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Global Fixed Income Outlook & Strategy

US bond yields now look range-bound, as a tentative effort to extend last year's rally was buried under a winter avalanche of new jobs, in our view. Read more to find out what this could mean to Federal Reserve policy.

Market Recap & Outlook

January payrolls jumped 353,000, following an up-revised 333,000 in December 2023. Average hourly earnings climbed to 4.5% year-over-year, far ahead of inflation. With Purchasing Managers' Index (PMI) also signaling expansion, we believe that the US economy looks to be starting the year in fine shape.

Loomis Sayles Research now looks for the US economy to grow at or near its full employment trend of about 2% this year, given the initial momentum we are starting with, plus the clear gains in real incomes. Fiscal policy seems unlikely to significantly slow the economy, as we are looking for a Federal deficit of more than $1.6 trillion. Capital expenditure intentions also remain positive, and corporate earnings are trending positive, in our view. We do not see many obvious growth threats outside of commercial real estate, where the pain has been well-telegraphed and price discovery and has the potential to be well-advanced.

With the economy looking stronger, we believe that Federal Reserve policy cuts may be delayed for longer. We now look for the first cut of 25bp in June, and a total of 5 cuts may leave the policy rate at about 4.0% at year-end. We believe that the result may be a range-bound Treasury market this spring, and a modest further rally later if the recent trend of 2% core inflation becomes entrenched.

Europe is also seeing wages running ahead of Consumer Price Index (CPI) inflation, and this may be enough to keep the largest countries out of recession in 2024, in our view. We believe that growth will likely be slower than in the US for another year, but positive growth and wage concerns are expected to delay any European Central Bank (ECB) rate cuts into the latter half of the year.

Japan remains the one G-7 nation where we expect a rate hike, but this may only be from -0.1% to plus 0.1% on the policy rate. In our view, the yen remains spectacularly weak on Purchasing Power Parity (PPP) metrics, so more upside inflation or growth surprises are clear risks for the Bank of Japan.

Chinese equity investor sentiment is so poor that some kind of rally seems likely, in our view. We believe back door monetization via new credit lines from the central bank to the policy banks is likely to be part of any solution for anemic equities and falling property prices. In our view, there is little risk to headline inflation from such measures for now given headline deflation but a weaker RMB over time from the expansion of the RMB domestic monetary base is certainly possible.

Our Strategy

Our bond strategy is little-changed: we are duration-neutral ex-Yen, credit cautious, and look for a weaker USD at some point later this year, as the potential for falling US interest rates could affect the currency sentiment.

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Important Disclosures

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