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# Market Review

Global Market Strategy @ Natixis Investment Managers Solutions

## Economic & Political News

Economic data continued to come in strong in July, supported by steady progress in the vaccine rollout and the easing of mobility restrictions. The US economy expanded at an annualized rate of 6.5% in the second quarter and the labour market added 850,000 jobs in June (the largest gain since last August). This rebound in activity led the US CPI to surprise on the upside for its third consecutive month in June, headline inflation came in at 5.4% YoY (vs. 4.9% expected) and core inflation at 4.5% YoY (vs. 4% expected). However, although specific factors such as tourism and car rentals remained behind the increase, there were also signs that inflationary pressures were broadening. But the spread of the Delta variant has somewhat shifted fears from inflation to growth, slightly weakening sentiment. The Euro Area continued gathering pace in July as suggested by its services PMI, which pointed to the steepest expansion in 15 years. In addition, the Area's economy grew more than expected (+2% non-annualized) in the three months through to the end of June, marking a comeback after two straight quarters of contraction.

The Federal Reserve's (FED) recognition that "the economy has made progress toward" the bank's goals was viewed as paving the way for the future tapering of monthly asset purchases. However, during his remarks, Powell underscored that the committee's marker of "substantial further progress" has not yet been reached. Moreover, because of its strategic review, the European Central Bank (ECB) adjusted its inflation aim to a more symmetric 2% target (versus the previous target of "below, but close to 2%"), while housing costs will also begin to be considered in future calculations.

Progress was made on the bipartisan infrastructure bill towards the end of July, but a partisan bill via budget reconciliation remains an option, though its size will likely be compromised given opposition from more centrist Democrats. In addition, the debt ceiling became operative again after a two-year suspension, placing pressure on the Democrats to outline a plan to either increase the limit or suspend it again; the US is currently on a path to default as early as October or November. Furthermore, the European Union (EU) set its 55% emission reduction target for 2030, which includes plans to introduce a Carbon Border Adjustment Mechanism (CBAM) that has created tensions with trading partners across the globe.

## Equities

Despite the highest inflation prints in decades, equity markets continued to grind higher, supported by the decline in long-term rates. Growth stocks benefited the most from the decline in yields and outperformed cyclical stocks for their second month in a row. In addition, with over 50% of the S&P500 companies having reported earnings by the end of July, almost 90% of them have beaten expectations. At the same time, of the 59% of the STOXX600 companies reporting, 67% of them have exceeded expectations.

On a regional basis, developed markets outperformed emerging ones, returning +1.8% and -6.7%, respectively. Within developed markets, the S&P500 (+2.4%) outperformed both the STOXX600 (+2%) and the FTSE 100 (+0.5%) thanks to growth stocks' performance. Indeed, the Russell 1000 Growth returned +3.3% and the Nasdaq 100, +2.8%. Moreover, July was another bullish month for European equity markets, logging a sixth consecutive monthly gain. The CAC 40 increased 1.4%, followed by the FTSE MIB and the DAX, which increased 1.6% and 0.1%, respectively. The IBEX35, on the other hand, declined 1.1% amid rising Covid cases, which led authorities to tighten leisure restrictions. The best performing developed markets' sectors were Health Care (+3.8%), Real Estate (+3.7%) and Information Technology (+3.6%). The worst performing sectors were Energy (-6.2%), Consumer Discretionary (-0.3%) and Finance (-0.1%).

## Fixed Income

Government bond yields continued to fall across the board in July. The US 10-year yield dropped 25bp, placing it 57bp off its March's peak (it closed the month at ~1.22%), which typically implies rising concerns regarding growth; the US 2y10y spread continued to tighten (-18 bp to 104bp). However, some analysts have pointed to the US Treasury decision to use some of its cash holdings instead of issuing debt (while the FED kept purchasing at an elevated pace) as a large driver of July's yields decline.

Moreover, core European yields followed its American counterpart: the 10-year German Bund yield declined 25bp to -0.46% and its 2y10y spread tightened 16bp to 30bp. In addition, OATs fell 23bp to -0.1%, BTPs 20bp to 0.62% and Gilts 15bp to 0.57%. Lastly, corporate debt spreads also declined: US IG and HY tightened 5bp and 26bp, respectively; EU IG and HY tightened 1bp and 14bp; and EM IG and HY tightened 28bp and 49bp.

## Emerging Markets

The MSCI Emerging markets fell by 6.7% in July, significantly underperforming the MSCI World (+1.8%), as Chinese authorities continue to increase the scrutiny applied to the technology sector. In addition, at the end of the month, the Chinese Communist Party announced new rules barring for-profit tutoring in core (compulsory) schools (a USD 120 billion sector) in order to ease financial pressures on families, triggering volatility in the largest equity market in Asia.

At the index level, the best performing emerging market (in USD terms) was India (+0.9%), followed by Taiwan (-2.2%) and South Korea (+5.7%). From a regional perspective (in USD terms), emerging Europe led, increasing 0.2%, while emerging Latam and Asia returned -4.1% and -8.1%, respectively.

## FX & Commodities

The DXY index, which measures the US dollar against a currency basket, stayed relatively quiet throughout the month, falling 0.28% to 92.2 and finding some support since the June FED meeting. The US dollar weakened against every major currency. It lost 0.1% to 1.19 against EUR, 0.5% to 1.39 against GBP, 2.1% to 0.9 against CHF, 1.3% to 109.7 against JPY. Conversely, it strengthened against AUD (+2%) and remained stable against CNY (at 6.4 CNY per USD).

Gold prices increased 2.4% to USD1,814 per ounce in July, supported by progress in vaccination campaigns in emerging markets, especially in India, as well as by persistent inflation concerns and volatility across cryptos. Oil prices posted another positive month as the summer break boosted demand. In addition, while OPEC+ failed to reach an agreement on production increases at its early July meeting, members did finally agree on how to unwind the output cuts during the month. Thus, OPEC's production rose 610 thousand barrels per day in July to levels not seen since April 2020 when the production cuts were established. However, this increase in supply was offset by a strong recovery in demand, which led the WTI to increase 0.7% to USD 74 per barrel and the Brent to rise 1.6% to USD 76.3 per barrel.