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Article MARKET COMMENTARY

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Tom Watts recaps the week and looks ahead to next week.

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This week just ended

With much of the headlines in North America this week focussing on the moon passing between the Sun and the Earth, it would take some pretty large financial news to avert even economists' gaze. However, standout US inflation figures, released on Wednesday did just manage to eclipse the lunar spectacle...

Coming in at 3.5% on an annual basis, ahead of expectations of 3.4% and rising from 3.2% last month, the data showed that price rises in the US show no signs of disappearing into the shadows just yet. Gasoline and shelter accounted for more than half of the increase in the Consumer Price Index this month with food prices only rising 0.1%. This suggested that the pick-up in inflation during January and February could not be solely attributed to businesses raising prices at the start of the year as many economists had argued.

Coupled with last week's stronger than expected jobs data, investors quickly pushed back their expectations for the US Federal Reserve to start their rate cutting cycle in the summer. Expecting now only two rate cuts instead of the three envisaged by Fed officials last month, markets are pricing in just a 17% chance the Fed will cut rates in June, down from a roughly 62% chance a week ago. Investors also pushed bets for a July cut closer to 41% from around 76% last week.

Sadly, markets can't just do what the moon managed this week and block it all out, with US indices the worst affected by the persistently strong data, with the broader S&P 500 falling 0.95%, and the technology heavy Nasdaq slipping 0.84%. In the bond markets, the two years note yield, which typically moves in step with interest rate expectations, rose 22 basis points to 4.97%, after hitting its highest level since mid-November.

Stoking inflation worries further, Oil prices rallied after three sons of a Hamas leader were killed in an Israeli airstrike in the Gaza Strip, fuelling worries that ceasefire talks could stall. The strike also raised concerns that the continued conflict could drag in other countries, particularly Hamas-backer Iran, the third largest producer in the OPEC group.

Also enjoying its place in the sun this week, the European Central Bank (ECB) held rates steady on Thursday, whilst signalling it could start cutting as soon as June. The bank sought to remove language committing it to holding rates steady for a "sufficiently long duration", suggesting easing is on the way. ECB President, Christine Lagarde, said in Thursday's press conference that if a fresh assessment increased policymakers' confidence that inflation is heading back to target, then it "would be appropriate" to cut interest rates, a comment taken as affirmation of a June move.

Much like the moon moving in front of the sun, it seems that the recession the UK economy slipped into towards the end of last year could also just be a phase, as monthly data released on Friday showed the economy grew by 0.1%, largely boosted by the manufacturing sector. January's reading was also revised to show the sun has been shining on the economy more than thought with growth of 0.3%, up from 0.2% earlier reported, showing the domestic economy started 2024 on a stronger footing, with the three-month average growth rate rising to 0.2% in February from zero in January, the highest such reading since August.

Such data is likely to reinforce the Bank of England's cautious tone around the prospect for interest rate cuts, with the economy on track to slightly exceed the central bank's expectation for a 0.1% expansion in the first quarter.

With such a raft of positive news and rising metal and oil prices aiding the commodity heavy FTSE 100, the index made its way past the symbolic 8,000 mark, just short of a record high. Not too bad for an index that has endured its fair share of criticism of late, often considered a place where the sun don't shine...

This coming week

After a busy week for European markets, seemingly gearing up for a central bank rate cut in June on the continent and the UK blue chip index getting close to all-time highs, the US index has been somewhat shunned by investors.

The beginning of the coming week should rectify this somewhat, with Monday seeing a raft of US data being released from various sources. Perhaps the most striking will be US Retail Sales figures due to the association with the consumer. How much the average person on the street is spending at the shops acts as the primary gauge of consumer spending, which in turn, accounts for most overall economic activity. The data also gives us some insight into how various retailers are faring on what is becoming an increasingly competitive sector.

Alongside the data we also have the latest Empire State Manufacturing Index reading, a survey of manufacturers from the New York State area. Respected by economists due to its sheer breadth, the survey of about 200 manufacturers in New York state which asks respondents to rate the relative level of general business conditions. The data is also useful as it acts as a leading indicator of economic health, businesses react quickly to market conditions and changes in their sentiment can be an early signal of future economic activity such as spending, hiring and investment.

During the middle of the week, attention will be firmly on domestic shores as not only do we receive a speech from Bank of England (BoE) Governor, Andrew Bailey on Tuesday evening, but the Office for National Statistics also releases its inflation numbers the following day. With those at the BoE seemingly visibly torn in their rate setting committees, the week's CPI data could go a long way it helping to form a clear path for the central bank to start cutting rates in July.

The coming week should be wrapped up here in the UK too as the domestic equivalent of the US's earlier retail sales figures is released here. With news that the country's largest supermarket, Tesco, saw profits soar by 160%, to £2.3 billion, whilst commenting that price pressures are easing 'substantially' amid the cost-of-living crisis, I will be interesting to see if more broad, official figures back this sentiment up.

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