The week in seven charts

Chart #3
The dollar as the only effective hedge against inflation

Read more on p2

Will the strength of the dollar continue to cause collateral damage?

FANGS still in bear market and 10-year U.S. Treasury bonds break the 4% threshold, as US inflation surprised once more. Each week, the Syz investment team takes you through the last seven days in seven charts.

Charles-Henry Monchau
Chief Investment Officer

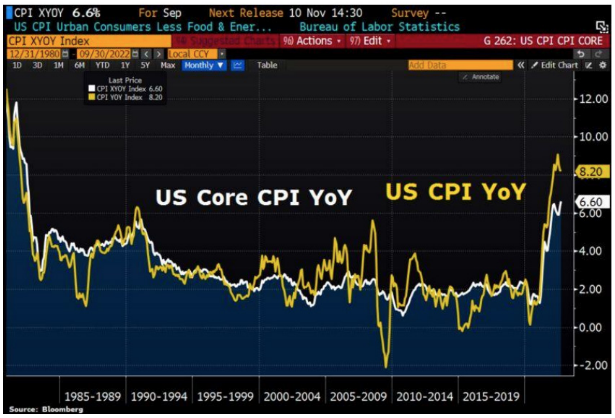
Chart #1 —

US inflation continues to surprise on the upside

It was the most anticipated number of the week: the US inflation figure for September. And once again, the price increase turned out to be higher than expected. The CPI index rose 8.2% year-over-year versus expectations of 8.1%. The CPI for core goods and services continues to accelerate to 6.6% y/y, its highest level since 1982, while housing costs are rising sharply. We note that while price increases for goods are slowing, price increases for services are accelerating.

From a macroeconomic perspective, inflation remains well above wage inflation, meaning that real wages continue to fall (and have done so for 18 consecutive months). This isbad news for consumer spending.

US CPI (y/y)



Source: Bloomberg

Chart #2 —

A dramatic market turnaround on Thursday

The release of the US inflation figures initially caused the stock and bond indices to fall. However, during the session we saw a dramatic recovery, with the S&P 500 rising 5.5% from the day's lows. This is the fifth reversal in market history in a single session. Among the factors explaining this sudden wave of buying, the positioning of hedge funds (very defensive and therefore "forced" to buy stocks in the event of a reversal) and record levels of protection (put options) that force market makers to cover themselves on the rise.

While some analysts interpreted this reversal as a sign that market lows may have been reached, the euphoria was short-lived as the S&P 500 lost 2.4% the next day following the release of the University of Michigan's opinion survey showing that households expect inflation to remain relatively high in the future.

For the week, the S&P 500 is down 1.5%. Since the beginning of the year, the US equity index is now down 24.8%. At this stage of the year, this is the 6th worst performance in history after 1931 (Great Depression), 2008 (subprime crisis), 1937 (year of recession), 2002 (bursting of the internet bubble) and 1974 (year of record inflation).

Note that international stocks, bonds, gold and oil all ended the week in the red.

Worst performance of the S&P 500 since 1928 after 198 trading days

Rank	Year	First 198 Trading Days	Day 199 to Year-End	Full Calendar Year	Next Calendar Year
1	1931	-34.2%	-19.6%	-47.1%	-14.8%
2	2008	-31.7%	-11.2%	-39.3%	23.5%
3	1937	-31.1%	-10.9%	-38.6%	24.5%
4	2002	-26.7%	4.6%	-23.4%	26.4%
5	1974	-25.4%	-5.7%	-29.7%	30.9%
6	2022	-24.8%	?	?	?
7	1962	-20.3%	10.6%	-11.8%	18.9%
8	2001	-19.1%	7.4%	-13.0%	-23.4%
9	1966	-16.7%	4.3%	-13.1%	20.1%
10	1930	-16.5%	-14.3%	-28.5%	-47.1%
11	1990	-16.4%	11.3%	-7.0%	25.7%
12	1946	-15.3%	4.0%	-11.9%	0.0%
13	1940	-15.1%	0.0%	-15.1%	-17.9%
14	1977	-13.0%	1.8%	-11.5%	1.1%
15	1957	-12.3%	-2.3%	-14.3%	37.4%

Source: Charlie Bilello

Chart #3 —

The dollar as the only effective hedge against inflation

While the vast majority of asset classes remain anchored in their bear market, the dollar continues to appreciate against other currencies. The euro and the pound are depreciating even further, while the dollar/yen is getting dangerously close to the psychological 150 mark, and the dollar/Swiss franc is back above parity. It is clear that the dollar is currently the only asset that is appreciating in this phase of rising inflation. It is the best performing asset in 2022.

Performance of different asset classes in dollars

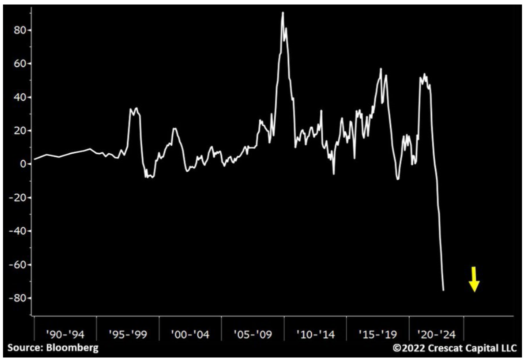
Source: MUFG

Chart #4 —

Will the strength of the dollar continue to cause collateral damage?

The strength of the dollar is causing dislocations in many financial markets. The collapse of the pound was partly due to factors endogenous to the situation in the United Kingdom. But the strength of the dollar has exacerbated the pound's fall. The stronger greenback makes energy prices even more expensive for oil and gas importing economies and contributes to inflationary pressures. But the dollar's strength (and the weakness of the yen) could challenge the peg in some countries. This risk is currently present in Hong Kong, where the central bank's foreign exchange reserves have just suffered the largest decline in their history. This collapse in reserves indicates that the peg is currently under severe pressure, forcing the central bank to deploy very significant resources to defend it. Will the peg withstand the attacks of speculators?

Annual changes in Hong Kong's foreign exchange reserves in billion HKD (year-on-year)



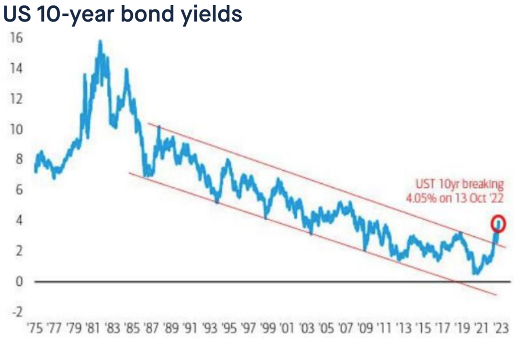
Source: Tavi Costa, Crescat Capital, Bloomberg

Chart #5 —

The end of a 30-year bull market?

Following the release of the inflation figures, the yield on 10-year U.S. Treasury bonds rose above the symbolic 4% threshold. As the chart below shows, this rise in yields could mean the end of a 30-year bull market for US bonds.

US 10-year bond yields



Source: BofA

Chart #6 —

FANG+ stocks remain in a bear market

The Nasdaq index once again underperformed the other US equity indices last week with a decline of -3.1%. Large cap technology stocks - and in particular the famous GAFAs - continue to correlate strongly with US bonds. Coincidentally or not, there is also a high correlation between the FANG+ index (GAFAs) and the size of the Swiss National Bank's balance sheet.

The SNB had accumulated these securities during the years when it was trying to counter the strength of the Swiss franc. Now, it is a matter of allowing the franc to appreciate, which prompts the SNB to sell assets denominated in foreign currencies, including the GAFAs accumulated on the balance sheet.

SNB balance sheet size (white) vs. FANG+ index (yellow)

Source: Bloomberg

Chart #7 —

Have Ark Invest ETF funds finally reached their lows?

A true icon of the "covid years" bull market, Cathie Wood was the first to enter the "bear market" as her Ark Invest funds peaked in the first part of 2021. Since these highs, the Ark Innovation ETF is down 78%. The trajectory of this fund seems to follow that of the Nasdaq between 1993 and 2003. If history repeats itself, the Ark Innovation fund could be near the lows. Before experiencing the same type of rebound as the Nasdaq from 2003.

Ark Innovation ETF (in white) and the Nasdaq index between 1993 and 2003 (in blue)

Source: Bloomberg, HolgerZ

For further information

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