Opinion | 11 September 2020

Round and round and round she goes...

...where equities will stop, nobody knows...


wheel of fortune

Source: Shutterstock

A quick return to the red

I've got to say, I wasn't expecting to return to the red screens quite so soon as has happened. And I'm equally struggling to find clear drivers for a return to the market pattern we saw yesterday.

The big news of the day was the ECB meeting, which our Eurozone economists cover in detail in this note. Yes, there were some risks to trying to talk the Euro down, though Mme Lagarde seems to have erred on the side of caution here, and the initial response seemed to show markets disappointed with the perceived level of opposition to further Euro strength, though that did dissipate during the rest of the day, so no lasting damage done it seems.

Perhaps a more likely candidate for the sell-off was the US Senate vote on a Republican stimulus bill, estimated at around $500-$700bn, but the vote went along party lines, so failed to achieve enough votes to go to the floor. At this stage, it looks to me as if there is virtually no chance of a pre-election stimulus bill, and with supplemental unemployment benefits running out after their extension in August, it's easy to see why Democrats would be reluctant to hand a deal to President Trump. Both sides can play this to political advantage, so the polls will be the guide as to who is gaining the most from the political impasse.

And Brexit, which has been an unpleasant background noise all week, finally surfaced in FX space, with EURGBP pushing above 0.9240, with threats of potential legal action by the EU on the UK the catalyst for markets to start taking this seriously.

Day ahead

In G-7 space today, we have US inflation for August as the dominant release. The July figure surprised with its strength. The index rose 0.6%MoM, taking inflation to 1.6%YoY. While still well down on target levels, it was a decent jump and reflected the strength of the immediate post-lockdown recovery. The 0.2% MoM August recovery expected by the consensus of forecasters is a more modest affair and reflects the slowing in the rebound since July. If it happens this way, it will leave US inflation at 1.6%.

I think the market risk (not the risk to the outcome, which is 50:50 around the consensus forecast, but the risk-reward surrounding this release) is skewed towards a stronger inflation figure. With the Fed in "ignore inflation mode", anything which pushed the inflation rate above last month's rate could see US 10Y Treasury yields rise sharply, steepening the yield curve, and in raising the risk-free discount factor, push down on an equity market that seems more open to the idea of declines than it has been for some time.

It's a quiet day in Asia today - we may see Chinese monetary data released, or it may come out over the weekend or early next week.

Today's ASEAN releases are covered in our sister note, ASEAN Bytes.

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