

# Blog Post

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## WEEKLY MARKET UPDATE

March 25, 2019



**UK Prime Minister Theresa May changed course and met with European Union (EU) leaders late last week. Find out more in this edition of “The Week in Review.”**

### Last Week Review

**U.S. yield curve moves closer to inversion.** Following a dovish Fed and weaker-than-expected manufacturing data, interest rates moved lower across both the U.S. and Germany. The U.S. yield curve further flattened last week, with the 10-year Treasury yield (2.44%) just 12 basis points above the 2-year Treasury yield (2.32%) and even with the 3-month yield (2.44%)<sup>1</sup>. Also, the Germany 10-year bond yield (-0.02%) dropped below zero for the first time since 2016<sup>2</sup>. Global equities dropped 0.5% last week, with gains following the Fed meeting overcome by growth concerns at the end of last week<sup>3</sup>.

**Fed scales back rate hike forecasts in its March meeting.** Following a pivot to a more patient stance in January, the Federal Reserve left policy unchanged in its meeting last week, given subdued inflation and global economic growth concerns. Updated Fed official forecasts revealed a preference to keep interest rate policy unchanged for the rest of 2019 and hike one more time in 2020. Previously, the Fed had been forecasting two hikes in 2019 and one hike in 2020. Market expectations remain below the Fed's with markets implying about a 61% probability of a Fed rate cut by year-end. In other comments, the Fed announced it would slow the pace of its balance sheet reduction in May and conclude the process in September<sup>4</sup>.

**Growth concerns rise following weak Europe manufacturing data.** Flash Purchasing Managers' Index (PMI) data was released late last week, with below-consensus manufacturing data across Europe and the U.S. Readings in Europe (47.6) and Germany (44.7) remain in contractionary (below 50) territory and were especially disappointing since many investors were

looking for signs of a recovery. The U.S. figure also was below consensus and prior levels, but remains in expansionary territory at 52.5. Services PMI data continues to hold up better across the regions, with the U.S. (54.8) and Europe (52.7) somewhat lower than February levels but still above 50.

**The EU offers conditional seven-week Brexit delay.** Following a ruling that her Brexit deal could not be voted on by UK parliament for a third time, UK Prime Minister Theresa May changed course and met with European Union (EU) leaders late last week. EU leaders agreed to extend the March 29 Brexit deadline to May 22 if the Brexit deal is passed by parliament, or April 12 if the UK has no credible path forward on Brexit. The situation remains very fluid, but the recent developments increase the odds of either a no-deal outcome or a long delay to Brexit that could result in UK elections and/or a second referendum. Parliament will meet this week to possibly vote on the Brexit deal for a third time or take additional measures pertaining to Brexit<sup>5</sup>.

### **This Week Preview**

**U.S.-China trade discussions set to continue.** Trade officials from the U.S. and China will meet to discuss some of the more difficult issues such as the quantity of purchases by China and protection for U.S. intellectual property. U.S. President Donald Trump stated that the current tariffs are likely to stay in place for a substantial time period as China hasn't adhered to previous deals. Robert Lighthizer, the U.S. chief trade negotiator, says predicting the timing of a successful deal is difficult due to major issues that still must be resolved. Without a deal, U.S. tariffs on \$200 billion of goods from China would potentially increase from 10% to 25% at an unspecified future date<sup>6</sup>.

**Little change expected in global inflation data.** Inflation data will be released this week in Germany and the U.S. Recent downward movement from Consumer Price Index (CPI) readings in the U.S. at headline and core levels may show a similar pattern for core Personal Consumption Expenditures (PCE). With the exception of last July and a few months in 2012, the Fed's preferred inflation measure has failed to hit the 2% target consistently over the last decade. Consensus expectations call for a 1.9% year-over-year core PCE reading, which would be in-line with the prior level. Outside the U.S., inflation has slowly decreased in Germany after reaching a peak in October 2018. Economist surveys show headline CPI levels of 1.5% y/y in Germany. Low inflation and slowing economic growth have led to a pivot amongst many central banks globally to move away from plans to tighten monetary policy.

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#### End Notes

1. Bloomberg, 2-Year nominal U.S. Treasury rates using data available as of 18Mar2019 – 22Mar2019. Bloomberg, 10-Year nominal U.S. Treasury rates using data available as of 18Mar2019 – 22Mar2019. Bloomberg 3 Month nominal Treasury rates using data available as of 18Mar2019 – 22Mar2019.
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3. Bloomberg, MSCI ACWI (All Country World Index) returns 18Mar2019 – 22Mar2019.
4. Federal Open Market Committee. (March 20, 2019). Chairman Powell's Press Conference [Interview transcript]. Retrieved on 22Mar2019 from <https://www.federalreserve.gov/monetarypolicy/files/monetary20190320a1.pdf>.
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6. Davis, Bob. The Wall Street Journal. High-Level U.S.-China Trade Talks to Resume in Final Push for Deal. Retrieved on 19Mar2019 from <https://www.wsj.com/articles/lighthizer-mnuchin-to-travel-to-beijing-11553015413>.