



CIO OFFICE MORNING MARKET WRAP

7 January 2025

Yesterday's price action can be accounted for in terms of too much of a good thing being a bad thing, or likewise good news becoming bad news. Stocks fell and Treasury yields rose, as a gauge of US services business confidence pointed to quickening growth in December, and a subindex indicated lingering price pressures. The market got hit as a sell-off in technology stocks, the longest duration sector, followed. Nvidia sank about 6% and semiconductors gave up 2%. A separate report showed stronger labor demand boosted by business services. Signs of upwards pressures both on economic activity and price gauges sent Treasuries lower along the curve, with the longer end underperforming. The S&P 500 lost 1.1%, while the Nasdaq shed 2.1%. Rate-sensitive discretionary and IT megacaps led markets lower, with a gauge of the "Magnificent Seven" giving up 2.3%. The economy-sensitive Russell 2000 index of smaller companies dropped by 1.1% as well, whereas bitcoin tumbled by more than 5%. Money market funds bet that the Fed would not cut interest rates before July amidst rising inflationary pressures. The yield on the 10-year note climbed to the highest since April, to settle at 4.68%, while the 30-year closed at 4.9%. Underwhelming demand at the 10-year auction also exercised upward pressure on yields. The US dollar was well bid at the lows of the session as traders pushed out Fed rate cut bets. Brent crude posted gains in six of the last seven sessions with speculators increasing net long positions despite no clear catalysts. Gold was supported by renewed Chinese central bank's buying, that anyway failed to move prices significantly.

Services activity accelerated in December as some businesses made preparations ahead of higher tariffs under the new administration. The headline ISM index rose above expectations to 54.1, while new orders accelerated modestly. Notably, the prices paid component rose to a high of 64.4, under higher uncertainty tied to Washington's new policies. Overall, spending momentum remained quite solid, though it was difficult to distinguish between real business demand and precautionary behaviours. A separate report showed vacancies topped all estimates in November, to rise to 8.1 million. The uptick points to a job market in better shape, with the much-watched vacancies per unemployed person holding steady at pre-pandemic levels. This ties in with Powell's signaling at the December meeting that the central bank's focus had returned firmly to inflation. Shortly investors will have the opportunity to scrutinize the minutes of that meeting to be released today. The highlight for the week remains anyway the Friday's jobs report, projected to show moderating hiring in December to a level that's still healthy.

While US market participants have continued to be on high alert for inflation developments, the CPI release in the euro area was overall benign. European inflation moved up again in December, but on higher energy costs, rather than domestic cost pressures. Generalized disinflation seems to be firmly in place, that should allow the ECB to continue cutting the policy rate, to as low as 2% from the current 3% level, according to some forecasts.

Markets this morning:

Stocks in Asia followed US equities lower after investors pushed back on Fed cut bets in the wake of data suggesting inflation pressures may be reawakening. Equities were lower in Australia and Japan, while US futures contracts were steady following the prior session's losses. Pessimism on Chinese bond markets touched unprecedented levels, as yields on Chinese sovereign bonds reached a 300bps gap with US peers despite the stimulus measures announced by the Beijing authorities. Hong Kong banks are hoarding liquidity despite the central government's calls to help out struggling businesses via increased lending. Samsung Electronics missed earnings estimates on costly efforts to regain market share in the AI chip and smartphone arenas. Oil gained for a second day following a report of another drop in US inventories, while bitcoin fell below \$100,000.

Upcoming Key events/data:

The FOMC minutes to be published later today will shed light on what prompted the Committee to cut at the December meeting, as well as on the details of how the Fed sees the balance of risks related to growth and inflation evolve. The 30-year Treasury auction will be closely watched after the two previous ones, on 3- and 10-year tenors, failed to draw enough investor interest. The noisy jobless claims numbers should lose some of their significance ahead of the Friday's jobs report. Finally, the euro area producer price index will complement yesterday's CPI release, while consumer confidence will provide an update on consumer sentiment in Europe.

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