MARKET FLASH: THE SWISS NATIONAL BANK CLEARS THE WAY FOR RATE CUTS

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Central banks in Switzerland and Japan made diametrically opposing decisions over interest rates but both with the intention of influencing their currencies. The Swiss franc has risen by more than 15% since the end of 2019 and exports have failed to return to pre-Covid levels. As a result, the Swiss National Bank chose to steal a march on market expectations by cutting interest rates by 25bp, a move designed to relieve pressure on the franc. The Bank of Japan, in contrast, finally exited its negative rate regime by raising rates to the 0/0.10% bracket and abandoning its Yield Curve Control mechanism. Just when the annual Shinto negotiations had resulted in wage rises of more than 5%, the aim was to stop the yen falling and curb inflation from imports.

Like the ECB, the Fed is implying markets will have to wait until June before a first rate cut occurs. The Fed also raised growth expectations- by 60bp in 2024, 20bp in 2025 and 10bp in 2026- and said inflation would be more persistent. It sees an extra 20bp in Core PCE this year and an extra 10bp for headline inflation in 2025. The Fed's dot plots imply a less generous rate cutting trajectory than in December 2023 but markets were reassured by Jerome Powell sticking to plans to cut three times this year. Markets are now 65% betting on a first move in June. The Fed could also slow the pace of quantitative tightening from May. Equity and bond markets both rose on the news.

Higher immigration in the US has no doubt played some part in this miraculous disinflation by relieving labour market tensions, along with a productivity bounce. As a result, the Fed has more room to move than the ECB. The eurozone is in no position to pre-empt Fed rate cuts as that would risk weakening the euro and boosting imported inflation, especially as energy is once again trending higher. Brent crude is now trading above $85. The ECB is also out of step with the Fed over quantitative tightening The LTRO/TLTRO programmes have ended but the ECB is due to step up its balance sheet shrinking in July.

Even so, despite the prospect of real interest rates remaining high for another few months, this week's economic data showed growth was holding up. PMIs suggest a possible rebound in eurozone activity even if manufacturing in Germany is still ailing. In the US, PMI are still in expansionary territory and regional Fed indicators tend to support the soft landing scenario.

Equity markets have performed very well since the end of October so we think it is time for some tactical profit taking. The environment is ripe for a market consolidation: equity risk premiums leave no room for disappointment over consensus expectations for miraculous disinflation. Over the short term, end-of-quarter portfolio adjustments will see profit taking

and switches into fixed income. At the same time, the implicit correlation with the S&P 500 is now at a 10-year low. In our view, bond markets now offer a more attractive risk/return profile. We have in particular reinforced our US duration.

EUROPEAN EQUITIES

More optimistic economic indicators pushed European markets higher. Cyclicals, and especially property and banks, led gains. Composite PMI came in at 49.9, or higher than the 49.7 expected and services stayed in expansionary territory above 50 for the second month in a row. Only manufacturing remained subdued. Germany's ZEW investor sentiment index rebounded sharply in March, rising for the 8th consecutive month.

The first sign of central bank easing came from Switzerland which eased rates by 25bp. The Bank of England, however, left rates unchanged but no committee member voted in favour of a rate hike. Christine Lagarde at the ECB said the bank would not embark on a rate-cutting trajectory after a first cut. The tide has turned but the tone is still cautious.

In company news, **Kering** issued a profit warning, the first cloud to appear in a sector which had enjoyed a rather upbeat earnings season. The group cited a steep drop in revenues at **Gucci** which represents about half of group sales, as well as stagnation in China.

The UK's consumer products giant **Unilever** is to lay off 7,500 people and spin off its ice cream division, a segment which was weighing on margins because of rising costs. The moves should be finalised by end 2025 and save €800m over the next three years.

In tech, German's **Nemetschek** (software) posted excellent 2023 results, proof of its resilience during a transition to cloud products. However, the company was more cautious than expected for this year and the stock sold off. France's **Atos** plunged after **Airbus** ended talks to acquire its bag data and security division.

In AI news, now an essential topic on equity markets, **Nvidia**'s GTC conference provided good news for European companies: Europe's IT services leader **SAP** unveiled a partnership with **Nvidia** for its **SAP Business AI** platform. **Siemens** reinforced its cooperation with **Nvidia** for immersive real-time visualisation, **Schneider** in data centre infrastructure and **Novo Nordisk** in the creation of a super computer in Denmark to drive innovation in healthcare.

US EQUITIES

Indices pushed to fresh highs with the Nasdaq jumping 2.9% and the Dow Jones and Russell 2000 making similar gains.

Investors focused on the **Nvidia** conference where the new Blackwell super AI chip was unveiled, a partnership with **Cadence Design Systems** among others. That was followed on Wednesday by Jerome Powell's comments which highlighted the fact that interest rates were at peak levels in this monetary policy cycle.

A few quarterly reports emerged, most of them well-received by markets. **Fedex** gained ground when its third-quarter earnings guidance was higher than expected. The group said cost savings had helped it cope with reduced demand. Chip maker **Micron** beat expectations across the board and raised full-year guidance, a token of its successful AI positioning. **SuperMicro Computer** ended a period of strong market gains after a share sale turned out to be trickier than expected.

In apparel, **Lululemon** posted upbeat figures but the share price fell as soft US demand is likely to persist in this quarter. **Nike** followed suit by warning on 2024 sales.

Apple continued to struggle with legal issues: the rumour of a partnership with **Google**'s **Gemini** was eclipsed by the Department of Justice's decision to sue the group for monopolising smartphone markets.

JAPANESE EQUITIES

The NIKKEI 225 and TOPIX jumped by 5.17% and 5.06%, respectively. In the first round of responses, wages increased on average by 5.28% in large companies and 4.42% in small & medium sized companies and the Bank of Japan exited negative interest rates on March 19th, the first upward move in 17 years. It also decided to abolish its Yield Curve Control (YCC) and suspend new purchases of ETFs, reversing the large-scale monetary easing policy which had been in place since April 2013. On the other hand, the BoJ governor clearly stated, "Based on the current economic and price outlook, accommodative financial conditions will continue for the time being", and the bank said JGBs could still be bought. The policy change itself had already been widely priced in and confirmation of the bank's accommodating stance worked against bearish sentiment, triggering Yen weakness and sending stock markets to fresh all-time highs.

The yen traded in the mid 148s against the dollar initially before jumping to the high 151s after the BoJ's decision. It ended the period around 151.

EMERGING MARKETS

The MSCI EM Index had gained 1.38% this week as of Thursday, continuing to outperform developed markets thanks to **South Korea** and **Taiwan**, up 5% and 2.1% in USD. Brazil also rose 1.24%. **China** closed up 0.76%, while **India** was almost flat, underperforming other major markets.

In **China**, industrial production rose 7% YoY in January and February, or ahead of the 5.2% estimated. Exports were 7.1% higher, or much better than the 1.9% expected, thanks to the ongoing global industrial upturn. Infrastructure investment grew 9% YoY, helped by the special sovereign bond and the new PSL loan. Corporate capex also increased by 9.4% YoY, largely driven by external demand and new energy. On the other hand, retail sales in the same period missed expectations by only rising 5.5% YoY. The recovery in consumption is underway but consumers remain cautious. 1Y and 5Y LPR were kept unchanged at 3.45% and 3.95%, respectively. The State Council released an action plan to open up the domestic banking/insurance markets to foreign investment. Shareholder return is the key topic during this results season. Results at **Tencent** were in line but management doubled the buyback envelope to 3-4% of market cap. **CATL** also announced a special dividend thanks to strong cash generation. **PDD** posted another all-around strong result, driven by **China** market share gain, overseas expansion and enhanced monetisation. **Tencent Music** also reported a beat on sustained subscription momentum. **Ping An**-s fourth-quarter earnings missed expectations. BYD's Indonesia EV factory is to start production in early 2026. **Ant Group** is planning to set up independent boards for its international, database and digital technology operations.

In **South Korea**, President Yoon called for inheritance tax reforms to remove barriers for companies to participate in the Value Up programme. The government will freeze electricity tariffs going into the parliamentary elections on 10 April. **Samsung** will supply W1tn of AI accelerators to aid their AI ambitions. Jensen Huang said that they are testing Samsung's HBM with "high expectations".

Taiwan's central bank surprised markets by raising its policy rate by12.5bp to 2% to guard against risks to inflation driven by higher electricity tariffs. **TSMC** is looking at building advanced packaging capacity in Japan. **Mediatek** formed a strategic alliance with **Phison** for next-generation AI services. **Pegatron** said they had joined **Nvidia's** supply chain for GB200.

In **India**, the gross direct tax collection for the financial year ending March 31 jumped 18.74% YoY to over 22.3 trillion rupees. The trade deficit widened marginally in February as the nation's import bill rose amid strong domestic demand and rising crude prices. The government announced a new E-vehicle policy lowering import duty from 100% to 15% to attract investments in manufacturing and is studying a tax cut for hybrid cars. A JV between China's **SAIC** and **JSW group** plans to roll out high-end electric cars in **India**. **TVS** approved a $228m bonus issue of preference shares. Airtel unit **Bharti Hexacom** got **SEBI** approval for an IPO.

In **Brazil**, the industry ministry launched a number of investigations into the alleged dumping of industrial products by **China**. **Lula** asked **Petrobras** to reduce its dividend and state-owned banks to cut spreads.

CORPORATE DEBT

CREDIT

Central banks remained centre stage. The Fed said it was planning on three rate cuts by the end of this year. However, there were more signs of the robust US economy with PMI coming in at 52.2. In the end, yields on 10-year US Treasuries fell 8bp to 4.24%. Yields also eased in Europe: the 10-year German Bund fell from 2.46% at the beginning of the week to 2.37%. The surprise move came from Switzerland whose central bank cut rates from 1.75% to 1.5%.

Credit spreads remained tight around 110bp for investment grade with low volatility overall due to strong inflows. But high yield spreads widened slightly by around 10bp to 345bp with pressure resurfacing on issuers like **Ardagh Packing** or **SFR** (**Altice France**) due to their heavy leverage and uncertainty over debt restructuring.

The new issues market, however, stayed busy with deals from **Shaeffler**, **CBR Fashion** and **Fnac**. In financials, **ASR** raised €500m with an RT1 at 6.625%. The news event of the week concerned Austria's **Raiffeisen**. The group was due to issue a new AT1 to refinance its next call but cancelled the deal just before pricing over a supposed US enquiry into the bank's plan to repatriate earnings from Russia. The rumour, however, had no impact on Raiffeisen's AT1 bonds.

Between March 14 and 21, investment grade returned 0.17% thanks to rates easing. The segment is now down only 0.08% YTD. High yield lost 0.3% over the same period but was still up 1.6% YTD thanks to spreads staying resilient over the quarter.

CONVERTIBLES

The convertibles market ended the period higher -despite the recent bounce in inflation- after the Fed said it would stick with its plan to cut interest rates three times this year. Jerome Powell said it would be appropriate to ease "some time this year".

In company news, chip maker **Micron** revised sales guidance higher for the coming quarters thanks to strong demand for AI products. The news benefited the entire tech sector and especially **Western Digital** and **Seagate Technology**.

In Europe, meal delivery group Delivery Hero announced plans to buy in €400m-worth of its 2025 convertibles at 94.75% and €100m of its 2026 convertibles at 89%.

The only new issue over the week was from Japan's **Infroneer Holding** which raised JPY 60bn with a zero-coupon bond due 2028 and with a 15% premium.

GLOSSARY

- Investment Grade: bonds rated as high quality by rating agencies.
- High Yield: corporate bonds with a higher default risk than investment grade bonds but which pay out higher coupons.
- Senior debt benefits from specific guarantees. Its repayment takes priority over other debts, known as subordinated debt.
- Debt is considered to be subordinated when its redemption depends on the earlier payment of other creditors. To offset the higher risk, subordinated Senior debt has priority over other debt instruments.
- Tier 2 / Tier 3 : subordinated debt segment.
- Duration: the average life of a bond discounted for all interest and capital flows.
- The spread is the difference between the actuarial rate of return on a bond and the rate of return on a risk-free loan with the same maturity.
- The so-called "Value" stocks are considered to be undervalued.
- Markit publishes the Main iTraxx index (125 leading European stocks), the HiVol (30 highly volatile stocks), and the Xover (CrossOver, 40 liquid and speculative stocks), as well as indices for Asia and the Pacific.
- EBITDA: Earnings before Interest, Taxes, Depreciation, and Amortization.
- Quantitative easing describes unorthodox monetary policy from a central bank in exceptional economic conditions.
- Stress Test: a process which simulates extreme but possible economic and financial conditions so as to assess any impact on banks and measure their resilience to these events.
- The PMI, for "Purchasing Manager's Index", is an indicator of the economic state of a sector.

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