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Monthly commentary
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GLOBAL MACRO VIEWS

Three lessons from recent central bank moves

Actionable insights for investors

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A flurry of central bank activity is underpinning a market melt-up, led by the U.S. Federal Reserve (Fed) kicking off its rate cutting cycle with a surprise 50 basis points (bps) move. The combination of aggressive global monetary easing at a time when financial conditions are already loose should provide downside protection to risk assets, though headwinds of uncertainty warrant a selective approach to portfolio positioning.

After the Fed's September surprise, the Bank of England (BoE) kept the Bank rate steady, while the European Central Bank (ECB) stuck to its data-dependent script. The Bank of Japan (BoJ) struck a dovish tone, hinting another rate hike may be months away, while the People's Bank of China had a whatever-it-takes moment to spur sentiment. Despite the different policy outcomes, investors have common themes to consider as they navigate the uncertain macro landscape.

1. **Rate decisions are evidence based**

   First, policymakers are emphasizing an ongoing data-dependent, meeting-by-meeting approach to future decisions. Fed Chair Jerome Powell explicitly stated that the committee is in no rush to further reduce rates. The Bank of England made a nod to the "absence of material developments" since their last meeting. They will cut rates "gradually over time" dependent on the evolution of economic data. The ECB has a similar stance, cautioning against a "pre-determined" path. The Bank of Japan added that they will look carefully at incoming data and assess the impact of the previous policy moves.

Aggressive global monetary easing at a time when financial conditions are already loose should provide downside protection to risk assets

2. Economic activity appears resilient

Second, economic outlooks appear resilient. This is a Fed looking to "recalibrate" its policy stance, taking advantage of an economy still in "a good place" to engineer a soft landing. The BoE also noted that growth has been resilient, and there was even a more dovish tone in Japan with a nod that upside risks to inflation have receded. As for weakness in German activity, the ECB said the recent deterioration was already baked into their projections, though we see greater need for caution after disappointing economic data since.

3. Diverging policies create investment opportunity

Third, the degree of divergent policy paths has a shelf-life, opening opportunities across fixed income. Our base case is for six rate cuts of 25 bps each for the Fed at consecutive meetings until June. Data will drive the direction, however, with attention turning to upcoming payrolls prints and inflation data at the margin; the bar is high for another 50 bps cut, in our view, particularly after the strong September U.S. payrolls report. **Our take:** *We hold a neutral stance on U.S. duration amid a growth slowdown, upgrading a long-standing underweight.*

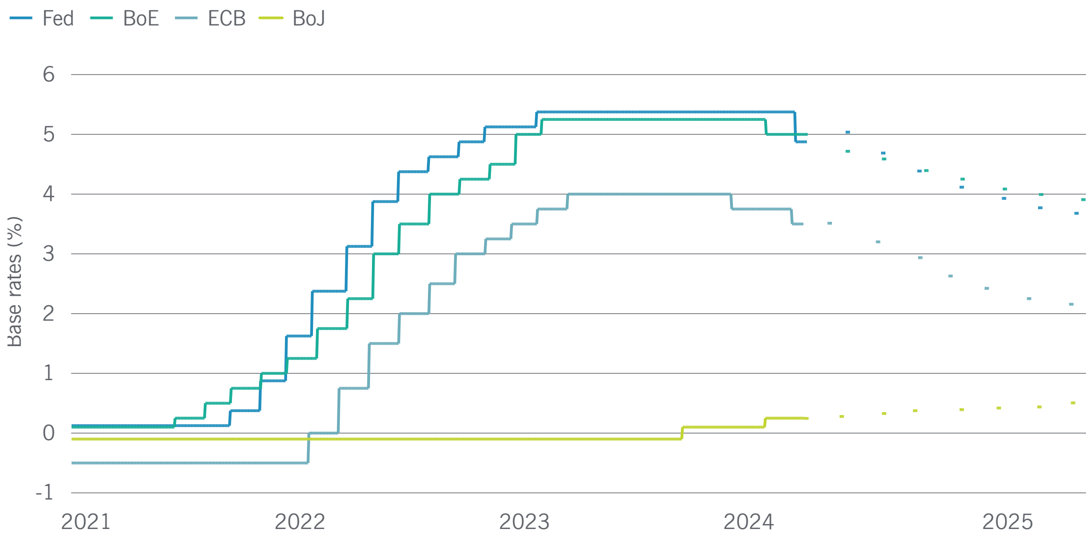
For the U.K., as focus turns to the fiscal backdrop and the upcoming budget, policymakers' reluctance to follow major peers in a swifter cutting cycle could be challenged as stubborn services inflation should ease as labour market slack builds. A potential period of tax rises and public spending cutbacks could warrant a steeper rate-cutting cycle in 2025, challenging our base case for a quarterly pace of cuts. **Our take:** *leaning into duration in U.K. gilts.*

Signs of stagnating growth in Q3 2024 alongside softening services inflation in the eurozone has us embracing a more cautious tone. We now expect the ECB to cut at consecutive meetings, aligning more broadly with our U.S. policy path expectations through mid-2025. **Our take:** *seeking core exposure in German bunds and pockets of periphery, namely Spain and Greece, for attractive carry.*

In Japan, when Governor Ueda was asked about a rate increase by year-end, he emphasized no timetable to hiking in mind. This leads us to believe that an October rate hike is unlikely. We anticipate the next 25 bps move later this year when there is greater evidence that real wages are feeding sustainably into consumption, followed by two more hikes through mid-2025. **Our take:** *taking advantage of the steepness of the Japanese government bond curve to favour under-owned ultra-longs.*

All in, while the Fed ostensibly gave the green light for risk assets to rally, data will drive decisions. That keeps us positioned with an up-in-quality tilt across fixed income assets, and seeking tactical opportunities to capture the whirlwind of policy moves. After all, there could be more surprises in store.

MISPRICED EASING EXPECTATIONS PROVIDE AMPLE OPPORTUNITIES



Source: Bloomberg, as of September 30 2024

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Endnotes

Sources

All market and economic data from Bloomberg, FactSet and Morningstar.

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