

# Weekly Macro & Markets View

## Highlights and View

- **The S&P 500 rises to a record high on solid labour market data**

Positive employment data are particularly encouraging for the consumer outlook as other parts of the economy, particularly manufacturing, remain under pressure.

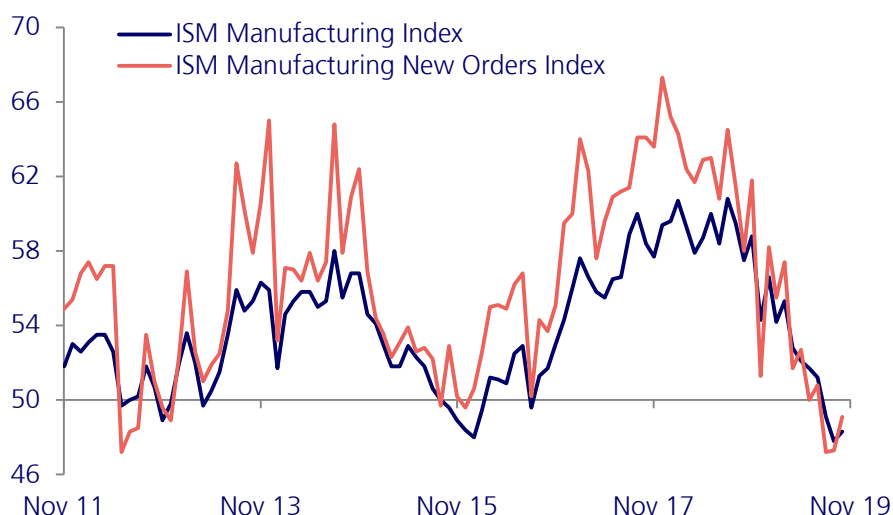
- **The EU grants another Art. 50 extension as the UK heads for new elections**

While the election outcome is hard to predict as tactical voting will play an important role, the risk of a no-deal Brexit has been significantly reduced for now.

- **PMI data show that while growth remains subdued in most regions, signs of stabilisation are appearing**

Global growth appears to be in a bottoming stage but, given an extended economic cycle and elevated political uncertainty, a stronger rebound continues to look unlikely.

## Stock markets defy mixed economic signals



Source: Bloomberg

Gaining 1.5% last week, the S&P 500 reached a new record high on Friday, rising above the top reached back in July. While the market was trading range-bound for most of the week, it managed to break out after Friday's solid labour market data. 128'000 new payrolls were created in October while September's number was revised up by 44'000 to 180'000. Particularly inspiring was the tick-up in the participation rate to 63.3%, a six-year high. A rising participation rate would be a crucial ingredient in extending the current business cycle as it would help to mitigate the increasing labour market tightness. The positive employment data even put potential worries about another weak ISM Manufacturing print in the background. The headline number ticked up less than expected to 48.3 with new orders remaining in contractionary territory as well, though improving from last month's level. A positive signal for the global economy came from new export orders jumping back above 50 from the very weak level the month before. As was widely expected, the Fed further cut its target rate by 25bps to a range of 1.5 – 1.75%. The Fed's chair, Jerome Powell, indicated that the FOMC is likely to pause for now unless incoming data show a significant deterioration. It will be challenging to manage a soft landing, but the first estimate of Q3's GDP shows that growth has now slowed to 1.9%, which is roughly the current trend growth rate.

## Credit: Notably underperforms equity despite ECB buying

In a week where US equity indices set new records, driven by a rate cut by the Fed, optimism around US-China trade negotiations and continued signs of stabilisation in global economic data, the credit market notably lagged. Cash credit spreads widened in most sectors, while CDS was marginally better but still lagged the strength in equities. There seems to be little room for upside in credit, given poor fundamentals, but the demand/supply picture will keep a cap on spreads near term. Flows remain generally robust, with the exception of the US

leveraged loan market, while supply picked up in both Europe and the US, with November expected to be a strong month. The ECB actively kicked off its asset purchases, with some reports emerging that it submitted orders of around 40% for new issue covered bonds. However, given the weak fundamental picture investors continue to remain discerning around quality as seen not only in the weak performance of high yield, but also in the pulling of the first leveraged loan deal in a month, that would have financed dividends and increased leverage.

---

## US Munis: Good performance should continue into year-end

US municipals bonds continue to enjoy good performance with YTD total return now close to +7%. We expect strong near-term performance, benefiting from seasonal support as a year-end rally, which has occurred almost every year, would usually start in November. Supply has spiked in the past two months and will likely remain robust in the near future, but inflows into mutual funds remain strong and will absorb new issuance. According to the most recent quarterly Fed flow of funds statistic, banks' holdings continue to decrease and now only

account for 12% of Munis outstanding, but mutual funds and direct retail purchases have more than compensated for the reduction in exposure from institutional investors after the impact of the reduction of the corporate tax rate. The ratio between municipal and Treasury yields has risen from recent multi-year lows but remains below the five-year average level. This could rise further if there is a sharp Treasury rally, given that volatility remains elevated for government bond yields.

---

## Switzerland: Back in deflation, but growth appears to be bottoming

Macro data show slightly better momentum in October, indicating that the worst may be over in terms of the industry led downturn. The Manufacturing PMI rebounded from a 10-year low and is now consistent with stable conditions in the industrial sector. Employment plans improved, inventories were cut back and new orders strengthened, suggesting that sentiment remains intact with more positive dynamics going forward. The KOF leading indicator edged higher and points to a bottoming out of annual GDP growth, which was dismal at only 0.3% in

Q2. While global headwinds remain, these latest prints support our view of a further expansion in the Swiss economy. Consumer prices are falling again, for the first time since 2016, with the headline CPI at -0.3% YoY in October. Weakness was broad-based and poses a problem for the SNB, given limited space to inject further stimulus. We therefore maintain our view that rates will be left unchanged, unless global conditions deteriorate more markedly.

---

## Asia: PMIs remain fragile, but hope for a stabilisation emerges

As often, China's two PMI versions are deviating. While the official NBS Manufacturing PMI hit an eight-month low of 49.3, the Caixin Manufacturing PMI reached a two-year high of 51.7. SMEs active in the eastern coast region are benefitting from stronger new export orders more than the big state-owned companies. We believe the overall trend remains fragile. Elsewhere in emerging Asia, the October readings came in softer than last month, except for Korea and Malaysia. However, a one-month figure tends not to provide a comprehensive picture.

Hence, we look at a broader time frame to interpret an overall trend. While Indonesia's Manufacturing PMI continues to deteriorate, falling from 49.1 to 47.7 in October, data for Korea, Taiwan and Malaysia pointed to a potential bottoming out in the last three months. The October new export orders for Korea and Taiwan, while slowing from 50.2 to 48.6 and from 47.9 to 46.3 respectively, seem to still be on track for a tentative stabilisation. Nevertheless, more data are needed to confirm a sustainable trend.

---

## Japan: Cryptic BoJ statement on forward guidance

The Bank of Japan left its policy rates and asset purchase programme unchanged. We think the BoJ's statement about the revised forward guidance was cryptic, allowing it to be interpreted in many ways. Separately, we note that the BoJ does not seem to be overly concerned about the impact of weak global demand on domestic demand. Retail sales picked up strongly in September just before the consumption tax hike, up 7.1% MoM and 9.1% YoY, but we expect a payback in October due to the tax hike and the impact of the big typhoon. Following a steep downturn

in consumer sentiment for nearly two years, the latest small recovery is mainly based on an increased willingness to buy durable goods over the next six months. Industrial production gained steam in September on strong capital goods production. We believe the producers' growth outlook for October is too optimistic and expect a setback instead. Finally, labour market data deteriorated with overall employment shrinking, but notably, the number of female workers rose by 140k to a record high of 30mn. Japanese equities are supported by strong foreign buying.

## What to Watch

- In the US, the latest ISM Non-Manufacturing Index will show whether the spill-over from a weak manufacturing sector remains contained while the University of Michigan's consumer sentiment survey is expected to show a continuation of households' upbeat mood
- In the Eurozone, we will watch Services PMI and retail sales data for hints of a broadening out of the slowdown and German factory orders for signs of stabilisation in industrial demand. In Spain, general elections will be held on Sunday, November 10.
- In Australia and Malaysia, we believe the RBA and BNM will keep policy rates unchanged on Tuesday, while there is a chance that the Bank of Thailand could cut its policy rate by 25bps on Wednesday, earlier than we expected.
- In Japan, the Reuters Tankan and wage data will be in our focus. In Taiwan, we expect October exports to be roughly unchanged in YoY terms. Australia's September retail sales, home loans and trade balance will be released, as will Q3 GDP prints for Indonesia and the Philippines.

#### **Disclaimer and cautionary statement**

This publication has been prepared by Zurich Insurance Group Ltd and the opinions expressed therein are those of Zurich Insurance Group Ltd as of the date of writing and are subject to change without notice.

This publication has been produced solely for informational purposes. The analysis contained and opinions expressed herein are based on numerous assumptions concerning anticipated results that are inherently subject to significant economic, competitive, and other uncertainties and contingencies. Different assumptions could result in materially different conclusions. All information contained in this publication have been compiled and obtained from sources believed to be reliable and credible but no representation or warranty, express or implied, is made by Zurich Insurance Group Ltd or any of its subsidiaries (the 'Group') as to their accuracy or completeness.

Opinions expressed and analyses contained herein might differ from or be contrary to those expressed by other Group functions or contained in other documents of the Group, as a result of using different assumptions and/or criteria.

The Group may buy, sell, cover or otherwise change the nature, form or amount of its investments, including any investments identified in this publication, without further notice for any reason.

This publication is not intended to be legal, underwriting, financial investment or any other type of professional advice. No content in this publication constitutes a recommendation that any particular investment, security, transaction or investment strategy is suitable for any specific person. The content in this publication is not designed to meet any one's personal situation. The Group hereby disclaims any duty to update any information in this publication.

Persons requiring advice should consult an independent adviser (the Group does not provide investment or personalized advice).

The Group disclaims any and all liability whatsoever resulting from the use of or reliance upon publication. Certain statements in this publication are forward-looking statements, including, but not limited to, statements that are predictions of or indicate future events, trends, plans, developments or objectives. Undue reliance should not be placed on such statements because, by their nature, they are subject to known and unknown risks and uncertainties and can be affected by other factors that could cause actual results, developments and plans and objectives to differ materially from those expressed or implied in the forward-looking statements.

The subject matter of this publication is also not tied to any specific insurance product nor will it ensure coverage under any insurance policy.

This publication may not be reproduced either in whole, or in part, without prior written permission of Zurich Insurance Group Ltd, Mythenquai 2, 8002 Zurich, Switzerland. Neither Zurich Insurance Group Ltd nor any of its subsidiaries accept liability for any loss arising from the use or distribution of publication. This publication is for distribution only under such circumstances as may be permitted by applicable law and regulations. This publication does not constitute an offer or an invitation for the sale or purchase of securities in any jurisdiction.

---

Zurich Insurance Company Ltd  
Investment Management  
Mythenquai 2  
8002 Zurich

173001566 (01/16) TCL

