The Weekly Snapshot

22 April 2024

ANZ Investments brings you a brief snapshot of the week in markets

Markets were in a risk-off mode following a period of growing tensions between Iran and Israel, which culminated in a retaliatory strike by Israel on Iran late in the week. Luckily, markets viewed Israel's response as being limited and designed to minimise escalation.

Nevertheless, international equity markets were sharply lower, with other news being centred around inflation and central bank rhetoric. The S&P 500 Index in the US delivered five back-to-back days of decline, meaning it finished the week down 3.0%. Technology stocks were amongst the biggest losers, given a significant pull-back in this sector, which saw the Nasdaq 100 Index fall 5.4%. Nvidia, the chip company that has driven the sector's recent strong gains, was down 13.6% over the week.

Markets in most of the other major regions also declined, although losses in European markets were muted. The biggest loser was Japan, whose equity market has recently been trading at record highs. The Nikkei 225 Index fell 6.2% as inflation data there surprised on the softer side. It comes as its central bank only recently began raising interest rates and ahead of its next policy meeting this week.

With equity markets on the back foot, you would have thought that safe-haven bonds would have been higher. However strong economic data continues to weigh on the market, which saw the US 10-year bond yield rise 10 basis points to 4.63% (when bond yields rise, their prices fall). However, New Zealand bond yields were 3 basis points lower.

Surprisingly, the price of oil did not head drastically higher – in fact, following a brief push higher on news of Israel's strike, the price of a barrel of West Texas Crude actually fell by around $3 over the week to $83, although the price of gold did hit an all-time high.

What's happening in markets?

Speaking at a central bank forum last week, and on the back of the prior week's stronger-than-expected inflation reading (where March CPI came in at 0.4%, and annual inflation at 3.5% - both higher than forecast), US Federal Reserve Chairman, Jerome Powell, said there had been a *"lack of further progress"* this year on the inflation front. He went on to say its interest rate committee would need greater confidence that inflation is moving sustainably towards 2% before it would be appropriate to ease policy.

> ***"The recent data have clearly not given us greater confidence, and instead indicate that it's likely to take longer than expected to achieve that confidence"*** he said.

The Fed has previously indicated that it intends to cut interest rates this year, however, the timing of such a move is now up for debate given sticky inflation and persistent economic strength. Markets had been expecting the first cut to come in June, but following last week's remarks, this has shifted to September, with some even suggesting the first interest rate cut may not take place until 2025.

The remarks highlighted the widening gap between expectations for the US Federal Reserve and other central banks, in particular, the European Central Bank, whose president, Christine Lagarde, also spoke last week. Europe has seen inflation continuing to head lower, while the US has seen it edge higher.

> ***"If we don't have a major shock in developments, we are heading towards a moment where we have to moderate the restrictive monetary policy that we have, in reasonably short order"*** she said.

Meanwhile in New Zealand, the key focus was also on inflation data, where the annual rate of CPI dropped to 4% in March, down from 4.7% in December. While price increases are the smallest since June 2021, it was still higher than the 3.8% the Reserve Bank of New Zealand had itself been forecasting – and above its 1-3% target range.

The biggest driver behind overall inflation were increases in housing and household utility costs. Non-tradeable inflation was 5.8%, which was almost as high as the 5.9% reported in December. Non-tradeable inflation typically looks at the prices of goods and services that do not face foreign competition and is therefore a good indicator of domestic demand and supply conditions.

What's on the calendar?

The focus this week will be on data in the US, including first quarter GDP (Gross Domestic Product) and the US Federal Reserve's preferred measure of inflation – the core PCE (Personal Consumption Expenditures) Index. In the fourth quarter of last year the US economy grew at a blistering pace of 3.4%, so market watchers will be keen to see if this has slowed, while signs of higher-than-expected PCE inflation could add to market worries over future policy when it comes to the path of interest rates.

Elsewhere, investors will be looking to the Bank of Japan's interest rate decision on Friday. At its last meeting the central bank called an end to its negative interest rate policy, but recent inflation data has come out softer than expected, while the yen has fallen to its lowest level against the US dollar since 1990. The market expects Japanese interest rates to continue to rise, however, they are not anticipating any change this week.

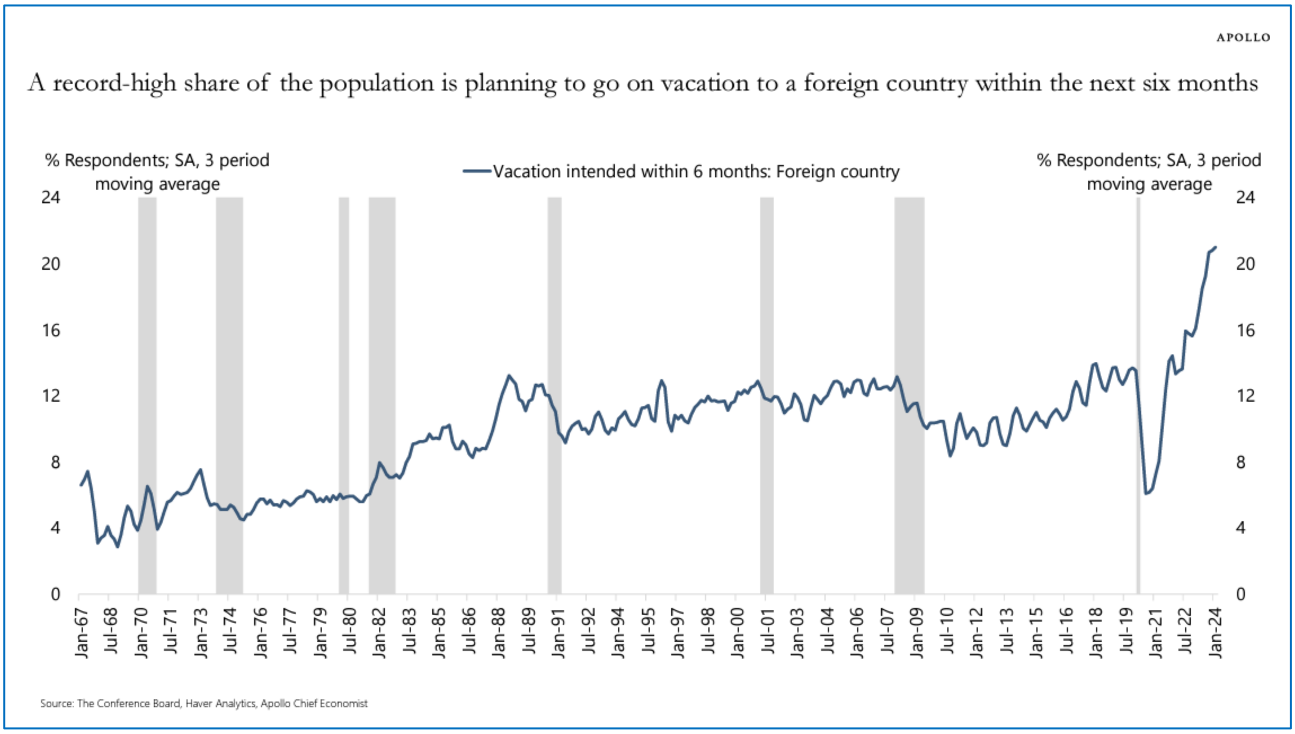
Finally, all eyes will be on first quarter earnings season, with investors looking to see how companies are coping in the high interest rate environment.

Chart of the week

The below chart shows that a record number of US consumers plan to vacation in a foreign country in the next 6 months. Over 20% plan to visit a foreign country, well above the pre-pandemic levels of 10-14%.

Greater demand for travel is being driven by wealth gains. Thanks to a significant rise in the stock market and cash flows from bonds, US households have more money to travel on airplanes, stay at hotels, eat at restaurants, go to sporting events, amusement parks, and concerts. That is why inflation in the non-housing service sector continues to be so high.

The bottom line is that interest rates could stay higher for longer if strong gains in employment and wealth continue to provide a tailwind to consumer services.



Here's what we're reading

Josh Brown:
Three things to remember in times like these. Click here.

Jason Zweig:
Instead of viewing behavioural economics as a window, we should regard it as a mirror. Click here.