Weekly Macro and Markets View

25 March 2024

Highlights and View

The Fed continues to signal three rate cuts this year

The relatively dovish statement is not fully consistent with recent pickups in price pressure and the FOMC lifting its forecast for Core PCE inflation by year end.

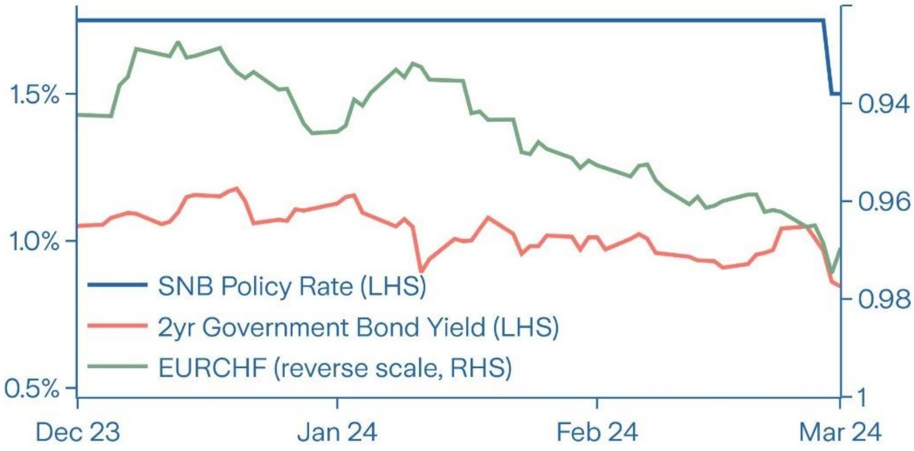
The Bank of Japan hikes rates for the first time in 17 years, ending eight years of negative interest rates

In a well-signposted move, the BoJ was the last of the central banks to lift rates above zero, while ending explicit yield curve control, though policy will remain accommodative.

Equity markets continue to power higher as policy makers signal a desire to cut interest rates

Messaging from the Fed and the BoE, as well as the surprise cut from the SNB, bolstered investor confidence that policy easing is finally a reality, lifting many stock markets to record levels.

The Swiss National Bank cuts rates in a surprise decision



Source: Bloomberg

In a surprise decision, the Swiss National Bank cut the policy rate by 25bps last week, reducing it from 1.75% to 1.5%. The rate cut was the first among the G10 and triggered a weaker Swiss franc and falling yields on Swiss government bonds. The SNB has again shown that it is not afraid of surprising markets. It appears that the central bank was keen to move ahead of the ECB, rather than waiting for the next quarterly policy meeting in June as had been anticipated. The rate cut was motivated by a much more benign inflation outlook, with the updated inflation forecast showing inflation averaging 1.4% in 2024, 1.2% in 2025 and 1.1% in 2026 – down by around 50bps from the December forecast despite the lower policy rate. The SNB was motivated to lower its forecast based on lower goods inflation, which is partly the result of the stronger franc over the past year, and limited domestic second-round effects, including on wages. While we agree with the SNB's view on inflation, we still see sticky domestic inflation as a risk to the outlook, with further rent increases to impact CPI in coming months along with resilient services demand. For now, we maintain our view of two rate cuts in 2024, but the risk has tilted towards a more front-loaded rate cutting cycle by the SNB.

US

The Fed shrugs off elevated inflation numbers

As expected, the Fed kept rates unchanged at its meeting last week. Interestingly, the FOMC and particularly Chair Powell seem unconcerned about the recent reacceleration in inflation. The dot plot showed the median 2024 dot unchanged at three cuts this year, although it was a close call as one member did raise their projection for the fed funds rate this year. Somewhat inconsistently, the relatively dovish statement came despite the Fed lifting its year-end Core PCE inflation forecast from 2.4% to 2.6%. Not only is the FOMC signalling that they won't reach their target this year, but that they expect to miss it by a wider margin. They also marginally lifted the projection for the long-term neutral rate, a process we think is likely to continue in the coming quarters. Financial markets welcomed the Fed's dovish position following the two robust inflation reports in January and February, with the S&P 500 rising by 2.3%, its best week so far this year. Not surprisingly, Treasury yields fell.

UK

The BoE hawks change their mind as inflation falls substantially

Price pressure and particularly services inflation keep falling in the UK. Headline CPI inflation slowed to 3.4% YoY in February from 4.0% the month before while core inflation dropped to 4.5% YoY from 5.1%, which will be welcome news for the Bank of England. As was widely expected, the BoE kept rates unchanged at its meeting last week, but with the remaining two hawks now also voting to leave rates rather than to hike them the decision came with a dovish tilt. Gilt yields fell substantially, particularly at the shorter end of the spectrum. Meanwhile, the latest batch of economic data indicates that the UK has emerged from its technical recession. The Composite PMI was at 52.9 in March, signalling moderate growth, while retail sales were flat in February following the strong rebound in January, contrary to consensus expectations of a small drop. Supported by dovish central banks and decent economic numbers, the FTSE 100 enjoyed its best week since September 2023, rising by 2.6%.

Japan

The ending of NIRP comes as no surprise

In a move widely expected amongst financial markets and anticipated in last week's Weekly, the Bank of Japan finally lifted interest rates out of negative territory, with no adverse consequences as a result. The policy rate was lifted 10bps to a range of 0 to 0.1%, while ETF and REIT purchases were ended and yield curve control concluded. This comes as inflation finally appears to be sustainable, helped by the more aggressive than expected wage negotiations in recent weeks. Indeed, last week saw CPI tick higher at the headline level to 2.8% YoY in February from 2.2%, while core, ex food and energy, eased a little, to a still elevated 3.2% YoY. Although economic growth is rather lacklustre, the PMIs improved for March, with Services up to 54.9 and Manufacturing, at 48.2, inching towards expansionary territory. Despite the BoJ tightening, JPY continued its weakening trend, down 1.6% against the USD on the week. The carry trade remains robust, with Japanese rates still extremely low relative to other nations. We are encouraged by the news flow and remain broadly constructive on Japan's prospects.

LatAm

Both the Central Bank of Brazil and Banxico reduce their monetary policy rates

In a unanimous decision, Brazil's central bank cut the Selic rate by 50bps, bringing it down to 10.75%, in line with market expectations. However, its statement indicated that it plans to cut the rate again by 50bps in May and anticipates smaller reductions thereafter. The inflation forecasts were maintained at 3.5% and 3.2% for 2024 and 2025, respectively, and the Selic rate is expected to close at 9.0% in 2024 and 8.5% in 2025.

In Mexico, the central bank unexpectedly cut the monetary policy rate by 25bps, leaving it at 11%. This was a divided decision, with four members voting in favour of a 25bp cut and one member voting to keep the rate unchanged. In its statement, the bank clarified that future decisions would depend on the data, and it anticipates that interest rates will remain high.

We expect both Brazil and Mexico to continue easing. The dynamics of domestic inflation and movements in the Federal Reserve's rates will be key factors.

Equities

Investors ride the wave as markets hit new highs

It doesn't take much to keep the current momentum rolling in global equity markets, but nonetheless, investors were quick to embrace last week's flurry of news. After so many dashed hopes of rate cuts over the last year or so, both the Fed and the BoE provided the clearest indication yet that cuts were imminent, while the SNB actually pulled the trigger. The UK's FTSE index enjoyed a relatively rare jump of 2.6% on the week, eclipsing other European stock markets and the 2.3% gain by the S&P 500, though some Asian markets did better as investors 'buy the mo'. Japanese equities continued to lead the way, as they have thus far this year, with the TOPIX up 5.3% on the dovish tightening by the BoJ, while Korea's KOSPI was up 3.1%, helped by news that Samsung was endorsed by Nvidia as a chip provider. In the US, Alphabet jumped almost 7% on the week in a possible venture with Apple, which showed that the technology sector remains super-hot. There is no doubt that momentum in markets is strong, though there are signs that stocks are a bit ahead of themselves in the short term.

What to Watch

- In the US, consumer sentiment and personal spending numbers will give important insights into the current state of US households while no significant change is expected for Core PCE inflation.
- In the Eurozone, this shortened week sees key March inflation releases. Spanish CPI is out on Wednesday, followed by Italian and French figures released while markets are closed on Friday. Inflation is expected to decline marginally further in March. German unemployment figures are out on Thursday.
- PMI data for China and many other countries across Asia will be key to watch. Japan will publish major activity data, including industrial production, Tokyo CPI, retail sales, job data, and the Tankan Survey. In Australia, inflation data will play a crucial role in guiding the RBA's policy direction.

Disclaimer and cautionary statement

Zurich Insurance Group Ltd

Investment Management
Mythenquai 2
8002 Zurich

173008049 01/22) TCL