

Markets welcome the latest inflation news from the US, eurozone, and UK



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Disinflation continues

Inflation reports from the US, eurozone, and UK suggest that their rate hike cycles may have come to an end.

Volatility is expected

I still expect some volatility as there is still significant uncertainty around the timing of when rate cuts will begin.

A change in sentiment?

All in all, I think we may look back on the last several weeks as the start of significant change in market sentiment and global risk appetite.

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I have to confess that between my husband and me, we are not very “street smart” when it comes to raising teenagers. I’m embarrassed to admit that we didn’t realize our 17-year-old daughter was hosting a party in our basement until the next morning when our doorbell camera revealed a steady stream of late-night guests. Fortunately, I have a better sense of when a party is getting started in the markets. Last week’s inflation reports from the US, eurozone, and UK were certainly welcome guests, going a long way in convincing markets that these central banks are finished hiking interest rates.

The disinflation trend continues

The US Consumer Price Index print for October indicated continued progress on the disinflationary front. Markets took this as a strong signal that the US rate hike cycle has ended. That data was quickly followed by readings on eurozone and UK inflation, as well as the US Producer Price Index, which markets interpreted to mean that rate hikes among Western developed central banks have come to an end.

However, at the same time, we received some data last week showing that those same Western developed economies are cooling. For example, US retail sales for October experienced their first decline since March. And the decline of industrial production in the eurozone was worse than expected. So why are markets so happy?

Recent events have been positive for markets

First of all, this is what Western developed central banks want to happen. They want their economies to cool to hopefully ensure disinflation continues. In addition, the US avoided a government shutdown without any drama this month, passing a short-term ladder spending plan that kicks the can down the road to early 2024. But the key reason for rising global risk appetite is that markets are looking through today and out to 2024; they are discounting the start of rate cuts later in the first half of the year and an economic recovery in the back half of the year.

Yields on the 10-year US Treasury, the 10-year UK gilt and 10-year European bonds such as the Italian 10-year bond have fallen in recent days. And stocks have risen.¹ I believe markets are anticipating a global economic recovery, with other major economies such as China and Japan likely to contribute to a second half recovery with supportive fiscal and monetary policy in the near term.

Volatility may present opportunity

But while a party seems to have started in markets, I expect some volatility in the near term. There is still significant uncertainty around the timing of when rate cuts will begin, and so we could see a pattern of "bad macro news is good news for markets" and vice-versa in the near term. However, I would take advantage of these opportunities to add long duration fixed income exposure and also find more attractive entry points for equities.

Is this the start of a change in sentiment?

All in all, I think we may look back on the last several weeks as the start of significant change in market sentiment and global risk appetite, as markets seem to like what they anticipate will unfold in the months to come. We will need to remain very vigilant, however, recognizing the long and variable lags of monetary policy might throw a wrench into the future that markets are currently discounting – although that is certainly not my base case.

Giving thanks

This week we will celebrate Thanksgiving in America. While the date on the calendar is US-specific, the sentiment of expressing gratitude is universal. First, I would like to thank our clients for putting trust in us. Second, I would like to thank my colleagues; I am grateful to work with such a talented group of people who care so much about our clients. Finally, I can't help but express how incredibly grateful I am for my family – even my daughter, our resident party planner.

Dates to watch

Next week, I will be taking a break from Weekly Market Compass following the Thanksgiving holiday. I look forward to returning the first week in December to discuss our 2024 investment outlook.

Date	Report	What it tells us
Nov. 21	Federal Open Market Committee meeting minutes	Gives further insight into the central bank's decision-making process.
Nov. 22	UK Autumn Forecast Statement	Provides an update from the government on the state of the UK economy.
Nov. 23	Eurozone manufacturing and services flash Purchasing Manager's Index	Indicates the economic health of the manufacturing and services sectors.
Nov. 23	Account of European Central Bank monetary policy meeting	Gives further insight into the central bank's decision-making process.
Nov. 23	Japan Consumer Price Index	Tracks the path of inflation.
Nov. 24	US manufacturing and services flash Purchasing Manager's Index	Indicates the economic health of the manufacturing and services sectors.

Notes

¹Source: MSCI. The MSCI World Index returned 3.0% for the week ending Nov. 17, 2023. The MSCI World Index is an unmanaged index considered representative of stocks of developed countries.

Important information

Past performance is not a guarantee of future results.

An investment cannot be made directly into an index.

This does not constitute a recommendation of any investment strategy or product for a particular investor. Investors should consult a financial professional before making any investment decisions.

All investing involves risk, including the risk of loss.

In general, stock values fluctuate, sometimes widely, in response to activities specific to the company as well as general market, economic and political conditions.

Fixed-income investments are subject to credit risk of the issuer and the effects of changing interest rates. Interest rate risk refers to the risk that bond prices generally fall as interest rates rise and vice versa. An issuer may be unable to meet interest and/or principal payments, thereby causing its instruments to decrease in value and lowering the issuer's credit rating.

Alternative products typically hold more non-traditional investments and employ more complex trading strategies, including hedging and leveraging through derivatives, short selling and opportunistic strategies that change with market conditions. Investors considering alternatives should be aware of their unique characteristics and additional risks from the strategies they use. Like all investments, performance will fluctuate. You can lose money.

The risks of investing in securities of foreign issuers can include fluctuations in foreign currencies, political and economic instability, and foreign taxation issues.

Investments in companies located or operating in Greater China are subject to the following risks: nationalization, expropriation, or confiscation of property, difficulty in obtaining and/or enforcing judgments, alteration or discontinuation of economic reforms, military conflicts, and China's dependency on the economies of other Asian countries, many of which are developing countries.

Disinflation, a slowing in the rate of price inflation, describes instances when the inflation rate has reduced marginally over the short term.

Inflation is the rate at which the general price level for goods and services is increasing.

The Consumer Price Index (CPI) measures change in consumer prices as determined by the US Bureau of Labor Statistics.

The Producer Price Index (PPI) is compiled by the Bureau of Labor Statistics and measures the average change over time in the selling prices received by domestic producers for their output.

A basis point is one hundredth of a percentage point.

The Federal Open Market Committee (FOMC) is a 12-member committee of the Federal Reserve Board that meets regularly to set monetary policy, including the interest rates that are charged to banks.

The eurozone (also known as the euro area or euroland) is an economic and monetary union of European Union member states that have adopted the euro as their common currency.

UK gilts are bonds issued by the British government.

GDP (Gross domestic product) is a broad indicator of a region's economic activity, measuring the monetary value of all the finished goods and services produced in that region over a specified period of time.

Tightening monetary policy includes actions by a central bank to curb inflation.

Duration is a measure of the sensitivity of the price (the value of principal) of a fixed income investment to a change in interest rates. Duration is expressed as a number of years.

The yield curve plots interest rates, at a set point in time, of bonds having equal credit quality but differing maturity dates to project future interest rate changes and economic activity.

The opinions referenced above are those of the author as of November 20, 2023. These comments should not be construed as recommendations, but as an illustration of broader themes. Forward-looking statements are not guarantees of future results. They involve risks, uncertainties and assumptions; there can be no assurance that actual results will not differ materially from expectations.