FE Investments

GOVERNMENT BONDS FALL AS MARKETS PUSH BACK THEIR EXPECTATIONS FOR FED RATE CUTS

This week has witnessed considerable volatility in government bond markets as traders tackled conflicting signals from the US economy. The monthly nonfarm payrolls report, released last Friday, showed a mixed picture, with strong job growth but rising unemployment and a noticeable slowing of wage inflation. This was seen as positive for the chances of a rate cut by the Federal Reserve before summer. However, a small but surprising increase in CPI was followed by an increase in producer price inflation, while consumer spending shows no signs of slowing. This adds weight to the argument in favour of keeping rates high, and US treasury bonds led other government debt lower.

In the UK, monthly GDP turned positive in January after the economy entered recession in 2023. It is good to see an increase, but one month's data is not enough to get excited about. It also complicates things for the Bank of England as it conflicts with the slight deterioration in the jobs market. With the exception of Japan, markets are expecting little movement from central banks in the next few rounds of interest rate meetings.

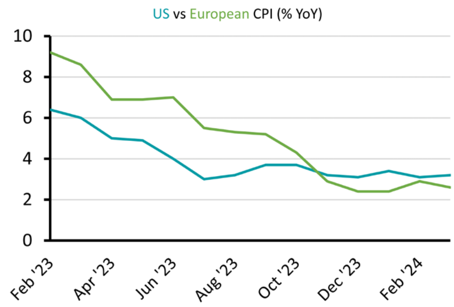
THE MARKETS THIS WEEK

FTSE 100	S&P 500	Nikkei 225	MSCI Europe	Hang Seng	US 10 Yr	UK 10 Yr	Brent Crude	Gold	Iron Ore	GBP USD
+1.09%	-0.01%	-1.56%	+0.40%	+2.29%	-0.21%	-0.17%	+1.57%	+0.79%	-10.97%	-0.62%

US: RISING INFLATION AND STRONG SPENDING WEIGH ON US GOVT BONDS

US inflation increased unexpectedly driven by strong prices rises in some services. CPI increased from 3.1% to 3.2% as rising insurance, health and housing costs offset a decline in energy costs. US treasury yields fell after last week's employment figures showed unemployment had risen and wage inflation slowing. However, treasuries declined, pushing yields up, as the inflation update and strong consumer spending forced markets to reconsider whether the Federal Reserve will cut rates as early as expected.

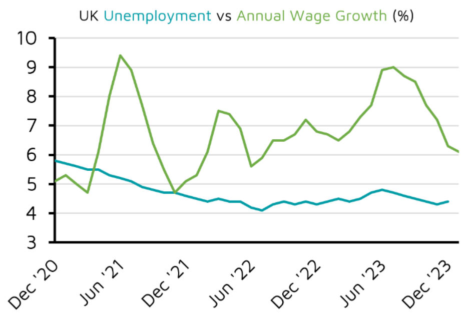
A number of Wall Street figures, including JP Morgan chief executive Jamie Dimon, warned the Federal Reserve to be cautious about reducing rates. The Fed's is meeting to set interest rates next week and it is expected to leave them unchanged. Meanwhile, a big drop in German inflation helped the case for an early rate cut in Europe as two members of the ECB suggested rate cuts are likely soon. The Bank of Japan is also setting interest rates and the yen has been rising in anticipation of a rate hike following above inflation pay settlements.



UK: GDP RISES IN JANUARY BUT SIGNS THE JOBS MARKET IS COOLING

The jobs market in the UK remains robust but there are more signs of a slowdown. Unemployment increased slightly to 3.9% and the number of people who are economically inactive increased again. Wage inflation also continues to slow and recruitment firm Reed reports that job vacancies have fallen to the lowest in three years.

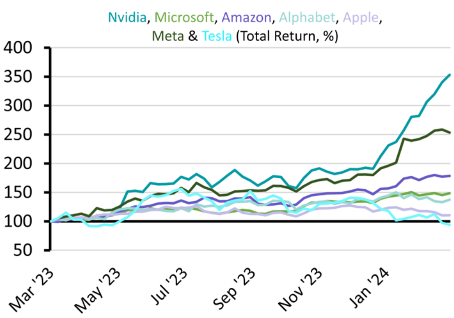
The UK economy returned to growth in January after entering recession in the second half of 2023. Monthly GDP increased by 0.2%, mainly due to a pick-up in services activity. However, growth remains weak. After adjusting for inflation, GDP declined by 0.1% over the three months to end of January. Bank of England governor Andrew Bailey said the UK is close to or at full employment but says the Bank of England does not need to see any deterioration in employment before cutting rates as the risks of wage growth fuelling further bouts of inflation has receded. The data means the outlook for interest rate cuts remains unchanged ahead of next week's interest rate meeting as sterling fell slightly.



TECH: TESLA APPEARS OUT OF STEP WITH OTHER US TECH GIANTS

US tech stocks have been mostly unaffected by signs that US interest rate cuts may be delayed. In contrast to 2023 when inflation or employment updates regularly moved markets, this year tech stocks have been unmoved by the changing outlook for interest rates. Instead, they have been driven by good earnings updates and investor enthusiasm for growth stocks. However, Tesla and Apple have started to diverge from other tech giants as disappointed sales updates and other negative news drag on share prices.

Apple's sales in China have slowed as buyers look for cheaper, domestic alternatives and it is facing regulatory pressure in Europe. Tesla is also facing headwinds as demand for pricier electric cars has fallen and it loses market share. In China local firms now sell far more than Tesla and it is facing growing competition elsewhere. Tesla has cut prices to boost sales, but its shares tumbled in January after it said sales would be noticeably lower in 2024 and they fell again this week as analysts forecast there will be no sales growth in 2024.



Data sourced from St Louis Federal Reserve, Office for National Statistics and Yahoo Finance