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Global Markets Weekly Update

ECB's Lagarde: "The worst part is behind us" in inflation fight

Highlighted Regions

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U.S.

Stocks resume advance as earnings season kicks off

Stocks moved higher over the week, with large-cap growth stocks and the technology-heavy Nasdaq Composite Index outperforming the broader market. Several tech giants recorded solid gains, including Facebook parent Meta Platforms and chipmaker NVIDIA. Energy stocks underperformed as oil prices pulled back early in the week. The week brought the unofficial start of earnings season, with the nation's four largest banks—JPMorgan Chase, Citigroup, Bank of America, and Wells Fargo—reporting fourth-quarter results on Friday. Markets were scheduled to be closed the following Monday in observance of the Martin Luther King, Jr. Day holiday.

Consumer inflation surprises on the upside, producer inflation on the downside

Data releases on the week's light economic calendar came in roughly in line with expectations, but investors appeared to pay especially close attention to inflation data. Stocks wavered a bit on Thursday morning following the Labor Department's release of consumer price inflation data. Headline prices rose 0.3% in December, a tick more than expected, but core (less food and energy) costs also rose 0.3%, in line with consensus. For 2023 as a whole, core prices rose 3.9%, marking the slowest 12-month pace since mid-2021.

Feedback

Producer price data, released Friday morning, was somewhat more encouraging. Headline wholesale prices fell another 0.1% in December, marking the third consecutive monthly decline. For 2023 as a whole, prices rose 1.0%, while core prices increased 1.8%, less than expected and below the Federal Reserve's overall inflation target of 2.0%.

The labor market appeared to be in good shape as the new year began. The Labor Department reported that 202,000 workers filed for unemployment benefits in the previous week, well below expectations and the lowest number since mid-October, while 1.83 million filed continuing claims, also the lowest level since October.

Business owners and consumers grow a little less pessimistic

Two surveys released during the week indicated that both small business owners and consumers remained pessimistic about the economic outlook, although somewhat less so than in recent months. The RealClearMarkets/TIPP Economic Optimism Index stayed in negative territory in January but rose to its highest level since April. The optimism increase among investors was particularly notable, probably reflecting December's strong market performance. The NFIB Small Business Optimism Index also rose more than expected and hit its highest level since July.

Fixed income investors appeared unswayed by the modest upside surprises in the consumer inflation data, with the yield on the benchmark 10-year U.S. Treasury note falling back below 4% over the week. (Bond prices and yields move in opposite directions.) Our traders noted that, while the Treasury auction sizes were unchanged, the Federal Reserve Bank of New York's use of reverse repurchase agreements (or reverse repos) declined to its lowest level in a year on Thursday. Reverse repos encourage banks to place money with the Federal Reserve, thereby draining assets from the banking system and cooling growth and inflation. This may suggest that the Fed's program of quantitative tightening—a contractionary tool—could soon slow and eventually come to an end.

According to our traders, short-maturity municipal bond yields increased. Regarding muni market technicals, reinvestment cash from January coupon payments countered an uptick in new issuance, and the new issues that reached the market were met with strong demand.

Our traders reported that the high yield bond market felt generally firmer amid broad risk-on sentiment and as equities rallied before the release of consumer price data. They noted that the higher-than-expected consumer inflation data seemed to have a negligible impact on investors, and the deals that came to the market were well received.

Index	Friday's Close	Week's Change	% Change YTD
DJIA	37,592.98	126.87	-0.26%
S&P 500	4,783.83	86.59	0.29%
Nasdaq Composite	14,972.76	448.69	-0.26%
S&P MidCap 400	2,728.63	16.13	-1.90%
Russell 2000	1,950.96	-0.18	-3.75%

This chart is for illustrative purposes only and does not represent the performance of any specific security. ***Past performance cannot guarantee future results.***

Feedback

Source of data: Reuters, obtained through Yahoo! Finance and Bloomberg. Closing data as of 4 p.m. ET. The Dow Jones Industrial Average, the Standard & Poor's 500 Stock Index of blue chip stocks, the Standard & Poor's MidCap 400 Index, and the Russell 2000 Index are unmanaged indexes representing various segments of the U.S. equity markets by market capitalization. The Nasdaq Composite is an unmanaged index representing the companies traded on the Nasdaq stock exchange and the National Market System. Frank Russell Company (Russell) is the source and owner of the Russell index data contained or reflected in these materials and all trademarks and copyrights related thereto. Russell® is a registered trademark of Russell. Russell is not responsible for the formatting or configuration of these materials or for any inaccuracy in T. Rowe Price's presentation thereof.

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Europe

In local currency terms, the pan-European STOXX Europe 600 Index ended the week little changed, as traders assessed the prospect of interest rates staying higher for longer than previously expected. Major stock indexes were mixed. Germany's DAX added 0.66%, France's CAC 40 Index gained 0.60%, and Italy's FTSE MIB ticked modestly higher. The UK's FTSE 100 Index fell 0.84%.

European government bond yields endured a volatile week as dovish comments by European Central Bank (ECB) policymakers were offset by moderating market expectations for an interest rate cut in the near term. The benchmark 10-year German government bond yield ended the week near 2.2%. In the UK, the yield on the benchmark 10-year government bond edged higher after data indicated that Britain's economy grew slightly more than expected in November.

ECB's Lagarde says worst of inflation fight likely over

ECB President Christine Lagarde said in an interview on French television said that she thought "the worst part is behind us" in the battle to bring down inflation. She also asserted that interest rates had probably reached their peak. "I think that rates, barring any further shocks or unexpected data, will not continue to go up," she said. "And if we win our fight against inflation, and if we are certain that inflation will indeed be at 2%, at that point rates will start to go down." However, she declined to say when these rate cuts would occur.

Eurozone data indicate economy may still be stalling

Official data indicated that the labor market remained resilient amid an economic slowdown. The euro area unemployment rate stood at 6.4% in November, down from 6.5% in October. However, there are some signs that the labor market might be correcting. Total hours worked fell slightly in the third quarter—the first since the end of 2020—while job vacancies have declined in recent months. Meanwhile, retail sales volumes shrank 0.3% sequentially in November, after growing 0.4% in October.

Germany's industrial output unexpectedly declined 0.7% sequentially in November, in part because of shrinking orders in manufacturing. New orders increased by 0.3% month over month on a seasonally adjusted basis, falling short of expectations.

UK economy bounces back in November

The UK economy grew 0.3% in November, reversing a decline of the same magnitude in October, thanks to strong gains in services and industrial businesses. This month-over-month uptick in gross domestic product came in above the consensus forecast for a 0.2% expansion in a FactSet poll of analysts. Nevertheless, the economy still struggled over three months through November, contracting 0.2% on widespread weakness across manufacturing industries.

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Japan

Japan's stock markets registered strong gains over a holiday-shortened week (they were closed on Monday), with the Nikkei 225 Index rising 6.6% and the broader TOPIX Index up 4.2%. The continuation of highly stimulative monetary policy and weakness in the yen, which boosted Japan's exporters, helped the indexes rally to their highest levels in almost 34 years.

Meanwhile, the yen hovered at its lowest levels in around a month, weakening past JPY 145 against the U.S. dollar, as a hot U.S. inflation print tempered expectations about how soon the Federal Reserve might cut interest rates. The yield on the 10-year Japanese government bond fluctuated around 0.6% during the week, struggling for clear direction.

Economic news supports continuation of highly stimulative monetary policy

Investors appeared to scale back their bets about the likelihood that the Bank of Japan (BoJ) could imminently reverse its negative interest rate policy. The chances of near-term policy normalization had already receded in the aftermath of the deadly earthquake in Japan's Noto Peninsula, the impact of which the central bank continued to assess during the week.

The latest economic data releases appeared supportive of monetary policy continuity. Headline wage growth slowed sharply in November, while the Tokyo core consumer price index, a leading indicator of nationwide price trends, rose 2.1% year on year in December, the slowest pace since June 2022, and down from 2.3% in November. The BoJ has repeatedly stated that it will maintain its ultra-accommodative monetary policy stance until it sees a sustainable rise in inflation driven by wage growth.

Prime Minister Fumio Kishida said recently that the government would mobilize all its policies to ensure that growth in disposable income exceeds price rises. The chief of Rengo, Japan's biggest trade union federation, said that it is very important to achieve wage increases for the second year in a row at this year's spring shun to pay negotiations and at a level even higher than in the round of talks held in 2023.

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China

Chinese equities retreated as data showed that China's deflationary cycle persisted into December, raising expectations of increased government support in 2024. The Shanghai Composite Index declined 1.61%, while the blue chip CSI 300 gave up 1.35%. In Hong Kong, the benchmark Hang Seng Index fell 1.76%, according to FactSet.

The consumer price index fell 0.3% in December from the prior-year period, the third monthly decline, easing from November's 0.5% drop as lower pork prices continued to weigh on food prices. The producer price index declined 2.7% from a year ago compared with November's 3% drop, and marked the 15th monthly decline. The latest inflation data raised expectations for some analysts that China's central bank would lower its key policy rate and inject more cash into the financial system at its next policy meeting amid worries that sustained deflation will increasingly weigh on the economy.

In other economic news, China's exports rose a better-than-expected 2.3% in December from a year earlier, up from a 0.5% rise in November. Exports to Europe and Southeast Asian nations improved, while U.S. shipments fell following a brief rise in November. Imports edged up 0.2% in December, rising from November's 0.6% decline. December's improved results were likely boosted by the low base effect of China's pandemic lockdowns in the prior-year period, which dampened economic activity. The overall trade surplus rose to USD 75.34 billion, up from November's USD 68.39 billion. However, China's exports fell 4.6% in 2023, its first annual decline in seven years as global demand softened.

Feedback

In geopolitical developments, Chinese officials announced new sanctions on five U.S. defense companies in response to the U.S.'s latest weapons sales to Taiwan. Measures included freezing the U.S. companies' local assets and prohibiting domestic organizations from initiating any transactions with them. The move was largely seen as a retaliation after the U.S. State Department approved an estimated USD 300 million in possible military sales to Taiwan that were disclosed in December.

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Other Key Markets

Mexico

During the week, the government issued inflation data for December. Headline inflation was 0.7% month over month, while the year-over-year rate was 4.7%. Both numbers were marginally above expectations, which T. Rowe Price emerging markets sovereign analyst Aaron Gifford attributes to volatile prices of non-core items. However, Gifford also noted that core inflation readings—which exclude more volatile food and energy costs—were slightly lower than expected. Month-over-month core inflation was 0.4%, while the 12-month core inflation rate was 5.1%.

Overall, Gifford believes that Mexican central bank officials will be pleased with the core readings. However, he expects them to remain vigilant against broader inflation—and unlikely to consider imminent interest rate cuts—until there are clearer signs of longer-lasting disinflation.

Brazil

Brazil's government reported that inflation in December increased 0.56% month over month, which was slightly higher than expected. However, the underlying data in the inflation report were mixed. For example, a big part of the upward surprise was non-core food prices, which could be discounted by central bank officials. However, there has been some deterioration in the inflation picture, as indicated by services price inflation picking up a bit, as well as some higher inflation in manufactured goods. Considering the upward surprises in recent inflation readings—most of which stems from price increases of non-core items—policymakers could become more cautious regarding the pace of Brazilian disinflation.

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