

# Weekly Macro & Markets View

## Highlights and View

- **The ISM surveys show business sentiment in the US rising to the highest levels since early 2019**

Both the manufacturing and services surveys, and strong new orders in particular, point to a continuation of the solid economic rebound, though employment remains weak.

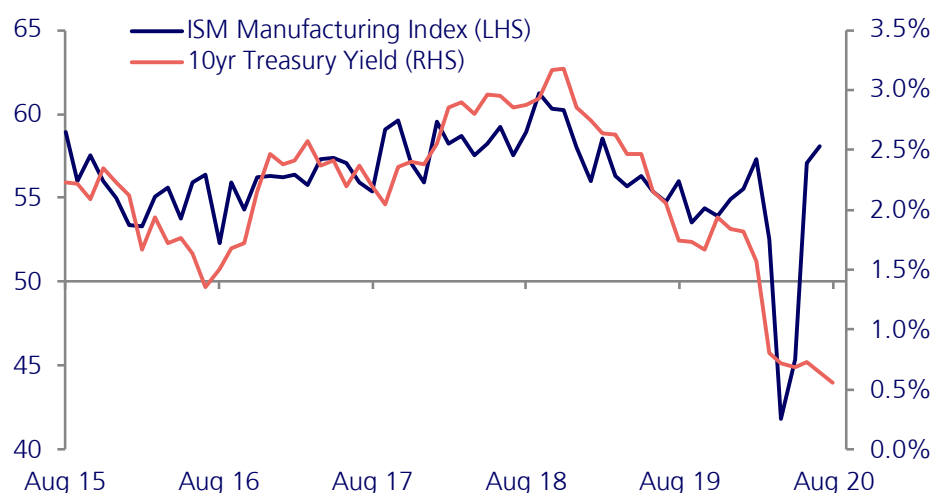
- **Global PMIs rose above 50 in July and are now consistent with an expansion in the world economy**

Improving growth momentum is encouraging and supports the basecase of a deep but short-lived recession. Weak hiring plans remain a risk to a sustainable recovery.

- **Core bond yields hit new lows while inflation expectations rebound, leaving real yields at historical lows**

Upside for yields is limited, but current levels appear stretched given further improvements in economic activity and rising inflation expectations.

## The ISM surveys rise further as the economy continues to heal



Source: Bloomberg

Despite ongoing uncertainty regarding the extension of fiscal support measures, the S&P 500 managed to eke out a small gain on Friday, rising six days in a row. That was the longest winning streak since April 2019 when the S&P 500 rose eight days in a row. While an agreement on the fiscal front still doesn't seem to be imminent, President Trump signed four executive orders over the weekend, including a temporary payroll tax deferral and continued expanded unemployment benefits. Meanwhile, the economy continues to heal from the biggest drawdown in decades. Both the ISM Manufacturing as well as the ISM Services (formerly Non-Manufacturing) surveys came out better than consensus expected and rose to 54.2 and 58.1, respectively, the highest levels since Q1 2019. Solid new orders point to a continuation of the strong rebound in business activity, though the employment component remains weak which is a bit disappointing, particularly with regard to the service sector. Nevertheless, last week's labour market data were on the positive side. 1.8mn new jobs were created in July, lifting the three-month total to 9.3mn. The unemployment rate fell to 10.2% from 11.1% in June. Initial jobless claims resumed their downtrend, falling to 1.2mn last week, after two weeks of picking up. The latest drop could be distorted by the expected end of additional unemployment benefits at the end of July, however.

## Bonds: Core bond yields fall to new lows despite rising inflation expectations

Core bond yields fell to new lows last week despite improvements in economic activity and rising inflation expectations. The 10yr US Treasury yield hit a new closing low of 0.51% on Tuesday, before yields rebounded slightly towards the end of the week, with all curve steepening since April now reversed. The 10yr gilt yield fell below 0.1% for the first time, helped by negative rate expectations, while Bund yields reached levels last seen in May in the midst of lockdowns and prior to the deal on the EU's recovery fund. While upside to yields is limited given central bank actions and

economic vulnerabilities, these levels appear stretched. Inflation expectations have also rebounded strongly, leaving real yields close to historical lows. In addition, debt issuance plans released by the US Treasury last week surprised on the upside, indicating less favourable supply conditions than expected. Given stretched levels, we suspect yields can edge higher, though political and geopolitical tensions – along with new virus infections – pose a risk to that view.

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## Eurozone: Further strong gains in retail sales and industrial production

There was further evidence of a V-shaped recovery in the Eurozone economy last week. Eurozone retail sales gained another 5.7% MoM in June after a 20.3% surge in May, bringing them back above pre COVID-19 levels. In the industrial sector, country-level data available so far also show an impressive rebound in June. For example, output was up 8.9%, 12.7% and 8.2% MoM in Germany, France and Italy respectively. However, in contrast to the retail sector, overall Eurozone industrial output was likely still well below pre COVID levels. Nevertheless, taking the retail

sales and industrial production data together suggests that for now the V-shaped recovery in the region continues despite some increases in virus cases, notably in Spain, and still weak external demand, which should support risk assets in the region. Indeed, the Euro Stoxx 50 was up around 2.5% last week. Finally, with most companies having now reported, Q2 corporate earnings showed a sharp fall of around 25% YoY for Euro Stoxx 50 companies, but this was still around 20% better than expected.

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## Switzerland: Activity and confidence rebound

The Manufacturing PMI rose firmly in July, boosted by strong gains in current output and a pickup in hiring plans. Consumer confidence also rebounded and is now almost back to its pre COVID level, supported by an ongoing stabilisation in the job market. The KOF leading indicator also snapped higher in July, indicating a broader recovery in domestic demand following the collapse in Q2. These data are supportive of a return to positive growth in the third quarter and in line with the basecase of a relatively robust recovery for Switzerland, though further improvements are

clearly dependent on the path of lockdowns and infections both at home and abroad. Elsewhere, pressure on the SNB to intervene in forex markets appears to have eased following progress on the EU's recovery fund, which helped to weaken the Swiss franc against the euro. Conditions are still fragile, however, with recessionary and deflationary forces in play, and the SNB is likely to remain active in forex markets for the foreseeable future.

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## Australia: Activity rebounds, but lockdowns in Victoria will probably decelerate the recovery

June data confirmed a further rebound in activity. Retail sales grew by 8.2% YoY, exceeding the pre COVID-19 level while the trade balance rose from AUD 7.3bn to 8.2bn on the back of strong global demand for iron ore. The housing market held up well throughout the crisis with home prices, while ticking down a little in July, still up by 8% YoY. Nevertheless, we doubt the recovery will be smooth as infection rates rose further, mainly in Victoria. Last week, Melbourne declared a 'stage four' lockdown for another six weeks until mid-September, with all shops

except essential businesses now closed. Victoria accounts for around 23% of national output and 26% of total employment. Therefore, a blow to employment and a contraction in activity in Victoria will weigh heavily on the recovery process of the country as a whole, notably in Q3. This might, however, prompt further monetary and fiscal stimulus before long.

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## Argentina: The government reaches an agreement with bondholders

The Argentine government reached an agreement with main bondholder committees to restructure USD 66bn of foreign currency debt issued under international law (~20% of public debt). The deal consists of exchanging the current bonds for others denominated in USD or EUR with maturities between 2030 and 2046. The new bonds will begin to pay interest in July 2021 and amortize as of July 2024. Likewise, it includes 3% haircuts for some issues and an average coupon rate of 3.75% and 3.11% in dollars and euros. The Congress has approved the restructuring of

foreign currency debt issued under Argentine law for an amount of USD 44bn (~13% of public debt), of which private investors hold USD 14.7bn. Debt restructuring should reduce Argentina's debt service burdens and risk premia. The focus will now be on restructuring the USD 44bn Stand-by Arrangement with the IMF. Negotiations with the IMF should begin in the coming weeks.

## What to Watch

- In the US, small business optimism will show whether small firms have managed to keep up with larger firms' improving sentiment while retail sales are expected to rise further.
- In the Eurozone, data on June industrial production for the region as a whole is likely to show a second consecutive month of strong output growth.
- China's economic indicators for July are expected to show a further pickup in activity, while Japan's Eco Watchers Survey will probably inch a bit higher in July following the strong surge in June. Malaysia's GDP Q2 is likely to show a sharp contraction, while India's high inflation should persist. We expect Australia's unemployment rate to remain elevated in July amid Victoria's lockdown.

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