December 13, 2024

Weekly Investment Insights

It has been a big week for France, with Notre Dame finally reopening after five years of reconstruction, and Francois Bayrou being named France's fourth Prime Minister of the year. Bayrou has received a lukewarm welcome and will now have to take on the great challenge of getting a 2025 budget through parliament.

Donald Trump has been named Time Magazine's Person of the Year, as the figure who is considered to have had the greatest impact on world affairs in 2024, "for better or for worse", as described by editor in chief Sam Jacobs. To celebrate the recognition, Trump kicked off the trading day by ringing the opening bell at the New York Stock Exchange on Thursday morning.

In the US, tech stocks brought the broader market lower at the end of the week, while European markets were little moved by the ECB's interest rate decision.

All eyes will be on the US next week as investors patiently await another much-anticipated rate cut from the Fed, along with fresh economic forecasts.

ECB cuts deposit rate by 25bps to 3%, keeping the door open to further easing

The ECB cut interest rates by 25 basis points at its December meeting, removing the reference to the need for a "sufficiently restrictive" policy rate. At the same time, it lowered its inflation and growth forecasts. The euro was unchanged after the widely anticipated cut.

This is the fourth cut in borrowing costs since the ECB began lowering rates in June this year, taking the rate to its lowest level since March 2023. The decision was accompanied by a warning that growth in the Eurozone will be weaker than originally forecast, reaching 0.7% in 2024 and 1.1% in 2025.

The ECB noted that inflation is heading in the right direction and is expected to fall to 2.1% in 2025, just shy of its 2% target. However, the EBC said it will continue to monitor progress and take a 'data-dependent and meeting-by-meeting approach' to determine the future path of monetary policy based on potential changes to this inflation outlook.

With Donald Trump likely to reignite inflation at home, and the Eurozone lagging the US in terms of growth, the ECB is expected to cut rates more than the Fed next year until it reaches a neutral rate. The key question now is: what is a neutral rate for the ECB? Markets expect up to five more 25bps cuts by September 2025, which would take the deposit rate to 1.75%. On the other hand, most policymakers see the neutral rate as being somewhere between 2% and 2.5%.

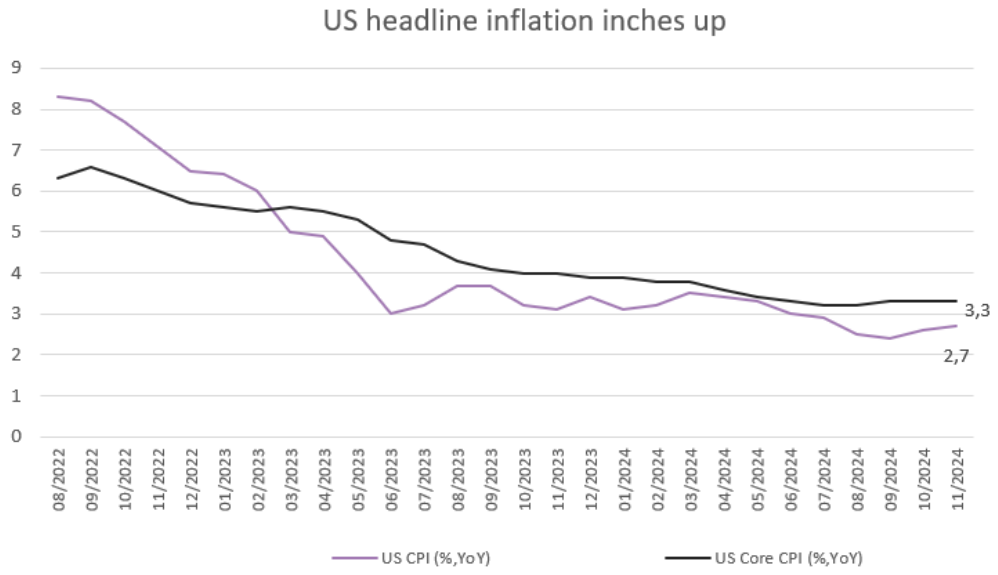
US inflation rises to 2.7% in November

US inflation edged up to 2.7% YoY last month, up from 2.6% prior and matching expectations. The rise is partly influenced by low base effects from last year: Energy costs declined less (-3.2% vs -4.9% in October). Around 40% of the monthly increase in inflation was due to the shelter component, with government figures slow to catch up with more timely real-life trackers which show costs therein are already on a downward slope.

Core inflation held steady at 3.3%, also in line with forecasts.

Following the release, which was free from any nasty upside surprises, traders see another 25bp cut at next week's FOMC as a "done deal". That would bring interest rates to a new target range of 4.25-4.5%. However, as we move into the new year, that trajectory of rates becomes trickier to chart. The Fed must keep policy firm enough to anchor inflation close to 2% but relaxed enough to prevent further cooling in the labour market. Potentially inflationary policies from Trump, including trade tariffs and an immigration crackdown, complicate that task further.

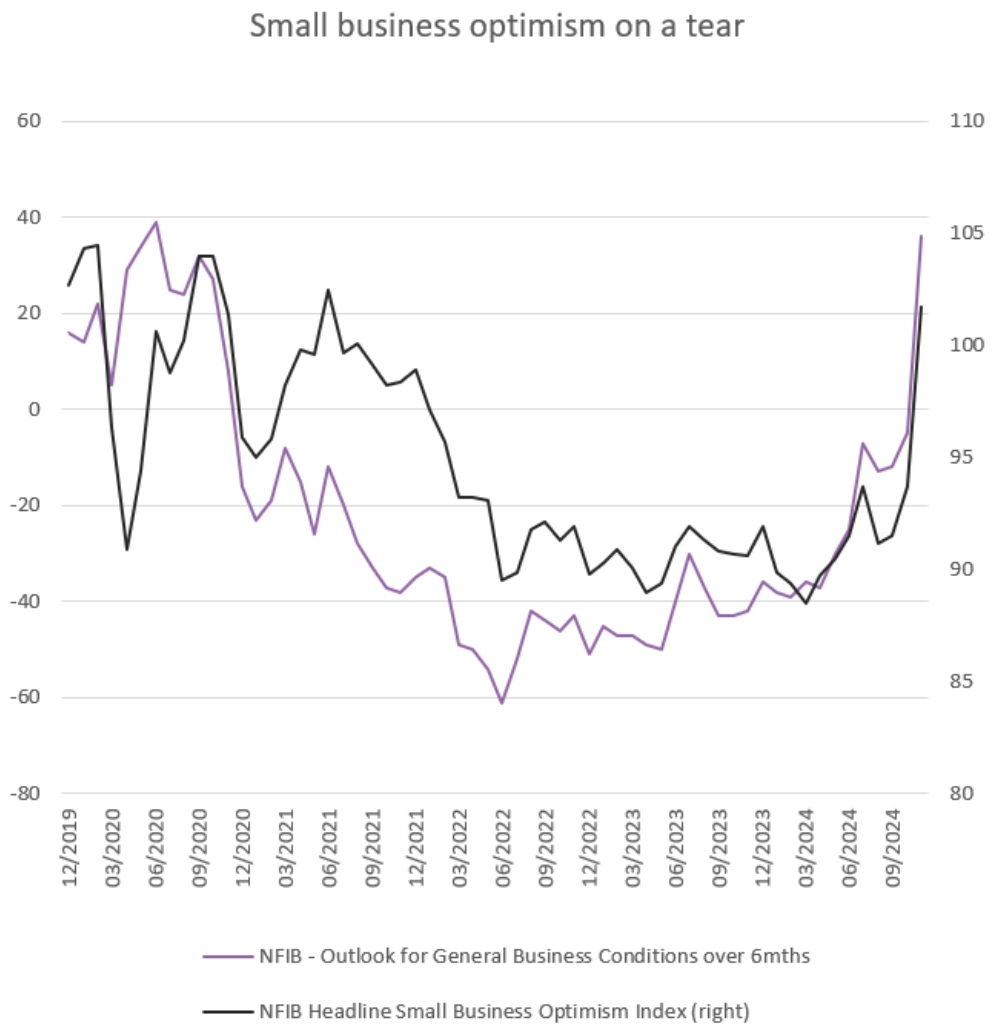
The Fed will likely want to give itself as much optionality as possible.



Source: Bloomberg, BIL

US Small Business Optimism hits highest level since June 2021

With the **composite PMI at a 31-month high**, we know that **activity among America's large corporates is running strong**. But **what about the small companies** that **account for roughly half of US gross domestic output**? The **NFIB survey**, which focuses on Main Street rather than Wall Street, shows that they are **increasingly optimistic about the future** too. This is particularly following the **election of Trump** which could usher in a **major shift in economic policy**: owners are particularly **hopeful about tax and regulation policies** that promote domestic growth as well as a relief from inflationary pressures. The **net percent of owners expecting the economy to improve** rose 41 points from October to a net 36%, the **highest since June 2020**. Expected credit conditions also improved, but from low levels.



Source: Bloomberg, BIL

Swiss Franc Weakens on SNB surprise

On Thursday, the Swiss National Bank cut its interest rate by a larger-than-expected 0.5 percentage points amid undue strength in the Franc with traders having piled into the perceived safe-haven as of late. Consensus expectations among economists had pointed to a smaller 0.25 percentage point cut. The Franc fell by around 0.6% after the announcement, pulling away further from a near-decade high against the euro.

The move marked the steepest drop in borrowing costs since the SNB's emergency rate cut in January 2015 when it suddenly quit its minimum exchange rate with the euro.

Against a backdrop of decreasing inflationary pressures, the SNB tweaked its wording to say it will "adjust its monetary policy", stepping away from a more explicit statement signaling "further cuts". However, this doesn't mean further easing is off the cards. Incoming President Martin Schelgel has said he wouldn't rule out the use of negative rates.

Calendar for the week ahead

Monday – US, Eurozone, UK, Japan Flash PMI (December). China Industrial Production, House price Index, Retail Sales, Unemployment and 1-Year MLF Announcement. Eurozone Labour Costs and Wage Growth (Q3).

Tuesday – UK Unemployment and Pay data. Germany IFO Business Climate Index (December), ZEW Economic Sentiment (December). US Retail Sales, Industrial Production (both November), and NAHB Housing Market Index (December).

Wednesday – UK Inflation (November). Eurozone Inflation (Final, November). US Building Permits and Housing Starts (November), Federal Reserve Monetary Policy Meeting with refreshed economic projections.

Thursday – Bank of Japan and Bank of England Monetary Policy Meetings. Germany Gfk Consumer Confidence (January). France Business Confidence (December). US GDP Growth (Q3, Final), Weekly Jobless Claims, Existing Home Sales (November)

Friday – Japan Inflation (November). China Loan Prime Rate. UK Retail Sales (November). US Personal Income and Spending and PCE Inflation (November), Michigan Consumer Confidence (December, Final). Eurozone Consumer Confidence (December, Flash).

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