Stock Markets Soar on Falling US Inflation

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Global stock markets rallied to record highs on Friday, buoyed by news of a significant decline in US inflation. Investors are increasingly optimistic that the Federal Reserve will accelerate interest rate cuts in response to the easing inflationary pressures.

The S&P 500 index surged above 5,750, marking a nearly 34% gain year-over-year. European markets also experienced strong growth, with the Stoxx 600 index reaching a new record high.

The Federal Reserve’s preferred inflation measure, the Personal Consumption Expenditure (PCE) price index, fell to 2.2% in August, the lowest level since February 2021. This unexpected drop has fueled expectations of a more aggressive rate cut at the Fed’s upcoming meeting in November.

The prospect of a 0.5 percentage point reduction in interest rates, rather than a smaller quarter-point cut, has gained momentum following similar declines in inflation rates in France and Spain. This suggests that the European Central Bank may also implement a rate cut before the end of the year.

While global growth has been hampered by a slowdown in the US and China, recent economic stimulus measures in China have boosted investor confidence. The Chinese government has taken steps to lower borrowing costs, stimulate the housing market, and increase social benefits.

James Knightley, chief international economist at ING, said the Fed would be under pressure to maintain the pace of cuts to interest rates after a series of indicators showed the economy was weakening.

“The latest Conference Board consumer confidence report suggests households are becoming much more concerned about job security, which implies intensifying headwinds for consumer spending for all income groups,” he said.

“In an environment where inflation is looking much better behaved, the market pressure for ongoing substantial Fed interest rate cuts will persist.”

However, economists remain cautious about the outlook for the US economy, citing potential headwinds from rising unemployment and declining consumer confidence. If these trends continue, there may be a need for even more aggressive interest rate cuts to prevent a recession.