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Monetary tightening policies still hitting markets

Overview

The markets last week continued the decline that began in the preceding week, in the wake of the Jackson Hole Symposium and the Fed Chairman's undeterred plans to continue monetary tightening to curb inflation.

The monthly employment report released in the US last Friday was a mixed bag, with unemployment rising to 3.7% and job creation slowing (but still strong). This news on jobs seems incapable of denting the upward trajectory in US monetary policy, although the rise in the participation rate is good news for the Fed as it could lead to a slowdown in wage growth, which would mean less inflationary pressure in that department.

Unemployment rate up and job creation slowing in the US

Last month the US economy added 315,000 jobs in the non-farm sector – slightly more than the 298,000 expected by the consensus but well below the 528,000 reported for July. The unemployment rate rose by 0.2 percentage points to 3.7% whereas no change had been expected. But wages did not soar month on month. They rose by 5.2% year on year.

The S&P 500 gave up 3.19% while the tech-heavy Nasdaq, which is more sensitive to interest rate expectations, shed 3.92%.

Bond yields edged up, with the US 10-year yield rising to 3.19%, while the short end of the curve eased slightly.

In Europe, persistent inflation and the energy crisis continued strongly impacting market sentiment and undermining the economic outlook. Germany has pledged EUR 65 billion to help households pay their energy bills, partly through a windfall tax on energy companies. Sweden is providing credit guarantees to Nordic electricity companies amounting to SEK 250 billion (USD 23 billion).

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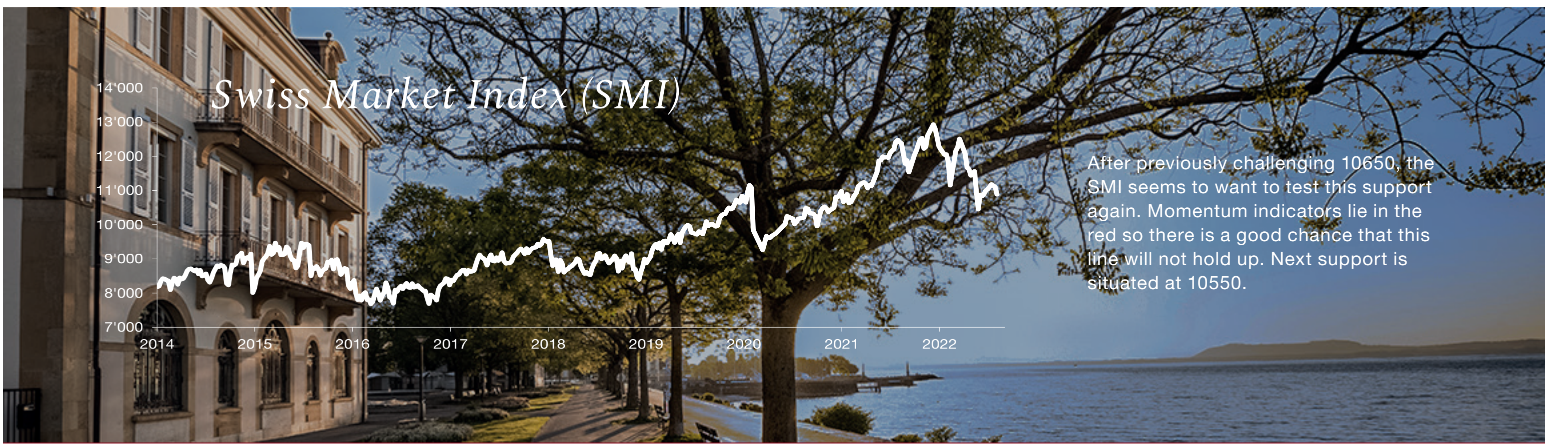
The ECB will announce its rate decision on Thursday. At this stage, an increase of 50 basis points seems most likely.



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	0.98	0.98	10'891.71	3'544.38	13'050.27	6'167.51	7'281.19	3'924.26	11'630.86	27'650.84	972.02
Trend	↑	→	↓	↓	↓	↓	↓	↓	↓	↓	↓
YTD	7.58%	-5.83%	-15.41%	-17.54%	-17.84%	-13.78%	-1.40%	-17.66%	-25.66%	-3.96%	-21.10%

(values from the Friday preceding publication)

Wall Street is not Main Street

It can be hard to keep a cool head when inflation is surging and a recession is looming on the horizon. Many newbie investors are simply choosing to dump their stocks while they wait for the economic outlook to recover.

Firstly, we should always bear in mind that the stockmarket tries to foresee events. Rising prices, a possible recession, geopolitical stress and the associated implications for energy supply: all these factors are here and now priced in by the market. As such, these will no longer influence share prices unless new information hitherto unbeknown to investors suddenly disrupts their trajectory.

Research abounds to demonstrate the predictive ability of financial markets on the real economy. Stocks fall before an economic downturn and rebound before the recovery. Exiting the market in anticipation of a recession potentially denies access to future opportunities, especially since history has shown that a recession does not necessarily mean a market decline, and vice versa. For example, in 2001, the markets continued to tumble for another year after the recession ended. In 2008, markets fell before the economic downturn took hold, responding to media coverage of the subprime crisis.

Consequently, identifying a correlation between shifts in financial markets and shifts in the real economy is a challenge. This is why, in times of uncertainty, sophisticated investors tend to retreat into the stocks of companies which they consider to be ‘high quality’. Such companies are all about efficiency in the performance of their business – in terms of governance, transparency of financial statements, and environmental risks. In this way, they minimise their own risks and are only partially affected by the systemic risks common to the entire market. It is often these companies that fare best in the long term.

At the moment, the best bet for investors is diversifying exposure across different sectors that are expected to grow significantly, as opposed simply to pulling one’s money from the market.

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