

Weekly Macro & Markets View

Highlights and View

- **US economic data remain mixed, but sentiment improves**

Retail sales and industrial production fell in April but both consumer and small business optimism have improved, signalling a pickup in momentum.

- **China's economic activity data for April mostly disappoint**

A closer look reveals distortions and some bright spots, though headwinds remain as the trade dispute with the US intensifies.

- **Surprisingly, incumbents win elections in Australia and India**

Equity markets celebrate the victory of the Liberal-National Coalition under PM Morrison in Australia's federal elections. Exit polls in India indicate a win for the BJP-led National Democratic Alliance. Political stability in both countries is welcome.

Digging deeper into China's double dip data



Source: NBS, Bloomberg

Following strong readings for March, China's economic indicators published for April disappointed, showing that the economy is facing headwinds. To some extent the disappointing data reflect a normalisation following the usual wild swings in Q1 caused by statistical distortions due to the different timing of Lunar New Year. Industrial production growth tumbled from 8.5% YoY in March to 5.4% last month, but this partly reflects a restocking by manufacturers to claim higher VAT deductions before the April VAT cut. Adjusting for this impact still shows production so far this year was higher than in Q4 last year. However, weak data for cement and auto production are a concern. Fixed investment growth fell to an eight-month low of only 5.7% YoY in April as manufacturing investment slowed considerably, while infrastructure investment grew moderately and property investment remained firm. Home sales in higher-tier cities will probably remain the bright spot this year. Nominal retail sales growth fell to only 7.2% YoY, the slowest growth since 2003, but we note that April last year had two more holidays than this year, distorting growth to the downside. We also note that online sales were up a brisk 25.3% YoY in April, growing at the fastest pace since summer last year. Consumption should be supported by tax cuts and a reduction in social security contributions that have been implemented recently.

US: Consumer and small business optimism are rising

The S&P 500 ended the week with a loss of 0.8% as trade worries keep weighing on investors' sentiment. Meanwhile, economic data paint a mixed picture of the current situation. Retail sales fell in April, signalling a continuation of Q1's weakness in consumer spending into the second quarter, though the numbers are likely to be distorted due to seasonal adjustments. In addition, both industrial and manufacturing production fell in April as well. On the other hand, small business optimism ticked up in April, indicating that global growth worries and the

trade dispute with China have not meaningfully affected the domestic economy yet. A solid pickup in the University of Michigan's Consumer Sentiment Index in May, mainly driven by improved expectations, is reassuring as it may point to increased household spending ahead. Similarly, a pickup in building permits and housing starts, as well as stronger home builder sentiment, are signalling a stabilisation in the housing market.

Eurozone: Trade newsflow dominates Eurozone equity markets as data remain mixed

Eurozone equity markets were driven again by news flow on global trade tensions, with news mid-week that the US would postpone its decision on imposing auto tariffs on the EU by six months, helping to offset a harshening in rhetoric between the US and China and leaving Eurozone equity markets up around 2% on the week overall. However, sentiment still appears fragile. In terms of data, there was a modest softening in the ZEW economic expectations indicator for Germany, a useful leading indicator of industrial production, while actual industrial output was down

modestly in March (-0.3% MoM) for the Eurozone as a whole, bringing the YoY growth rate to a lacklustre -0.6% YoY. The second estimate of Eurozone Q1 GDP was unrevised from the first estimate of 0.4% QoQ (1.2% YoY). German GDP growth also came in at 0.4% QoQ (after zero growth in Q4), although this probably exaggerates the underlying pace of growth given how weak manufacturing confidence in particular is at the moment, especially with no end to global trade tensions in sight yet.

Australia and India: Election surprises

PM Scott Morrison's led Liberal-National centre-right coalition surprisingly won Australia's federal election for a third term, having lagged the Labor Party in polls until recently. Votes are still being counted, but it is likely that an absolute majority in the House of Representatives will be achieved by a slim margin. In the Senate, however, despite an increase in seats, the coalition will fall short of a majority and need support from smaller parties. Australia's equity market index, the ASX200, surged 1.7% to a 12-year high as the coalition will continue with more business

friendly policies, supporting the still firm labour market. We expect the RBA to cut policy rates soon as the election is now out of the way. Meanwhile, exit polls in India suggest a clear majority for the BJP-led NDA coalition in lower house elections that ended today, which also comes as a surprise to many observers. Final results are scheduled for Thursday. Both the Nifty 50 and the BSE Sensex 30 indices spiked up by 3.7%, closing at fresh record highs and celebrating policy continuity.

Bonds: Market pricing remains downbeat, but fairly realistic

Bond yields have failed to rebound, as the latest twists in the US-China trade dispute have added to and amplified concerns around the slowing global economic cycle. The 10yr Treasury yield sits just above 2.40% and remains precariously close to the recent low of 2.37% reached in March. The decline in yields partly reflects a repricing of Fed expectations, with Fed funds futures consistent with two rate cuts by the end of 2020, and with a 70% probability of a cut by the end of 2019. Headwinds from higher yields are also coming from Europe, where the 10yr Bund yield has

fallen below the 10yr JGB yield for the first time since 2016. This does not reflect strength in Japan, but weakness in Europe, where growth expectations continue to be revised down. Bond markets are also pricing in a more pessimistic outlook than equity markets. Despite this, a near-term rebound in yields looks unlikely given trade worries, continued poor macro data, and a fragile economic cycle.

Credit: Outperformance could be ebbing soon

Credit was mixed last week as tentative signs emerged suggesting that the outperformance in general and versus equities could soon be ebbing. A number of signs suggesting cracks in the credit rally have begun to emerge as weak fundamentals begin to bite. Despite strength in oil prices, the US high yield energy sector was notably weaker as bankruptcy concerns about Weatherford prompted energy bonds to drop sharply, causing the entire US high yield space to notably lag that of Europe. On the other hand, despite positive news from the US in US-EU trade

negotiations, European investment credit modestly underperformed US credit, as peripheral products were weak amid rising populist rhetoric ahead of the EU elections. The supply/demand technical picture is also getting more mixed. US credit ETFs have been seeing outflows since early April, while global high yield suffered heavy outflows last week and EM flows are also getting weaker. These warning signs are worth monitoring, as modest weakness can sometimes lead to a deeper correction, which we expect in the medium term anyway.

What to Watch

- The flash Eurozone PMIs and German ifo survey will be useful to see the impact, if any, of the recent escalation of the US-China trade dispute on business confidence, while the EU elections will be watched closely to see how well populist parties do.
- Following the release of GDP data in Japan that showed stronger growth than expected in Q1 (+.21% QoQ annualised, 0.8% YoY), the focus will move to export and CPI data for April. In Asia, Korea's first 20-day exports for May will give us an indication as to whether a turnaround for the better is becoming visible. Thailand's exports and industrial production data for Taiwan and Singapore in April as well as Q1 GDP data for Taiwan, Thailand and Singapore will also be in focus.
- This week's flash PMIs for the G3 economies will show if April's stabilisation was more than just a temporary respite.

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