FE Investments

WEEKLY MARKET COMMENTARY BY ROB GLEESON

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US INFLATION SLOWS BUT BOND MARKETS HAVE BECOME LESS OPTIMISTIC ABOUT RATE CUTS

This week has been tough for bond investors. The general picture is unchanged as the US jobs market remains robust and CPI inflation is falling. Core inflation is a bit more sticky but, again, this was expected. Yet bonds have fallen. In the UK, there is a further complication from the upcoming budget. The chancellor is widely expected to change government borrowing rules and a significant change could free up billions in potential additional borrowing to fund the government's growth plans. This week brought several warnings about whether bond markets tolerate a big increase in government borrowing. With the yield on 10-year gilts now above 10-year treasuries this could be a sign of nervousness among bond investors.

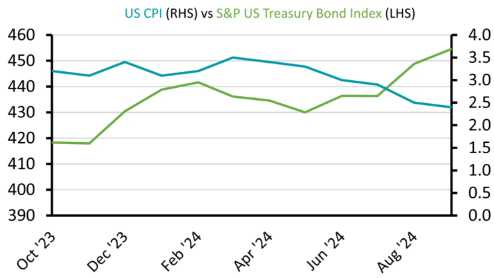
Equity markets have been a bit calmer, with the exception of China, as US markets appeared to accept the strong non farm payroll report as more evidence of a soft landing for the US economy. The strength of the recent Chinese rally has been remarkable, but this week's volatility shows that the pressure is on the Chinese government to deliver sufficient fiscal stimulus to convince markets it may actually work.

THE MARKETS THIS WEEK

FTSE 100	S&P 500	Nikkei 225	MSCI Europe	Hang Seng	US 10 Yr	UK 10 Yr	Brent Crude	Gold	Iron Ore	GBP USD
-0.36%	+1.27%	+2.40%	+0.44%	-6.53%	+0.25%	+0.17%	+0.18%	-0.12%	-2.31%	-0.75%

US: LOWER INFLATION MEANS MARKETS SEE SMALLER FED RATE CUT

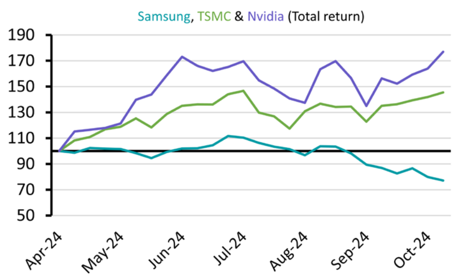
Headline inflation slowed to 2.4% in September, however, this was slightly short of the 2.3% many analysts expected. Meanwhile core inflation (excluding more volatile food and energy costs) edged up slightly to 3.3%. Markets appear to view this inflation reading as adding to the case for a 0.25% rate cut at the next meeting in November after last week's Non Farm Payroll employment data showed the US created far more new jobs than expected. Average wage inflation also ticked up slightly in September.



Markets have rapidly revised down their expectations for interest rates. Bond values rose steadily in the first half of 2024 as falling inflation raised hopes of swift interest rate cuts. Recent weeks have seen bonds reverse a lot of these gains as yields have been driven up as better news on inflation and the jobs market mean central banks have fewer reasons to bring interest rates down. Concerns that large additional amounts of UK government borrowing in this month's budget have also contributed to UK gilts falling in value.

TECH: PRIVATE EQUITY STILL PUTTING A PREMIUM ON AI COMPANIES

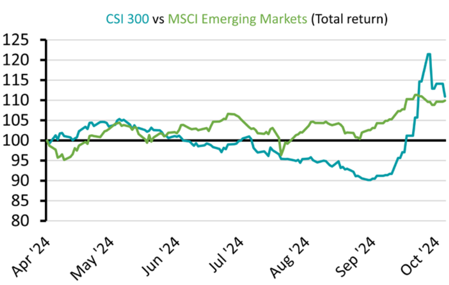
Last week OpenAI raised $6.6bn from private investors including Microsoft, Nvidia and Sequoia Capital. The artificial intelligence company launched ChatGPT a year ago to kick off the AI boom. This is the most a startup has ever raised and values OpenAI at $150bn. The company is projected to burn through $5bn this year on $3.6bn in revenue and is now more valuable than all but 17 companies in Europe. Competitors such as Anthropic's Claude, Google's Gemini and Elon Musk's xAI are also chasing high valuations.



The valuation of OpenAI shows private equity investors still place a premium on AI companies as investors in listed companies appear unsure of their lofty valuations. Prices for many tech companies peaked in July and have not recovered. Chinese AI firms are also launching products in the US. Meanwhile, Samsung issued an apology to investors for falling behind in the AI chip race. Despite tripling its operating profits for the year, investors have not been impressed. Its shares have lost a third of their value in the past six months.

CHINA: MARKETS APPEAR UNCERTAIN ABOUT GOVERNMENT SUPPORT

The Chinese equity rally was interrupted this week as trading resumed following the Golden Week public holiday. Chinese stocks soared after the central bank promised a bumper stimulus package to boost financial markets and restore confidence in the property sector. Between 18 September and 8 October the CSI 300 gained 35% after the central bank said it will boost share buying by institutional investors. However, Chinese markets fell 7% on Wednesday before picking up later in the week.



The Chinese government has also promised fiscal stimulus to address the country's economic problems, but the lack of detail worried investors and stocks fell. Chinese shares steadied after the finance ministry promised more details of the scheme. Investor sentiment is mixed with Goldman Sachs, HSBC and Blackrock upgrading their outlook for China. However, Invesco, JP Morgan and Nomura are concerned that the rally is overdone and the stimulus package is not be big enough to overcome the country's troubles.

Data sourced from S&P Global, US Bureau of Labor Statistics and Investing.com