

Market Weekly Insights

28th October 2024

Global Outlook

Japan’s Bonds Yield Joins Global Debt Selloff Rally as Uncertainties on Fed Outlook Rises

Yields on Japan’s 40-year government debt rose by 1.5 basis points to 2.535% on Wednesday, following the US 10-year Treasury yield eclipse of 4.23% for the first time since July. This surge joins the ongoing global debt selloff and securities selling pressure in Europe and Asia as traders bet against an aggressive US interest rate cut.

Global bond traders are reassessing their positions as the resilience of the U.S. economy, along with changing election dynamics, weakens the case for aggressive easing by the Federal Reserve. Uncertainties surrounding Japan’s upcoming lower house election and expectations for further Bank of Japan policy normalization also contribute to the yield run-up.

Earlier last week, Fed officials sounded cautious about the pace of future rate cuts after economic data showed that hiring over the past three months was stronger than initially estimated. The prospect of elevated US rates continues to be higher as traders become speculative about the Fed’s next action.

Central Bank Keeps Rates High as Ethiopia Restructures Debt and Secures IMF Support

Ethiopia will maintain high interest rates for the remainder of 2024 to manage inflation driven by an overhaul of its foreign exchange policy. In July, the central bank raised the key rate to 15% as part of a transition to an interest-rate-based monetary framework, which has helped ease inflation from 29% to 17.5% in September. Despite eased inflation, food prices are expected to rise temporarily due to a 30% devaluation of the Ethiopian Birr. The reforms, which included tax increases and a shift to an interest-rate-based policy, helped Ethiopia secure IMF support as it restructured \$29 billion in foreign debt. The government anticipates inflation will fall below 10% by 2025 as the economy adjusts.

The government rolled out temporary subsidies on fuel, heating oil, and medicines to support vulnerable groups, with plans to phase them out. Debt restructuring talks are progressing, set to conclude by early 2025. The IMF forecasts over 6% growth this year, driven by improved agricultural productivity as farmers gain better access to foreign currency. Gross foreign reserves have doubled, with the central bank soon publishing data. These reforms aim to attract foreign investment in agriculture and mining, reflecting Ethiopia’s commitment to economic resilience amid inflation control and debt management.

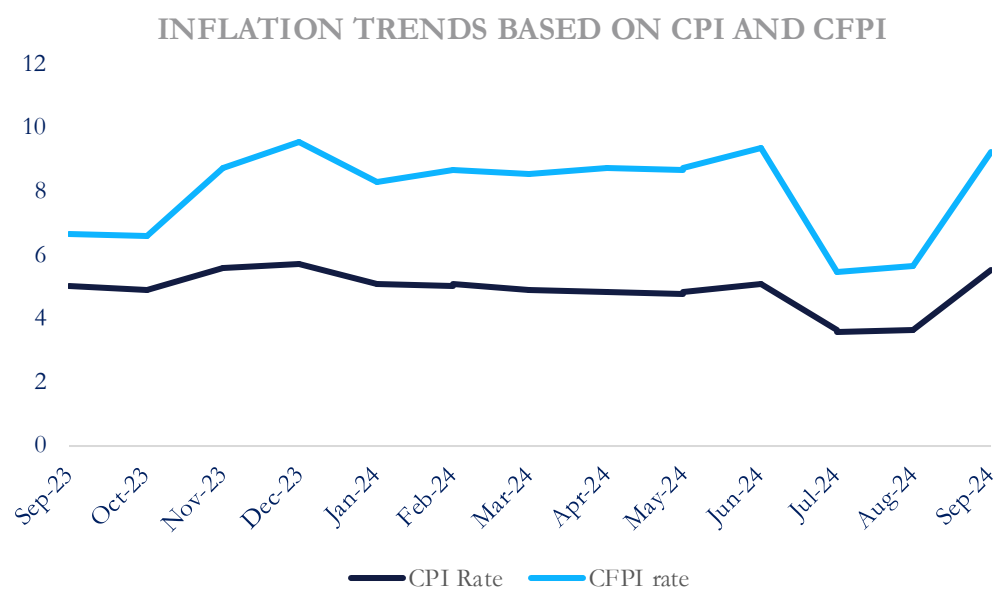
Sources: Bloomberg

S&P 500	\$5,808.12 -0.03%
DJIA	\$42,114.40 -0.61%
NASDAQ	\$18,518.61 +0.56%
Russell 2000	\$2,207.99 -0.49%
FTSE 100	\$8,248.84 -0.25%
Nikkei 225	\$37,913.92 -0.60%
WTI Crude	\$68.33 -4.81%
10-yr Treasury	4.25%

India Holds Rates Steady Amid Inflation Watch

India's inflation remains on a monitored path toward the Reserve Bank of India's (RBI) 4% target, though caution is warranted, as emphasized in the RBI's October Monetary Policy Committee (MPC) minutes. While inflation edged up month-over-month to 5.49% in September, driven largely by rising food prices, the MPC maintained the repo rate at 6.50% for the tenth straight meeting, signaling a 'neutral' policy stance. This approach underscores the RBI's commitment to flexibility in managing inflation risks.

Though most MPC members supported holding rates steady, newly appointed external member Nagesh Kumar advocated for a 25-basis point cut, citing anchored inflation expectations and softer domestic and export demand. Kumar suggested a cut could stimulate private investment and demand amid slowing industrial activity. However, RBI Governor Shaktikanta Das and other members cautioned against early rate reductions, warning that doing so might undermine recent progress in tempering inflation. This prudent stance indicates the RBI's current priority is maintaining inflation control over immediate growth incentives, adopting a careful, wait-and-see approach before any potential policy adjustments.



America This Week

U.S. Home Sales Hit 14-Year Low

U.S. existing home sales fell by 1% to an annual rate of 3.84 million last month, the lowest since October 2010. This highlights the ongoing affordability crisis and high-rate environment for homebuyers. Prospective buyers, hoping for relief from mortgage rates, have largely paused purchases, contributing to a stagnating housing market. However, expectations for falling rates have not materialized; instead, rates on 30-year fixed mortgages rose by 70 basis points to 6.85% since the Federal Reserve's rate cut in September. This increase follows stronger-than-anticipated economic data, which has caused the Fed to signal restraint on further rate cuts, thereby maintaining upward pressure on bond yields and, consequently, mortgage rates.

Housing supply also remains constrained, with around 20% fewer homes on the market compared to five years ago. Homeowners, many of whom locked in low rates during the pandemic, are disincentivized to sell, further restricting inventory and sustaining price growth. As mortgage rates persist at elevated levels, affordability challenges are likely to continue, keeping potential buyers sidelined and impacting the market into next year.

Sources: Reuters

US EXISTING HOME SALES (IN MILLIONS)



Booming Credit Market Fuels Junk Debt Surge

Weaker businesses are seizing opportunities in a booming credit market to refinance debt, bolster balance sheets, and fund dividends. September saw \$109.7 billion in junk-rated bonds and loans issuance, marking the third-highest monthly total since 2005. Investor optimism, driven by strong labor market data and low concerns about a recession, has fueled demand for speculative-grade debt, with spreads between junk bonds and U.S. Treasuries falling to near 14-year lows.

Companies have successfully pushed their debt maturities further into the future, with junk-rated obligations due in 2025 dropping from \$347 billion last year to just \$65 billion. Additionally, junk loans issued in September funded dividends for business owners, reflecting aggressive market behavior. Higher interest rates have made it harder for private-equity firms to sell portfolio companies, prompting them to use debt to pay shareholders instead.

Some deals illustrate the market's optimism, such as Belron International's record \$9 billion junk-debt issuance, which funded both refinancing and shareholder dividends, though it resulted in a credit downgrade. Meanwhile, Chobani issued \$650 million in bonds with flexible payment terms, raising more than planned due to high demand. Despite rising average bond coupons—up to 6.34% from 5.7% in 2022—analysts see the increases as manageable, as companies refinance debt previously issued at ultra-low rates during the Fed's zero-interest policy period.

Macro Highlights

U.S. Bond Yields Hit Highest Levels Since July

U.S. 10-year bond yields surged to 4.26% last week, rising to their highest point since July, as the bond market continues to experience a dramatic selloff. The selloff pushed yields in the two and 10-year treasury bonds to their highest points since mid-summer, as investors considered the possibility of slower U.S. rate cuts and the upcoming American general election.

Traders' initial aggressive rate cut projections have steadily decreased following the Federal Reserve's 50 basis point rate cut in September. Current interest rate swaps show the market pricing in federal reserve rate cuts of approximately 128 basis points through September 2025, down from 195 basis points immediately following the September cuts.

Sources: Microsoft Start, Wall Street Journal, Bloomberg

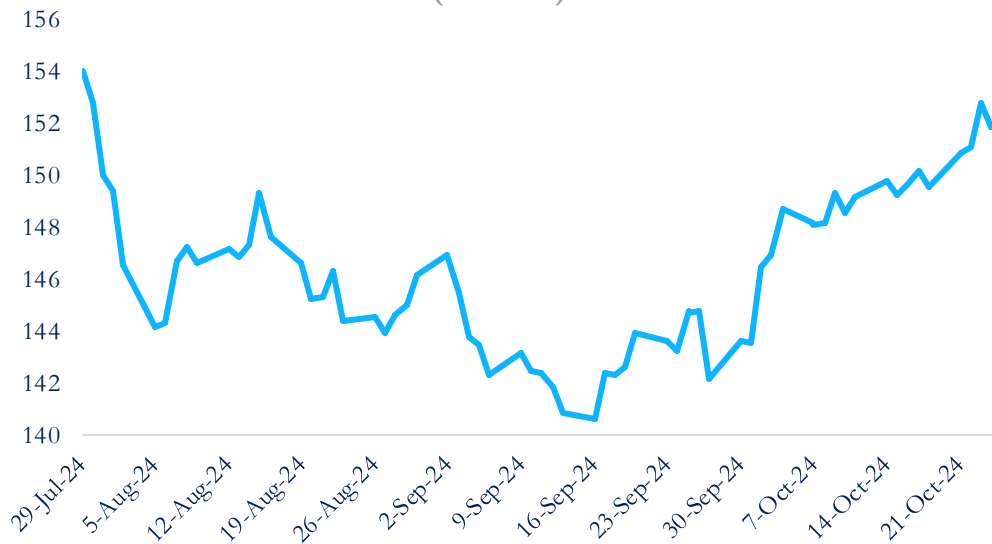
Analysts are forecasting continued struggles for treasuries over the coming months, as the presidential election and November Federal Reserve meeting loom large over the bond market to close out 2024. Treasury volatility has also increased, with the ICE Bank of America index rising to a yearlong high, likely indicating a turbulent bond market over the coming months.

Dollar Rally Stalls after Hitting 3-Month High vs Yen

The dollar's rally stalled Thursday, slowing a four-week-long streak of gains. The greenback had been in solid form recently, with gains in 16 of the last 18 sessions as of Thursday as it pushed three-month highs early this week against the euro and Japanese yen. The run primarily stemmed from robust U.S. economic data and unexpected divergence in global central banks' pace of interest rate cuts, driving trader optimism in the currency. Thursday's dollar slump comes from a lower-than-projected weekly jobless claims report and robust U.S. economic data following the Federal Reserve's September rate cut. Recent comments and data from the bank's board members have damped hopes of significant and frequent rate cuts over the coming months.

The dollar index, which measures the dollar against a basket of foreign currencies, fell 0.22% to 104.21, with the euro up 0.17% at \$1.0799 after hitting a nearly four-month low of \$1.076 on Wednesday. The dollar declined by 0.58% against the Japanese yen, reaching 151.86. The dollar has also been affected by changes in the upcoming U.S. Presidential election, shifting alongside the race dynamics. It will likely continue to be volatile in the near term as the markets weigh the race's outcome in November.

USD TO JPY CLOSING PRICES
(IN USD)



Job Growth Slows in October

U.S. unemployment claims fell unexpectedly last week, reflecting recovery from Hurricane Helene and Milton, though continuing jobless claims rose to their highest level since 2021, suggesting a challenging job market. Initial claims for state unemployment benefits dropped by 15,000 to 227,000 for the week ending Oct. 19, partly offsetting hurricane-related surges. However, the number of people continuing to receive benefits rose by 28,000 to 1.897 million by mid-October, indicating slower hiring and the impact of ongoing events such as Boeing's worker strike and layoffs at Stellantis.

Sources: Bloomberg, WSJ, Reuters

Despite disruptions, economists believe the labor market remains soft but not in decline, with hiring focused on replacements rather than growth. The Fed’s Beige Book reported slight employment growth in early October, with low worker turnover and limited layoffs. Nonfarm payroll growth for October is expected to slow, with estimates between 100,000 to 125,000, down from 254,000 jobs added in September.

The Federal Reserve is monitoring these developments before its next policy meeting, though recent rate cuts to 4.75%-5.00% reflect efforts to support the economy amid rising unemployment. The labor market data will likely influence the Fed’s policy and voter sentiment ahead of the U.S. presidential election on Nov. 5.

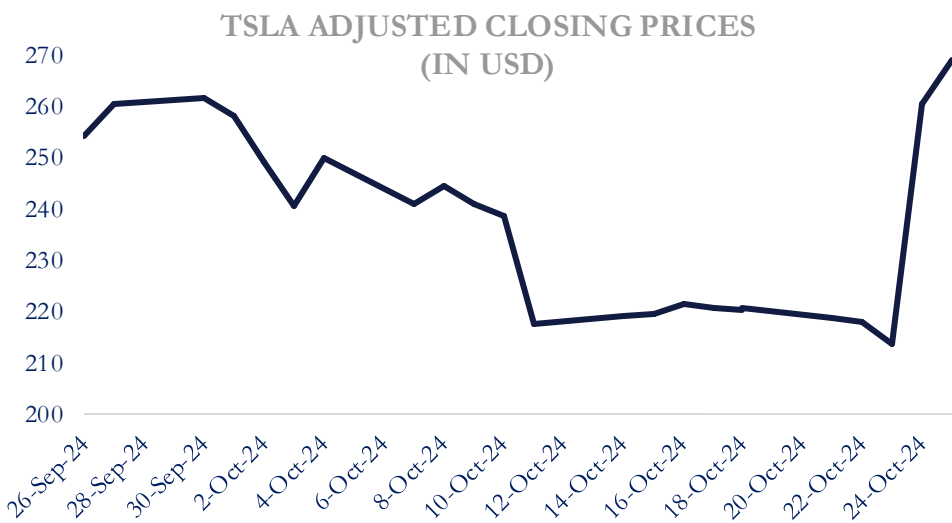
Industry News

Tesla Shares Record Biggest Gain in Over a Decade

Tesla's recent third-quarter announcement highlighted significant growth prospects and economic implications. CEO Elon Musk projected a 20-30% increase in vehicle sales next year, assuaging investor concerns and reinforcing Tesla's commitment to its core electric vehicle (EV) business. As a result, Tesla's shares soared by nearly 21%, adding over \$140 billion to its market value—the most significant gain since 2013.

Investors were also reassured by Tesla's cost-cutting measures, with the cost of goods sold per vehicle dropping to an all-time low. This improvement, combined with Tesla's ability to maintain a profit margin of 17.05%, beat Wall Street expectations and indicated effective management of production costs despite economic pressures.

Musk's reiteration of Tesla's plans to expand its vehicle lineup, including launching an affordable model in 2025 and advances in Full Self-Driving (FSD) software, signals a strategic approach to capitalizing on affordability and technological innovation. Although regulatory challenges remain for Tesla's envisioned robotaxi services, the company's focus on diversifying revenue streams appears promising. The announcement alleviated fears about aggressive pricing strategies hurting margins. It highlighted Tesla's capacity to balance innovation and profitability, perhaps signaling a turnaround for the EV maker struggling with an increasingly competitive market.



Arm Set the Stage for a Trial in December after Canceling Qualcomm’s Chip Design License Over Legal Dispute

Arm Holdings has canceled Qualcomm’s chip design license, raising the stakes in an intellectual property dispute that will go to trial in December. In defense of their case, Qualcomm accused Arm of using leverage to increase royalty rates for its intellectual property. Many of Qualcomm’s chips use Arm’s design architecture, meaning revoking its license potentially puts billions of dollars of revenue at risk.

Sources: Reuters, Financial Times

However, this was not the first time Qualcomm and Arm had been involved in a dispute. The relationship between the two companies soured in 2022 when Arm sued Qualcomm over its \$1.4bn acquisition of chip design group Nuvia. On Arm’s side, they claim the deal led to using its intellectual property without permission. As a result, Arm felt it necessary to take formal action requiring Qualcomm to remedy its breach or face termination of the agreement.

McDonald’s Pull Their Quarter Pounders Supply Amidst US E.coli Concerns

McDonald’s has temporarily removed its Quarter Pounder from menus in four U.S. states after an E. coli outbreak linked to 49 infections and one death. The CDC identified fresh onions and beef patties as possible sources of contamination and is working with McDonald’s to investigate. Following the announcement, McDonald’s shares dropped by 10%.

The strain, known as “O157”, can cause symptoms like severe stomach cramps, diarrhea, vomiting, and fever, posing risks for children and older adults. The outbreak is the latest in a series of food safety incidents in fast-food chains; in 2022, Wendy’s removed Romaine lettuce from sandwiches following a similar E. coli-linked outbreak.













McDonald’s has not indicated when it will resume Quarter Pounder sales in the affected areas but stated its commitment to rigorous safety protocols as investigations continue. This incident has raised further concerns over ingredient sourcing and food safety across the industry, signaling possible regulatory scrutiny ahead.

Genesys Confidentially Submits for U.S. IPO

This week, Genesys, an AI-driven call center software company, confidentially filed for a U.S. IPO, signaling the rising investor interest in AI-focused businesses. The move aligns with an uptick in tech IPOs as investors regain interest in startups leveraging generative AI amidst recovering market sentiment. Backed by private equity giants Permira and Hellman & Friedman, Genesys seeks to capitalize on its AI-powered growth, reporting over \$1.6 billion in cloud platform revenue in the last quarter, a year-on-year increase of more than 35%. Analysts suggest this IPO could act as a "litmus test" for AI demand, potentially paving the way for other AI firms considering public offerings.

Genesys's strategic partnerships with major tech players like AWS, Google Cloud, and Microsoft enhance its appeal, offering robust integrations across technology, retail, and industrial sectors. With companies like Cerebras Systems also entering the IPO race, successfully launching AI-driven IPOs could further validate the sector's growth potential, potentially bolstering valuations for future tech listings.

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Sources: Financial Times, Reuters