

Weekly Update

CO | EXTERNAL PUBLICATION

Inflation pressure – much ado about nothing?



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Two weeks after an unexpected surge in US wage growth triggered a global market sell-off, [price data surprised on the upside again last Wednesday](#), with consumer prices printing at +0.5% MoM in January and 0.3% excluding volatile items. However, the core index remained stable at 1.8% YoY.

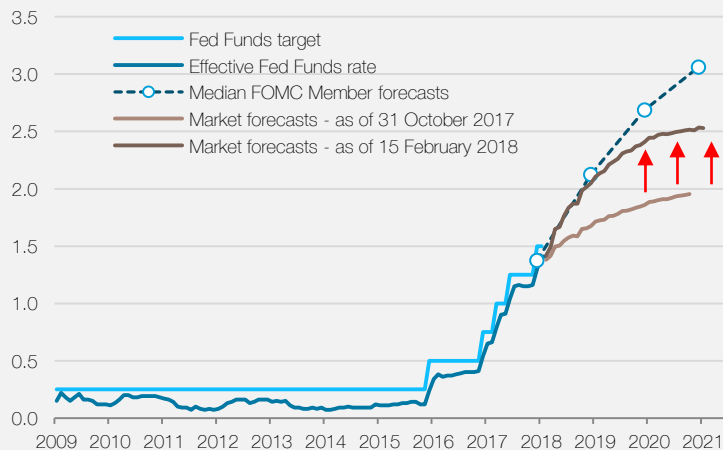
The pressure, coming from strong growth, a tight labour market and the tax boost, encouraged Bloomberg analysts to [reassess the US Federal Reserve's rate path](#). They now expect three rate hikes this year with a probability of 82%, bringing them more in line with the Fed's own projections. In turn, the 10-year US Treasury yield hit a four-year high at 2.91% and the 10-year German Bund rose to 0.76%, a level last seen in mid-2015.

[This time, global equity markets reacted well to the rise in consumer prices](#), with the MSCI AC World index up 4.1% in dollars from its February 8 low. Reflation will translate into greater pricing power, stronger corporate sales and ultimately higher earnings – provided rising wage costs do not start weighing on profit margins. Against a background of robust economic activity and global trade, corporate profits are expected to grow 14.2% this year for the MSCI AC World after 15.3% last year. In the US, earnings forecasts have been revised sharply higher in anticipation of a tax boost in coming months.

Also, [the latest earnings data pointed to strong momentum at the turn of the year](#), convincing investors that companies will be able to grow their business. In the US, 80% of S&P 500 companies have reported their figures so far. On average, earnings have been 5% better than awaited in Q4 while earnings-per-share (EPS) have risen 15% YoY. The good surprise is broad-based, with 10 sectors out of 11 delivering positive growth. European and Japanese companies are also reporting healthy earnings growth.

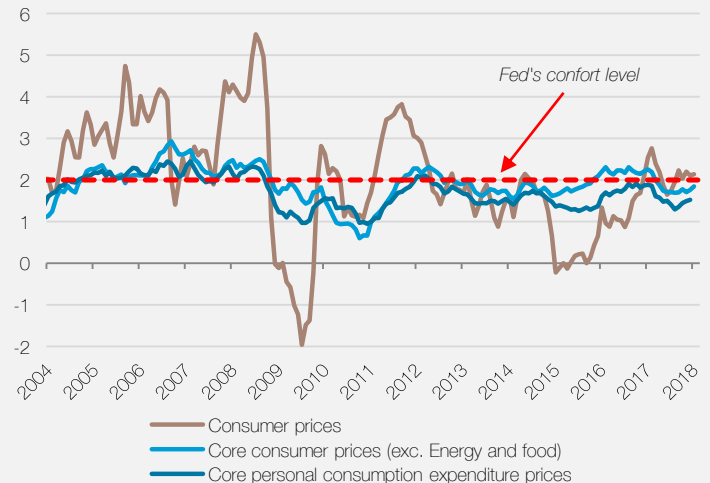
However, [we should not bury our heads into the sand](#). Solid corporate profit growth should help global equities continue to perform well in 2018 but returns will be less strong than in 2017. At this late stage in the US economic cycle with monetary policy tightening and higher long-term interest rates, [global equity volatility will be higher this year compared to last year](#).

Market expectations are now more in line with Fed projections
FOMC projections, Fed rate hike expectations, Fed Funds target (%)



Sources: SGPB, Bloomberg, 31/01/2018

Gradual rise in US inflation
US headline CPI, US core CPI, core PCE (%)



Sources: SGPB, Bloomberg, 31/01/2018

This week and next

EUROZONE

- Eurozone industrial production fell 0.4% in December after a strong November (1.3%). While the decline was expected, it proved stronger than surveyed (0.1% MoM).
- GDP growth eased down to 2.7% YoY in Q4 from 2.8% in Q3.



Next week's key events		Per.	Prev.	Cons.
20 Feb	Consumer confidence	Feb	1.3	--
21 Feb	Manufacturing confidence	Feb	59.6	--

UNITED KINGDOM

- While manufacturing output is still doing well (0.3% MoM in December), industrial production ended the year in negative territory (-1.3% MoM).
- Despite some weakness in consumer prices in January (-0.5% MoM), inflation remains above the Bank of England's target (3.0% YoY in January), which could soon trigger a rate hike.



Next week's key events		Per.	Prev.	Cons.
21 Feb	Jobless Claim Change	Jan	8.6k	--
22 Feb	GDP, YoY	Q4	1.5%	--

UNITED STATES

- Last Wednesday, stronger-than-expected consumer price data hit bond markets. US inflation rose to 2.1% YoY in January while expectations were for 1.9%. As a consequence, analysts now forecast four rate hikes this year.
- Retail sales fell -0.3% MoM in January, industrial output printed at -0.1% MoM, while inventories rose further in December (+0.4% MoM).



Next week's key events		Per.	Prev.	Cons.
22 Feb	Initial jobless claims	Feb 17	230k	--
22Feb	Leading index	Jan	0.6%	0.7%

ASIA & EMERGING COUNTRIES

- In Japan, the current account balance was very disappointing last week, with ¥797.2bn in December vs an expected ¥1,056.9bn.
- In China, inflation printed at 1.5% in January after 1.8% in December. The trade balance slumped to 20.34bn yuan in February from 54.65bn in January. This can be explained by the fact that imports soared 36.9% YoY while exports only rose 11.1%.



Next week's key events		Per.	Prev.	Cons.
19 Feb	Japan: Trade balance (bn¥)	Jan	359	-1020
21 Feb	Japan: manufacturing PMI	Feb	54.8	--

Sources: Datastream, Bloomberg, 19 February 2018, Note: YoY = year-on-year; QoQ = quarter-on-quarter; MoM = month-on-month, P = preliminary figure, A = advanced figure, F = final figure, seasonally adjusted, ECB = European Central Bank

Our 6-month targets

	Thursday close	6mth target
EUR/USD	1.25	1.25
GBP/USD	1.41	1.28
USD/RUB	56.4	60
AUD/USD	0.79	0.72
EUR/CHF	1.15	1.18
USD/CNY	6.35	7.1
USD/CAD	1.25	1.37
USD/JPY	106	118
Brent	\$63.8	\$55
Gold	\$1352	\$1225

No change to our 6-month targets this week.

Forecast figures are not a reliable indicator of future performance

Question time

Past performance should not be seen as a guarantee of future returns.

No Q&A this week.

Market performance

Past performance should not be seen as a guarantee of future returns.

Interest rates

	Last	1wk	3mth	YTD	12mth
EONIA (EUR)	-36 bp	0 bp →	-1 bp	-2 bp	-1 bp
3mth Euribor (EUR)	-33 bp	0 bp →	0 bp	0 bp	0 bp
3mth Libor (USD)	187 bp	6 bp ↑	45 bp	18 bp	83 bp
3mth Libor (GBP)	55 bp	2 bp ↑	2 bp	3 bp	19 bp
10-year US Treasury bond	293 bp	9 bp ↑	59 bp	52 bp	41 bp
10-year German bond	72 bp	1 bp ↑	34 bp	29 bp	34 bp
10-year French bond	89 bp	-2 bp ↓	28 bp	22 bp	-18 bp
10-year UK bond	167 bp	4 bp ↑	34 bp	44 bp	36 bp

Credit

	1wk	3mth	YTD	12mth
BAML EURO Corp. IG	-0.1% ↓	-0.8%	-0.6%	1.9%
BAML EURO Corp HY	-0.5% ↓	-0.1%	-0.5%	4.8%
BAML GBP Corp IG	-0.8% ↓	-1.1%	-2.7%	2.7%
BAML US IG	-0.5% ↓	-1.6%	-2.5%	3.4%
BAML US HY	-0.1% ↓	0.7%	-0.7%	4.5%
JPM Global EM Sov. Plus	-0.7% ↓	-0.1%	-2.0%	7.0%

Exchange rates

	Last	1wk	3mth	YTD	12mth
EUR/USD	1.25	2.1% ↑	6.1%	4.1%	18.0%
EUR/CHF	1.15	0.6% ↑	-1.0%	-1.5%	8.2%
GBP/USD	1.41	1.3% ↑	7.0%	4.4%	13.2%
USD/JPY	106	-2.4% ↓	-6.0%	-5.8%	-7.0%
USD/BRL	3.23	-1.8% ↓	-2.6%	-2.6%	5.6%
USD/CNY	6.35	0.3% ↑	-4.2%	-2.4%	-7.6%
USD/RUB	56.4	-3.5% ↓	-6.4%	-2.2%	-1.4%

Government bonds*

	1wk	3mth	YTD	12mth
United States (3-7yr)	-0.3% ↓	-2.0%	-1.7%	-0.3%
United Kingdom (3-7yr)	-0.1% →	-1.4%	-1.6%	-1.3%
Germany (3-7yr)	0.1% ↑	-1.6%	-1.0%	-1.9%
Japan (3-7yr)	0.1% →	-0.1%	0.0%	0.0%

Equities*

	Last	1wk	3mth	YTD	12mth
MSCI AC World	521	4.2% ↑	6.2%	1.8%	20.4%
Eurostoxx 50	3 390	0.4% ↑	-4.0%	-3.0%	5.4%
DAX	12 346	0.7% ↑	-4.9%	-4.4%	4.7%
CAC 40	5 223	1.4% ↑	-1.2%	-1.7%	9.4%
S&P 500	2 731	5.9% ↑	7.0%	2.4%	18.6%
FTSE 100	7 235	1.2% ↑	-1.1%	-5.5%	3.4%
SMI	8 918	1.8% ↑	-1.9%	-5.0%	8.6%
Topix	1 719	-2.6% ↓	-1.3%	-5.4%	13.0%
IBOV Brazil	84 291	3.4% ↑	19.0%	10.3%	24.0%
MICEX Russia *	2 265	1.7% ↑	6.3%	7.4%	6.0%
MSCI EM	1 203	3.4% ↑	8.7%	4.0%	31.0%
SENSEX 30 India	34 297	-0.3% ↓	4.8%	1.5%	23.4%
Hang Seng (H-K)	31 115	2.2% ↑	8.0%	4.0%	34.6%
Shanghai Composite	3 199	-1.9% ↓	-6.0%	-3.3%	-0.4%

Commodities

	Last	1wk	3mth	YTD	12mth
Brent	\$64	-1.3% ↓	2.8%	-4.3%	14.0%
Gold	\$1 352	2.7% ↑	5.7%	3.7%	10.1%
Silver	\$16.7	2.2% ↑	-1.8%	-1.8%	-7.0%

Source: Datastream, on 15 February 2018. 1wk = 1-week change, 3mth = 3-month change, 12mth = 12-month change, YTD = year-to-date change, YoY = year-on-year change, BAML = Bank of America Merrill Lynch, JPM = JP Morgan, IG = Investment Grade, EM = emerging markets. * Price return for MICEX equity index. Equities; total return in local currency. Government bonds = 3-7 year returns. Figures are rounded.

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