Confidence must be earned

Amundi ASSET MANAGEMENT

Weekly Market Review

The latest news from financial markets

Edition of 26 March 2018

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The week at a glance

- Market: The equity markets are still in a highly volatile phase. It was a volatile week for core sovereign bonds. The dollar weakened.
- United States: As expected, the Federal Reserve again hiked rates by 25bp, moving the target.
- Eurozone: Confidence is weakening, particularly among PMIs.

KEY FIGURE

5%

Increase in crude oil price in the week.

KEY FOCUS

Brexit: Agreement reached on a transition period from March 2019 to the end of 2020

British and EU negotiators have reached a political agreement on the terms of the transition period that will follow the United Kingdom's departure from the European Union in March 2019. During the 21-month transition period, the UK will remain subject to most of the obligations of EU members but will stop participating in decision-making processes (with a few guarantees in the event of decisions contrary to British interests). However, the "Brexit treaty" must be concluded before this agreement becomes legally binding, meaning additional hurdles must first be overcome, such as the question of the Irish border. Negotiations will continue on this issue and on the future framework of trade relations between the UK and the EU, which will come into effect following the transition period. The British pound reacted positively to the news, which was perceived as reducing the risk of a hard Brexit (at least in March 2019).

KEY DATES

April 26th	May 2nd	June 22nd
European Central Bank (ECB) monetary policy committee	Federal Reserve Bank (Fed) monetary policy committee	OPEC meeting - Vienna, Austria

Source: Amundi Strategy

Our weekly **analysis**

A Federal Open Market Committee more hawkish than it seems

The Fed raised the federal funds rate by 25 bps to 1.75% at its March monetary policy meeting. While the interest rate hike was widely expected, this meeting was long-awaited by the markets that sought i) to confirm the hawkish impression Powell left when making his testimony to the House Financial Services Committee and ii) to find out the new Central Bank forecasts, particularly since the recent passage of the Tax Cuts and Jobs Act.

Broadly speaking, the statement demonstrated that the Fed was confident about economic growth ("The economic outlook has strengthened in recent months") and inflation ("Inflation on a 12-month basis is expected to move up, in coming months"). This confidence was supported by upwardly revised growth forecasts for 2018 and 2019, while the unemployment rate was revised down for the next three years. The projected federal funds path was increased significantly for 2019 and 2020. However, despite this background, it is noteworthy that the inflation forecast remained broadly stable.

This a benign scenario for prices coupled with an unchanged median 2018 dot seemed to have disappointed markets: bonds rallied (yields dropped) while the US dollar lost against all the major currencies, a broad demonstration that markets question the capacity of the Fed to raise rates more than is already priced. Chairman Powell fulfilled expectations of a more hawkish Fed, yet markets were clearly positioned for an even more hawkish stance.

It is very interesting to note that i) only one "dot" kept the median dot for 2018 rising from three to four rate increases at this meeting and as such ii) depending on the upcoming data in the next months it is very likely that the median dot will increase to four hikes in 2018. Taking into account our current scenario for growth (2018: 3%, above the Fed and 2019: 2.4%), Core PCE inflation (2.0% for both 2018 and 2019, and thus also well-behaved) and our revised estimate for unemployment rate (2018: 3.7% and 2019: 3.6%), the possibility of 4 hikes in 2018 becomes increasingly likely.

However, given concerns regarding financial stability and US trade policy which are now becoming more prominent among market participants, a fourth hike is more likely to materialize later in the year, if macro projections are met and risks of a trade war abate.

Index	Return			
Equity markets	**03/23/18**	**1 W**	**1 M**	**YTD**
S&P 500	2644	-3.9%	-3.8%	-1.1%
Eurostoxx 50	3312	-3.6%	-3.8%	-5.5%
CAC 40	5108	-3.3%	-3.9%	-3.8%
Dax 30	11946	-3.6%	-4.3%	-7.5%
Nikkei 225	20618	-4.9%	-5.8%	-9.4%
MSCI Emerging Markets (close -1D)	1197	-1.4%	-1.6%	3.4%
Commodities - Volatility	**03/23/18**	**1 W**	**1 M**	**YTD**
Crude Oil (Brent, $/barrel)	70	5.1%	3.4%	4.1%
Gold ($/ounce)	1344	2.3%	1.2%	3.2%
VIX	23	7.3	6.6	12.1
FX markets	**03/23/18**	**1 W**	**1 M**	**YTD**
EUR/USD	1.23	0.3%	0.3%	2.6%
USD/JPY	105	-0.7%	-1.5%	-6.5%
EUR/GBP	0.87	-1.1%	-1.0%	-1.9%
EUR/CHF	1.17	0.0%	1.7%	0.0%
Credit markets	**03/23/18**	**1 W**	**1 M**	**YTD**
Itraxx Main	+60 bp	+10 bp	+5 bp	+15 bp
Itraxx Crossover	+289 bp	+38 bp	+16 bp	+57 bp
Itraxx Financials Senior	+67 bp	+16 bp	+10 bp	+23 bp

Index	Return			
Fixed Income markets	**03/23/18**	**1 W**	**1 M**	**YTD**
EONIA	-0.37	--	-	-2 bp
Euribor 3M	-0.33	--	--	-
Libor USD 3M	2.27	+7 bp	+31 bp	+58 bp
2Y yield (Germany)	-0.61	-2 bp	-7 bp	+2 bp
10Y yield (Germany)	0.54	-3 bp	-11 bp	+11 bp
2Y yield (US)	2.28	-1 bp	+4 bp	+40 bp
10Y yield (US)	2.84	-1 bp	-3 bp	+43 bp
Eurozone Sovereigns 10Y spreads vs Germany	**03/23/18**	**1 W**	**1 M**	**YTD**
France	+24 bp	-1 bp	-4 bp	-12 bp
Austria	+20 bp	-1 bp	+8 bp	+5 bp
Netherlands	+16 bp	-1 bp	+11 bp	+5 bp
Finland	+11 bp	-2 bp	-2 bp	-7 bp
Belgium	+29 bp	-	-1 bp	+8 bp
Ireland	+43 bp	--	-4 bp	+19 bp
Portugal	+123 bp	+4 bp	-16 bp	-29 bp
Spain	+75 bp	-6 bp	-20 bp	-39 bp
Italy	+135 bp	-6 bp	-6 bp	-24 bp

Source: Bloomberg. Amundi Strategy - 03/23/2018 - 3.00pm