Weekly Market Commentary (week ending Oct 27) 31.10.2023

Last week, government bond yields fell slightly, corporate credit markets generated positive total returns, oil prices fell and equity markets ended the week with gains of around 1%.

US equities were the exception to the rule, as they were heavily influenced by the results published by members of the "Magnificent Seven" (Apple, Microsoft, Meta, Amazon, Alphabet, Nvidia and Tesla). However, weekly closing prices masked the intra-week volatility that investors had to contend with - best illustrated, in our view, by our favorite index for measuring uncertainty, the VIX, which broke the 20 mark for the first time since March due to uncertainty surrounding the US regional banking system.

Last week's developments are perhaps not all that surprising, given the geopolitical situation, the Federal Open Market Committee (FOMC) embargo, the start of third-quarter earnings season in the US and the European Central Bank's (ECB) policy meeting. In such periods of high volatility, separating the noise from the signals could be described as an art; on the whole, we think there were more positive lessons from this volatile week of price action.

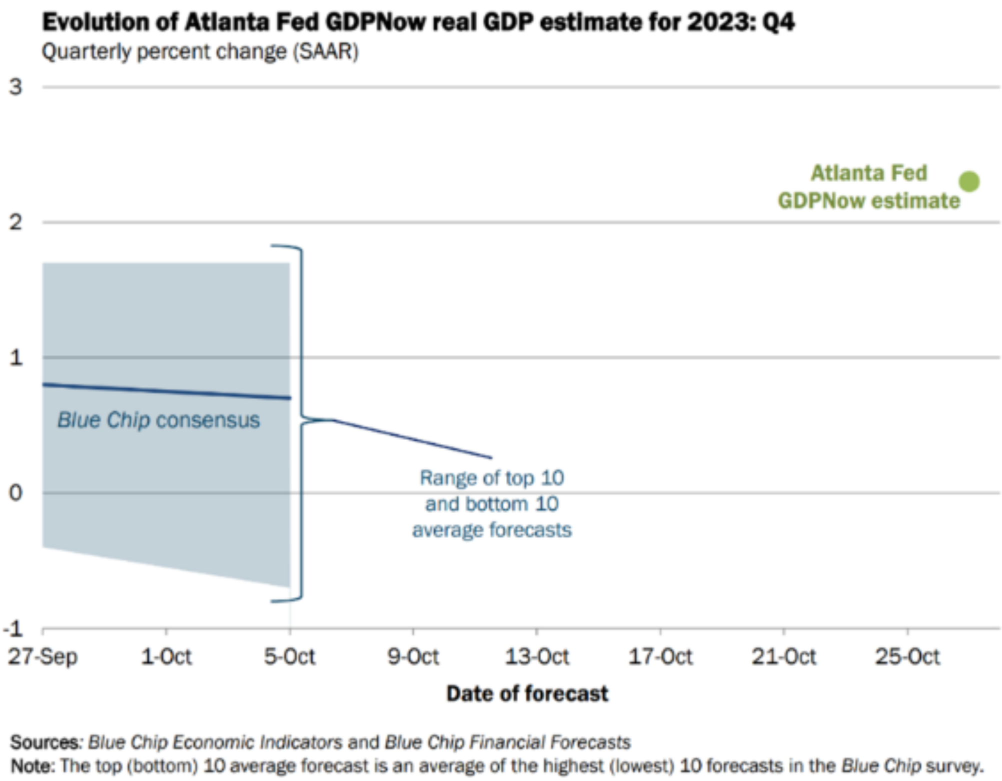
In China, the signal was clearly given that weak growth will not be tolerated. President Xi Jinping visited the People's Bank of China (PBOC) - the first known visit since he came to power ten years ago. The visit was followed by an announcement that China will issue an additional RMB 1 trillion in central government special bonds in the fourth quarter, increasing government spending by 0.8% and bringing China's central budget deficit to 3.8% for 2023. Looking ahead to the week ahead, the key event will be the once-in-a-five-year Central Conference on Financial Work (CFWC), and investors will be watching for macroeconomic policy adjustments, particularly with regard to the real estate sector and local government financial vehicle debt.

In the eurozone, the ECB kept key rates unchanged at 4.5% (the rate on main refinancing operations), in line with market expectations, and is likely to continue to depend on data for future policy adjustments. However, in a nod to recent history, the Committee acknowledged the weakness of activity data and the tightening of financial conditions. Weak activity was evident in the eurozone's October PMI (purchasing managers' indexes), surprising again on the downside and continuing to contract to 46.5 from the expected 47.5. Both sub-components - manufacturing and services - contracted. With the tightening of monetary policy in the eurozone complete, forecasters are now competing to see who can correctly predict the first easing of monetary policy. Currently, the OIS (Overnight Index Swap) market in the eurozone estimates that the first key rate cut will take place in June 2024, one easing ahead of the USA, whose forecast calls for policy to remain unchanged until September.

In the United States, the preliminary GDP estimate for the third quarter was revised upwards to 4.9% quarter-on-quarter (QoQ), with initial estimates for third-quarter growth of just 2. Consumption was the main driver of growth, for both goods and services. Investor reaction was limited, as they had built in high expectations for the third quarter and seemed more concerned about forecasting the extent of the slowdown in the fourth quarter.

However, two potential obstacles to fourth-quarter growth may have been overcome. Firstly, Mike Johnson has been elected by his Republican colleagues as Speaker of the House of Representatives; after three weeks of turmoil and the failure of three candidates, his appointment should reduce the likelihood of a government shutdown in November, given that prior to his appointment, he had come out in favor of a short-term spending deal. Secondly, the UAW (United Auto Workers) has reached a tentative agreement with Ford and offered a similar contract proposal to GM (General Motors). This could mark the beginning of the end of a 6-week strike involving 45,000 employees. As in the third quarter, the risk to US growth in the fourth quarter is higher than expected.

Chart of the week: Risk of a rise in US GDP in Q4



2023.10.31.Atlanta Fed
Source: Federal Reserve Bank of Atlanta, "Atlanta Fed GDP Now Estimate for 2023: Q4", October 27, 2023.

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