EMBARRASSMENT FROM OMICRON AND BY FED

There is some embarrassment in the financial markets. The granitic certainties, tempered by the successes of the central banks and the fiscal policies undertaken to vaccinate the economies affected by COVID-19, are showing some signs of trembling. In November, the world stock exchange index, the MSCI World, fell 2.8%, the S&P 500 0.8% and the Stoxx Europe 600 2.6%. However, the more conservative Swiss index, the SMI, dominated by pharmaceutical and food stocks, remained almost unchanged, while the NASDAQ-100 technology index even gained 1.8%. What stirred things up was the discovery of a new variant of the coronavirus called B.1.1.529 or Omicron. Fears of a slowdown in economies due to new lockdowns prompted a revival of the early 2020 pandemic. Fears of travel restrictions, thus with related benchmark stocks on the brakes, and returning to one's homes to wait out the worst, working on computers, instead supported pandemic stocks, thus specific pharmaceuticals and information technology. This was a portfolio rotation that pushed towards information technology stocks and vaccine manufacturers, while, implying a slowdown in economies, cyclicals were penalized, particularly energy, with oil dropping over 15% (Brent) in the month.

Omicron arrived to disrupt a scenario that seemed well laid out and supported by a powerful underlying optimism. Stock markets seemed to be unimpeded in their ride to new records. The third-quarter corporate earnings season had ended very well, with 80% of the companies in the S&P exceeding expectations. And fears that demand would continually be frustrated by bottlenecks in the production chain also seemed to be fading. The Baltic Exchange Dry Index, which measures the cost of ocean freight, had fallen 40% from the previous month's highs. The International Monetary Fund's October World Economic Outlook estimated global economic growth of 5.9% in 2021 and

4.9% in 2022: an optimistic outlook only slightly adjusted (-0.1%) in relation to the July forecast.

The markets seemed only marginally concerned by the prospect of tapering (reduction of bond purchases). Federal Reserve (FED) Chairman Jerome Powell's announcement to reduce bond purchases by 15 billion per month to zero in June 2022 seemed to be a foregone conclusion and did not provoke much reaction: Powell had also hinted that he would not raise rates as long as inflation is deemed "transitory."

But then even Powell, in front of the Senate Banking Committee, admitted that perhaps the time has come to withdraw the term "transitory". With core inflation at 4.6% (compared to expectations of 4%), a level not touched since 1991, and 12-month inflation expectations exploding to 7% in October (6.5% in September), the pressure on the FED is increasing. In addition, hourly wages rose 4.8% over the past 12 months and unemployment fell to 4.2%, while the labor force rose to a 12-month high.

Markets, therefore, remain uncertain as they wait to see how much the Omicron variant will be able to curb growth. The development of oil prices is decisive for inflation expectations. Joe Biden's activism in this area makes explicit the need to contain the price of oil to encourage growth and the transition to a new green economy. But if oil prices fall, or at least remain in a range between 70-80 USD per barrel, will it be because the virus will succeed in undermining growth? Or because a global interest in not killing it will emerge? The uncertainty of November will remain at least until the next FED meeting on December 14-15, 2021.

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