22 March 2024

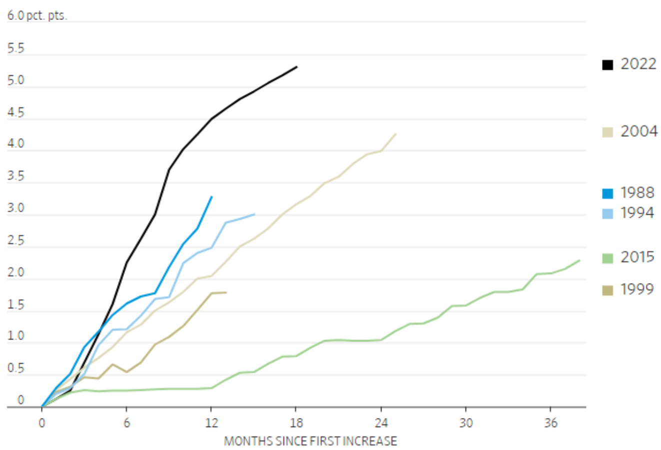
Central Banks: From Enemy to Friend of Investors

The good performance of the stock market over the past 15 months is primarily attributable to the actions of central banks. In 2022, due to the beginning of a significantly more restrictive monetary policy, they were still the "biggest enemy" of investors, but since last year, due to the looming end of the interest rate hike cycle, they have once again become the "greatest friend." Thus, in 2023, the DAX gained 20 percent in value and added another eight percent in the first nearly three months of this year. For the first time, the 18,000-point mark, our year-end target, was surpassed.

Fed and ECB take interest rate cuts into consideration

After the US Federal Reserve raised interest rates by 525 basis points in leaps and bounds between March 2022 and July 2023, speculation has been rife about the timing of the first rate cut. At the beginning of the year, most market participants agreed that such a move could occur in March. However, with the US economy continuing to grow robustly, near-full employment prevailing in the labor market, and the slowdown in inflation recently stalling, interest rate expectations have been pushed back. The first downward interest rate move is now expected in June or July. Following the FOMC meeting on Wednesday evening, Fed Chair Powell confirmed that he and his colleagues continue to believe that interest rates can be lowered in three steps of 25 basis points each this year. However, the Fed still needs a bit more confidence that the decline in inflation will continue toward the target of two percent.

Cumulative change in the US key interest rate since the first interest rate hike



Source: Wall Street Journal. Federal Reserve

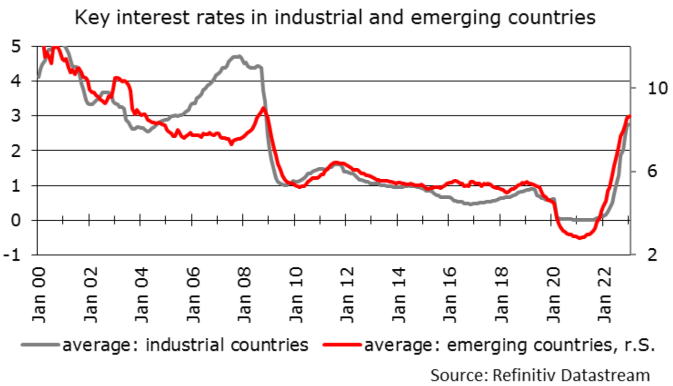
We expect the US inflation rate (measured by the PCE price index) to decrease to 2.4 percent by the June meeting and to have good chances of inflation rates below two percent starting from September. Against this backdrop, we consider interest rate cuts at the FOMC meetings on July 31, September 18, and November 7 to be likely. Even sustained strength in the labor market, according to the Fed chief, would not be a reason to delay interest rate cuts for too long. However, if an unexpected weakening occurs, the central bank could start cutting rates earlier. From today's perspective, three more interest rate cuts per year are anticipated for the years 2025 and 2026. As some investors had expected the Fed to dampen rate cut expectations, US stock markets closed at record levels after Powell's press conference.

Signs of an imminent interest rate cut are also increasing from the European Central Bank. The inflation rate has now fallen to 2.6 percent, mainly because the upward pressure on food prices has slowed significantly. While food prices were nearly 16 percent higher than the previous year in March 2023, the rate of increase has since weakened to just under four percent. A further decline to around two percent is likely in the coming months. Only service prices are currently rising significantly above average, at four percent, and we expect this increase to slow to 2.5 percent by summer. An interest rate cut at the next ECB Governing Council meeting on April 11 is unlikely; instead, we may have to wait until June 6 for the first rate cut. This time, the ECB could preempt the Federal Reserve in the monetary policy shift.

From an economic perspective, however, an earlier interest rate cut in the Eurozone would be desirable. The economy remains in a worryingly weak state, even though we do not expect a recession in the strict sense (two consecutive quarters of negative GDP growth). However, leading indicators show that the manufacturing sector continues to be under significant pressure. Particularly in Germany, industrial companies assess the situation very negatively, even if sentiment may be worse than the actual situation. Nevertheless, the services sector has shown signs of recovery recently. Interest rate cuts are likely to benefit not only the construction industry but also many smaller businesses that need refinancing this year and where high capital costs are leading to declining profitability. The earlier the ECB reacts, the better.

Japan as a monetary policy laggard, Switzerland as a trailblazer

This week, two central banks that are not typically in the spotlight, the Bank of Japan (BoJ) and the Swiss National Bank (SNB), stole the show. The SNB reduced its key interest rate from 1.75 percent to 1.5 percent. Most observers had expected this move to happen at a later date. However, since the inflation rate in Switzerland has been consistently below the two percent mark since July 2023 and recorded the lowest price pressure since autumn 2021, at 1.2 percent recently, the move seems logical from our perspective. The central bank expects the inflation rate to remain below two percent in the coming years. While the SNB is the first central bank of a major industrialized country to cut interest rates again, it is by no means the first to adopt a more expansionary monetary policy. In emerging markets, several central banks have already cut interest rates over the past six months, with the Brazilian central bank being the latest to announce its sixth rate cut.



The situation in Japan is quite different. The Bank of Japan (BoJ) has ended its twelve-year monetary policy experiment with negative interest rates. It abolished the negative benchmark interest rate of -0.1 percent and set a new target range of 0.0 to 0.1 percent. It also ended most of the unconventional monetary policy measures it had taken since the global financial crisis of 2008 by ceasing stock purchases and lifting the target for long-term government bond yields. However, this monetary policy decision is primarily symbolic. The BoJ will continue its quantitative easing, committing to purchasing Japanese government bonds at roughly the same pace as before, currently about six trillion yen (40 billion US dollars) per month. "Punishment" may not be the right word for this policy, and "normalization" is thus somewhat exaggerated. While this decision has been celebrated by many as a signal that the major financial and economic crisis that began in 2008/2009 can now be finally put to rest, one should not forget one thing: in the past, interest rate hikes by the Bank of Japan have almost always been a sure indicator that the next crisis is looming. Let's hope it's different this time!

Carsten Klude

Market data

Stock marktes	As of 22.03.2024 15:20	14.03.2024 -1 week	20.02.2024 -1 month	Change versus 20.12.2023 -3 months	20.03.2023 -1 year	29.12.2023 YTD
Dow Jones	39671	2,0%	2,9%	7,0%	23,0%	5,3%
S&P 500	5300	2,9%	6,5%	12,8%	34,1%	11,1%
Nasdaq	16415	1,8%	5,0%	11,1%	40,6%	9,4%
DAX	18201	1,4%	6,6%	8,8%	21,9%	8,7%
MDAX	26606	1,3%	3,3%	-2,7%	0,0%	-2,0%
TecDAX	3425	0,1%	1,9%	2,6%	6,3%	2,6%
EuroStoxx 50	5022	0,6%	5,5%	10,8%	21,9%	11,1%
Stoxx 50	4393	-0,1%	2,9%	7,6%	16,3%	7,3%
SMI (Swiss Market Index)	11667	-0,5%	1,8%	4,7%	9,6%	4,7%
Nikkei 225	40888	5,4%	6,6%	21,4%	51,7%	22,2%
Brasilien BOVESPA	127722	0,0%	-1,7%	-2,4%	26,6%	-4,8%
Russland RTS	1109	-2,2%	1,4%	3,1%	13,1%	2,3%
Indien BSE 30	72832	-0,4%	-0,3%	3,3%	26,4%	0,8%
China CSI 300	3545	-0,5%	3,9%	7,5%	-10,0%	3,3%
MSCI Welt	3435	1,5%	4,9%	10,0%	28,2%	8,4%
MSCI Emerging Markets	1048	0,0%	2,9%	5,1%	11,2%	2,4%
Bond markets						
Bund-Future	132,26	25	-100	-556	-571	-496
Bobl-Future	118,16	58	142	-113	-112	-112
Schatz-Future	105,76	16	36	-69	-67	-78
3 Monats Euribor	3,93	2	2	3	103	4
3M Euribor Future, Dec 2024	3,02	-1	17	67	22	72
3 Monats $ Libor	5,59	0	0	-4	64	0
Fed Funds Future, Dec 2024	4,60	-7	9	70	171	77
10 year US Treasuries	4,22	-8	-7	36	73	35
10 year Bunds	2,33	-7	-2	38	22	33
10 year JGB	0,73	-4	1	17	49	11
10 year Swiss Government	0,63	-11	-23	-4	-36	-7
US Treas 10Y Performance	586,57	0,2%	0,3%	-2,4%	-2,9%	-2,4%
Bund 10Y Performance	550,12	-0,1%	-0,4%	-3,0%	-0,2%	-2,7%
REX Performance Index	441,92	0,1%	0,0%	-2,0%	0,4%	-1,3%
IBOXX AA, €	3,38	2	-1	31	-14	31
IBOXX BBB, €	3,97	2	-3	20	-59	21
ML US High Yield	7,89	-1	-15	2	-114	10
Commodities						
MG Base Metal Index	394,59	-0,5%	4,9%	2,7%	-2,1%	0,9%
Crude oil Brent	85,60	0,5%	4,0%	6,3%	16,0%	10,2%
Gold	2173,43	0,7%	7,2%	6,8%	9,9%	5,2%
Silver	24,91	0,3%	8,0%	2,3%	10,8%	2,7%
Aluminium	2223,49	0,8%	3,0%	1,7%	-0,1%	-5,2%
Copper	8818,84	0,4%	4,7%	3,9%	1,4%	4,2%
Iron ore	110,94	0,0%	-13,3%	-17,7%	-13,5%	-18,6%
Freight rates Baltic Dry Index	2240	-4,7%	37,3%	4,2%	45,3%	7,0%
Currencies						
EUR/ USD	1,0819	-1,0%	0,2%	-1,1%	1,0%	-2,1%
EUR/ GBP	0,8580	0,5%	0,4%	-1,0%	-1,9%	-1,0%
EUR/ JPY	163,55	1,1%	0,8%	4,1%	16,2%	4,6%
EUR/ CHF	0,9711	1,0%	1,9%	2,7%	-2,2%	4,9%
USD/ CNY	7,2292	0,5%	0,5%	1,3%	5,0%	1,8%
USD/ JPY	151,26	2,0%	0,8%	5,3%	15,2%	7,2%
USD/ GBP	0,79	1,1%	0,5%	0,5%	-2,8%	1,1%

Source: Refinitiv Datastream

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