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Amundi ASSET MANAGEMENT

Weekly Market Review

The latest news from financial markets

for the exclusive attention of professionals

Edition of January 9, 2023 By Amundi Institute

The week at a glance

• **Markets:** Bond yields are down.

• **United States:** Average Hourly Earnings decelerated to 4.6% year-on-year.

• **Eurozone:** Inflation decelerates to 9.2% over 12 months in December.

KEY FIGURE

9.2%

Euro area inflation in December

Focus

The EU has been lucky with the weather so far. Record seasonal temperatures will likely have side-effects on crops, water reserves and winter activities but have at least kept gas storage levels high. Forecasts suggest temperatures will stay above norms until mid-February at least. From an energy standpoint, this winter should be fine and spring storage levels are expected to bode well for next winter.

This largely explains the steep drop in prices in gas futures over the next 12-month maturities. Moreover, the plunge looks more fundamental than technical in nature and would require strong catalysts to reverse.

Supply uncertainty remains alive for 2023. On the positive side, we expect fewer outages, more renewable output and more infrastructure to process liquefied natural gas (LNG) imports. On the negative side, Russian flows will be missing from day one and probably for the whole year, while Chinese demand will likely rebound (partly boosting its LNG imports in addition to its domestic gas production and gas throughput from Russia). Without structural replacement solutions, continued energy savings would then be required in the EU.

EU gas prices are no longer offering a premium relative to Asian benchmarks and to coal prices. It will thus be harder for EU to attract LNG from abroad and to keep industrial companies that can choose their energy sources from favoring coal instead of gas. We see prices rebounding later in the first quarter above €100MWh, necessary to constrain gas demand.

Key Dates

12th January	26th January	31st January	1st & 2nd February
December Consumer Price Index (CPI), United States	Fourth quarter and 2022 GDP, United States	Fourth quarter and 2022 GDP, Euro area	US Federal Reserve & European Central Bank monetary policy committees

Source: Amundi Institute

Our weekly analysis

On markets, as the new year begins, each week has been different

In the last trading sessions of 2022, bond yields were driven up by renewed central bank talk that the fight against inflation was still far from being won and that interest-rate hikes were still expected. For example, on 24 December, Isabel Schnabel, a member of the Executive Board of the European Central Bank, stressed that her institution should resist market pressures and perhaps raise its key rates beyond 3% (versus 2% currently expected for the deposit facility) were inflation expectations trends to make that necessary. And, in fact, in both Germany and France, 10-year government bond yields ended 2022 at year-highs (above 2.5% for the German Bund and 3.0% for the French OAT). The 10-year U.S. yield also clawed back some ground to end the year at around 3.8%.

Meanwhile, equities continued to consolidate in December after having rallied in October and November. During the first few trading sessions of 2023, the trend reversed itself. Equities began the year very well (especially in Europe), while yields fell. A major cause is the release of lower inflation figures that were far below expectations in the main European countries (including in France, where inflation was expected higher). The decline in the U.S. Institute for Supply Management (ISM) manufacturing index, and the deceleration in U.S. wages, also helped. In the next few weeks, no doubt markets will continue to test the determination of central banks to stay the course in monetary tightening, against a backdrop where inflation will, yes, remain very high, but on a receding trend (which has already begun in the U.S. and is still recent and awaiting confirmation in Europe) and where new signs of worsening (albeit moderate) of the economy could emerge.

Indice	Performance			
Equity markets	01/06/23	1 W	1 M	YTD
S&P 500	3861	0.6%	-2.0%	0.6%
Eurostoxx 50	3999	5.4%	1.5%	5.4%
CAC 40	6830	5.5%	2.1%	5.5%
Dax 30	14542	4.4%	1.4%	4.4%
Nikkei 225	25974	-0.5%	-6.9%	-0.5%
SMI	11119	3.6%	0.1%	3.6%
SPI	14237	3.7%	0.6%	3.7%
MSCI Emerging Markets (close -1D)	984	2.9%	1.1%	2.9%
Commodities - Volatility	01/06/23	1 W	1 M	YTD
Crude Oil (Brent, $/barrel)	80	-6.8%	0.9%	-6.8%
Gold ($/ounce)	1863	2.1%	5.2%	2.1%
VIX	22	-0.1	-0.6	-0.1
FX markets	01/06/23	1 W	1 M	YTD
EUR/USD	1.061	-0.9%	1.3%	-0.9%
USD/JPY	132	1.0%	-3.4%	1.0%
EUR/GBP	0.88	-0.6%	2.0%	-0.6%
EUR/CHF	0.93	0.7%	-1.2%	0.7%
USD/CHF	0.99	-0.3%	0.1%	-0.3%

Source: Bloomberg, Amundi Institute – January 6, 2023 – 15:00 pm

Indice	Performance			
Credit markets	01/06/23	1 W	1 M	YTD
Itraxx Main	+83 bp	-8 bp	-9 bp	-8 bp
Itraxx Crossover	+431 bp	-43 bp	-32 bp	-43 bp
Itraxx Financials Senior	+91 bp	-9 bp	-10 bp	-9 bp
Fixed Income markets	01/06/23	1 W	1 M	YTD
ESTER OIS	98.76	+4 bp	+14 bp	+2 bp
EONIA	-0.51	-	-	-
Euribor 3M	2.25	+12 bp	+26 bp	+12 bp
Libor USD 3M	4.81	+4 bp	+8 bp	+4 bp
2Y yield (Germany)	2.59	-18 bp	+52 bp	-18 bp
10Y yield (Germany)	2.20	-37 bp	+40 bp	-37 bp
2Y yield (US)	4.27	-15 bp	-9 bp	-15 bp
10Y yield (US)	3.58	-29 bp	+5 bp	-29 bp
Eurozone Sovereigns 10Y spreads vs Germany	01/06/23	1 W	1 M	YTD
France	+50 bp	-4 bp	+5 bp	-4 bp
Austria	+61 bp	-2 bp	-	-2 bp
Netherlands	+33 bp	--	+4 bp	--
Finland	+59 bp	+2 bp	+2 bp	+2 bp
Belgium	+62 bp	-3 bp	+1 bp	-3 bp
Ireland	+50 bp	-6 bp	+4 bp	-6 bp
Portugal	+99 bp	-2 bp	+8 bp	-2 bp
Spain	+105 bp	-4 bp	+4 bp	-4 bp
Italy	+198 bp	-16 bp	+13 bp	-16 bp

Asset Class

	MARKET	AMUNDI ANALYSIS
Equity	Global equities fell slightly this week. The MSCI World Index decreased by -0.3%. The U.S. market underperformed its European peer this week. The Japanese stock market also ended the week in negative territory (-0.84%). Emerging markets performed well, ending the week at +2.9% as the reopening of China brought investors back to the Chinese market.	The European market closed sharply higher this week (+4.37%), thanks to better than expected economic activity data and lower inflation readings. The US Federal Reserve's Hawkish commentary did not affect the Eurozone market much compared to the U.S. market. All European sectors were in positive territory, with the exception of the energy sector. The best contributors were the consumer discretionary and real estate sectors.
Fixed Income	German 10-year yields fell 30 basis points over the week, from 2.57% to 2.27%. Eurozone inflation returned to single digits for the first time since August and was below expectations, fueling hopes that inflation has peaked. This figure reflects slowing inflation in Germany, France, Italy and Spain. The U.S. 10-year yield fell 18 basis points. The U.S. labor market remained strong last month and wage gains slowed, bolstering hopes that the economy could avoid a recession and giving the US Federal Reserve (Fed) room to slow interest rate hikes.	The slowdown in inflation in the Eurozone masks persistent underlying pressures. Core inflation hit a record high of 5.2% in December. It is on this measure that the European Central Bank (ECB) should focus. In addition, President Christine Lagarde warned that there are good reasons to believe inflation could pick up again in January. According to the Governor of France's central bank, François Villeroy de Galhau, the peak in borrowing costs should be reached around the summer, and the ECB will then be "ready to stay at this terminal rate for as long as necessary".
Credit	Spreads tightened at the very start of the year, mostly in the credit default swap space and among high yield bonds in both the U.S. and Europe, supported by positive risk sentiment. Lower-than-expected inflation prints for December in major Eurozone countries like Germany and France drove bond yields lower and, together with falling gas prices, supported risky assets, ultimately driving stronger demand for spread products, together with some compression in risk premiums.	The primary market re-opening proved to be quite busy, confirming the return of demand in the very first days of the year. The latest macro data in the Eurozone shows a constructive mix with, on the one hand, more resilient-than-expected Purchasing Managers' Index (PMI), especially in the service sector, and on the other hand, lower-than-expected inflationary pressures. Despite recent outperformance of speculative grade, we are keeping our preference for higher quality within credit markets, as the macro picture remains challenged by high inflation and weakening growth.
Foreign Exchange	The U.S. dollar has registered a wild start in 2023, with stronger-than-expected labour market data (ADP suggesting more than 235K jobs have been added in December) reminding us that the Fed's fight against inflation may not be over yet. The US dollar strengthened vs most G10 currencies in the first week of the year, with Norwegian krone the clear looser. Mixed picture within Emerging Markets, with Russian Ruble, THB, MXN and China yuan renminbi up for the week, whilst BRL, Columbian peso and ARS lagged behind.	We believe it is early for the U.S. dollar to sell off whilst the Fed does seems to intend to provide a reflationary impulse to the cycle (Japanese yen and Swiss Franc are only alternatives to the U.S. dollar). Yet i) the recent progress in U.S. inflation (in turn weighing on U.S. rates volatility), ii) the Chinese reopening, and iii) the narrowing Fed-ECB terminal rate differential point to a stronger U.S. dollar downward trend for second half-year 2023.
Commodities	Commodities were down sharply by -5.0% this week. Precious metals were the only commodity safe havens. Energy, gas futures in particular, underperformed, pricing-in unusually mild seasonal temperatures in the EU. Base metals also weakened ahead of the Chinese holiday season, while surging Covid infections offset prospects of economic reopening.	EU gas prices are no longer offering a premium relative to Asian benchmarks and to coal prices. It will thus be harder for the EU to attract liquefied natural gas abroad and to encourage industrial companies that can choose their energy sources to favor coal instead of gas. We expect prices to mean-revert by late first quarter. Crude oil's technicals and supply/demand balance do not suggest a rebound just yet either, but we remain constructive in the medium term.

Economic Indicators

	MARKET	AMUNDI ANALYSIS
United States	The Institute for Supply Management (ISM) manufacturing index moved to a two-and-a-half year low of 48.4, from 49.0, in line with consensus. During 2022, the ISM index dropped 10.4 points, its biggest annual retreat since the Great Recession. The December reading is another sign that the economy was losing momentum at the end of last year, as the majority of the components points to stagnation in activity.	Continued easing in input costs and continued deterioration in activity fundamentals are the key takeaways from the report. The fall in the headline index was driven by a renewed deterioration in the new orders index, to 45.2, from 47.2, a level usually seen in recessionary environments. The production index fell to 48.5 from 51.5. In addition to slowing domestic demand, the new export orders index also fell to 46.2 from 48.4. The prices paid index dropped to only 39.4 from 43.0; the employment index, in contrast, rallied to 51.4, from 48.4.
Eurozone	The final December Eurozone composite Purchasing Managers' Index (PMI) came in at 49.3, up from 47.8 in November, as the services index improved to 49.8, from 48.5, and the manufacturing index to 47.8, from 47.1. While the indicator registered a sub-50 reading for the sixth consecutive month, signaling sustained weakness in economic activity, the improvement still shows that the strength of the downturn moderated.	The Eurozone economy continued to deteriorate but with less negative momentum, suggesting the contraction in the economy in the fourth quarter may be milder than feared. Cooling price pressures have helped moderate the decline in economic activity, with a marked slowdown in manufacturing inflation. Further expansion in staffing levels and a rising workforce remained a feature of both sectors. Yet, demand conditions remain fragile as clients have retrenched and manufacturing activity is processing backlogs in the absence of new work inflows.
Japan	The consumer confidence index rebounded to 24.2 in December, after a three-month decline since August. Household inflation expectations for one year ahead stayed at historical highs, at 4%. Overwhelmingly, 63.9% of households expect prices to increase by at least 5% within a year.	The Bank of Japan (BoJ) surprised the markets by expanding the yield curve control band in December, on the back of firming underlying inflation. As household inflation expectations remain sticky and the output gap is closing thanks to reopening, we expect the BoJ to continue with policy normalisation in 2023, first dropping the yield curve control target then ending the Negative interest rate policies (NIRP).
Emerging Market	Turkish Inflation came in at 64.3% year-on-year in December, lower than in the previous month (84.4%) and consensus expectations (67.2%). The main drivers of this decrease were: i) base effects due to an elevated December 2021 number on the back of the currencies crisis; ii) a sharp fall of inflation in transport due to lower energy inflation and adjustments in auto brackets; and iii) lower food inflation thanks to better weather conditions.	We expect inflation to continue to slow thanks to the same drivers and the economic slowdown in the next six months but to stick around 50% year-on-year in the second half of the year. Indeed, pre-election measures (raises in the minimum wage, civil servants salaries and pensions, fiscal boost, etc.) should support inflationary pressures. Moreover, risks are tilted to the upside if higher currencies pressures and/or deterioration of inflation expectations materialise.