Weekly Market Commentary (week 7)
20.02.2024

US government bond yields moved higher, but the phrase "range-bound" probably best sums up price action in most markets last week. The relative calm was perhaps unsurprising considering that much of Asia was on vacation for the Lunar New Year and the US was recovering from Super Bowl LVIII between the Kansas City Chiefs and the San Francisco 49ers, which took place in Las Vegas. The positive and negative aspects of last week's economic data neutralized each other. It was a good week for carry strategies.

In Asia, Australia's unemployment rate rose to 4.1%, with only 500 jobs created in January, another sign that policy rates are beginning to take effect. However, the main surprise came from Japan, which unexpectedly entered a technical recession - two consecutive quarters of contraction - in the fourth quarter. Growth contracted by -0.1% quarter-on-quarter (QoQ), compared with consensus forecasts of +0.2%.

The growth report highlighted Japan's dependence on external demand, with a contraction in domestic consumption and business investment, and inflationary pressures weighing on purchasing power. In our view, this will complicate and perhaps delay the exit from the Bank of Japan's negative rate policy, which is expected to begin raising rates in March or April. Over the year as a whole, the Japanese economy grew by 1.9%. Unfortunately, this was not enough to prevent Germany from becoming the world's third-largest economy in 2023.

UK recession: it's technical

In Europe, the UK took center stage; the unemployment rate unexpectedly fell to 3.8%, and although wage growth continued to fall, it fell more slowly than economists expected. Consumer prices remained stable in January (unchanged from December), while overall and core consumer prices rose by 4.0% and 5.1% year-on-year.

Robust employment data should be good news for the Bank of England (BoE); inflation should resume its decline in February as base effects take hold. This news was followed by a headline announcing that the UK had entered a technical recession, with growth in the fourth quarter contracting by -0.3% on the previous quarter. A technical recession was the consensus view, but the fourth-quarter contraction was larger than expected, with net trade one of the main contributors. As a result, the UK economy grew by just 0.1% in 2023. The overnight interest rate swap market forecasts that the BoE will cut its key rates by 75 basis points in 2024, starting in August. However, weak data could put pressure on the BoE to ease rates sooner.
In the US, core prices were flat in January (unchanged from December), rising by 3.9% year-on-year. Economists were expecting prices to fall to 3.7%, but the rise in rents took forecasters by surprise, increasing by 0.6% month-on-month.

Nine of the thirteen categories posted declines, with the sales control group (used to calculate gross domestic product) contracting by 0.4% month-on-month. The report's weakness could be attributed to the difficult weather conditions in January. It could also be a sign that consumers are finally turning inward amid higher borrowing costs.

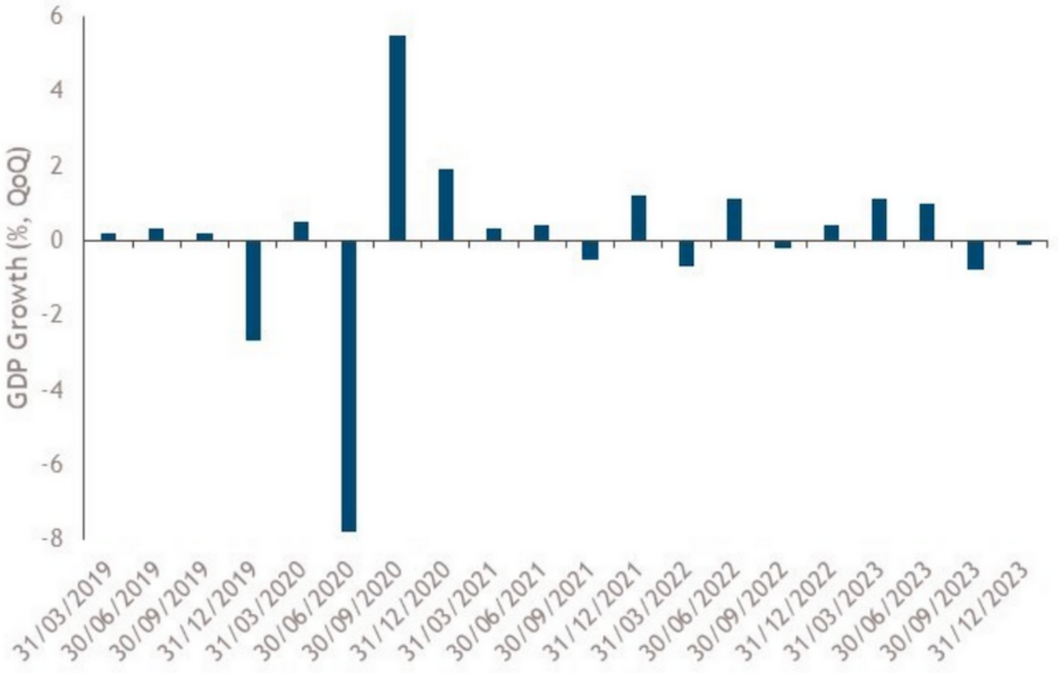
Bears, Bulls and Superbowls

One of the arts of investing is separating the signals from the noise. This week, fixed-income investors will focus on the surprising weakness of growth and consumer data, while fixed-income investors will talk about the rigidity of inflation data.

For those interested in noise, New York Times sportswriter Leonard Koppett introduced the Super Bowl indicator in 1978. This indicator predicts that if the winner of the Super Bowl belongs to the American Football Conference (AFC), the S&P 500 index will decline over the following year. Conversely, if a team from the National Football Conference (NFC) wins, the stock market will rise.

From 1967 to 2015, the indicator's accuracy rate was 82%. Over the past six years, however, the indicator has lost its luster - it was correct only once between 2016 and 2023, bringing its success rate down to 75%. The Kansas City Chiefs' victory in the AFC should delight stockholders.

Chart of the week: Japan - Unexpected technical recession



2024.02.20.Japan - Unexpected technical recession
Source: Bloomberg, February 16, 2024. For illustration purposes only.

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