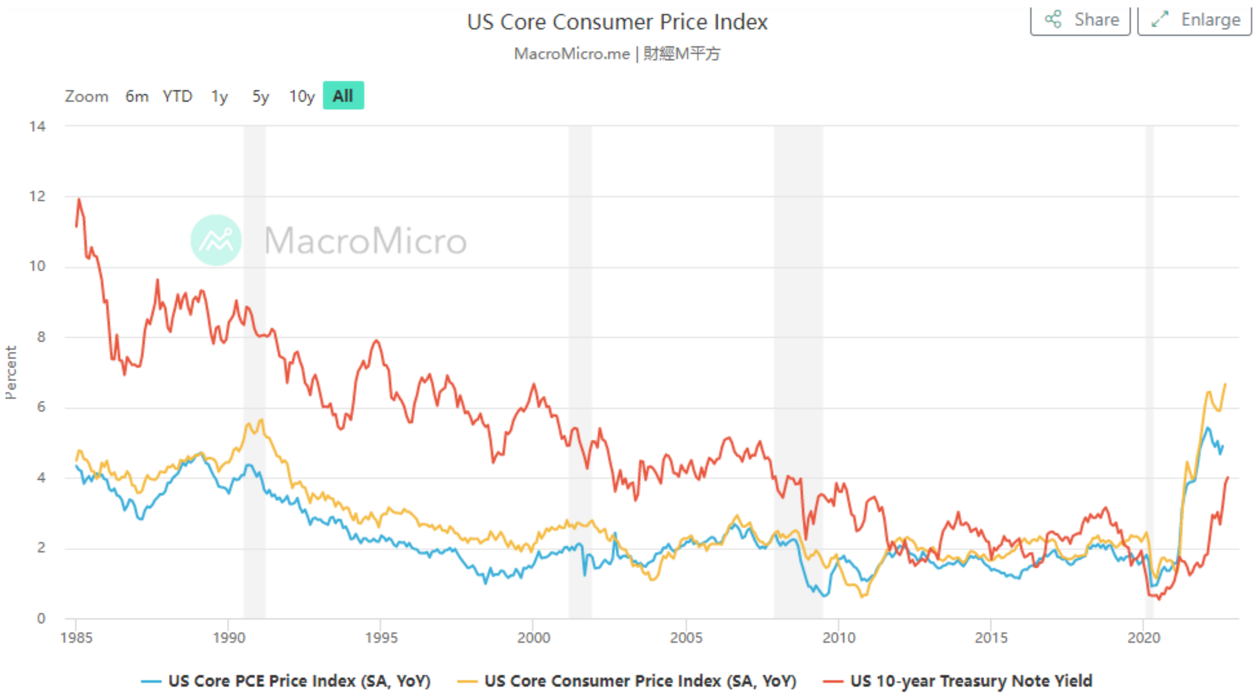
Market Comments 19 Oct 2022

The US CPI in September was higher than market expectations again, but the Dow jumped 2,000 pips, and crude oil and gold were weak.

Core CPI (monthly rate) in September announced last Thursday (13 October) rose 0.6%. In September, the consumer price index (CPI) rose by 0.4% (MoM), the September CPI (annual rate) increased by 6.6%, and the September CPI (seasonally adjusted) rose by 8.2%, all of which were higher than market expectations. Among them, the annual CPI also hit a new high in the past 40 years. The US Producer Price Index (PPI) (MoM) also rose 0.4% in September, beating expectations for a 0.2% rise. After the US inflation CPI data release, the market generally believes that the Federal Reserve will be in the interest rate meeting on 3 November to raise interest rates by 75 basis points and may be "on the board". The dollar rose briefly to a maximum of 113.70, driving non-US currencies to plunge in the short term. After the sharp decline in US stocks, the market reversed sharply soon after. The US dollar index fell to around 111.50, the lowest recently, with non-US currencies generally rising against the US dollar in varying degrees and US stocks soaring significantly. This is also in line with my discussion of the "pressure of dollar depreciation" mentioned in the previous article. At the same time, please note that this "period of devaluation of the dollar" may be limited in scope. As Europe is still subject to the "energy crisis" and geopolitical and military crisis following the "Russia-Ukraine war", the pressure to depreciate the euro, the largest counterparty currency to the dollar, remains. This may continue to limit the "devaluation" of the dollar.

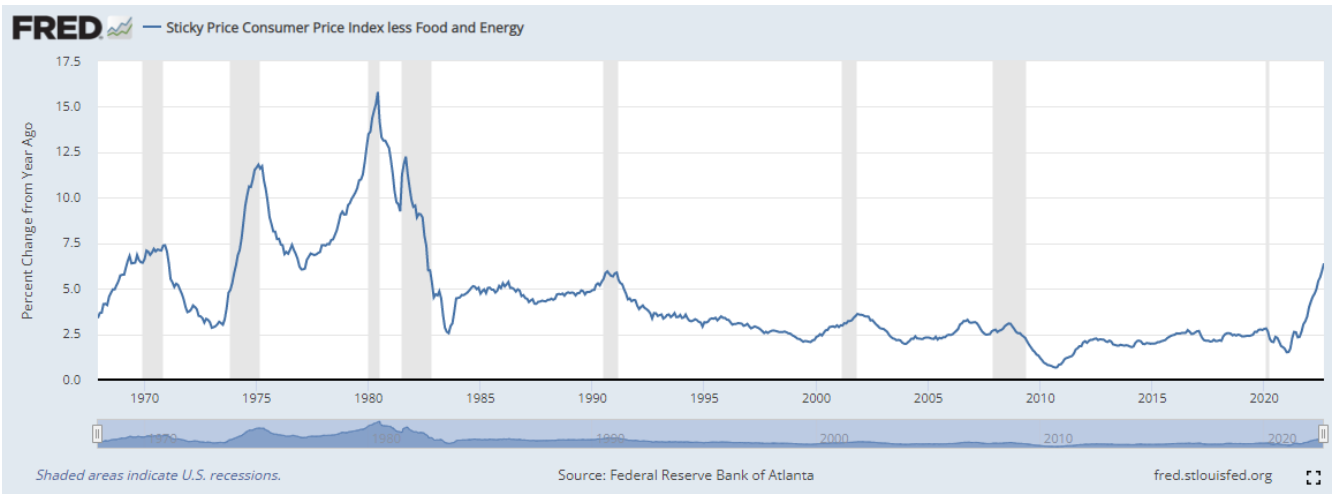
Among the many inflation data, the "monthly growth rate of core CPI" that investors focus on and the "monthly growth rate of sticky inflation CPI" announced by the Federal Reserve Bank of Atlanta remains high.

<u>The "monthly change of core CPI"</u> refers to the CPI data released each month by the US Department of Labor, excluding food and energy, two volatile components that are sensitive to natural disasters, oil prices and seasonal factors, and is an assessment of price changes in a range of goods and services that the average household may purchase. The monthly core CPI rate is a crucial indicator of inflation and the dollar's purchasing power. Also, please note that food and energy usually account for nearly 1/4 of the CPI.



Source: MacroMicro. The core consumer price index (Core CPI) can accurately express the current price level after deducting energy and food that are more sensitive to prices. The core Personal Consumption Expenditures Price Index (PCE) is the core consumer price index minus the rent factor, so it is more representative. The PCE price index represents inflationary pressures. The US 10Y Treasury yield tends to add in an inflation factor, so unless there is a deflationary situation, the US 10-year Treasury yield should be higher than inflation year-on-year. From the figure, we can also see that over the past 40 years (1980-2020), the yield on the US 10Y Treasury is basically higher than the core consumer price index (Core CPI) and the core Personal Consumption Expenditures Price Index (PCE). When the US 10Y Treasury yield is close to or even lower than the price level, a real negative interest rate situation occurs, revealing that bond yields are undervalued (i.e. bond prices are overvalued).

The "sticky inflation CPI monthly rate" is published monthly by the Federal Reserve Bank of Atlanta and is calculated to include a subset of goods and services that change in price relatively infrequently, such as rent, medical costs, etc. Once prices for these items have risen, it is difficult for them to fall. As the prices of these goods and services change relatively little, investors consider them to be a better indicator of future inflation expectations than items with more frequently changing prices. A sticky price can be explained as a cost incurred when a company changes its price. From the figure below, we can see that the current "sticky inflation" is very obvious, and the rise is apparent, so the US inflation is still high, and there is no "turning point".



Source: Federal Reserve Economic Data website. The current "sticky inflation" is very obvious, and the rise is apparent, so the US inflation is still high, and there is no "turning point".

After the US CPI data release, reflected in the financial and foreign exchange markets, the US 10Y Treasury yield note surged above 4.00%, hitting a high of 4.08%, and is now consolidating around 4.015%. The US 2Y Treasury yield, which is more sensitive to interest rates, immediately exceeded 4.5%, a new high since 2007, and is now hovering around 4.445%. The market's risk appetite has since emerged slightly, with the three major US stock indices, the Dow Jones, S&P 500 and Nasdaq, finally seeing a "phase" of bottoming out and rallying after three consecutive quarters of declines. Non-US currencies also finally took a "breather" and started to rise to varying degrees.

- *The Dow surged 2,200 pips (from 28600 to 30800), or 7.69%*
- *The S&P 500 rose 265 pips (from 3500 to 3765), or 7.57%*
- *The Nasdaq rose 950 pips (from 10430 to 11380), or 9.11%*
- *The US dollar index DXY fell 220 pips (from 113.70 to 111.50), or 1.94%*
- *EURUSD rose 220 pips (from 0.9630 to 0.9850), or 2.29%*
- *GBPUSD rose 490 pips (from 1.0920 to 1.1410), or 4.49%*

- *AUDUSD rose 170 pips (from 0.6170 to 0.6340), or 2.76%*
- *NZDUSD rose 225 pips (from 0.5500 to 0.5725), or 4.09%*
- *USDJPY rose 290 pips (from 146.40 to 149.30), or 1.98%*
- *USDCHF fell 155 pips (from 1.0070 to 0.9915), or 1.54%*
- *USDCAD fell 330 pips (from 1.3980 to 1.3650), or 2.36%*
- *USDCNH fluctuated in a narrow range between 7.2380 and 7.1580, or 1.11 %*

Non-US currencies against the Japanese yen, in the context of "the strength of the USDJPY", continued, and "the general rebound and rise of non-US currencies against the dollar" started a wave of rises, of which GBPJPY rose the most, rising by about 1,000 pips in a week or so (from 12 October to 18 October). If you add the rise in the GBPJPY since the BOJ intervened at the end of last month to "devalue the yen", that's a cumulative gain of around 2,100 pips (from 149.00 to 170.00), or 14.09%.

- *USDJPY rose 290 pips (from 146.40 to 149.30), or 1.98%*
- *GBPJPY jumped 1000 pips (from 160.00 to 170.00), or 6.25%*
- *EURJPY rose 600 pips (from 141.00 to 147.00), or 4.26%*
- *AUDJPY rose 370 pips (from 90.80 to 94.50), or 4.08%*
- *NZDJPY rose 470 pips (from 80.50 to 85.20), or 5.84%*
- *CADJPY rose 390 pips (from 105.00 to 108.90), or 3.71%*
- *CHFJPY rose 450 pips (from 145.50 to 150.00), or 3.09%*
- *SGDJPY rose 400 pips (from 101.00 to 105.00), or 3.96%*

At the same time, in the Asia-Pacific stock market, Bitcoin also started to rise to varying degrees in response to the fall of the US dollar.

- *CHINA50 rose 600 pips (from 12300 to 12900), or 4.88%*
- *CHINAH rose 330 pips (from 5450 to 5780), or 6.06%*
- *HK50 rose 910 pips (from 16120 to 17030), or 5.65%*
- *TWIX rose 28 pips (from 480 to 508), or 5.83%*
- *JP225 rose 1,470 pips (from 25850 to 27320), or 5.69%*
- *AUS200 rose 270 pips (from 6500 to 6770), or 4.15%*
- *Bitcoin rose 1830 pips (from 18100 to 19930), or 10.11%*

Crude oil and gold are weak, falling again or looking towards September lows or even lower.

This time, the slightly stronger market risk over the past few days failed to boost gold and crude oil. With high global inflation, central banks in most countries around the world implemented monetary tightening policies, and the outlook for global growth was bleak. Predictions from significant institutions, including the IMF that the world economy will fall into recession next year are "rife", and the price of crude oil and gold, which are linked to economic growth, continue to weaken and remain inclined to fall and consolidate at lower levels. In the early days of the "Russia-Ukraine war", gold also showed a "risk-averse attribute"; the highest price reached around US$ 2,050 per ounce. With the "Russia-Ukraine war" gradually falling into a stalemate, gold's safe-haven properties were crushed by the "safe-haven properties" of the stronger US dollar and continued to fall. It is currently trading sideways at around US$1,650 per ounce.

WTI's low around 26 September-27 September this year was around 76.50, which is where crude oil was earlier this year. Brent's low on 26 September-27 September this year was around 83.50, and the price at the beginning of the year was around 77.50. If crude oil continues to fall, WTI and Brent oil may first look at 76.50 and 83.50. At the same time, if gold falls again, it may fall below the low of around US$1,610 an ounce at the end of September this year.

- *WTI fell 780 pips (from 89.80 to 82.00), or 8.69%*
- *Brent oil fell 670 pips (from 95.90 to 89.20), or 6.99%*
- *XAUUSD fluctuated in a narrow range between 1 683.00-1640.00, or 2.62%.*

In addition, OPEC announced the decision to "cut production by 2 million barrels per day", which is expected to be implemented between November 2022 and the end of next year. This may make crude oil bullish in the short term. At the same time, it has recently been reported that the US Biden administration plans to release 10 million to 15 million barrels of oil from its Strategic Petroleum Reserve to balance the market needs. There was also a degree of "hedging" against the "OPEC" production cuts. At present, the market has not reacted much. Therefore, this round of crude oil decline directly reflects the market's concern that countries worldwide may fall into economic recession in at least the next 1-2 years. At the same time, the 20th National Congress of the Chinese Communist Party has clearly stated its commitment to "green development" and "energy revolution", i.e., to continue to promote "clean coal", "electric vehicles", etc., to "promote harmony with nature", to renew its commitment to reach peak carbon emissions by 2030, to achieve carbon neutrality by 2060, and to invest heavily in "renewable energy". Therefore, the author believes that in the medium and long term, the demand for crude oil may further weaken, and the price of crude oil may fall further.

Short-term risks:

Please pay attention to the release of China's Current Account data for September next Tuesday (24 October), as well as China's Q3 GDP (annual rate) and China's Q3 GDP (quarterly rate). GDP is the broadest measure of economic activity and an important indicator of the health of China's economy. At present, the market's expectations for China's Q3 GDP quarterly rate and Q3 GDP annual rate are 3.5% (previous -2.6%) and 3.4% (previous 0.4 %). Suppose the released data is significantly better than expected. In that case, it may be good for the RMB, and it also benefits the economic growth hopes of some economies that rely on the Chinese market. It is also important to keep an eye on the release of US Gross Domestic Product (GDP), 3rd Quarter 2022 (Advance Estimate) next Thursday evening (27 October), US September "Orders for non-defense capital goods excluding aircraft", and US September durable goods orders (monthly) data. The data will have a big impact on the dollar trend, and the overall trend of non-US currencies is subject to the dollar, so it also needs to be focused on. Meanwhile, USDJPY is approaching 150, a "key psychological level", so please pay attention to the Bank of Japan's interest rate resolution next Friday (28 October) and be wary that the BOJ may intervene again to depreciate the yen.

Sandy Wang,

11:10 am SGT time, 19 Oct 2022