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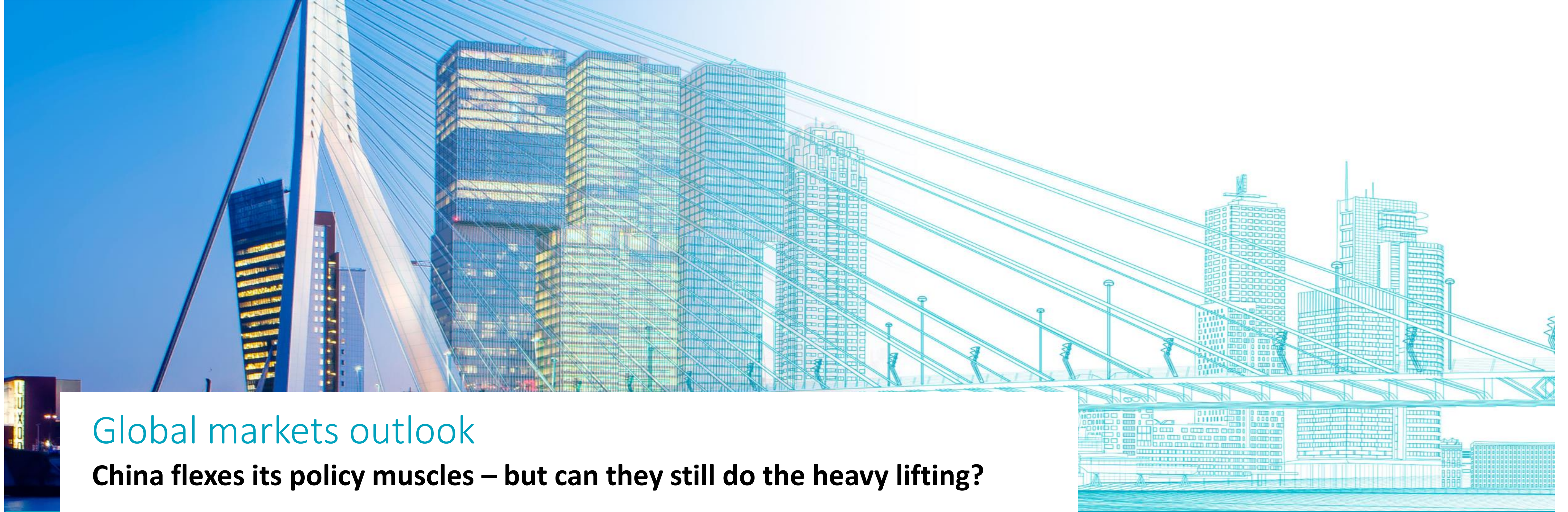

Global markets outlook

China flexes its policy muscles – but can they still do the heavy lifting?

January 2022

For professional investors

Sustainable Investing Expertise by ROBECOSAM

Heat Map Asset Returns (in euros)

MULTI ASSET	1mo	3mo	YTD	1YR	3YR	5YR
Oil Index (USD)	14.0%	2.8%	62.2%	62.2%	-4.8%	-6.5%
GSCI Commodities (USD)	6.5%	3.4%	51.0%	51.0%	8.2%	1.3%
Global real estate (UH, EUR)	5.8%	13.8%	39.6%	39.6%	12.5%	6.6%
MSCI World local currency	4.0%	8.1%	24.2%	24.2%	21.5%	14.5%
MSCI World (H, EUR)	3.9%	7.9%	23.3%	23.3%	19.8%	12.7%
MSCI World (UH, EUR)	3.2%	9.8%	31.1%	31.1%	21.9%	13.3%
Gold (USD)	2.9%	4.0%	-4.3%	-4.3%	11.0%	8.4%
Global high yield (H, EUR)	1.5%	-0.6%	1.5%	1.5%	5.1%	3.1%
Emerging Markets (LC)	1.5%	-0.9%	-0.2%	-0.2%	12.0%	10.5%
EMD local currency (UH, EUR)	1.2%	-0.8%	-2.8%	-2.8%	3.9%	2.5%
Emerging Markets (UH, EUR)	0.8%	0.6%	4.9%	4.9%	11.1%	8.2%
EMD hard currency (UH, EUR)	0.5%	-0.7%	-1.8%	-1.8%	2.2%	1.3%
Cash (EUR)	0.0%	-0.1%	-0.5%	-0.5%	-0.5%	-0.4%
Global investment grade bonds (H, EUR)	-0.2%	-0.2%	-1.7%	-1.7%	4.7%	2.7%
Global Gov Bonds (H, EUR)	-1.0%	0.0%	-3.1%	-3.1%	2.1%	1.3%
Global inflation-linked bonds (H, EUR)	-1.8%	2.9%	4.5%	4.5%	5.9%	3.2%

Fixed Income	1mo	3mo	YTD	1YR	3YR	5YR
High Yield US (UH, USD)	1.9%	0.7%	5.3%	5.3%	8.8%	6.3%
High Yield Europe (EUR)	0.8%	-0.3%	3.5%	3.5%	5.6%	3.9%
Inflation-linked US (UH, USD)	0.3%	2.4%	6.0%	6.0%	8.4%	5.3%
Inflation-linked Europe (EUR)	0.1%	1.7%	6.3%	6.3%	5.3%	3.2%
EMD local currency (UH, EUR)	0.1%	0.3%	-0.8%	-0.8%	3.0%	2.0%
EMD hard currency (UH, EUR)	0.0%	1.1%	4.8%	4.8%	5.6%	2.9%
Europe Senior Financials (EUR)	0.0%	-0.7%	-0.6%	-0.6%	2.6%	1.9%
Investment Grade US (UH, USD)	-0.1%	0.2%	-1.0%	-1.0%	7.6%	5.3%
Investment Grade Europe (EUR)	-0.1%	-0.7%	-1.0%	-1.0%	2.6%	1.8%
Europe Non-financials IG (EUR)	-0.2%	-0.6%	-1.2%	-1.2%	2.7%	1.7%
Japan Gov Bonds (H, JPY)	-0.3%	-0.2%	-0.6%	-0.6%	0.1%	0.3%
US Gov Bonds (H, EUR)	-0.8%	0.0%	-3.5%	-3.5%	2.5%	1.2%
Euro Covered Bonds (EUR)	-0.8%	-0.7%	-2.2%	-2.2%	0.8%	0.7%
Global Gov Bonds (H, EUR)	-1.0%	0.0%	-3.1%	-3.1%	2.1%	1.3%
Spain Gov Bonds (EUR)	-1.4%	-0.6%	-3.1%	-3.1%	3.2%	2.6%
Italy Gov Bonds (EUR)	-1.4%	-1.5%	-3.0%	-3.0%	5.0%	2.9%
German Gov Bonds (EUR)	-1.7%	0.2%	-2.7%	-2.7%	1.1%	0.8%
France Gov Bonds (EUR)	-1.8%	-0.2%	-4.1%	-4.1%	1.8%	1.4%

Equities: Country Indices	1mo	3mo	YTD	1YR	3YR	5YR
France (EUR)	6.5%	9.9%	31.9%	31.9%	17.8%	11.1%
Italy (EUR)	5.9%	7.7%	27.3%	27.3%	18.1%	10.9%
Switzerland (CHF)	5.9%	10.6%	23.7%	23.7%	18.9%	13.0%
Eurozone (EUR)	5.8%	6.4%	23.3%	23.3%	15.2%	8.0%
Korea (KRW)	5.6%	-1.8%	1.3%	1.3%	14.6%	8.7%
Germany (EUR)	5.2%	4.1%	15.8%	15.8%	14.6%	6.7%
Spain (EUR)	5.2%	-0.4%	10.3%	10.3%	3.4%	1.4%
UK (GBP)	4.8%	4.7%	18.4%	18.4%	7.1%	4.7%
USA (USD)	4.5%	11.0%	28.7%	28.7%	26.1%	18.5%
Global equities (LC)	4.0%	8.1%	24.2%	24.2%	21.5%	14.5%
Japan (JPY)	3.6%	-2.1%	6.7%	6.7%	15.0%	10.6%
Global equities (EUR)	3.2%	9.8%	31.1%	31.1%	21.9%	13.3%
Brazil (BRL)	2.9%	-5.5%	-11.9%	-11.9%	6.0%	11.7%
Australia (AUD)	2.7%	2.0%	17.0%	17.0%	13.3%	9.5%
Netherlands (EUR)	2.6%	3.4%	27.7%	27.7%	17.8%	10.6%
India (INR)	2.1%	-1.3%	23.2%	23.2%	18.6%	18.3%
Emerging Markets (LC)	1.5%	-0.9%	-0.2%	-0.2%	12.0%	10.5%
Asia ex Japan (LC)	1.0%	-1.4%	-3.1%	-3.1%	11.8%	10.7%
Emerging Markets (EUR)	0.8%	0.6%	4.9%	4.9%	11.1%	8.2%
Hong Kong (HKD)	-0.3%	-4.7%	-11.8%	-11.8%	-0.2%	4.7%
Russia (RUB)	-2.7%	-7.2%	15.1%	15.1%	17.1%	11.1%
China (HKD)	-3.2%	-6.1%	-21.7%	-21.7%	7.8%	9.4%

FX versus the EUR	current level	1M	3M	YTD	12M	1m	3m	Ytd	1yr
EURO/NORWEGIAN KRONE	10.02	2.2%	1.0%	4.4%	4.4%	10.25	10.13	10.48	10.48
EURO/AUSTRALIAN DOLLAR	1.56	1.6%	2.3%	1.4%	1.4%	1.59	1.60	1.59	1.59
EURO/INDIAN RUPEE	84.21	1.4%	2.2%	6.2%	6.2%	85.41	86.10	89.76	89.76
EURO/BRITISH POUND	0.84	1.3%	2.1%	5.9%	5.9%	0.85	0.86	0.89	0.89
EURO/SINGAPORE DOLLAR	1.53	0.9%	2.4%	5.0%	5.0%	1.55	1.57	1.61	1.61
EURO/CANADIAN DOLLAR	1.44	0.8%	2.1%	7.5%	7.5%	1.45	1.47	1.55	1.55
EURO/INDONESIAN RUPIAH	16135.59	0.8%	2.9%	6.6%	6.6%	16265.28	16612.38	17284.80	17284.80
EURO/BRAZIL REAL	6.34	0.6%	-0.6%	0.1%	0.1%	6.38	6.30	6.34	6.34
EURO/SWISS FRANC	1.04	0.4%	3.8%	4.0%	4.0%	1.04	1.08	1.08	1.08
EURO/CHINA RENMINBI	7.22	0.3%	3.3%	9.8%	9.8%	7.24	7.47	8.00	8.00
EURO/SOUTH KOREAN WON	1346.25	-0.1%	2.1%	-1.0%	-1.0%	1344.60	1375.11	1332.83	1332.83
EURO/HONG KONG DOLLAR	8.86	-0.3%	1.7%	6.4%	6.4%	8.84	9.02	9.47	9.47
EURO/US DOLLAR	1.14	-0.3%	1.8%	6.9%	6.9%	1.13	1.16	1.22	1.22
EURO/SWEDISH KRONA	10.29	-0.6%	-1.5%	-2.4%	-2.4%	10.23	10.14	10.05	10.05
EURO/RUSSIAN RUBLE	85.47	-1.6%	-1.5%	5.7%	5.7%	84.10	84.21	90.64	90.64
EURO/JAPANESE YEN	130.90	-2.0%	-1.6%	-3.7%	-3.7%	128.32	128.88	126.18	126.18

Source: Bloomberg

All market data to 31 December unless mentioned otherwise

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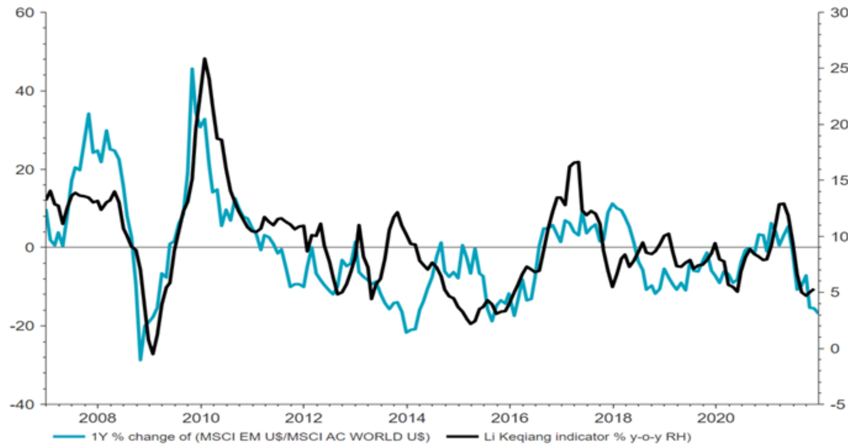
Theme of the month

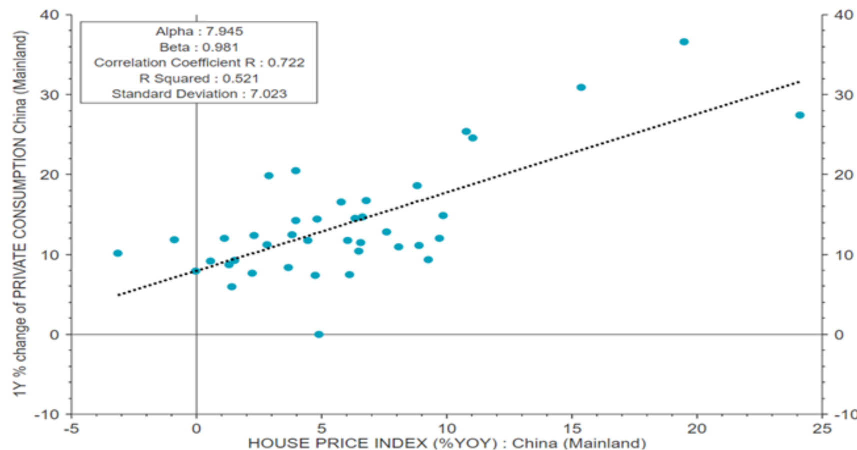
China flexes its policy muscles – but can they still do the heavy lifting? (I)

EM: feeling the pinch of a slowing China



Source: Refinitiv Datastream , Robeco

Economy: the correlation between house prices and consumption

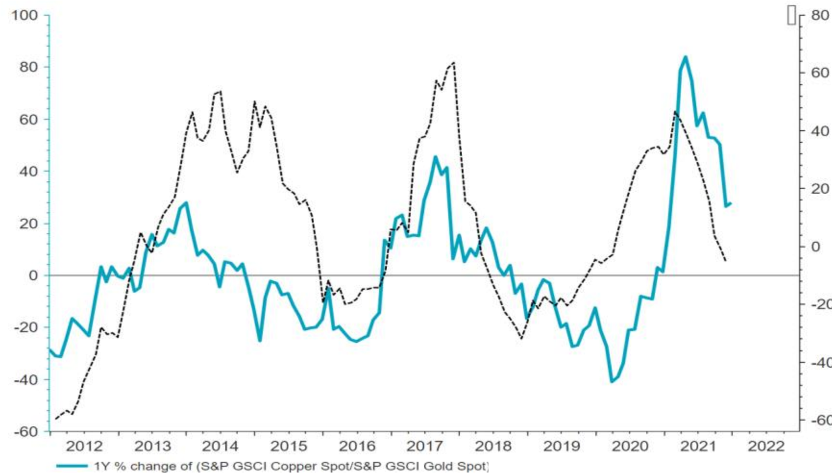


Source: Refinitiv Datastream & Robeco

- In 2022, China will likely be top of mind for investors, even disregarding the Winter Olympics to be held in Beijing. China has determined around 30-40% of global GDP growth in the last decade, and it led the economic cycle into recovery in 2020. However, in 2021, China's contribution to global growth faltered on the back of a policy-induced deceleration domestically while developed economies caught up.
- China's main domestic engines of growth – real estate, manufacturing and infrastructure – have been sputtering lately. With the monetary and fiscal impulse expected to decrease in the West into 2022, the fate of the Chinese growth trajectory becomes all the more important for the global economy. Therefore, now more than ever, investors should ask themselves: "What is on Beijing's 2022 wish list?" It is clear that emerging market equities have struggled compared to developed markets, with stock prices notably pulled down by Chinese equity performance. 2021 saw a remarkable socio-economic paradigm shift initiated by Chinese policymakers towards a more inclusive economy. 'Common prosperity' has been the buzzword, portraying a political agenda designed to reduce inequality through wealth redistribution, and by improving welfare policies at home.
- In terms of wealth inequality, Chinese society is largely on par with the US, with the richest 1% of households owning one-third of the country's wealth. It is President Xi Jinping's fear that if this inequality persists, it will erode the middle class. This would lead to polarization and the rise of the kind of populism seen in the US, potentially challenging the Communist Party. The Chinese political establishment realizes that the country's major problems are to be found at home, given a very high total debt-to-GDP ratio of 270%, an ageing population that is starting to gradually worsen the dependency ratio, and increasing environmental costs.

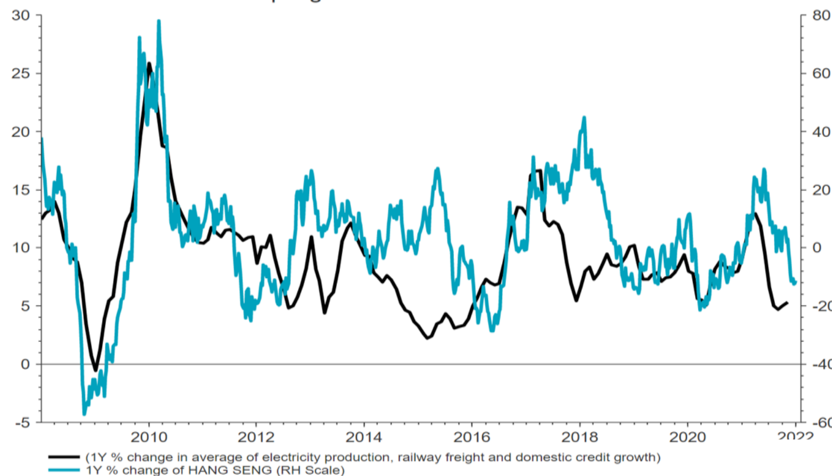
Theme of the month

Credit impulse leads global cyclical indicators



Source: Refinitiv Datastream & Robeco

The slowing of the Chinese economy is being felt across Asia



Source: Refinitiv Datastream , Robeco

China flexes its policy muscles – but can they still do the heavy lifting? (II)

> To address these long-term challenges, the Common Prosperity program is concentrated around boosting productivity growth and reducing economic inequality. Implementation is key, and so policy makers have tightened the thumbscrews on sectors with significant concentrations of wealth and market power, notably the real estate, technology and education sectors. The PBOC's three red lines policies – a liability-to-asset ratio of less than 70%, a net gearing ratio of less than 100%, and a cash-to-short-term-debt ratio of more than 1x – amounted to forced deleveraging in the real estate sector. The most infamous casualty of this was Evergrande, which is now entering a debt restructuring process.

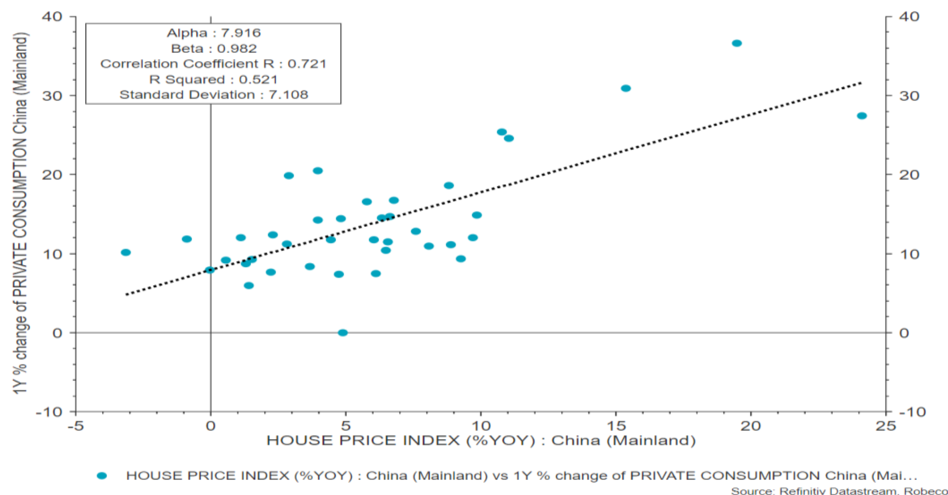
> The evidence is inconclusive as to whether this has worked, as it is hard to read the tea leaves in Beijing. The ongoing slowdown in housing sales and house prices from the crackdown hurts domestic consumption growth as the 'wealth effect' is eroded. There is historically a strong positive correlation between Chinese consumption growth and house prices, as the largest chunk of household wealth is determined by real estate assets. Lastly, there is another obstacle for domestic demand recovery: Omicron. Given the zero tolerance Covid strategy, and the evidence emerging about the ineffectiveness of the Sinovac vaccine to protect against Omicron (even after a booster), lockdown intensity could increase in China in the near term.

> Looking ahead, Chinese policymakers will have to show their agility and ability to slalom around all these downside risks to growth. Easing monetary policy through further RRR cuts and a bottoming out of the credit impulse in H1 2022, along with the use of fiscal stimulus and a loosening of housing regulations are the most obvious policy tools. Though China's policy muscles have clearly been flexed, the jury is still out on whether they can still do the heavy lifting.

All market data to 31 December unless mentioned otherwise

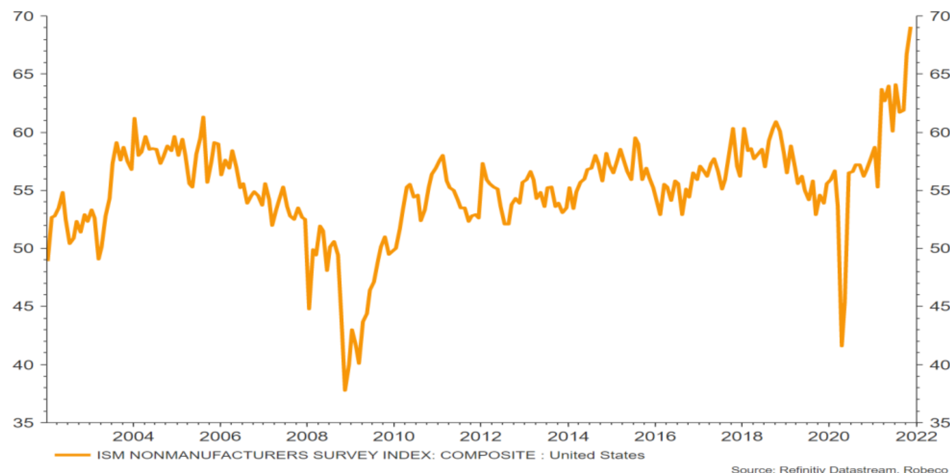
Economy (I)

China: strong correlation between house prices and consumption



Source: Refinitiv Datastream

The US economy is in full swing



Source: Refinitiv Datastream & Robeco

> As the new, more contagious Omicron variant started to outrun the Delta variant in parts of the developed world, lockdown intensity increased in the second half of December. Although this development has slowed macroeconomic momentum in developed economies somewhat, macroeconomic surprises to consensus remained in positive territory past month. Local lockdowns also increased in China, but so far the Chinese economy is continuing its recovery. The cost pressures for Chinese corporates eased to some extent, with the official China manufacturing producer confidence leading indicator rising to 50.3 in December from 50.1 in November. The Chinese services sector is also showing accelerating expansion, with the non-manufacturing index rising to 52.7 in December from 52.3 in November. However, slowing house prices and house sales following the policy crackdown in the real estate sector are inhibiting domestic consumption growth, leaving the tail risk of a hard landing of the Chinese economy still on the table.

> In the US, economic activity remained robust during December, even as the increase in the Omicron cases presented a drag around the turn of the year. The four-week moving average of US jobless claims even dropped further, touching the lowest level observed since 1969. Core capital goods orders signal an increase in investment while businesses are restocking inventories, contributing to economic growth in Q4. The latest inflation data from November show an increase in the core PCE of 4.7% (y-o-y), the highest since 1989.

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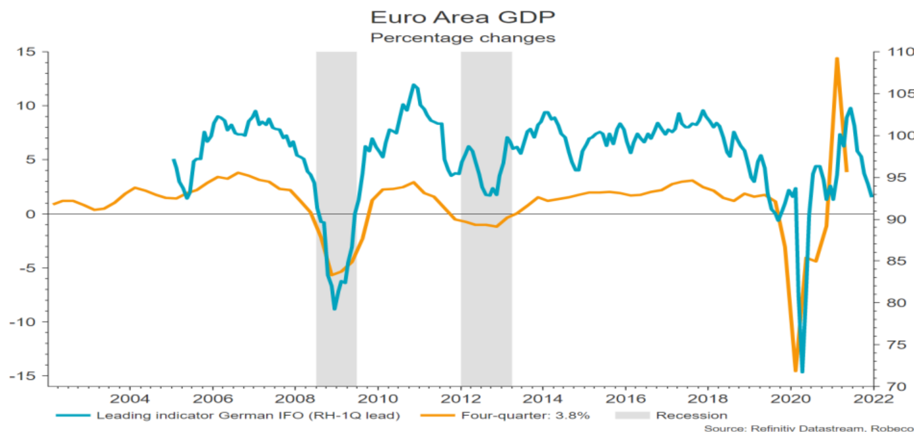
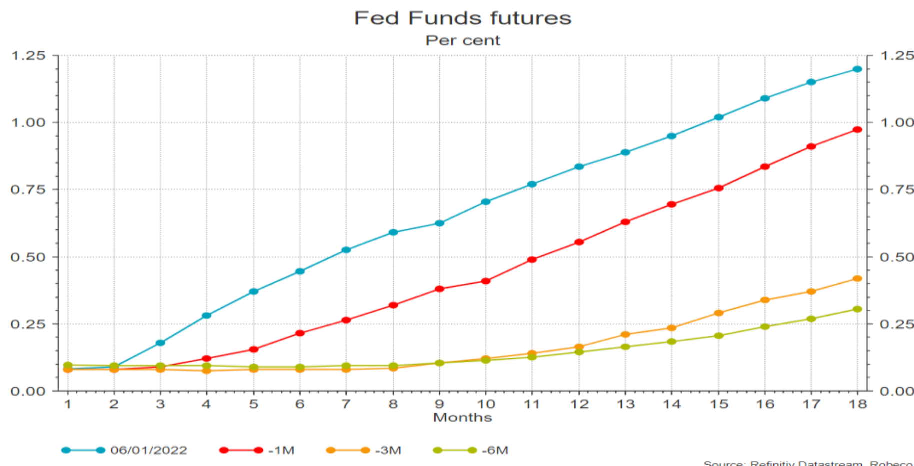
Economy (II)

IFO slump suggests Eurozone growth is losing pace in Q1



Source: Refinitiv, Robeco

Fed fund futures curve steepened after hawkish Powell comments



Source: Refinitiv, Robeco

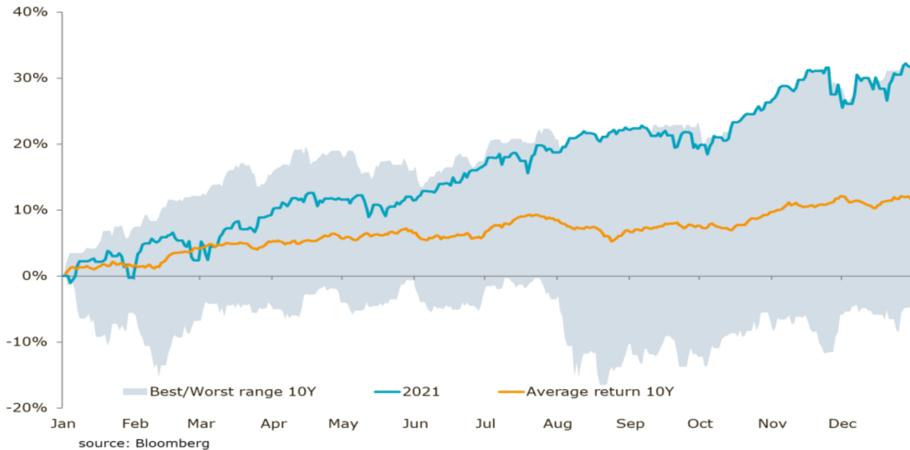
> In the Eurozone, the rise in Covid cases due to the Omicron wave has led to increased travel restrictions. The Google mobility index for the Eurozone declined in the last week of December. Another near-term headwind for the Eurozone economy is the ongoing energy crisis. Eurozone gas prices have been increasing 10-fold to EUR 100 per MWh, harming business sentiment. Downside risks to energy security remain in the face of increasing tensions between Russia and NATO. Tighter restrictions have weighed on Eurozone sentiment. The December PMI shows a notable decline in services activity in the Eurozone, led by Germany, which saw the services leading indicator fall below the level that signals contraction at 48.7 (down from 52.7 in November). The German IFO survey showed that pessimism about the first half of 2022 has increased. However, the Markit services sector survey shows providers are still optimistic about the 12-month outlook and expect the pandemic to be under control on this horizon.

> The third week of December brought further rate hikes by central banks in Norway, Chile, Mexico, Colombia, Russia, and Hungary. In the same week, the Bank of England also delivered its first pandemic-era rate hike, while the Fed announced it was speeding up the completion of its asset purchase program, paving the way for rate hikes in 2022. One might get the impression that global central banks are rushing to exit their loose policies, but that is not the case. In the world's second-largest economy, the Chinese central bank has recently shifted to a fully fledged easing mode, and in the world's third-largest economy, the Japanese central bank is only stepping away very slightly from a very accommodative policy.

All market data to 31 December unless mentioned otherwise

Equities (I)

MSCI World in euros had another double-digit return year



Source: Refinitiv Datastream & Robeco

Equity factors are going for quality

Source: Refinitiv Datastream , Robeco

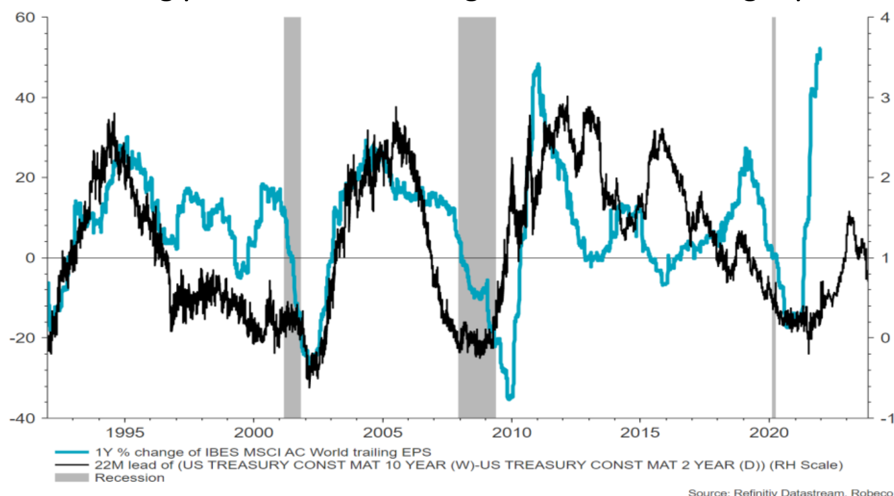
- Overall, 2021 was another stellar year for equities, but one with great underlying divergences at the regional and sectoral levels. The MSCI World Index in euros gained 3.2% in December to end the year 31.1% higher than the year before. Emerging markets fared less well, with the MSCI Emerging Markets index generating returns below their historical average with a total return of 4.9% (unhedged in euros), mainly due to a strong dollar, an early tightening cycle by emerging market central banks to tame inflation, and a policy-induced slowdown in China.

- The 2021 bull run was underpinned by low real interest rates and ample liquidity. Yet, this has not been a momentum driven bull market in which past winners were automatically future winners, as the momentum factor underperformed the AC World benchmark as well as other styles. As investors dropped their reflation trades in Spring 2021, the past winners of this trade lagged the more growth factor-tilted regions and sectors. After the steep multiple expansion of 2020, investors focused on corporate fundamentals, with the quality factor outperforming. This focus on healthy balance sheets is somewhat remarkable as the rising tide of earnings growth has lifted all boats, including those corporates with higher gearing ratios or lower cash levels. Value stocks had a good run as well, despite the reversal of the reflation trade, a largely sideways moving sovereign bond yield during the year, and negative growth surprises in the second half of 2021 on the back of the Delta variant Covid wave. Historically, low valuations of the value factor compared to the growth factor have also provided a tailwind.

- Sectors with a high correlation to medium-term inflation expectations like Energy did particularly well in 2021. Technology stocks benefitted from strong earnings justifying elevated valuation levels to some extent.

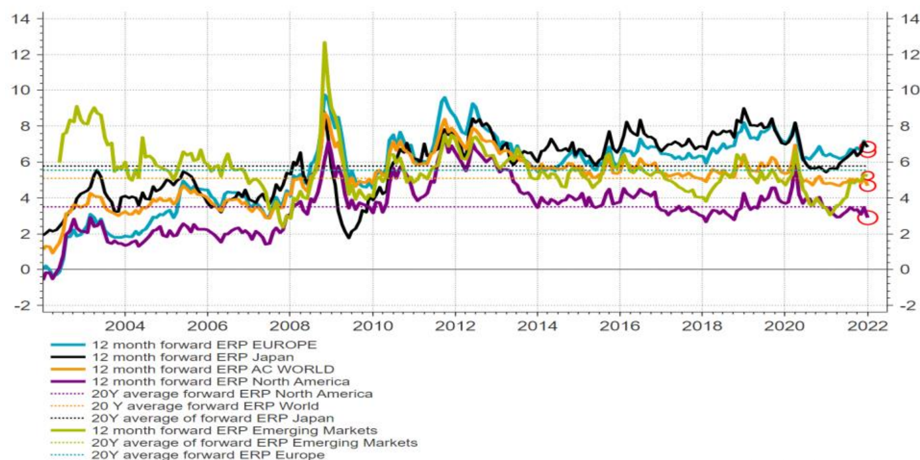
Equities (II)

Flattening yield curve: a warning shot for the earnings cycle



Source: Refinitiv, Robeco

Japan and Europe are above historical average risk premiums

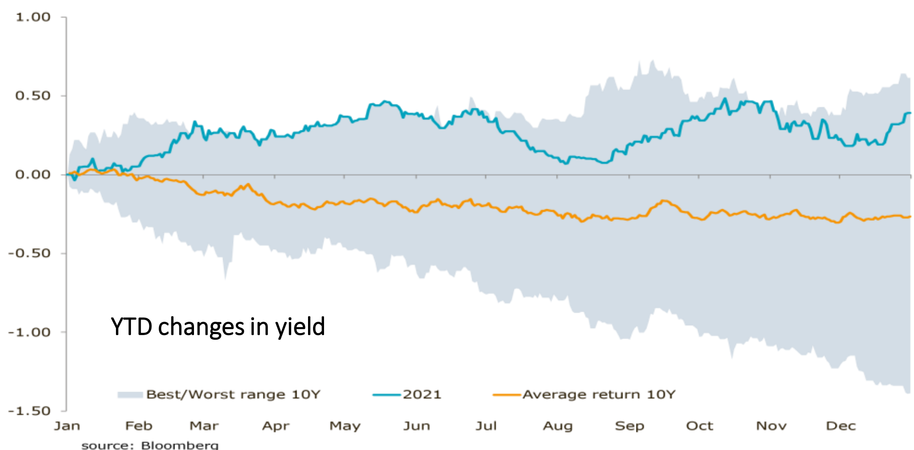


Source: Refinitiv, Robeco

- However, the few big winners have been increasingly determining overall index performance. A decreasing breadth is a late cycle phenomenon.
- Despite several indicators flashing late cycle or even bubble territory – the debt margin of retail investors is back at the levels seen in 2001 and 2007, and the Shiller CAPE is at 39.6 – other fundamentals suggest that this bull run is not exhausted. In our view, continuing positive economic momentum, the very low level of real interest rates and still-abundant liquidity are all highly supportive for equities. However, looking ahead, the thrust of these factors will diminish as the year progresses. From here, it's more likely that we're going to get the equity returns this year rather than next year or the year after that – returns will be front-end loaded, with a skew towards the first half. The excess liquidity that investors are enjoying will decline substantially once the tightening cycle in developed markets take shape. And it's very likely even the ECB will join the Fed and BoE in tightening by 2023 or 2024. The correlation between equity market returns and the balance sheet expansion of central banks has been very high and positive. If balance sheet expansion decelerates, equity markets will take a hit.
- Consensus earnings expectations are too low for next year given the above-trend nominal growth that we expect to materialize for developed economies. Margins are currently above trend, though they will only start to top out when corporate pricing power begins to erode later in 2022. So, we do see more upside in equities for at least the next few quarters, and equity risk premiums are still positive relative to bonds, keeping the TINA narrative alive.

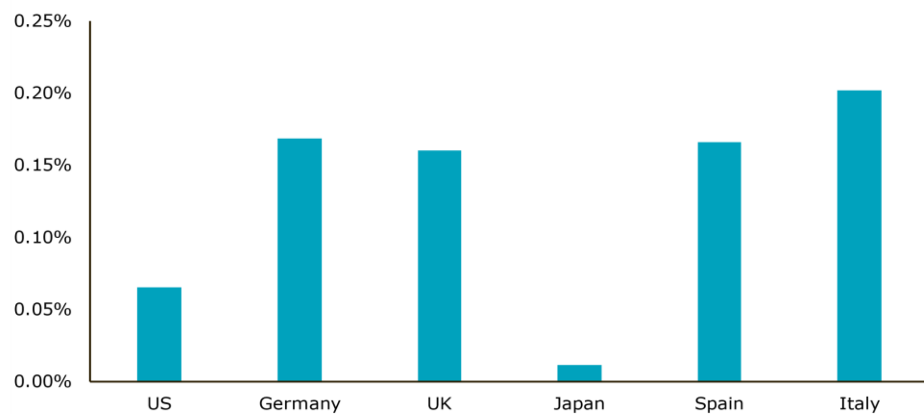
AAA Bonds

German 10-year yields in perspective: breaking bad



Source: Bloomberg, Robeco

10-year yields are moving higher



Source: Bloomberg, Robeco

> In December, 10-year yields found a bid and were pressured upwards. European rates led the way this month. The biggest rises were seen in peripheral 10-year yields, closely followed by the UK. It has become very clear from the latest round of central bank meetings that we have reached an inflection point in monetary policy. While not completely unexpected, the timing of the change in tone does add to the hawkishness of the message. It was delivered at a time that a more contagious Covid strain was starting to spread and the macroeconomic consequences of this were uncertain.

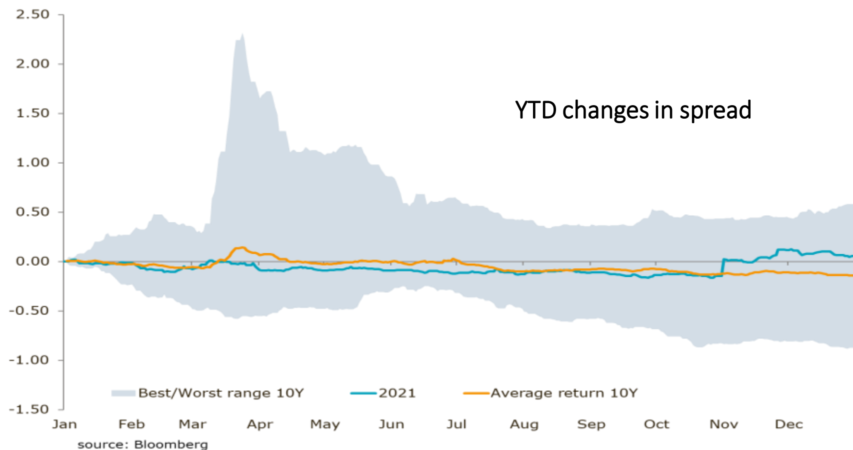
> The rise in European 10-year rates was triggered by the ECB announcement that bond purchases under the PEPP program will come to an end, and that the general asset purchase program will only slightly be increased to compensate. So, going forward, less structural support will be provided to peripheral rates.

> When comparing the year-to-date rate changes of the German 10-year yield in 2021 to the past decade, it immediately becomes obvious that it was a quite an extraordinary year. For a substantial part of the year, particularly in the first two quarters, the year-to-date changes were the highest we have seen over the past decade.

> We agree that inflation is transitory and will at some point start to come down, but think it will settle at a higher level than the past cycle. That is why we think that the terminal rate for this cycle will be higher than what the market currently expects.

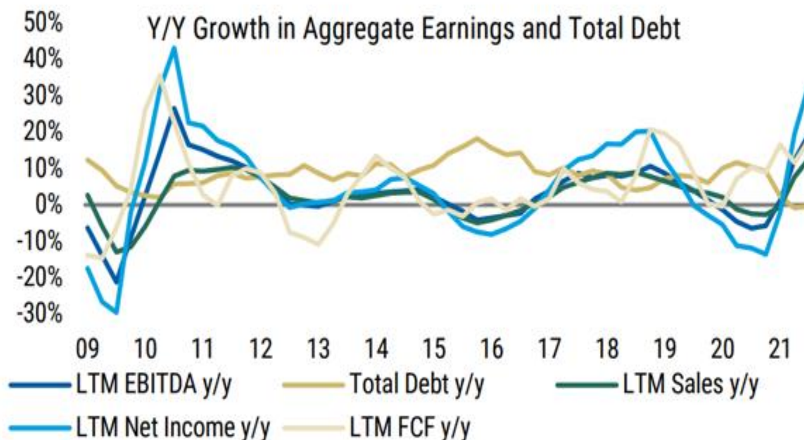
Investment Grade Credits

Investment grade credits spreads widened in December



Source: Bloomberg, Robeco

US investment grade fundamentals remain strong and supportive



Source: Morgan Stanley Research, Bloomberg

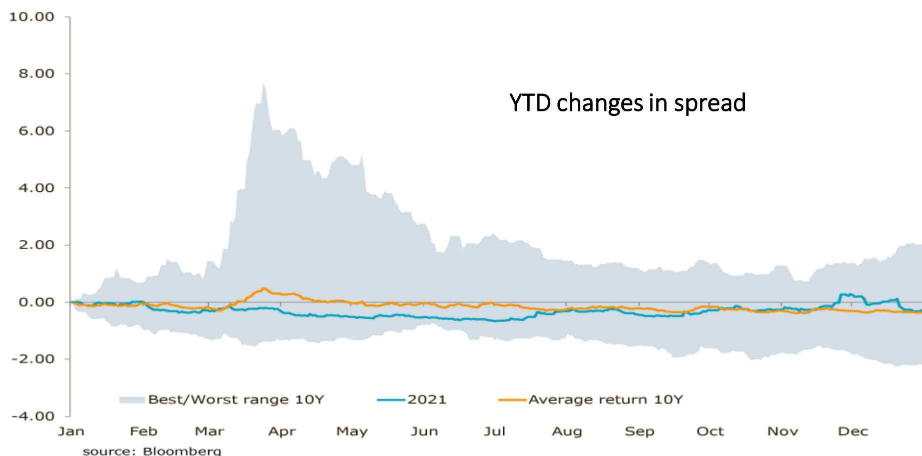
> Global investment grade bonds (denominated in US dollars) delivered a gain of 30 basis points in December. Hedged into euros, the index lost 20 basis points. The difference in performance is explained by the appreciation of the dollar against the euro. The spread tightened by 7 basis points and this tightening was the main driver of returns this month. 2021 is the first negative return year in three years for the asset class (denominated in US dollars). When one looks at 2021 in the context of the past ten years, then it was to some extent a boring year, with spreads remaining in a relatively tight range of around 20 basis points. What is striking is that in the final months of the year there was more upward pressure on spreads than usual.

> Over the last month, one thing has become very clear, and that is most major central banks have concluded that the time has come to start closing the taps on the immense amount of liquidity they have provided since the start of the pandemic. Normally, the beginning of a tightening cycle doesn't immediately lead to higher spreads, as the reason why central banks tend to hike is due to a strengthening economy. With economic growth in general expected to remain above trend, and earnings also expected to remain healthy, there is no reason to expect a sudden rise in default rates.

> As has been the case for quite a while, the risk for the asset class is not an immediate deterioration of fundamentals. This continues to leave the door open for tighter spreads. Given the tightness of the current spread and the relatively high duration of the asset class, we think spreads offer an insufficient buffer to absorb rising rates.

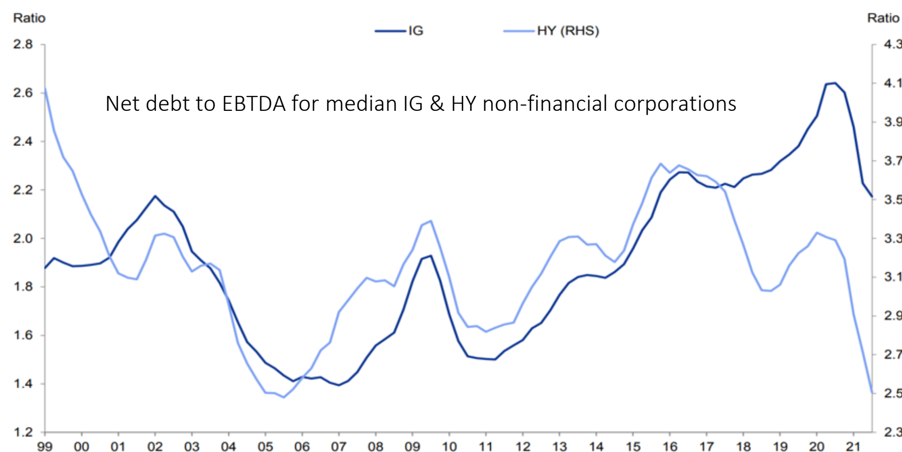
High Yield

Global high yield spreads widened for the third time in a row



Source: Bloomberg, Robeco

US high yield fundamentals remain supportive



Source: FactSet, Goldman Sachs Global Investment Research

> After three months of back-to-back widening, spreads tightened by almost 57 basis points in December. This almost completely reversed the widening of the last three months. The asset class increased in value by about 1.85%, mainly driven by spread compression. For the whole of 2021, spreads tightened by roughly 30 basis points and moved in a range of about 100 basis points. For the most part of the year, spreads moved in line with what happens on average during a year. The second quarter and November were the exceptions. Spreads were tighter in the latter and wider in the former compared to the 10-year average.

> The message of less-supportive monetary support is being echoed by more and more central banks. While the extent of change may differ across central banks, it is very clear that we are entering a different phase of monetary policy, and one of less support. The beginning of cutting back monetary support historically doesn't mean that spreads must widen: tighter monetary policy is mostly a consequence of improving economic fundamentals. We must admit though that at the start of the previous two monetary tightening cycles, inflation was not as high as it currently is. Historically, however, high inflation isn't a direct route to high yields, as high inflation periods tend to coincide with low default rates.

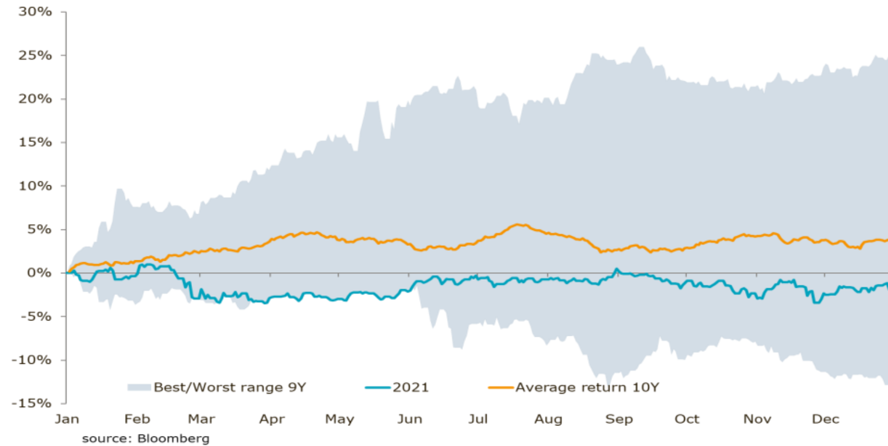
> Fundamentals in high yields are still supportive and spreads are roughly 160 basis points above the 21-year low reached back in 2007, so there is room for them to compress.

All market data to 31 December unless mentioned otherwise

ROBECO

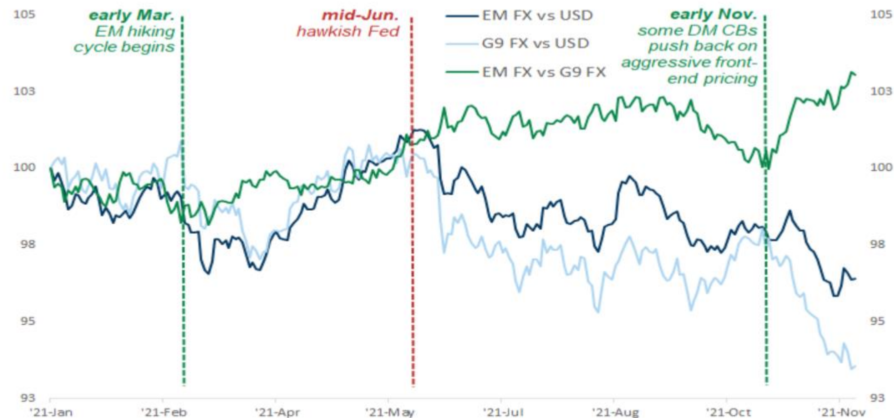
Emerging Market Debt

2021 returns were below the historical average for EMD LC



Source: Bloomberg

EM FX was challenged versus USD, but outperformed non-USD counterparts during 2021



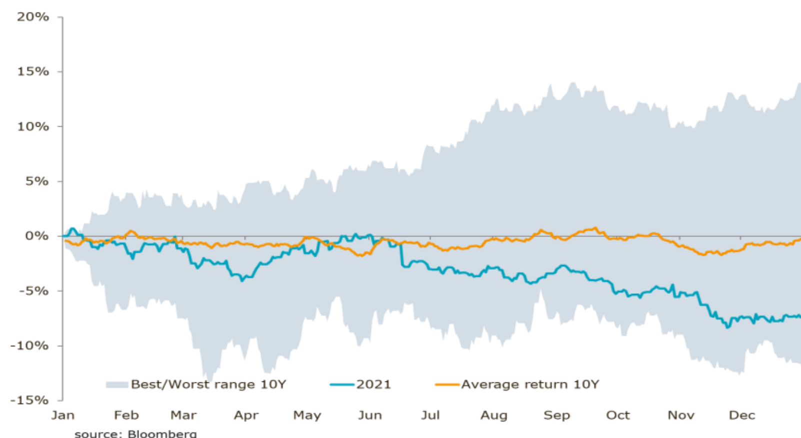
Source: Goldman Sachs

- Emerging market debt in local currency outperformed its developed sovereign counterparts like German Bunds over the year, despite generating a negative return of 1.8%. As an asset class with a risk profile between investment grade and high yield, it marginally outperformed European investment grade in 2021, but significantly underperformed high yield.
- While China embarked on a hard-handed policy crackdown in its domestic economy, several EM central banks pre-empted the Fed by embarking on a rate hike cycle to address mounting inflationary pressures. The most infamous example of an emerging country where inflation in 2021 spun out of control has been Turkey, as President Erdogan holds the view that lowering interest rates is the right medicine to tackle inflation. In December, the Turkish CPI was 36.1%.
- With the tightening cycle within EM well underway, an improving inflation outlook in EM could be reason for investors to enter the EMD LC universe again, as central banks have more leeway to focus on kick-starting growth again. However, emerging markets are not out of the woods yet when it comes to inflationary pressures, given the prospect of rising input costs for agricultural production (fertilizer) leading to higher food prices. Imported inflation will remain elevated as long as EM currencies remain under pressure due to unfavorable growth differentials versus the West.
- Whether the outlook for EMD LC brightens depends on when inflation in EM peaks versus the Eurozone, the stimulus effectiveness from China boosting intra-EM trade, and the extent of the spread of the Omicron variant. So far, it looks like EMD in LC will have another year of subdued returns given Fed rate hikes, elevated headline inflation and idiosyncratic risks (Russia-Ukraine tensions, Turkish monetary policy).

All market data to 31 December unless mentioned otherwise

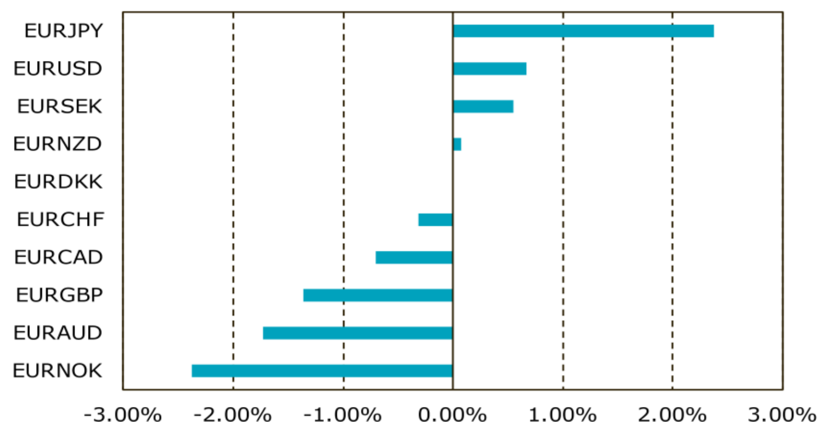
FX

EUR/USD: 2021 viewed from a10-year perspective



Source: Bloomberg, Robeco

G-10 currencies: defensives were the big winners



Source: Bloomberg, Robeco

> In December, no strong theme could be distilled from the returns from the G-10 currencies. This is not uncommon for this time of the year, as end-of-year flows and position squaring tend to dominate. In the perspective of the last 10 years, 2021 was a year of US dollar strength. The only seasonality that held was that the euro gained a bit of footing towards the final part of the year; otherwise, it was a year driven by Fed policy in which the dollar strengthened.

> Most central banks seems to have shifted towards a more hawkish stance. This was somewhat remarkable as this happened at a time when there was still great uncertainty around the impact of the Omicron Covid strain. This indicates that the focus of central banks is firmly on inflation and less so on other things. The surprise came from the BoE, which hiked rates in December after skipping a widely anticipated hike in November. The decision to hike was almost unanimous, while the market had only attached a 50/50 probability to such an outcome.

> The Fed also came out hawkish. With inflation firmly above 6% and the expectation that it will remain around that level for longer, the Fed felt compelled to react. It is clear now that for the Fed, the trade-off between inflation and employment is shifting. The currency market to an extent seems to have anticipated this shift, as the EUR/USD weakened in the run-up to the meeting, but failed to meaningfully do so afterwards. The odds continue to favor the US dollar.

All market data to 31 December unless mentioned otherwise

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