Chief Investment Officer (CIO)
MBF Boston University

Pierre-François Donzé
M. Sc. in Economics

Karine Patron
MScF Université de Neuchâtel

Banque Bonhôte & Cie SA - 2, quai Ostervald, 2001 Neuchâtel / Switzerland - T. +41 32 722 10 00 / contact@bonhote.ch

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