

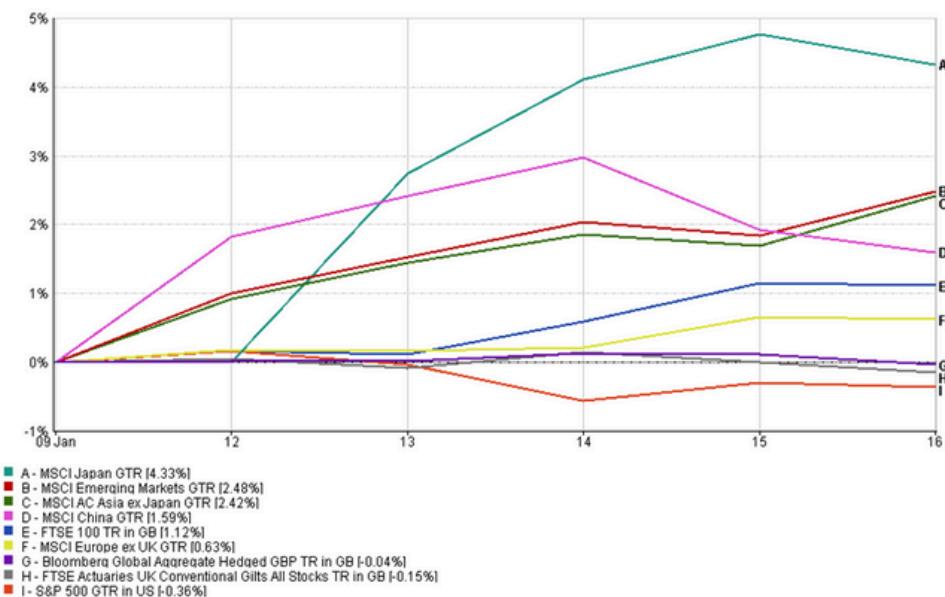
Market Matters

Cooling inflation, broadening leadership, and a reminder that this cycle is still alive!

Market Overview

Markets ended the week in a constructive mood, even if the leadership was not quite where investors have become accustomed to seeing it. The headline message from the chart is clear enough: Asia and emerging markets led; the UK quietly delivered another solid week; Europe made modest progress; and the US lagged, though without any sense of stress or disorder.

That pattern is important. It speaks to a market that is rotating and broadening rather than retrenching. The week's macro news, particularly on inflation, reinforced that tone: disinflation is continuing, growth is holding up, and the policy backdrop is becoming gradually more supportive, even if the next move from central banks is more likely to be based on patience rather than urgency.



09/01/2026 - 16/01/2026 Data from FE fundinfo 2026

Markets at a glance: rotation, not retreat

Looking at performance across the major regions, Japan was the clear standout, up over 4% on the week. Emerging markets and Asia ex-Japan followed closely behind, both delivering substantial mid-single-digit gains. China, while less spectacular, still finished comfortably in the black.

The UK continued to grind higher, adding a little over 1%, while Europe also made progress, albeit at a more measured pace. The laggard was the US, with the S&P 500 modestly lower on the week. That divergence should not be over-interpreted. US equities are coming off a very strong run, valuations are fuller, and the market has been digesting a heavy flow of earnings, inflation data and policy commentary. Against that backdrop, a pause while other regions catch up is both healthy and overdue.

Bond markets were broadly flat to slightly weaker. Global bond indices finished marginally negative, UK gilts slipped modestly, and US Treasury yields edged higher as the market reassessed the near-term pace of Federal Reserve easing. This was not a bond market revolt; it was simply the reflection of data that was 'good', but not so good as to force central banks to rush to alter their policy trajectory.

US inflation: cooling resumes, without the distortions

The most important macro development of the week was the US CPI release. After shutdown-related distortions clouded the previous report, December's data provided a cleaner read, and it was encouraging. Core CPI rose 0.2% month-on-month, below expectations, while the year-on-year rate held at 2.6%, matching the lowest level in four years.

Notably, the composition of inflation continues to improve. Core goods prices were flat, reinforcing the view that tariff pass-through has been much milder than feared. Used vehicles, appliances and repair costs all declined, offsetting firmer readings in shelter, recreation and airfares.

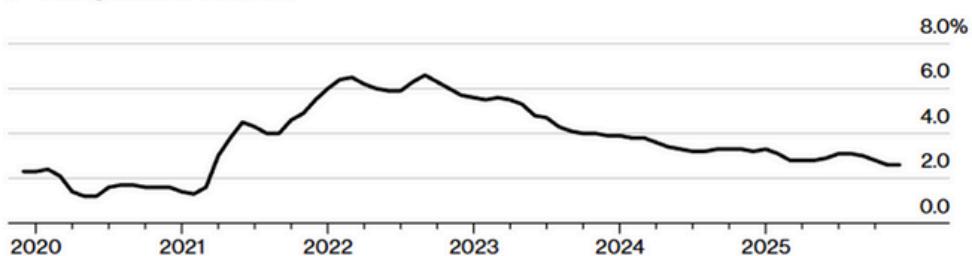
Underlying US Inflation Was Tame as 2025 Drew to a Close

Annual gain in core consumer price gauge matches smallest since 2021

■ Change in consumer price index ex-food, energy (MoM)



↗ Change in core CPI (YoY)



Source: Bureau of Labor Statistics

Note: October, November monthly CPI changes unavailable due to shutdown

Shelter inflation did pick up, rising 0.4% on the month, but that largely reflects a normalisation after earlier softness rather than a re-acceleration. Strip shelter out altogether, and core inflation was just 0.1% in December. The Fed's preferred 'supercore' services measure is now running at around 2.7%, down sharply from roughly 4% a year ago. The message here is not that inflation has been defeated, but that the trend remains firmly in the right direction. Disinflation is intact, goods inflation is no longer a threat, and services inflation is easing gradually as labour market pressures cool.

Policy implications: patience, not panic

Markets briefly flirted with a more dovish interpretation of the CPI print, but that enthusiasm faded quickly. Federal Reserve officials were careful to strike a balanced tone, acknowledging progress on inflation while emphasising that the labour market remains resilient.

Jobless claims fell to their lowest level since November, real wages are rising, and economic data more broadly continue to point to a soft landing rather than a stall. Against that backdrop, the Fed is widely expected to hold rates steady at its next meeting, after cutting three times into the end of 2025. The debate has shifted from whether rates will be cut further to how fast. That distinction is the central theme of the market narrative. A slower, more deliberate easing cycle is consistent with continued growth, stable earnings and modestly higher bond yields, not with financial stress.

The political noise around Fed independence resurfaced this week, but markets largely looked through it. While such rhetoric is unhelpful, it has not altered the underlying reality that inflation is falling and policy is already easing. Investors are focused on outcomes, not headlines.

Earnings season: good enough, but expectations matter

The US earnings season began with the banks, and results were mixed. There were solid performances in trading and investment banking, but net interest income remains under pressure, and costs are creeping higher. More telling than the numbers themselves was the market reaction: several banks sold off even after beating expectations. That speaks to positioning and valuation rather than fundamentals. Expectations had risen, and investors were quick to lock in gains. It is a reminder that at this stage of the cycle, earnings need to do more than just 'beat'; they need to surprise positively to drive sustained upside.

Elsewhere, technology regained some momentum later in the week following strong guidance from key AI canaries. As one of those canaries, Taiwan Semiconductor's update was particularly important, easing concerns that data-centre spending was peaking. Chipmakers hit fresh highs, and the broader tech complex stabilised after recent weakness. What is notable, however, is that tech leadership is becoming more selective. Investors appear increasingly comfortable backing the infrastructure and 'picks and shovels' of AI, while being more discriminating around the ultimate users of that capacity. That is (in my opinion) a healthy evolution rather than a warning sign.

UK: better data, but still a grind

The UK delivered a modest upside surprise with November GDP rising 0.3% month-on-month. A large part of that rebound reflected a recovery in car manufacturing, particularly Jaguar Land Rover, after earlier disruption. Services also expanded, which is more encouraging from a trend perspective. That said, this was not a decisive shift in the UK growth outlook. It reinforces the idea of a slow, uneven recovery rather than a strong upswing. Inflation continues to ease, real incomes are improving, and the Bank of England retains scope to cut rates later in the year, but growth remains constrained.

From a market perspective, the UK's appeal continues to lie in valuation, dividends and relative stability. In a world where investors are increasingly wary of concentration risk, that combination remains attractive, even if the macro story lacks excitement.

Japan and Asia: momentum builds

Japan was the standout performer, helped by a weaker yen, strong equity inflows and renewed focus on reform momentum. Political chatter around a possible snap election added intrigue, but markets interpreted it as broadly supportive rather than destabilising.

Across Asia more broadly, strength was driven by technology, semiconductors and improving regional growth data. The message from this week's performance is consistent with a theme we have been highlighting: the AI cycle is global, not just American, and Asia sits at its heart.

China also edged higher, supported by strong export data and a record trade surplus. Domestic demand remains uneven, but external resilience continues to provide a buffer. For emerging markets more generally, the combination of easing global inflation, a softer dollar and improving earnings expectations remains supportive.

This week...

Looking ahead, attention turns to the next wave of earnings, particularly in the US technology and consumer sectors. Key results from the likes of Netflix, ASML, Procter & Gamble and Johnson & Johnson will help shape sentiment around earnings durability and margins.

On the macro front, China's GDP and activity data will be closely watched, alongside UK inflation and labour market figures, which will feed directly into the Bank of England rate debate. In Japan, the Bank of Japan meeting will be scrutinised for any hints on the pace of policy normalisation.

Overall, the message from the past week is reassuring. Inflation is cooling, growth is holding up, leadership is broadening, and markets are rotating rather than rolling over. This remains a late-cycle environment that rewards selectivity, diversification and discipline, but there is little evidence yet that the cycle is ending.

Postscript 3pm Sunday - Greenland and tariff noise!

Over the weekend, the US signalled potential tariffs on a small group of European countries, framed around opposition to US ambitions over Greenland. As the news broke while markets were closed, a modest sentiment ripple at Monday's open would be unsurprising, particularly in Europe and other trade-exposed areas. At this stage, however, the episode still looks like geopolitical positioning rather than an imminent trade shock, with no detail on the scope, timing, or enforcement of tariffs.

For markets, the distinction remains important. Tariffs would be inflationary at the margin and negative for exporters, but investors are still assuming negotiation rather than execution. The absence of implementation mechanics, alongside ongoing legal uncertainty around the limits of presidential tariff powers (with a Supreme Court ruling due later this year), means this is being treated as background noise rather than a change in the investment backdrop – unless rhetoric hardens into action...



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