



# Global markets outlook

February 2024

# General overview

## Risk-on sentiment continues into January

MULTI ASSET	1mo	3mo	YTD	1YR	3YR	5YR
Oil Index (USD)	6.2%	-5.5%	6.2%	3.9%	25.3%	-0.9%
GSCI Commodities (USD)	6.2%	-5.3%	6.2%	0.1%	23.5%	9.0%
MSCI World (UH, EUR)	2.9%	13.0%	2.9%	17.0%	12.2%	12.6%
MSCI World local currency	1.8%	14.8%	1.8%	17.7%	9.6%	12.0%
MSCI World (H, EUR)	1.7%	14.3%	1.7%	15.8%	7.9%	10.1%
EMD hard currency (UH, EUR)	1.0%	6.3%	1.0%	5.4%	-0.1%	1.7%
Cash (EUR)	0.4%	1.0%	0.4%	3.6%	1.1%	0.5%
Global high yield (H, EUR)	0.0%	8.3%	0.0%	7.2%	-0.7%	1.4%
EMD local currency (UH, EUR)	-0.1%	5.1%	-0.1%	4.1%	0.8%	1.5%
Global investment grade bonds (H, EUR)	-0.2%	8.0%	-0.2%	3.0%	-4.1%	0.1%
Global Gov Bonds (H, EUR)	-0.6%	5.5%	-0.6%	1.2%	-4.7%	-1.3%
Gold (USD)	-0.7%	3.0%	-0.7%	5.7%	3.0%	8.1%
Global inflation-linked bonds (H, EUR)	-1.5%	4.9%	-1.5%	-1.3%	-5.0%	-0.9%
Global real estate (UH, EUR)	-1.9%	11.8%	-1.9%	-0.6%	5.8%	1.9%
Emerging Markets (UH, EUR)	-3.0%	4.1%	-3.0%	-3.0%	-4.0%	2.1%
Emerging Markets (LC)	-3.5%	5.7%	-3.5%	-0.5%	-4.9%	3.2%

Source: Robeco, Bloomberg

2 All market data to 31 January 2024 unless mentioned otherwise

Commodities finally caught up with the risk-on sentiment boosting other assets on the back of the easing of financial conditions and bumper US GDP prints in Q3 and Q4. The trigger was the escalation of tensions in the Red Sea and attacks on shipping, including a Russian cargo vessel. Oil prices rose sharply, though we believe there is plenty of excess supply from recent OPEC cuts and the US oil boom to cover the longer-term impact of supply disruptions and sanctions.

Bond yields rose as expectations about central bank pivots and the rate cutting cycle got ahead of the reality of strong economic growth and tight labor markets, which may signal that inflation is not defeated. By the end of January, yields had fallen back, as technicals did not confirm their move higher, delivering below-cash returns for the month. The US dollar was a significant beneficiary of the higher-for-longer rate outlook in the US. The trade-weighted dollar rose 2.1% over the month, according to Deutsche Bank.

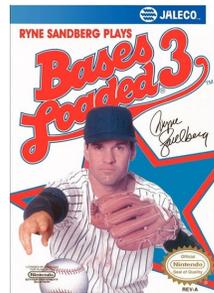
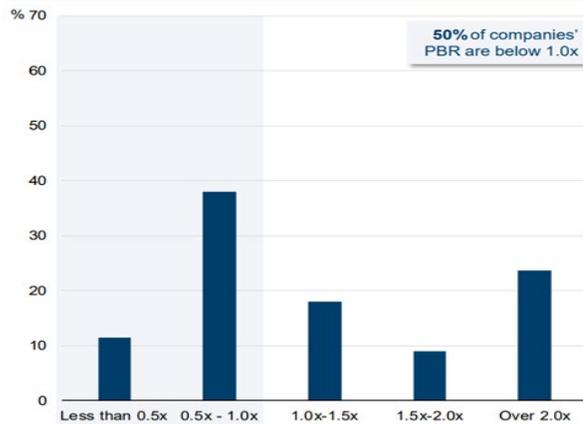
Within equities, Japanese stocks were the standout performer, returning 7.6% (in USD), while Chinese equities failed to respond to policy easing from the authorities, and sentiment remains rock bottom.

The US earnings season kicked off with banks doing ok and overall S&P 500 margins holding up, but the number of companies mentioning plans for lay-offs jumped significantly. The main course of Magnificent Seven announcements continue to beat expectations. So far, investors are rewarding the Mag7, but the field is narrowing further.

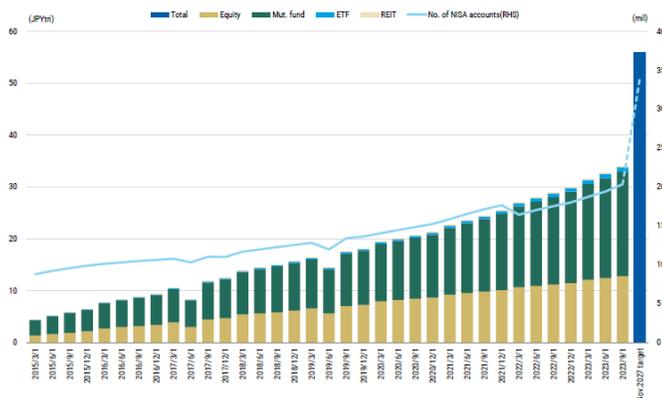
# Theme of the month

## Japan: All bases loaded, ready for a homerun?

PBR distribution of TSE Prime Market names



The regulator forces Japanese companies trading below book to come up with a plan



The best bull markets come from within: 22 mln Japanese invest Y33 trn. Expect this to double.

Source: JPX, FSA, Morgan Stanley

Despite its US origins, baseball is the main spectator sport in Japan. With more than 21 million local fans, the average game attendance in the Nippon Professional Baseball league is nearly 25,000 – impressive for a shrinking population of 125 million. We are rooting for opportunities in Japan, where bases are loaded and the batter is getting ready to put one over the fence. The equity, bond and currency markets are all at inflection points that makes them promising for investment. Let's discuss the three bases in reverse order.

### Third Base: Long Topix

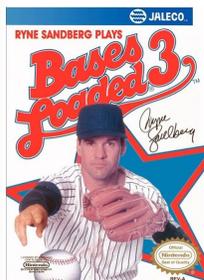
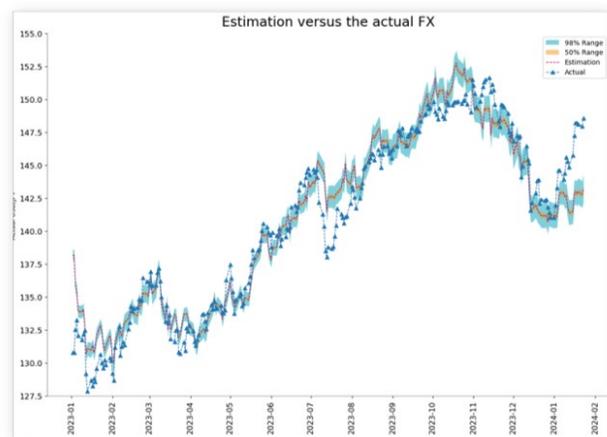
We are long the equity market via Topix futures. This trade already has momentum and may be the first to complete its run around the infield. Since the 1989 bubble high returns have been dismal (1.5% p.a.), but thanks to the much friendlier shareholder return policies, 10-year local returns have been 10.1% annualized – much better than 0% on savings and 0.5% on bonds. Japanese companies are under pressure from investors, the government, and more importantly, also from the regulator. The herd took more than 15 years post-Koizumi to finally move. Listed Japanese companies have been expanding share buyback programs, which totalled JPY 9.6 trillion (USD 65 billion) in 2023, setting a new high for a second consecutive year. Yet, the percentage of Japanese companies that trades below book is still remarkably high at a ballpark number of 50% (30% in Europe, 10% in US). Local investors start to see the opportunity. The Nippon Investment Savings Account (NISA) gives them another push in a country where most people are close to retirement but have 50% of their money in a savings account. The size of the tax-exempt savings scheme is likely to grow to USD 400 billion by 2027. It would be smart to recycle the ETFs held by the BoJ (6% of market cap) via a NISA-ready, tax-exempt ETF structure.

### Second Base: Short JGB

We are short the 10-year bond that trades at a yield of 0.7%. Last October the BoJ tweaked its policy by dropping the defense of the 1.0% level. This needs to be done carefully as financial repression must continue in the interest of debt sustainability. Even if inflation were to reach 2% consistently, Japan would not be able to afford paying 2% on its debts, let alone a positive real rate. Local insurers and banks must support their government at negative real rates. Be mindful also that academics will tell you that  $r^*$  (the natural rate of interest) in Japan is about a negative 1%. The market is distorted with more than 50% of JGBs held by the BoJ. Still, if short-term rates bounce off zero to reach 0.25%, some term premium will need to be offered, so rates between 1-1.5% are our base case.

# Theme of the month

## Japan: All bases loaded, ready for a homerun?



Our yen model shows recent divergence between the price and the spreads

Source: Bloomberg, Robeco

## First Base: Long JPY

We have taken a first step to go long the yen as negative momentum fades. The currency is about 30% undervalued on a real effective exchange rate basis and our model indicates that even with the current spreads, the yen has 5-7% upside. It seems counterintuitive to be long Japanese equity and be long the currency at the same time. Over the past decades, the obvious trade was to be short the currency when you want to go long the equity. Corporate profitability, however, has become far less dependent on international trade, and many companies have learned over many 'expensive yen' years to immunize themselves from the vagaries of the forex market. Still, the tail risk of the world's largest monetary experiment keeps us nimble with tight stop-loss levels.

## Play at the plate: Ueda-san the hitman!

For any chance of a successful homerun in Japan, we need a good hitter. Here we have to rely on BoJ governor Ueda to step up to the plate. Though dovish, Ueda seems to be more open-minded than his predecessor but due to his short tenure, he is an unpredictable hitter. Could he do something unpredictable? Ueda has already hinted we should not expect many hikes, and even removing the NIRP would require a bit more insight into inflation, and especially wage inflation. The next BoJ meeting will be on 19 March – just after the Shunto wage negotiations outcome on 15 March, but before the Fed. It will take some guts to move then. The next one is on 26 April and the one thereafter is already after the June Fed meeting, when the market generally expects US dollar short rates to be cut for the first time. It would be better to at least end the NIRP with one hike, before any hike would move against the US dollar cycle.

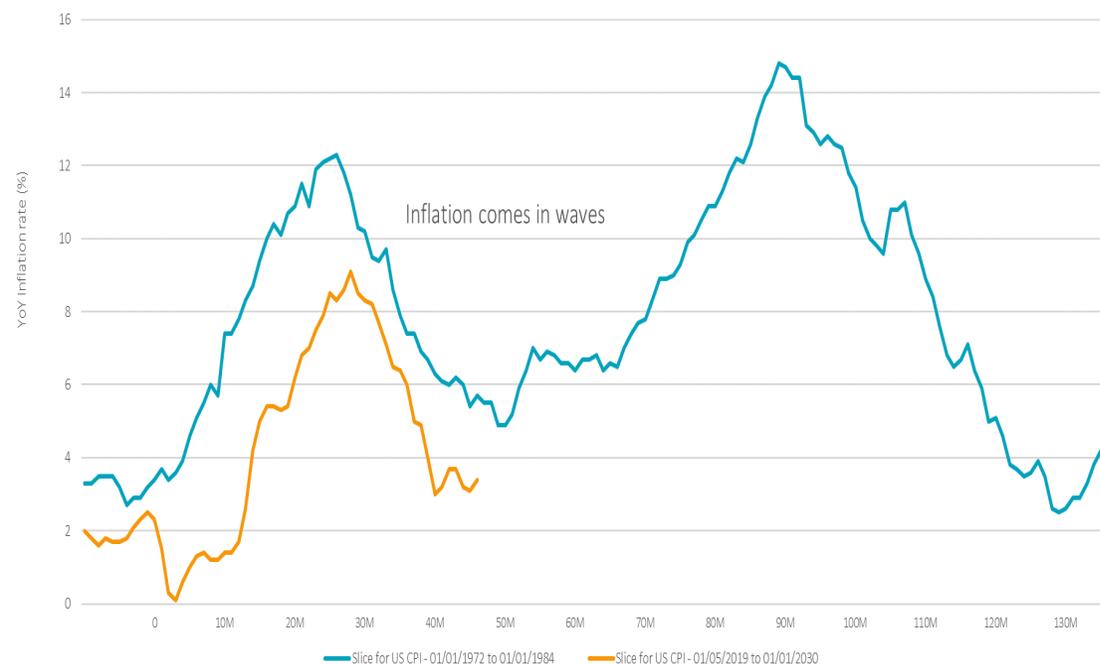
## Pitcher Powell

Indeed, our friendly pitcher is Fed chairman Jerome Powell. Recently, action in all three segments of Japanese financial markets was driven by the Fed's actions and words, not by Japan. For our Japanese bets to perform well, we need more stability in US rate and equity markets. We expect Powell to cut less than currently priced in. This will be an easy pitch for Ueda and will give him more time to hit the ball out of the stadium.

Time for a homerun!

# Economy

## Is the US inflation beast slain ?



Source: Refinitiv Datastream, Robeco

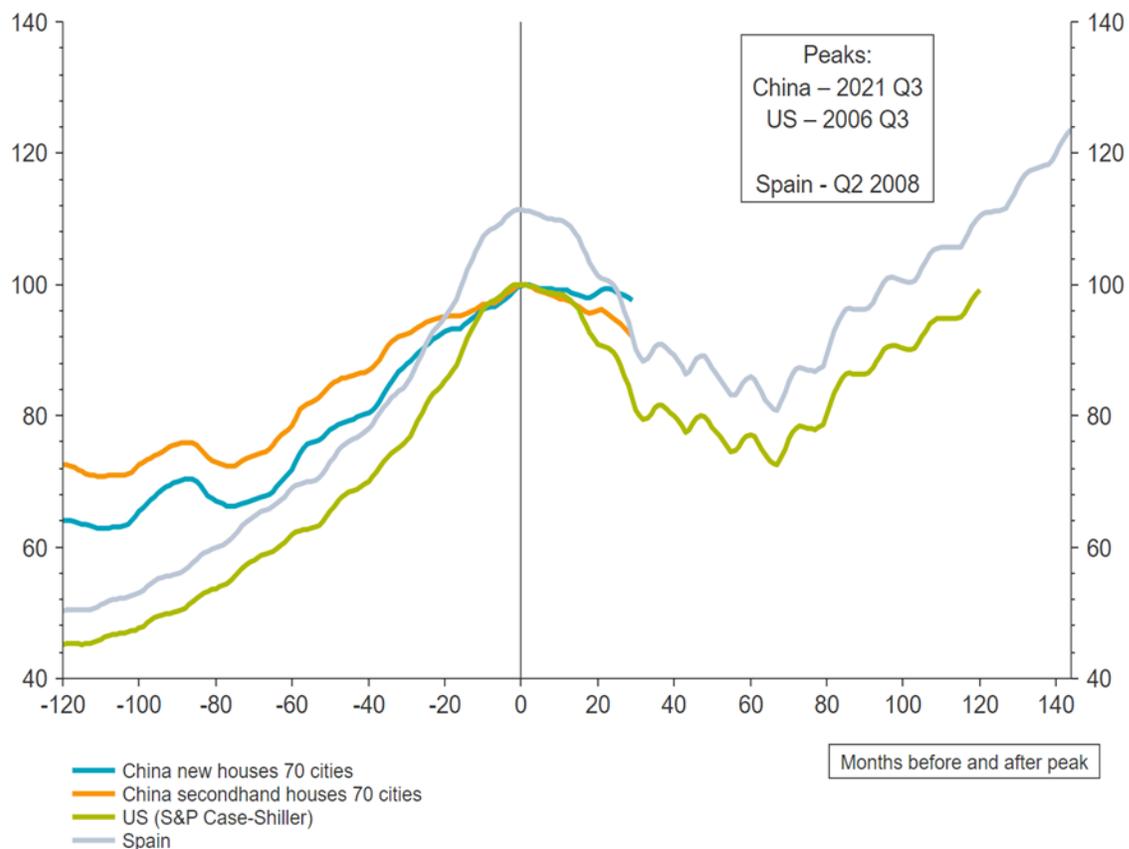
5 All market data to 31 January 2024 unless mentioned otherwise

In general, hopes continued in January for a soft landing in the US and for Europe to avoid recession, which meant risk assets kept up their momentum from November and December. US data surprised on the upside once again, with Q4 growth at annualised rate of 3.3%, while the unemployment rate remained at 3.7% in December. That was also echoed in various surveys, with the University of Michigan's consumer sentiment index rising to a two-and-a-half year high in January. Likewise in the Eurozone, where although growth has been weaker, the single currency area unexpectedly avoided a technical recession in Q4, as GDP was unchanged, rather than contracting by 0.1% as the consensus had expected.

Another important story was geopolitics, as the strikes from the Houthi rebels on commercial shipping in the Red Sea led to significant supply-chain disruption. Against that backdrop, oil prices rose again in January after three monthly declines, with Brent Crude up to USD 83/barrel mid-month. Most notably, freight costs have soared, with Drewry's World Container Index up to USD 3,964 per 40ft container as of 25 January. That's almost triple its levels from late October, when costs were at a post-pandemic low. Tailwinds of supply chain improvements on goods inflation are fading.

Our 2024 outlook does expect the pace of disinflation in the US to continue, but with harder yards ahead. Moreover, the history of previous cycles (see chart) suggests that inflation does not fall in a straight line – hence the Fed pushing against expectations of rate cuts. In addition, the January employment report confirmed the strong GDP growth as the US economy has added over 1m jobs since September 2023, delivering a massive upside surprise in January.

## China's domestic property price drawdowns have a way to go



Source: Refinitiv Datastream, Robeco

Deflationary forces in China's economy are considered structural, caused by the end of an unprecedented credit and investment expansion and China's demographic reversal, and the evidence is well documented. In the short term, the outlook is not much better. China's deleveraging efforts are slowing aggregate demand significantly and taking price indices into deflationary territory. With nominal GDP growth only 4.2% last year, the lowest since 1976 other than during Covid, and Chinese January M2 money supply growing 8.7% year on year, the slowest increase since November 2021, the spectre of a deflationary spiral is looming large.

Until there is a significant easing in fiscal policy, the economy is likely to lose momentum, and so the authorities are starting to announce policy measures. However, observers are sceptical that enough is being done, because the global manufacturing malaise and property issues are headwinds for the economy. We saw deflation for producer prices in 2023, and more recently consumer prices have also started to fall.

Concerns about the property market are front and centre, because for the Chinese consumer, housing is their largest asset. During 2023 we saw a significant rise in bank deposits as concerns about the direction of property prices drove consumers to spend less and save more.

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