Weekly round up (week 46)
21.11.2023

The rise in government bonds continued for the second week; since the beginning of the month, 30-year yields have fallen by 50 basis points in the USA and Germany.

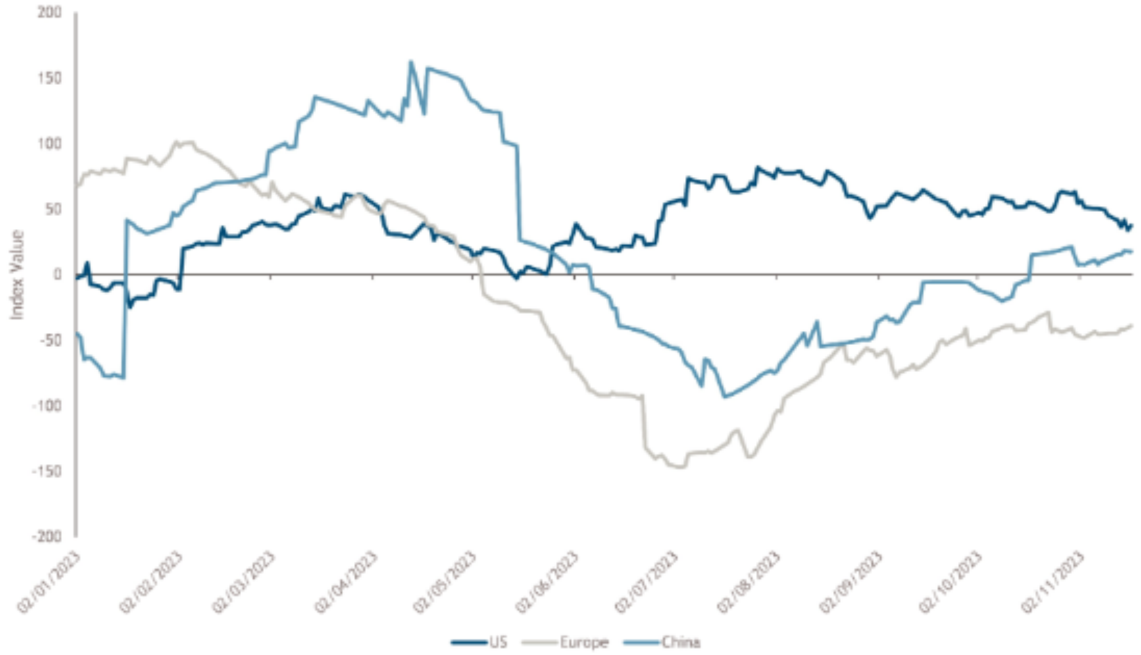
Corporate credit markets continued to keep pace with government debt, with U.S.-dollar-denominated credit outperforming. Global equity markets rallied, the VIX fell below 14 (a sign of renewed risk appetite) and the US dollar depreciated. The only exception to this trend has been energy prices, which continued to fall - the trend in Brent and WTI prices is now negative since the start of the year.

Last week, the US and China took center stage, offering investors positive political and economic headlines. President Biden signed the "phased" Continuing Resolution (CR). This extended spending deadlines to January 19 and February 2, averting a government shutdown. Mr. Biden also spoke at length with Chinese leader Xi Jinping at the Asia-Pacific Economic Cooperation summit in San Francisco. In a symbolic gesture enabling investors to assess the relationship between the two superpowers, the leaders agreed to begin negotiations on the renewal of the Science and Technology Agreement. This was the first major pact signed by the USA and China when they established relations in 1979 under the Nixion administration.

On the economic front, the news on inflation was positive: consumer prices were unchanged in October, and core prices rose by just 0.23% month-on-month, with both indices below the expected consensus. Core inflation now stands at 4%, its lowest level for two years. Looking at the price indices, economists will be encouraged by the extent of disinflation within the sub-components; the all-important homeowners' equivalent rent continued to moderate, and prices for hotels, air tickets and new vehicles also saw downward surprises. In China, retail sales continued to recover, driven by the service sectors, and industrial production surprised and exceeded investors' expectations. Only fixed-asset investment disappointed, dragged down by weakness in the real estate sector. However, it has been reported that China is now planning to provide at least 1,000 billion yuan of low-cost financing to the national urban village renewal and affordable housing program to help support the sector.

To take a broader perspective, beyond the weekly flow of positive news and price movements, we can use the economic surprise indices (see chart). For the USA (white line), we see that investors have always been surprised by the robustness of the economy. It was only from November onwards that the positive surprise began to dissipate, which could help explain investors' confidence in a soft landing and the end of the political cycle. For China (red line), the trough in activity relative to economic expectations was reached over the summer. The index has now turned positive, suggesting that investors are too pessimistic about real activity - this could explain the cheap valuations found in China. For the Eurozone (blue line), as for China, the peak of negative surprise was reached over the summer; economists have recalibrated their expectations but are still surprised by the level of weakness in the region. This partly explains the ECB's (European Central Bank) policy reassessment over the past month. The OIS (overnight interest rate swap) market estimates that the ECB should start easing policy in June, and reduce it by a total of 100 basis points by 2024.

Chart of the week: Economic surprise indices



2023.11.21.Surprise index
Source: Bloomberg, November 17, 2023