# Weekly Market Summary

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**The 3 Buzzwords to Spice Up Your Weekly Notes … Inflection Point, Delta Variant and OPEC+ Split!**
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A buzzword is a word or expression from a particular subject area that becomes fashionable for a period of time after being used a lot, especially via the internet, television and in the newspapers; It is also referred to as a trendy or "*a la mode*" jargon! According to management professor Robert Kreitner, "*Buzzwords are the literary equivalent of Gresham's Law*", i.e. they usually drive out good ideas. However, at times, a convenient buzzword can become co-opted into general speech and lose its usefulness.

This week, markets have responded negatively to a set of somewhat disappointing figures on the economic & well-being front. With health reports continuing to point towards rising Covid infections globally, a rise in US initial jobless claims - coupled with a weaker-than-expected US Services Index (ISM Non-Manufacturing) and European Sentiment indicator (ZEW Survey) - prompted investors and hedge fund managers to offload some of their stock holdings and park proceeds in "*safe*" government securities. Global stock indices sold mildly whilst government bond markets staged a remarkable rally – with the benchmark 10-year yield trading down to its lowest level since February (a short-lived low print of 1.25% was recorded yesterday, at a time the Federal Reserve projects 2021 annual growth / inflation at 7.0% / 3.4% respectively!)

So what was the trigger for this latest market turnaround and should investors now refrain from taking on more risks? To answer that, the following 3 explanations or buzzwords come straight to mind:

- **Inflection Point**: Activity indicators from around the world have started signalling that the best part of the global recovery might be behind us. Whether recent signs of a looming global economic slowdown are just a temporary blip or the start of a new trend, investors are taking no chances; Their worry is that the slowdown comes at a time when global central bankers are discussing removing stimulus and therefore any potential policy mistake can trigger an unwarranted tightening of global financial conditions and therefore derail the risk rally, badly hurting risk-correlated assets (equities, credit, commodities and commodity currencies).

  *Our own assessment of the global economic outlook is much more favourable, given the current extremely easy financial conditions (depressed / "repressed" interest rates, high equity market levels, tight corporate bond spreads and weakish US Dollar). The world economy will continue to successfully re-emerge from the pandemic in coming months, whilst central banks' policy normalization will be slower and more synchronized than in the past! In that context, yesterday's release of US Consumer Credit data (which showed a record monthly rise of $35.3 billion) and Wednesday's publication of the latest Fed minutes (which confirmed that the abrupt shift in the Fed's tone at the June 16th FOMC meeting wasn't as "hawkish" as its economic projections and famous "dot plot" of interest rate expectations suggested) are clear indications that things are just fine and risk-on trading will soon resume.*

- **Delta Variant**: A coronavirus variant that was first found in India is now the dominant strain circulating in the US, according to the Centres for Disease Control and prevention (CDC). This highly contagious strain is responsible for more than half of the USA's new coronavirus infections as of early July and more than 75% of all cases in the UK since mid-May. The World Health Organization (WHO) has called the delta strain "*the most transmissible of the variants identified so far*." That means that each infected person is on average infecting more people, ensuring that the delta strain remains the dominant strain worldwide. Top Fed and ECB officials have warned in recent days that the spread of the Delta coronavirus variant and low vaccinations in some part of the word poses threat to the global recovery and would have negative ramifications on future growth in the US and elsewhere (as that results in new restrictions / lockdowns worldwide).

*Fortunately, vaccination appears to provide good protection against Delta – although one dose seems to offer less protection than it did against other variants. Additionally, there is still little data available with regards to whether the delta variant causes more deaths. According to a recent study by the PHE (Public Health England), 117 of the 92,056 people infected with the delta variant in the UK up to June 21st died. That means a fatality rate of 0.1%, which is very low in comparison with other variants (though experts are quick to point out that the low rate of deaths largely has to do with the fact that a large proportion of the UK population is now vaccinated).*

- **OPEC+ Split**: A simple misunderstanding, a general disagreement or a grave crisis? Last Friday, the OPEC+ alliance was thrown into disarray as a worsening divergence between Saudi Arabia and the United Arab Emirates blocked an oil supply increase. At stake is the ability of the producers' alliance to retain its hard-won control over the oil market and ensure the stability of the global economic recovery amid growing inflationary pressures. As a reminder, OPEC+ has already been adding some of the crude supplies it halted last year in the initial stages of the pandemic. The 23-nation collation added about 2 million barrels a day to the market from May to July and the question before oil ministers last Monday (a meeting that got eventually cancelled, sending Brent oil prices briefly above $77.00 for the first time in 2-1/2 years) was whether to keep adding supplies in the coming months. A disagreement over how to measure production cuts (the UAE wanting to raise its own production quota after investing billions in new capacity over the past 2 years) upended a tentative deal to boost monthly output by 400,000 barrels a day between August and December this year. The last time Saudi and UAE clashed over oil policy was in December 2020, when the UAE floated the idea of leaving the oil cartel. That dispute ended in truce, but the breakdown in negotiations this time around was so severe that the Group could not even agree on a day for its next meeting.

  *The Middle East's most meaningful alliance is currently being tested by frictions relating to Economics (or economic rivalry). However, it will survive because the two Gulf Arab countries have many common interests, especially in the spheres of geopolitics and security. For this week, oil prices have remained extremely volatile. A prolonged impasse may prevent OPEC+ from filling a looming large supply shortfall, at least in the near term. On the other side, traders are also weighing another option as time passes: That the dispute could ultimately fracture the coalition and usher in a new price war!*

The above being said, there are still considerable risks ahead and key among those is the threat that Covid-related containment measures would need to be extended over the coming few weeks/months, removing all optimism associated with a projected solid second-half 2021 economic recovery. Still, we view investors' recent concerns about the end of the reflation trade as too premature and firmly believe that short- to medium-term risk appetite indicators will remain stable whilst any upcoming declines in risky asset prices are likely to be limited and short lived given the flood of central banks' money.

The bond market has rallied sharply over the last three months because investors meaningfully lowered their collective expectation of the peak in the benchmark o/n Fed funds rate. This was due to a combination of factors, not the least of which is a high probability we are near an inflection point for growth and inflation. Fundamentally, we are not comfortable with current market expectations and expect the recent bond rally (fast drop in yields) to lose steam and reverse hard.

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