



Weekly round up (Week 9)

As confidence in stable growth has grown in recent weeks, investors have turned their attention to the implications for inflation and what this means for the markets. As a result, inflation data took center stage last week.

Japan was the first to release data, with inflation beating expectations and consumer prices slowing less than expected. Core consumer prices for January fell in line with the Bank of Japan's (BoJ) 2% target, against expectations of 1.9%. However, overseas travel was seen as a technical factor that inflated the data.

Investors continue to wonder whether the end of Japan's negative interest rate policy will begin in March or April. We are not yet in a position to predict the achievement of a sustainable and stable inflation target," said Ueda.

US data point to a rate cut in July

Turning to the US, after the previous week's strong inflation data, investors looked for confirmation in the Federal Open Market Committee's (FOMC) favored Personal Consumption Expenditures (PCE) report. The data was in line with expectations, with the core PCE index up 0.4% in January and down to 2.8% year-on-year.

Bond investors will point to the acceleration in the six-month annualized core PCE index from 1.9% to 2.5%, but the report only confirmed that the FOMC will maintain its status quo until the summer. The overnight interest rate swap market is currently pricing in the first full 25 basis point (bp) cut for July.

Finally, the eurozone published its first price data for February. Disinflation continued in the region, but in the same way as elsewhere - at a slower pace, with prices falling by less than expected. Headline inflation fell to 2.6% and core inflation to 3.1%, against forecasts of 2.5% and 2.9% respectively. The European Central Bank (ECB) is likely to be encouraged by the fall in prices, and may feel vindicated in its decision to wait until summer before easing policy. The overnight interest rate swap market estimates an 86% probability that the ECB will cut rates by 25 basis points in June.

HY (High Yield) and EM (Emerging Markets) credit outperform as government bonds plummet

With central banks dampening expectations of second-quarter easing and a series of less-than-encouraging inflation data, February was a difficult month for government bond markets. The fall in interest rates was led by the front end of the curves - US and German two-year bond yields rose by 41 basis points and 48 basis points respectively.

The news was better for high yield corporate credit, which outperformed investment grade and generated a positive total return for the month. Emerging market (EM)

credit was also a big winner. Emerging market central banks have already begun to ease their key rates, and valuations and coupon rises remain attractive. In addition, the significant shortage of new supply and the underweighting of global investors looking to increase their exposure are encouraging a strong technical bid for stocks.

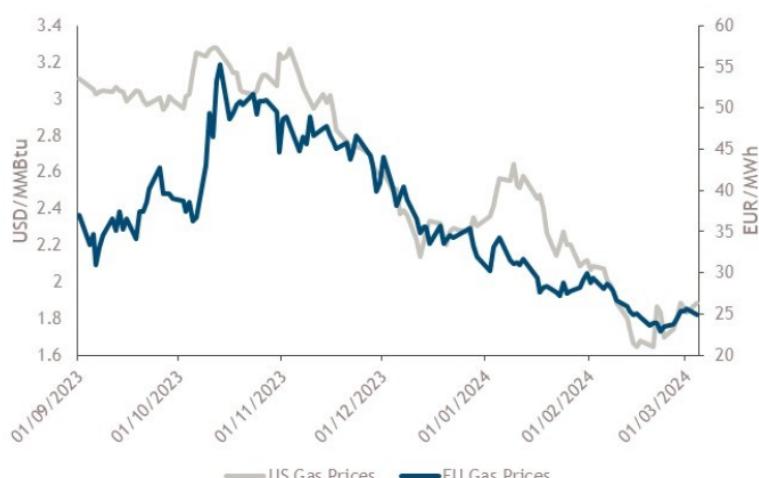
On the equity markets, it was another excellent month for the Magnificent Seven, which gained over 8%. Nvidia and Meta took center stage after reporting exceptional fourth-quarter earnings. However, Asian stock markets performed even better. Japan's Nikkei 225 surpassed its 1989 record, rising by over 10% in February, while the Shanghai Stock Exchange appreciated by over 9%, its best monthly performance since November 2022. At the same time, China's regulator curbed disruptive quant activity and state-backed funds bought 410 billion yuan (\$57 billion) worth of Chinese exchange-traded funds.

Oil and gas diverge

Foreign exchange markets remained in a wide range during the month, perhaps because geopolitical tensions did not escalate. At the same time, commodity markets were marked by divergences between oil and gas. Oil prices ended the month up 5%, as transportation costs and OPEC+ supply constraints took their toll.

By contrast, gas prices in the USA and Europe have fallen by over 40% and 50% respectively since October (see this week's chart). A mild winter and booming US production have led to a global supply glut; current US storage is 498 billion cubic feet (BCF) above the five-year average of 1,876 BCF, and European gas storage is 63% full, compared with the five-year seasonal norm of 46% for this time of year. This is good news for industrial activity and, together with the rebuilding of inventories, explains the forecast recovery in global manufacturing activity over the coming months.

Graph of the week - Since October, gasoline prices have collapsed: Europe -55%, USA -44%.





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