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Markets in a Minute

Guy Foster, Chief Strategist, discusses the anticipated Chinese fiscal stimulus package and how this can help arrest China's slide into deflation. Plus, Janet Mui, Head of Market Analysis, analyses fresh U.S. inflation data.

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What do the governments of the UK and China have in common? They're both left leaning, both have big majorities (the Chinese government having the benefit of a one-party system), and both are under pressure from investors to show they're taking some meaningful economic steps.

The Labour Party's political strategy of emphasising it's not the Conservatives was very successful during the election but left a void in terms of meaningful policy stances. However, Labour made the right noises, appealing to business that had, at times, been eschewed by the more populist stance of the former administration.

This week's International Investment Summit was one of those right noises. But it's symptomatic of how the government has yet to convince its doubters. Yes, it wants investment – but holding a summit two weeks before the Autumn Budget in the absence of meaningful steps to inspire more investment seems like a move that's likely to underwhelm.

What can we expect from the Budget?

Regarding the Budget itself, the government has been coy on what to expect. We're used to seeing Budget measures briefed out in advance, to the point where the event itself is characterised more by lame gags and point scoring than actual policy measures.

There's still time to formulate new plans to inspire new investment. However, the government appears to be more worried about whether its pledges to reform tax on non-domiciles and private equity carried interest will lose more revenue than they raise, as these changes could lead to mobile and incredibly wealthy individuals considering their options ahead of planned tax increases.

A few things could make the Budget easier for the government. The amount of spare funds it can spend while remaining on track to meet its fiscal rules may have risen to just over £20bn, as the economy has performed better than expected.

Although business leaders have been lambasting the government for talking the economy down, Friday's monthly gross domestic product (GDP) estimate suggests the economy returned to growth in August after pausing in July. While business surveys show anxiety over possible Budget measures, they also show current levels of activity remain relatively buoyant.

More meaningfully, the government could probably double this amount through some judicious rewording of the fiscal rules that would make a distinction between borrowing for expenditure and borrowing for investment. Based on the language used in Chancellor Rachel Reeve's Labour Party conference speech, in which she talked about a Budget for investment, we can assume the government will take this route.

However, there were indications last week that talk of increasing investment was beginning to concern investors. UK bond yields have started to rise, suggesting some anxiety over the amount Chancellor Reeves might need to borrow.

This serves as a timely reminder that the Chancellor needs to balance the competing interests of many different government departments, as well as the Office for Budget Responsibility and, ultimately, the gilt market.

France's €60bn public finance plan

Some additional political cover for the forthcoming UK Budget comes from the French equivalent, its Finance Bill, which has been proposed by Prime Minister Michel Barnier's new government. The plan involves €60bn of improvement to public finances, achieved through €40bn of spending cuts and €20bn of tax increases. This is with the aim of narrowing the forecast budget deficit from 6% to 5% of GDP.

Unlike the UK and Chinese governments, France's government has no majority at all and governs at the pleasure of a divided legislature. The far-left contingent has already tried to bring the nascent government down through a vote of no confidence but was unsuccessful.

It seems difficult for the Finance Bill to pass a legislative vote, but a procedural path exists under which it can be enacted without being voted upon. That offers some political cover for the minority parties to see the Finance Bill enacted without being tainted by it themselves. However, if they find the proposal too repellent, the vote of no confidence remains an option to bring the government down once more and send the country back to the polls.

China rally stalls

China's reopening last week after the Golden Week holiday was characterised by scepticism. A coordinated policy effort before the break rather petered out.

A press conference by the National Development and Reform Commission underwhelmed the market and was swiftly followed by another press conference on Saturday morning, hosted by Finance Minister Lan Fo'an.

A point of clarification here is needed: in any Western economy, the finance minister is usually the second most powerful position in government. However, in China, the finance minister ranks behind the president, prime minister, members of the Politburo Standing Committee, and a collection of vice premiers of the State Council.

So, while the Ministry of Finance is absolutely the right place to see some action, this press conference reflected a series of commitments to utilise borrowing already committed to. It lacked the commitment to new borrowing, or the confirmation of new consumer-focused incentives.

We are optimistic that China will follow through on its policy commitment. The government seems to understand what needs to be done and doesn't suffer the political cost of not getting it right straight away. The scale of commitment required would need to be sanctioned by the Standing Committee of the National People's Congress, which is due to meet in the week commencing 21 October.

Back to the U.S.

Apart from the sliding Chinese market, the main news of last week came from the U.S.

Obviously, all eyes were on Hurricane Milton, which caused a likely short-lived spike in jobless claims.

After a few months of reassuringly low inflation, the latest data has been a bit higher. The fact there was some strength in services inflation underpins the resilience of the U.S. economy, but it will likely cause the Federal Reserve to tread more carefully after its very sharp 0.5% interest rate cut in September.

Economic data takes a bit of a backseat for the next fortnight, as Friday marked the effective start of the third-quarter U.S. earnings season. The tone was set by JP Morgan and Wells Fargo, which kicked things off with strong results from both, and reassuring commentary on the state of the U.S. consumer. There seem to be no signs of weakening consumer spending at an aggregate level.

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