

# Weekly Macro & Markets View

## Highlights and View

- **The S&P 500 rises on trade hopes and decent data in a holiday-shortened week**

Real personal spending and consumer confidence ticked down but a rise in capital goods orders and shipments raises hopes of a re-acceleration in business activity.

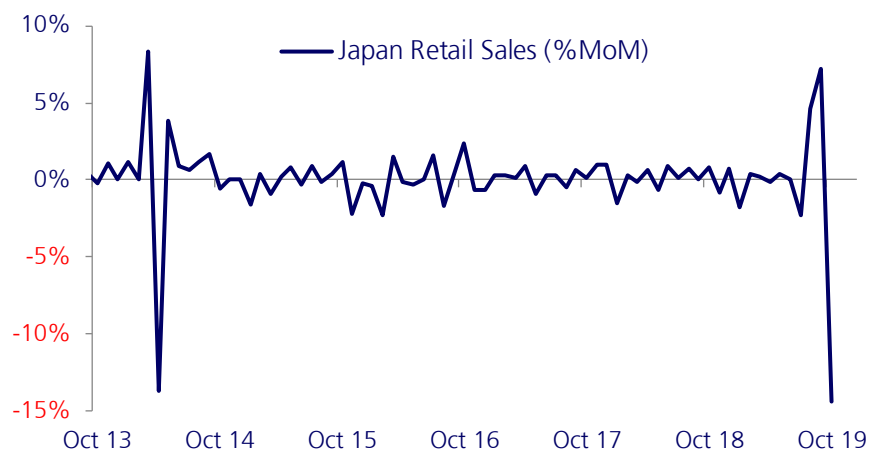
- **In Germany surprise winners were elected as the new SPD leaders over the weekend**

The outcome has increased political uncertainty as newly elected Norbert Walter-Borjans and Saskia Esken ran on a platform of renegotiating the coalition deal with the CDU.

- **The Reserve Bank of Australia provides comprehensive guidance on QE for the first time**

With space for two more rate cuts, QE is not an option for now. However, the RBA's forward guidance on QE shows a willingness to add further stimulus while keeping rates lower for longer.

## Consumption tax hike and typhoons hit Japan's retail sales



Source: METI, Bloomberg

Consensus had expected retail sales to fall in October following the increase in the consumption tax from 8% to 10%, but the resulting drop was much bigger than anticipated. Following some rush demand in September, which lifted retail sales by 7.2% MoM, the 14.4% slump in October was significant. The drop was even larger than after the 1997 and 2014 sales tax hikes (see chart), which is a surprise, as several measures were taken this time to avoid such a slump. We are not too worried about these numbers for various reasons. First, retail sales have been negatively impacted by two major typhoons. Second, consumer confidence has recovered significantly for two months in a row, following a 22-month drop, driven by a willingness to buy durable goods. Third, consumption is not only driven by retail sales, but also by services. In that respect we need to wait for the consumption activity indices published by the Bank of Japan and the Cabinet Office. We also need to keep an eye on consumption by seniors, who benefit less from the point reward system for cashless purchases at discount stores and do not benefit from free childcare at all. Today's release of the Q3 MoF Corporate Survey suggests that real GDP growth for Q3 may be revised to the upside. The contributions from capex and inventories were stronger than initially expected. However, we are concerned by the weak profit numbers reported in both the manufacturing and non-manufacturing sector.

## US: Consumer confidence ticks down in November

Following a short breather the week before, the S&P 500 continued its way up in a holiday-shortened week, gaining 0.99%. More hints regarding an imminent trade agreement between China and the US, helped by a positive tilt to economic data, lifted investors' spirits. Q3's GDP growth was revised up to 2.1%, helped by slightly stronger consumer spending. Household spending is expected to weaken in Q4, however, with real personal spending slowing to 0.1% MoM in October, the weakest since February. Consumer confidence, though still

at solid levels, also ticked down in November, driven by a deterioration in households' perception of their current situation. New homes sales fell by 0.7% MoM in October, though that followed September's post-recession high. On a more positive note, durable goods orders, and particularly capital goods orders, rose in October, following a couple of weak months. Finally, inflation pressure remains modest with the PCE Core Deflator ticking down to 1.6% YoY in October from 1.7% the month before.

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## Eurozone: More evidence of stabilisation, political uncertainty increases in Germany

There was more evidence of a stabilisation in economic activity in the Eurozone last week, albeit at a modest pace. The European Commission's Economic Sentiment Indicator increased to 101.3 in November from 100.8 in October. However, at the beginning of 2018 it was as high as 114.5, and it has been on an almost continuous downtrend since then. Loans to households grew by 3.5% YoY in October, up from 3.4% in September, while loans to non-financial corporations increased by 3.8% in October, up from 3.6% in September, also consistent with ongoing

modest growth in the region. ECB Chief Economist Philip Lane said last week that if more monetary easing was needed 'the best guide might be what we did in September, which was a little bit of everything'. He also indicated specifically that if the ECB thought it necessary to cut rates further into negative territory it would do so. Finally, in Germany political uncertainty has increased with the surprise wins of Norbert Walter-Borjans and Saskia Esken as the new SPD leaders over the weekend, as they ran on a platform of renegotiating the coalition deal with the CDU.

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## Switzerland: Firm growth in Q3 partly reflect industry effects

GDP grew at a solid pace in Q3, up 0.4% QoQ, with a reacceleration in annual growth from 0.2% to 1.1%. The expansion was broad-based, helped by solid exports, investment, and government spending. Growth was more uneven across industries, however, with the pharmaceutical sector giving a disproportional boost to activity. This shows that headwinds from a strong franc, depressed global trade and the slump in the Eurozone are still in place. Both the KOF leading indicator and the Manufacturing PMI also ticked down again in November and the

PMI remains consistent with contraction in the manufacturing sector. Going forward, we expect the economy to continue to expand, but at a sluggish pace, with growth broadly flat at around 1% in 2020.

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## Australia: The RBA comments on unconventional monetary policy

As the policy rate reaches a record low of 0.75%, there are discussions about the option of quantitative easing (QE) in Australia. However, the Reserve Bank of Australia (RBA) had provided little guidance on this topic until last week. In his speech on unconventional monetary policy Governor Lowe highlighted a few important points. First, QE is an option only when the cash rate reaches 0.25%. Second, inflation and employment data are what primarily drive the RBA's policy response. Third, a negative interest rate is 'extraordinarily unlikely'. Finally, if QE is to be

launched, the central bank would only consider buying government bonds in the secondary market rather than financial assets in the private sector. With the current levels of inflation and unemployment drifting further away from the RBA's target, we see the bar for QE not being that far off. However, given certain lags of previous easing and room for another two rate cuts, we expect QE will only become a consideration for the RBA in H2 2020 if weak data persist.

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## Credit: M&A surge indicates more leverage in the pipeline

Credit markets were firm last week, although lower quality parts of the market such as the US high yield energy sector lagged the rally, continuing the theme of dispersion within credit. Although supply last week was low, November ended as a very strong month for supply, with AbbVie's \$30bn M&A financing deal being a highlight. There was a surge in M&A related announcements, with 10 large deals announced on Monday itself, sending US stock indices to new records, also aided by optimism on a US-China trade deal. We believe that the heavy supply this year will

potentially lead to increased leverage as some of the cash raised is likely to be used for M&A and buybacks. While the current cost of debt is cheap for good quality borrowers, the ongoing dispersion indicates the risks for excessively leveraged corporates. Away from corporates, Moody's revised the outlook on German banks to negative while the FSB made some changes to the GSIB list, lowering Deutsche Bank by one notch and adding Toronto-Dominion bank to the list.

## What to Watch

- This is one of the heaviest weeks this year in terms of APAC economic data releases, so we will not go into details. All eyes will be on Asian manufacturing PMIs, as they provide useful guidance on future regional economic momentum. As for central bank policies, the RBA will probably pause its easing for now, waiting for confirmation on the impact of previous cuts, while the RBI is likely to deliver its last policy rate cut in 2019.
- In the Eurozone the final PMIs, the breakdown of Q3 Eurozone GDP and other data are likely to show some stabilisation, but also highlight an economy that remains fragile.
- In the US a range of crucial data including the ISM Manufacturing and Non-Manufacturing surveys as well as payrolls and consumer sentiment will give important insights into the current state of the economy.

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