



BANQUE
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1. EDITORIAL

SUMMER VOLMAGEDDON

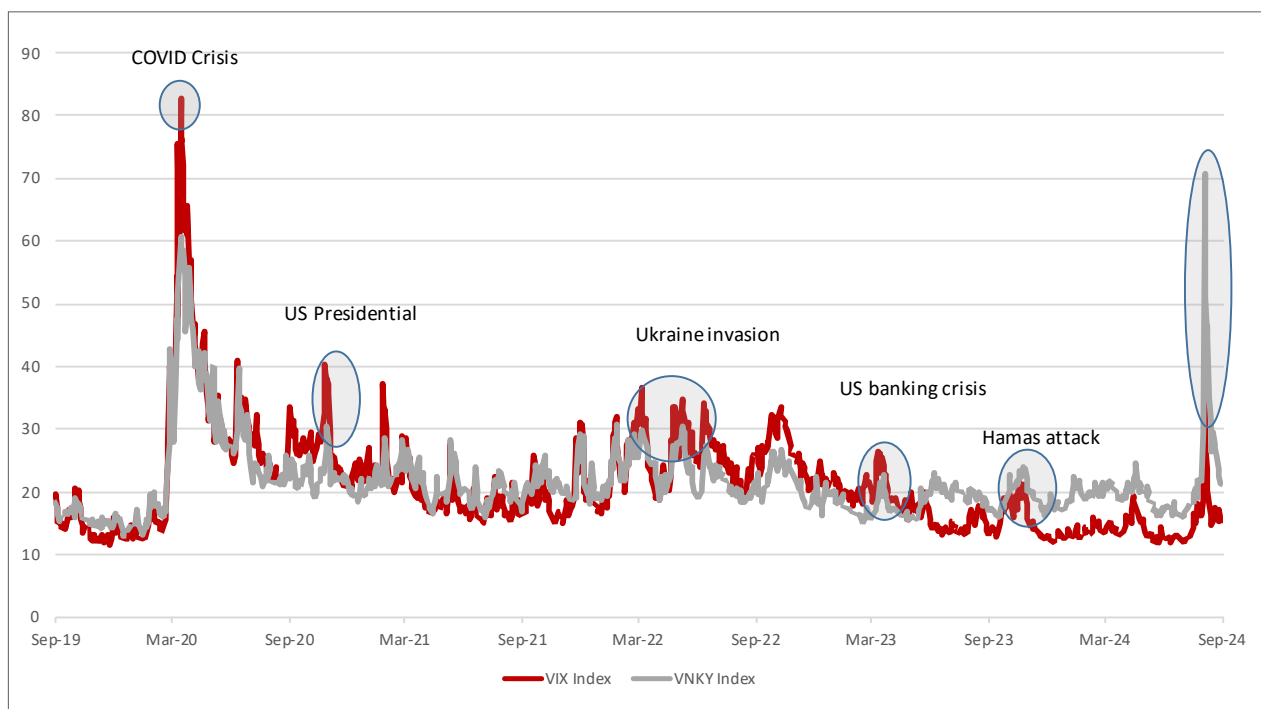
August has now ended with the US markets at their highest levels ever after a circa 2% rise for the month, US inflation figures published in mid-August are back below 3%, the September rate cut now seems to be on track, and Jerome Powell's Jackson Hall symposium reassured the last worriers. For someone who left on holiday at the end of July without worrying about stock market news, August was an uneventful and fairly good month.

A colleague, who left on holiday a week later, experienced a different story and will not remember this summer month as a leisurely stroll down memory lane. In early August, markets reacted with un-

precedented violence: the Nikkei lost 12% in a single session, and in the hours that followed - on Monday August 5 - the VIX index measuring the S&P500 implied volatility soared above 50 before ending at 38. The graph below puts this exceptional figure into context: the level of stress reached on August 5th was far higher than in any recent crisis in the US, and the VNKY Index - the Nikkei225 implied volatility - reached the COVID crisis highs. Today, the VIX index is at 17 and everything seems to be back to normal, which leaves us with two unanswered questions:

- What justified such a panic?
- Can we be sure that the fears of the beginning of the month are now a thing of the past?

G1 : VIX – S&P500 IMPLIED VOLATILITY & VNKY – NIKKEI225 IMPLIED VOLATILITY



Source: Bloomberg, Banque Eric Sturdza

The first question concerns the past, and will be easier to answer... This violent market stress was the result of a combination of three factors:

- Poor employment figures in the US, raising fears of an imminent recession
- Uncertainty about the trajectory of inflation.
- More technically (but not without effect, as shown by the Nikkei session mentioned above!), the sharp JPY appreciation led to some very sudden carry trade* unwinding.

A single one of these three uncertainties would not have triggered such a market reaction, but their concomitance led to this extreme and rare scenario. Before looking ahead, we need to look back at the days that followed the shock session of August 5. As shown in a study by Longview Economics of London, which examined the major Standard and Poor's selloffs, such downward accelerations are generally followed by other edgy sessions and retesting of the lows (in 13 out of 15 cases, for those who like statistics!). None of this happened in early August, and within 5 sessions, the VIX had returned to a value close to its long-term average (below 20), calm had returned.

The unwinding of leveraged positions on the yen was swift, and however costly it may have been, there was nothing systemic about it. Understandably, the effects were short-lived.

On inflation fears, we had to be a little more patient, but as mentioned in the introduction, mid-August data was good and confirmed the observed return to stability.

Of the 3 causes of the downward movement at the beginning of August, we still have to deal with unemployment, and to do this we need to say a word about the Sahm rule.

Claudia Sahm, an American economist who worked for the FED, observed that when the 3-month moving average unemployment rate rises by more than 50 basis points from its lowest levels for the year, the economy enters a recession. This type of acceleration in the unemployment rate occurred during the second quarter, helping to trigger the violent downturn at the beginning of the month. Will Sahm's rule apply once again? If so, the US economy will finally enter recession. The question is no more clear-cut at the end of August than it was at the beginning.

Claudia Sahm herself insisted on one point: "The Sahm rule is an empirical regularity. It's not a proposition; it's not a law of nature." In other words, statistical rules about the past can always be broken... Especially when so obviously highlighted by the FED!

Of the three alerts at the beginning of the month, two are surely behind us, the one concerning unemployment should keep us busy a little longer.

** Carry trade: borrow in a low-rate currency to buy higher-yielding assets. A pleasant operation unless the low-rate currency (the yen in this case) rises violently.*

2. FIXED INCOME

THE FEDERAL RESERVE CLEARLY BEHIND THE CURVE

“Data dependent”,
yes, but which ones?

The Fed completely underestimated the lag effect of its past rate hikes. This lag effect comes at the worst possible time, when the US economy is beginning to show worrying signs of slowing down. By proclaiming themselves “data dependent” but remaining obsessed with inflation figures to the detriment of others, they forgot that they had a dual mandate. They realized too late, when they noticed that their analysis had been distorted by inaccurate employment data published between April 2023 and March 2024. After correcting for a discrepancy of 818,000 jobs created over this period, the employment situation is not quite as bright as everyone thought. The mediocre Non-Farm Payrolls on Friday August 2 were enough to wake up the pundits who swore by a soft landing scenario just two months ago, and who are now telling us that the Fed will cut rates by 50bp twice before the end of the year. In the end, the bond markets were wrong in November-December 2023, because in the markets, to be right too soon is to be wrong. The five to six rate cuts anticipated at the end of last year will finally materialize in late 2024 and 2025.

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A FOMC encore at Jackson Hole

Jerome Powell was forced to deliver a dovish message at Jackson Hole in order to stabilize the markets and give some visibility to his monetary policy. Against this backdrop, logically US yields – especially long rates, which caused us so much pain from January to April – should return to their December 2023 levels. What should we do in such circumstances? Take a substantial part of your profits on the long end of the curve, if you had the wisdom (and bravery in April) to hold on to them. The US curve is in full bullish steepening mode, and that’s perfectly normal. Two things are clear: firstly, this steepening is not taking place at the expense of the long end of the curve. So duration was needed to make money. Indeed, it is perhaps worth remembering that in a steepening movement, even a violent one, as long as long rates are falling slightly, that’s where you need to be. Either to boost the performance of a bond portfolio, or to replay the role of natural hedge to equities in a diversified portfolio. In the credit market, it makes sense at some point to roll duration (selling short-maturity debt of a corporate issuer to reinvest in longer maturities of the same issuer) in high-beta credits and hybrids in particular, when the equity markets are close to their low point. Identifying this low point is the challenge we face over the coming weeks.

3. EQUITIES

“BUTTERFLY EFFECT” IN THE LAND OF THE RISING SUN

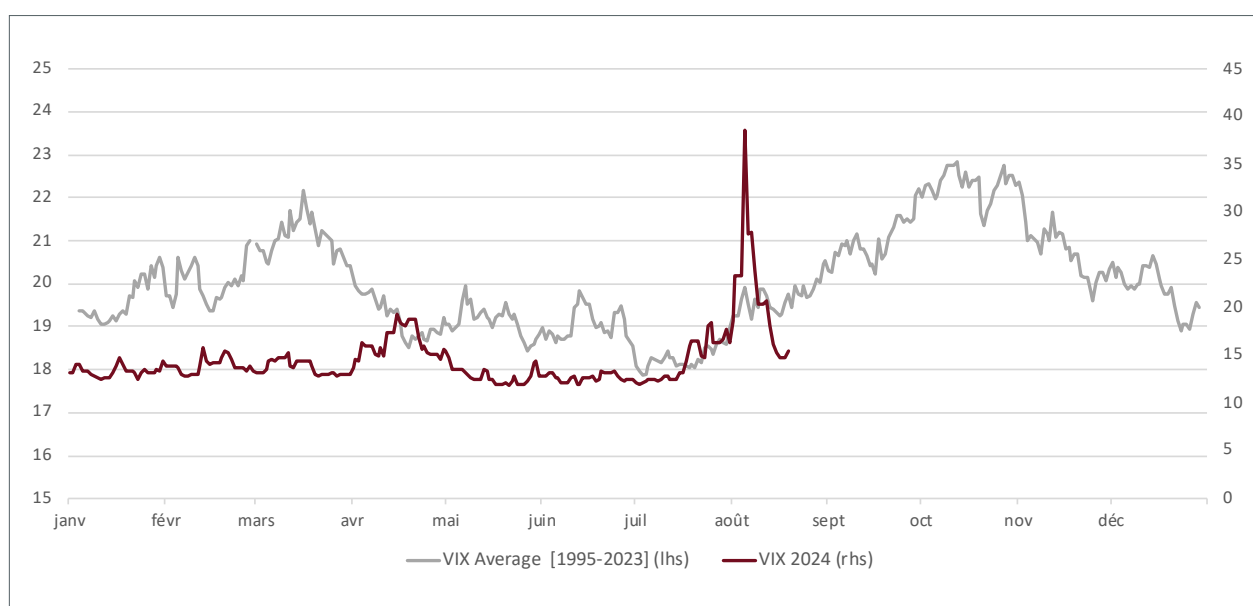
August was marked by an unusual spike in volatility in a traditionally quiet period. Although volatility historically tends to rise from August to November, global equity markets experienced a turbulent period, with a sharp correction in indices, exacerbated by low summer volumes.

In hindsight, the market crash can be traced to a number of factors and decisions. At the end of July, the Bank of Japan (BOJ) surprised markets with a 1st rate hike from 0.1% to 0.25%, triggering a 4% appreciation in the yen and subsequently a 20% drop of the Nikkei 225 index. This led to the unwinding of the infamous “carry trade” operations, where investors borrow in JPY to benefit from low interest rates and then invest in USD or EUR equities and bonds, often leaving the currency risk unhedged.

US and European indices fell in a ripple effect as the unwinding led investors to liquidate some positions and selling pressure was also amplified in thinly-traded markets. The S&P 500 lost 6% in two days, and the Nasdaq tumbled nearly 8% over the same period.

The VIX index, often referred to as the “fear gauge”, which measures the implied volatility of the S&P 500, rose from 16% to 50%. These levels were consistent with the ones reached at the worst point of the Covid crisis in March 2020. This move was also amplified by the general macro context. A day after the BOJ meeting, the release of disappointing US macro-economic data put more fuel on the fire and the panic movement. Indeed, the release of a lower-than-expected ISM manufacturing index and an upward sloping US unemployment rate led investors to reassess recession prospects.

G2: VIX INDEX VS. ITS ROLLING YEARLY AVERAGE



Source: Bloomberg, Banque Eric Sturdza

Fortunately, the situation normalized, and equities proved once again resilient. The S&P500 recovered 8% intra-month and closed higher than its end-July level, the Nasdaq also recovered but failed short of fully recovering its monthly losses. Far more impressively, the Nikkei 225 ended the month on similar levels to those reached 30 days ago.

Despite analysts' high expectations and fears of a worsening economic outlook, the earnings season looked reassuring enough at least for investors. In aggregate, companies reported better-than-expected results, bolstered by a resilient US and global economy. While results were deemed good enough to bring some relief, short-term uncertainties continue to prevail both on economic and political fronts, notably with the undecided upcoming US election, whose results could be the catalyst for further sector rotations.

5. PERFORMANCE

EQUITIES	30.08.2024	CURRENT	1 M	3M	6M	YTD	2023	2022	2021	2020	2019
MSCI WORLD	MSCI WORLD	3 661	2,5%	6,3%	9,7%	15,5%	24,4%	-17,7%	22,4%	16,5%	28,4%
	MSCI WORLD GROWTH	5 458	2,4%	6,2%	9,5%	18,4%	37,3%	-29,0%	21,4%	34,2%	34,2%
	MSCI WORLD VALUE	3 796	2,6%	6,3%	10,0%	12,6%	12,4%	-5,8%	22,8%	-0,3%	22,8%
WORLD & US	DOW JONES	41 563	1,8%	7,4%	6,6%	10,3%	16,2%	-6,9%	20,9%	9,7%	25,3%
	S&P 500	5 648	2,3%	7,0%	10,8%	18,4%	26,3%	-18,1%	28,7%	18,4%	31,5%
	S&P500 EW	7 116	2,3%	6,1%	7,9%	11,1%	13,8%	-11,5%	29,6%	12,8%	29,2%
	NASDAQ 100	19 575	1,1%	5,6%	8,5%	16,3%	55,1%	-32,4%	27,5%	48,9%	39,5%
	RUSSELL 2000	2 218	-1,6%	7,1%	7,9%	9,4%	16,9%	-20,5%	14,8%	19,9%	25,5%
	STOXX 600	525	1,3%	1,3%	6,2%	9,6%	16,6%	-9,9%	25,8%	-1,4%	27,9%
EUROPE	FTSE 100	8 377	0,1%	1,2%	9,8%	8,3%	7,7%	4,6%	18,4%	-11,4%	17,2%
	CAC 40	7 631	1,3%	-4,5%	-3,7%	1,2%	20,1%	-6,7%	31,9%	-5,0%	30,5%
	DAX	18 907	2,2%	2,2%	7,0%	12,9%	20,3%	-12,3%	15,8%	3,5%	25,5%
	IBEX 35	11 402	3,0%	0,7%	14,0%	12,9%	28,1%	-2,0%	10,5%	-12,7%	16,5%
	SWISS MARKET	12 437	1,0%	3,6%	8,7%	11,7%	7,1%	-14,3%	23,7%	4,3%	30,2%
	SPI SWISS	16 504	0,9%	3,2%	11,1%	13,3%	6,1%	-16,5%	23,4%	3,8%	30,6%
ASIA	MSCI EM	1 100	1,4%	4,9%	7,7%	7,4%	10,2%	-19,8%	-2,3%	18,8%	18,8%
	TOPIX	2 713	-2,9%	-2,2%	1,4%	14,6%	28,3%	-2,5%	12,8%	7,4%	18,1%
	HANG SENG	17 989	3,7%	-0,5%	8,9%	5,5%	-10,5%	-12,6%	-11,8%	-0,2%	13,0%
	CSI 300	3 321	-3,5%	-7,2%	-5,5%	-3,2%	-9,1%	-19,8%	-3,5%	29,9%	39,2%
FX & COMMODITIES	30.08.2024	CURRENT	1 M	3M	6M	YTD	2023	2022	2021	2020	2019
CURRENCIES	EUR-USD	1,105	2,1%	1,8%	2,2%	0,1%	3,1%	-5,9%	-6,9%	8,9%	-2,2%
	EUR-CHF	0,939	-1,2%	-4,1%	-1,7%	1,1%	-6,1%	-4,6%	-4,0%	-0,4%	-3,6%
	USD-CHF	0,850	-3,2%	-5,8%	-3,9%	1,0%	-9,0%	1,3%	3,1%	-8,4%	-1,6%
	USD-JPY	146,170	-2,5%	-7,1%	-2,5%	3,6%	10,5%	13,9%	11,5%	-4,9%	-1,0%
	USD INDEX	101,70	-2,3%	-2,8%	-2,4%	0,4%	-2,1%	8,2%	7,0%	-7,3%	1,2%
COMMODITIES	Gold	2503,39	2,3%	7,6%	22,5%	21,3%	13,1%	-0,3%	-4,2%	25,0%	18,3%
	Silver	28,86	-0,5%	-5,1%	27,3%	21,3%	-0,7%	2,8%	-13,6%	48,7%	12,7%
	WTI Crude Oil	73,55	-5,6%	-4,5%	-6,0%	2,7%	-10,7%	6,7%	59,1%	-21,5%	11,6%
	Natural Gas	2,13	4,5%	-17,8%	14,4%	-15,4%	-43,8%	20,0%	46,9%	16,0%	-25,5%
	Copper	9118,14	0,2%	-8,0%	8,5%	7,7%	0,9%	-14,1%	25,7%	26,0%	3,4%
FIXED INCOME	30.08.2024	CURRENT	1 M	3M	6M	YTD	2023	2022	2021	2020	2019
RATES	US 10 year gvt	3,90	(0,13)	(0,60)	(0,35)	0,02	0 bps	237 bps	60 bps	-100 bps	-77 bps
	German 10 year gvt	2,30	(0,00)	(0,37)	(0,11)	0,28	-54bps	275 bps	39 bps	-38 bps	-43 bps
BONDS	Global Aggregate USD hdg.	579,0	1,1%	3,9%	4,1%	3,2%	7,1%	-11,2%	-1,4%	5,6%	8,2%
	US Treasuries	2336,4	1,3%	4,5%	4,3%	2,6%	4,1%	-12,5%	-2,3%	8,0%	6,9%
	US IG Corporates	3333,4	1,6%	4,7%	5,2%	3,5%	8,5%	-15,8%	-1,0%	9,9%	14,5%
	US High Yield	2635,8	1,6%	4,6%	6,0%	6,3%	13,4%	-11,2%	5,3%	7,1%	14,3%
	Euro Government	240,3	0,4%	2,9%	2,4%	0,7%	7,1%	-18,2%	-3,4%	4,7%	6,3%
	Euro IG Corporates	252,6	0,3%	2,7%	3,3%	2,6%	8,2%	-13,6%	-1,0%	2,8%	6,2%
	Euro High Yield	464,7	1,3%	3,0%	4,4%	5,9%	12,8%	-11,1%	4,2%	1,8%	12,3%
	EM USD Aggregate	1244,8	2,1%	4,6%	6,5%	6,3%	9,1%	-15,3%	-1,7%	6,5%	13,1%

Source: Bloomber, 31/08/24

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