INVESTMENT STRATEGY
WEEKLY VIEW

For inquiries related to this article, please contact:
Christofer.Langner@bankfab.com

بنك أبوظبي الأول
FAB
First Abu Dhabi Bank

CENTRAL BANK CREDIBILITY FACES TESTS AS INFLATION SOARS

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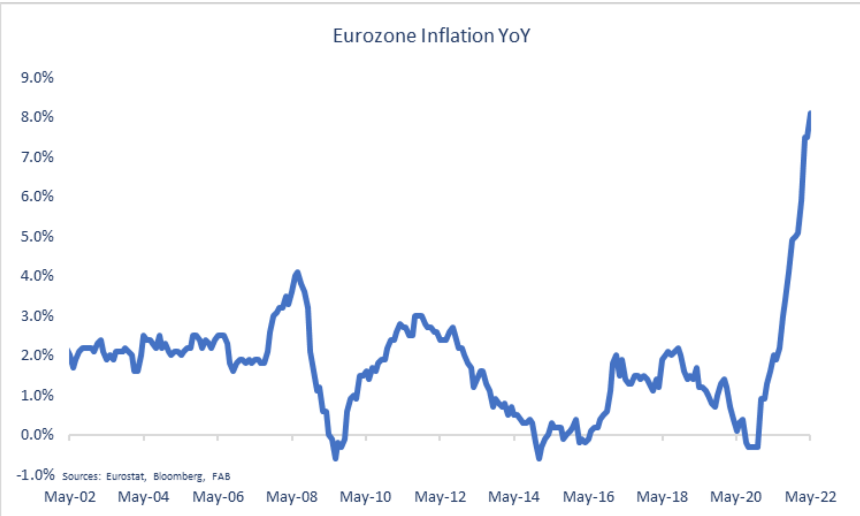
- Global bond yields soared last week after EU inflation hit a record
- The European Central Bank is expected to start hiking rates this week
- US job creation remained too strong for the Federal Reserve's comfort
- The inflation battles in Australia, Canada and New Zealand are ominous

Since Ben Bernanke enshrined communication and forward guidance as policy tools at the Fed, and was followed across the world, central bankers have worked hard to show markets that they mean what they say. That quest for credibility also involves showing that they are serious about keeping inflation in check. As price increases test the highest levels in decades, the credibility of these central banks is at stake. The plight faced by some smaller central banks, such as Australia, Canada and New Zealand is a cautionary tale. Rapid rate hikes in these countries have failed to bring inflation back to their targets. So, they keep hiking. As they have shown, it is worth not being complacent about how far central bankers will go to defend their credibility.

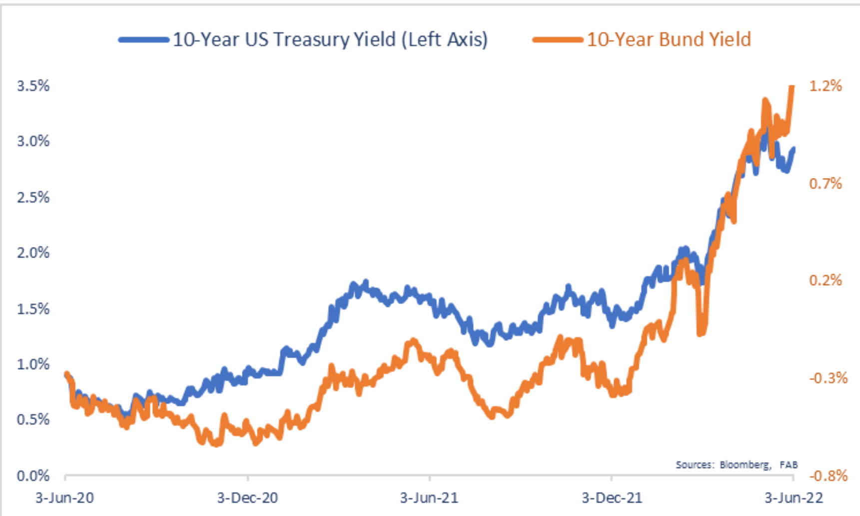
EUROZONE INFLATION AT A RECORD PRESSURES THE ECB TO START HIKING THIS WEEK



- Eurozone inflation hit 8.1% year-on-year in May, the highest in the history of the single currency.
- ECB Chairwoman Christine Lagarde has rebuffed calls for 50 basis points hikes starting in this week's meeting, simply saying that she expects benchmark rates in the country to be positive by September.
- Investors will be watching the ECB's announcement this week for signs of disagreement in the Governing Council, as some of the more hawkish members advocate for faster hikes.

BUND YIELDS AT THEIR HIGHEST SINCE 2014 SUGGEST TREASURY YIELDS COULD RISE

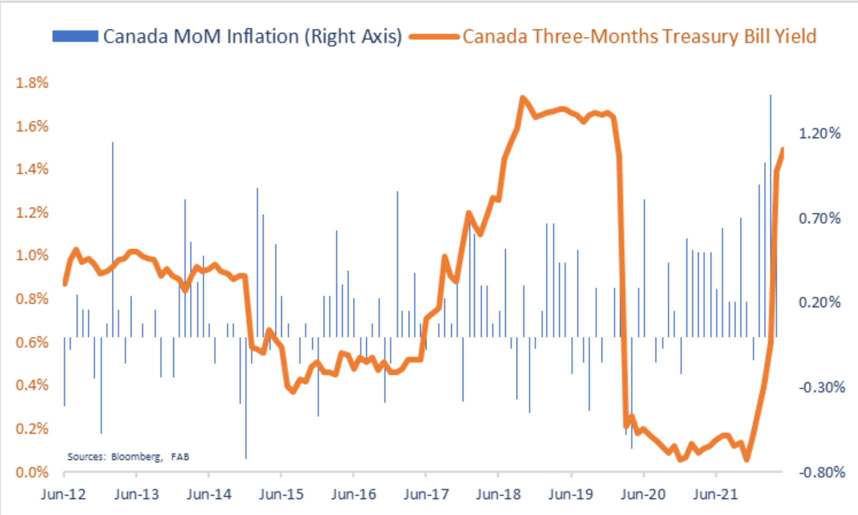
- The yield on the 10-year German bunds hit 1.27% on Friday, as Spanish bonos hit 2.44%, both the highest since 2014, as investors considered a hawkish tilt at the ECB.
- On the same day, the yield on the 10-year US Treasury surpassed 2.98% before retreating to 2.93%.
- The release of a record inflation print early last week caused bund yields to spike and reverberated in the Treasury market, with 10-year yields rising 19.5 basis points, their biggest weekly increase in two months.



US WAGES ARE STILL RISING TOO FAST TO SIGNAL SLOWDOWN IN INFLATION SOON

- Average hourly wages in the US rose 5.2% year-on-year in May, slower than the 5.5% of April, but still some 3 percentage points higher than their previous long-term average.
- The US created 390,000 jobs in May, beating the median estimate of economists of 318,000.
- With total job openings still at historic highs of 11.4 million, the labor market remains very strong.
- This suggests the Fed is likely to keep hiking at least until the end of the year to cool down the economy.

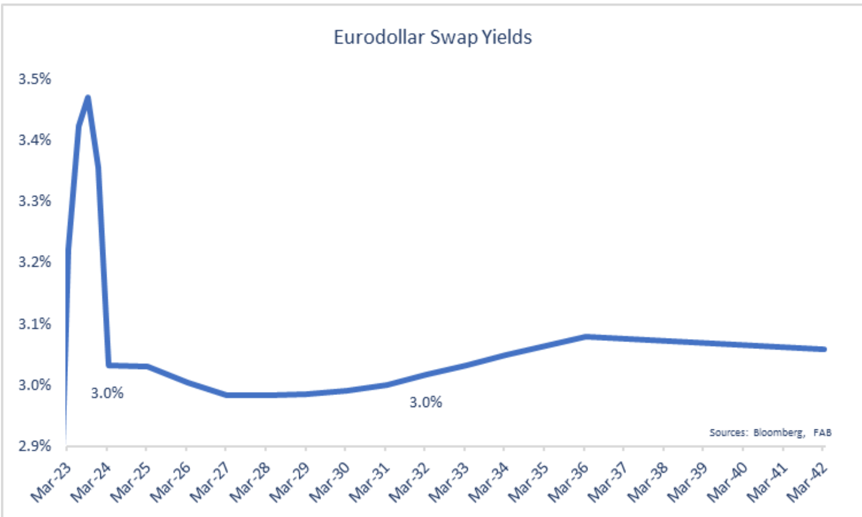
CANADA AND NEW ZEALAND OFFER A CAUTIONARY TALE TO THE FED AND THE ECB



- Both central banks, along with Australia's, are having to hike rates more than central bankers originally envisioned — and faster too.
- The Royal Bank of New Zealand recently hiked its cash rate to 2% on May 23rd, the highest level since 2016, and promised more hikes as inflation fails to abate.
- The Canadian central bank is considering hiking at a 75 basis points rate from its current 50 as month-on-month inflation remains much higher than the historical average.

A KEY RATES CONTRACT IS FLAGGING RECESSION WOES AS 2-10 YEAR CURVE FLATTENS

- The two- and 10-year Eurodollar swaps closed at 3% on Friday, and the short-end of the curve is yielding more than any maturity until 2032.
- That signals that many of the global investors who hedge their dollar positions using swaps now expect the US economy to contract within the next two years.
- This comes as the yield on 10-year US Treasury swaps, used by American investors to hedge their positions, was trading at 3.02% this morning, while the two-year was at 3.05%.



Asset Class	Positioning	Detail
Cash	Underweight	Putting cash to work in risk assets.
Fixed Income	Overweight	Keeping a slight overweight focused on EM dollar debt.
Equities	Overweight	Slightly overweight in Asia ex-Japan and US markets.
Alternatives	Underweight	However, reducing the underweight in hedge funds.