Article MARKET COMMENTARY

Market round-up: 30 October – 03 November

We recap the week and take a look ahead to next week.

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This week just ended

Even a week filled with central bank meetings and crucial economic data releases could not spook financial markets during Halloween week, with equities in particular up strongly for the week.

We had a triple-header of central bank meetings, the Bank of Japan (BoJ) kicked us off on Tuesday with the baton hamded to the Federal Open Market Committee (FOMC) on Wednesday and finished off by the Bank of England (BoE) on Thursday. Whilst the former still has not raised interest rates from their sub-zero level, the latter two are at the other end of the spectrum and questioning

whether they have reached a peak having risen interest rates up to 5.50% and 5.25%, respectively.

Debate around how long the BoJ's persists with its yield curve control (YCC) and ultra-loose monetary policy has continued to build. Their latest change was related to YCC whereby they effectively increased the ceiling on their 10-year government bond yield to 1%, in a sign they are beginning to slowly move away from the unorthodox policy of YCC.

Credible rumours circulated on Monday ahead of this week's BoJ meeting that they would announce a significant further change to YCC, with the Yen strengthening in the build-up to the meeting as a result. In the end, the central bank did communicate changes had been made to their YCC policy, by making the 1% ceiling discussed above a soft limit rather than hard. The market, clearly disappointed there wasn't more drastic change being implemented, made their feelings known as the Yen weakened -1.7% versus the US Dollar, losing all its previous day gains the previous day.

The FOMC, as expected, did not make any changes to policy at this meeting by leaving interest rates unchanged. The past 12-18 months the focus has been on how high the Federal Reserve (Fed) will raise interest rates – it is increasingly likely that we are there, with this the second meeting in a row they have left rates unchanged. Indeed, Fed governor Jay Powell reiterated that interest rates are at restrictive levels and the market is not pricing in any further interest rate rises from here. As such, the focus of markets seems to be shifting from 'how high?' to 'how long will they remain high?'.

Rounding off the central bank meetings was the BoE who pulled no surprises by voting in favour of keeping interest rates level. As with the Fed, the question for the BoE is how long do they expect to keep interest rates this high? The central bank reiterated its 'higher for longer' guidance by promising to keep interest rates "sufficiently restrictive for sufficiently long". In fact, BoE governor Andrew Bailey warned it is "much too early to be thinking about rate cuts". Despite this, gilt yields fell significantly on the day.

Although yields on US Treasuries have fallen this week, over the past few months they have risen dramatically due to a variety of reasons. One of these reasons is that an increased supply of US Treasuries will be required to finance the Treasury's increasing funding requirements. Hours prior to the FOMC meeting the Treasury announced the level of US Treasuries it would issue, which was lower than the market expected. This surprise was an additional factor behind yields falling this week.

Staying with the US, another surprise came from the latest reading of the ISM Manufacturing index, which tracks the general state of the US manufacturing sector. October's reading was released, which came in lower than all Bloomberg estimates at 46.7. A reminder that a reading below 50 indicates contraction, with the index remaining under 50 each month since October 2022.

The Fed would have been hopeful that any surprise frights would be restricted to Halloween celebrations and not the US jobs report published just before we went to print on Friday. As it happened, they would have welcomed the report which seemed to endorse the notion that their past tightening is starting to have the desired cooling effect on the US labour market. The bumper September Non-farm Payrolls figure was revised down by 39,000 jobs, while only 150,000 jobs were created during October, which is 30,000 less than consensus forecasts. Unemployment ticked up from 3.8% to 3.9%. Importantly, with all the focus on inflation, average hourly earnings continued to moderate, declining from 4.3% to 4.1%. This is likely a bit higher than the Fed would be comfortable with, but they will take comfort in its moderating trend. The report added further fuel to this week's rally in US Treasuries and other fixed income assets, as investors bet that the slowdown in the labour market make it more likely that the Fed has reached the end of its rate-rising cycle.

This coming week

Next week is shaping up to be a quieter one, following on from a busy week of both central bank meetings and data releases.

At the start of the week, we will be focusing our attention on the Euro Area, with finalised October readings for Services and Composite Purchasing Manager Indices (PMIs). The Eurozone PMIs have been a significant weakness in the bloc's economy, with the Eurozone Composite PMI out in contractionary territory (sub-50) each month since June after a stronger start to the year.

The strength earlier in the year in part came from optimism that Eurozone growth would benefit from China's re-opening and easing of lockdown rules due to their close trading ties – indeed, China is Europe's biggest trading partner. China's lacklustre rebound following this re-opening is being felt in Europe and this is indicated by the fact the Eurozone October Composite PMI is expected to remain at 46.5.

Wage growth and household spending for Japan is also on our list to focus on, which will be released after we awake on Tuesday morning. The update on the consumer is for September, where the picture has been quite negative. Whilst year-on-year earnings growth has been positive, when you account for inflation, it has been negative. Year-on-year Real Cash Earnings is expected to be -2.4%. This is understandably having an impact on Household Spending, which is expected to fall by a larger magnitude of -2.7% year-on-year.

Japan's Prime Minister, Fumio Kishida, has been feeling the effects of real wage losses for consumers, with his approval ratings falling. It is for this reason Kishida announced this week a stimulus package worth around $110bn. The consumer is at the heart of the plans, which includes income and residential tax rebates for low-income households.

Rounding off the week on Friday is a range of economic trade data for the UK, including a first look at Q3 GDP growth. Q1 and Q2 growth was not exactly booming, but it was in positive territory at 0.3% and 0.2% respectively. Whether this positive trend continues hangs in the balance with a consensus estimate of 0.0%. Regardless, economic growth is concerning across Europe – the Eurozone posted a negative Q3 GDP figure of -0.1% this week.

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