Weekly round up (Week 23)

Our weekly view of key developments in financial markets and economies looks at reactions to an important election week and rate cuts by the European Central Bank and the Bank of Canada.

June began on a positive note. Government bond yields fell, driven by weaker economic data and policy easing by the European Central Bank and the Bank of Canada. Both cut their key rates by 25 basis points, in line with expectations. Government yield curves flattened, with US and German 30-year bonds falling by 10 basis points over the week.

Total returns were positive for corporate credit overall, with investment-grade bonds. Most major equity markets have been positive since the start of the month, led by technology indices in the US, Taiwan and South Korea. So far, June's loser is energy. Crude oil fell 2% over the week after OPEC+ announced that, conditions permitting, it will begin to end voluntary supply cuts in October, and on optimism of a ceasefire in the Middle East.

Modi in trouble

Usually, at the beginning of each month, investors focus on key economic and employment data. June stood out for its electoral calendar, with 20% of the world's population going to the polls over the first weekend.

India experienced a roller-coaster ride, from the first exit polls that suggested a large victory for the ruling Bharatiya Janata Party (BJP), to the announcement that it had lost its majority in the single-party lower house of parliament.

However, with the BJP's 240 seats, Narendra Modi will win his third consecutive term as Prime Minister with the support of allied partners. Initial investor reaction was negative, with the Sensex falling 6% on June 4 on the perception that it might be more difficult for the BJP-led coalition to adopt tough reforms or implement welfare programs.

However, once the dust had settled, sentiment reversed. Investors may have realized that the BJP would learn from its mistakes, tone down its Hindu nationalist agenda and stick instead to pro-growth policies, including building infrastructure and cutting red tape in the manufacturing sector, while allowing the central bank to keep inflation low and stable. The Indian rupee ended the week relatively unchanged, and domestic stock markets rallied to end the week up 3%.

In our view, the fact that the Modi administration is being held back by certain forces could be positive; during the election campaign, Modi declared that he was an avatar of God.

Overwhelming Mexican elections

Mexico experienced the most important general elections in its history, with presidential, legislative and several local elections taking place simultaneously. Overall results showed that the outgoing coalition performed well at all levels, while the opposition coalition performed disappointingly.

Claudia Sheinbaum won a landslide victory and will succeed her mentor Andrés Manuel López Obrador (commonly known as AMLO) to become the country's first female president. Her coalition party won a two-thirds majority in the lower house and is poised to achieve the same result in the Senate. The new Congress will be sworn in on September 1, and the president-elect will take office on October 1.

In February, the outgoing administration led by AMLO submitted a wide-ranging package of reforms to Congress, some of which were seen as eroding Mexico's institutional framework and not being market-friendly. Judging by the reaction to the election result, investor concerns remain, with the Mexican peso depreciating by 5% over the week.

However, in our view, the Sheinbaum administration is unlikely to compromise macroeconomic stability - a key ingredient of its electoral success - by limiting central bank independence or relinquishing medium-term fiscal responsibility. The main challenge for the President-elect will be to sustain market sentiment by first reassuring investors, then proposing predictable, investment-friendly policies.

Financial markets reacted displeased from this electoral result commented in today's "reflection of the day".