Weekly Macro and Markets View

26 January 2026

Highlights and View

Japanese Prime Minister Takaichi announces a snap election and proposals to temporarily suspend the 8% food sales tax

Pro-stimulus fiscal policies, which raise concerns about fiscal largesse, are likely to add upward pressure on bond yields and prompt the Bank of Japan to hike policy rates in the near term.

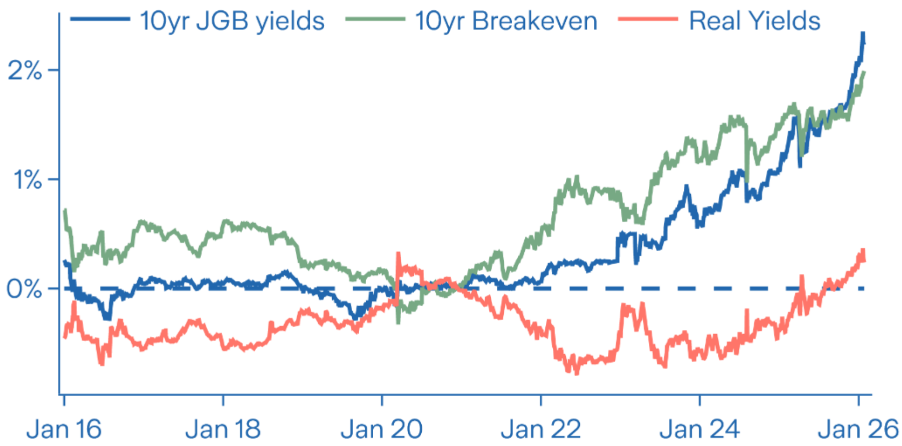
US President Trump backs away from military intervention to acquire Greenland and from the threat of 10% tariffs on eight European countries

Stocks declined on a combative stance from the US president in the days prior to his Davos address before rebounding as he then asserted that 'I won't use force' in his aspirations for Greenland.

UK headline inflation accelerated to 3.4% YoY at the end of last year

The move was driven by both goods and services, but inflation rates are expected to fall back over the course of the year.

Japan's Bond Market Faces Election-Driven Volatility



Source: Bloomberg

Long-dated Japanese government bond (JGB) yields have jumped, with 10-, 30-, and 40-year bonds now at 2.2%, 3.6%, and almost 4%, respectively— levels that were unthinkable just years ago. The jumps have been fuelled by rising inflation expectations and a creep higher in real yields, likely pricing in higher fiscal premiums. These moves have intensified since pro-stimulus Prime Minister Takaichi took office. Her push for a snap election on February 8 along with proposals like a two-year suspension of the 8% food sales tax have amplified concerns about fiscal largesse. Given the ongoing unfavourable dynamic between supply and demand, and with standby buyers including the BoJ and life insurers stepping back from the market, we see scope for long-dated JGB yields to rise further this year. Still, Japan's fiscal position has improved notably thanks to higher inflation, and the dominance of domestic holdings of JGBs, close to 90%, means a UK-style 'Truss moment' is unlikely. Last week, the Bank of Japan kept rates unchanged at 0.75%, maintaining a hawkish stance. Going forward, it's crucial that inflation expectations stay anchored near 2% and that the BoJ delivers credible policy, making near-term rate hikes increasingly likely.

Equites

Shaken, but standing firm amid a geopolitical maelstrom

The modest 0.2% decline in the MSCI World Equity Index last week masked an eventful week, in which President Trump lived up to his keynote billing at the much-anticipated WEF meeting. In a holiday-shortened US trading week, volatility returned to stocks with the VIX volatility measure jumping as the US president threatened potential military intervention in Greenland and a further 10% tariff on European countries, should they not support a US acquisition of the island. As investors took profits and sought protection, the S&P 500 fell more than 2% and global stocks retreated from record levels while gold jumped to a record high. However, as has become almost a trademark of current US policy, the president backed off from his threats. This, along with robust US economic data, boosted equities, with most global indices recovering the majority of their losses. LatAm indices bucked the trend, with the MSCI LatAm Index up a further 7.5% on the week. We believe beyond the geopolitical noise, investors will focus on strong equity fundamentals to keep the bull market in place.

Bonds

Market volatility picks up amid geopolitical and fiscal pressures

In a volatile week for financial markets, core government bond yields ended the week slightly higher, but with significant volatility intra-week. Treasuries sold off as the US intensified pressures over Greenland, but the move was later reversed as the situation de-escalated, with the 10yr Treasury yield roughly unchanged on the week. A sharp sell-off in Japanese government bonds, triggered by PM Takaichi's announcement of snap elections, was an additional driver of global volatility, though conditions stabilised following verbal interventions by government officials. European bond markets saw less dramatic moves, but gilt and Bund yields rose on the week as geopolitical developments confirmed the need for increased European defence spending, with fiscal implications. Looking forward, we expect US and European yields to continue to range trade on the back of constructive inflation data and the potential for further monetary policy easing, though with significant volatility amid fiscal and geopolitical pressures.

UK

Solid growth at the beginning of the new year

Business surveys show that the UK economy enjoyed a solid increase in output levels at the start of 2026 with the Composite PMI rising to the highest level in almost two years. Services activity was the main driver of the expansion, but manufacturing also picked up to a level not seen since August 2024. Meanwhile, the labour market continues to moderate. The unemployment rate remained at 5.1% in November, but employment numbers for December as well as comments in the latest PMI survey are pointing at ongoing headwinds. Inflation picked up in December with headline CPI accelerating to 3.4% YoY from 3.2% YoY the month before. Core inflation remained at 3.2% YoY. Retail sales picked up much more than consensus expected in December, showing that British consumers kept spending at the end of last year. UK stocks faced some headwinds in a volatile week, with the FTSE 100 falling by 0.9%, but small caps were one of very few markets globally to end the week marginally higher.

Eurozone

German activity gains traction

The Composite Eurozone PMI figure was unchanged in January and is consistent with slight activity expansion at 51.5. Details suggested two areas of concern. Firstly, firms have reported a decrease in employment levels. Secondly, firms have indicated surprisingly strong output price rises in January, signalling some upside risk to inflation. At a country level, Germany stood out positively as its Composite PMI rose to 52.5, with services expanding strongly at 53.3. This, combined with better sentiment from the ZEW survey and encouraging domestic production data, suggest the fiscal boost is beginning to work. In stark contrast, French PMIs fell to a contractionary 48.6, with services notably lagging manufacturing. The French domestic INSEE measure appears slightly better, particularly in manufacturing. Despite data weakness, France's political instability faded from the market's mind as Prime Minister Lecornu survived a no-confidence vote and passed a budget. Deficit reduction intentions remain inadequate, and we see downside risks for assets as the presidential election approaches.

LatAm

Equities start the year with strong momentum amid supportive inflows and a metals rally

LatAm equities have rallied 13.9% YTD, outperforming the MSCI EM Index (6.9%) and MSCI World Index (1.7%), supported by strong foreign investor inflows, US dollar weakness, and an exceptional rally in metal-related commodities. We remain constructive on LatAm equities. Brazil offers the greatest upside potential given the monetary easing cushion ahead. Certainly, the October presidential election will add volatility, with rising support for opposition candidates suggesting a competitive race. In Mexico, the monthly GDP index contracted -0.1% YoY in November 2025, well below consensus (1.2%). Agriculture led the weakness, though services also softened after having been the main pillar in prior months. The latest CPI reading was reported at 3.8% YoY, a positive outcome given concerns over the impact of tax hikes on certain products and new tariffs on non-FTA imports. We continue to expect Banxico to hold the MPR through Q1, though persistent downside inflation surprises and weak activity could bring forward an earlier resumption of the easing cycle.

What to Watch

- In the US, the Fed is widely expected to leave rates unchanged while the corporate earnings season is picking up steam.
- This week brings January inflation prints for Germany and Spain. We also receive consumer confidence data across the Eurozone, which continues to be an area of weakness.
- Japan's Tokyo CPI, Australia's inflation data, and India's Budget are key to watch.
- In LatAm, attention will be focused on central bank guidance from Chile and Brazil, with policy rates expected to hold steady.

Disclaimer and cautionary statement

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