November 16, 2020

Weekly Macro & Markets View

Highlights and View

- **Pfizer/BioNTech announce a COVID-19 vaccine with more than 90% efficacy**

  News of the vaccine was not unexpected, but its efficacy was and is a landmark in the fight to contain the virus, lifting sentiment and increasing the likelihood of success for other vaccinations in development.

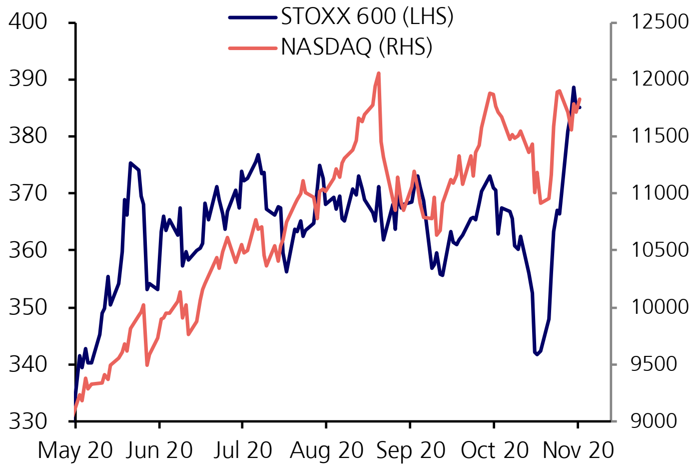
- **Equities surge on the vaccine news with cyclical and deep value names leading the charge**

  In a market rotation, 'stay-at-home' winners were sidelined with the more economically sensitive and cheaper valued stocks jumping, following prolonged underperformance.

- **RCEP, a comprehensive trade deal between the ten ASEAN nations, China, Japan, South Korea, New Zealand and Australia, was signed**

  Covering about one third of global GDP, RCEP is a big step forward in Asian integration and a strong show of trade cooperation, challenging the de-globalisation trend.

Vaccine news triggers market rotation



Source: Bloomberg

The announcement of a high efficacy rate for the Pfizer/BioNTech vaccine trial is unquestionably a positive development for lives and livelihoods. While it improves the prospects of mass vaccinations for next year and helps to bolster sentiment in the meantime, the near-term outlook is highly challenging. This tension was reflected in government bond markets last week, which saw global bond yields initially spiking higher on vaccine news, but the move was partly reversed as surging US infections came into focus. We suspect yields will remain well anchored for now, given near-term headwinds to growth and ongoing central bank support, though some volatility driven by vaccine news should not be ruled out. As government bonds sold off, equities surged, with the S&P 500 tacking on a further 2% gain on the back of the 7% in the prior week, and the dispersion within the asset class was meaningful. Many of the winning names that have benefited from the virus disruptions, including the large tech players, sold off, while banks, oil, leisure and entertainment names surged from highly depressed levels. This was also apparent in the broader indices, with the tech heavy NASDAQ slipping marginally, while underperforming European indices rebounded sharply. We maintain that the path of least resistance for stocks may well be higher into the end of the year, but a lasting outperformance of value versus growth sectors seems premature.

Credit: Vaccine news blesses the hardest hit

Credit markets rallied sharply last week after positive news on the vaccine development front boosted risk appetite. Spreads were notably tighter on the week with Europe outperforming the US, although some gains were given up later in the week, especially in US credit. Beyond the headline price action, however, a notable feature of the week was the positive impact on the companies hit hardest by COVID-19. Several cruise lines and airlines raised or are planning to raise capital in both stock and debt markets. US high yield issuance picked up while European issuance, including subordinated debt issuance, was robust with the EURO STOXX Banks index gaining 20% on the week. A note of caution, however, was evident in the Fed Senior Loan Officer Opinion Survey on Bank Lending Practices for Q3, which showed lending standards are still tightening while demand weakened further for corporate loans across sizes. Markedly though, since the Fed announced its credit programs, funding conditions in corporate bond markets have eased significantly, which diminishes the importance of bank loans in our view.

Eurozone: ECB President drops strong hint of more easing to come in December

Last week, ECB President Christine Lagarde was quite explicit in terms of indicating that the ECB was preparing to provide even more stimulus to the economy when it meets on December 10. She gave a broad of outline of the stimulus, saying that PEPP and TLTROs 'have proven their effectiveness' and are 'therefore likely to remain the main tools for adjusting our monetary policy'. She also emphasized that the duration of monetary policy was important. In terms of other developments, the EUR 750bn Next Generation EU initiative cleared another important hurdle last week, with the European Commission and European Parliament agreeing on some tweaks to the proposal that should now allow ratification in the European Parliament. Meanwhile, Eurozone equity markets rallied hard last week as encouraging news on vaccine developments led to a rotation by investors into previously beaten down value and cyclical stocks in which the region has a high weighting. The EURO STOXX 50 index was up around 7%, with the Spanish equity market up 13.6%.

UK: Strong recovery in Q3, but momentum starts to fade again

GDP rebounded by 15.5% QoQ in the third quarter, roughly in line with expectations, following the drop of 19.8% in Q2. The recovery was driven by a surge in consumer spending of 18.4%, while investment also grew by a solid 15.1%. Nevertheless, Q3 GDP was still almost 10% below its level in the final quarter of 2019 and the UK keeps lagging most of its regional peers. In addition, the monthly GDP numbers indicate that momentum was already slowing down towards the end of the quarter. Given the new lockdown measures implemented after that, the economy is likely to contract again in the current quarter. The weaker outlook does not bode well for the labour market. The unemployment rate rose to 4.8% in September from 4.5% the month before. The headline number continues to be distorted by furlough programs and misleading self-classification. The true rate is likely to be above 6% given claimant count measures and other employment figures. The government's recent extension of the furlough program will at least help to mitigate the near-term impact on the labour market.

China and Japan: Strong economic indicators

China's economic indicators for October remain solid. Exports, industrial production and fixed asset investment came in even stronger than consensus had expected, while real retail sales are back to pre-crisis levels. Services output growth even surged close to a three-year high and aggregate credit supply remains ample. China's biggest shopping festival ever, the Singles Day campaign (comparable to Black Friday), saw parcel volume increase by nearly 50% compared to last year's record, while sales volume by the big e-commerce giants surged. In other news, another default of a AAA-rated bond from an SOE in the coal sector raised eyebrows, though we do not believe that a broader default wave is likely.

Meanwhile, Japan's Q3 GDP growth was driven by a strong rebound in consumption and net exports, while capex continued to contribute negatively. A strong Eco Watchers survey for October and Reuters Tankan for November confirm Japan's recovery, though the third wave of COVID-19 infections may hit consumer sentiment again.

Asia: The signing of RCEP will boost Asian trade and cooperation

Following eight years of negotiations, the ten ASEAN countries, China, Japan, South Korea, Australia and New Zealand have finally signed the Regional Comprehensive Economic Partnership (RCEP) that is likely to become effective by the middle of next year. India, an initial negotiation partner, has refrained from joining, but will be able to join at a later stage in a fast-track accession process. Taiwan and Hong Kong are not participating. The trade deal affects countries that comprise about one third of the global population and contribute 30% of world GDP, a share that is expected to grow to 50% within ten years. RCEP sends a strong signal regarding trade cooperation amidst the latest de-globalisation trend and has been positively received by investors, with Asian equity markets opening on strong footing today. 65% of goods tariffs and quotas will be eliminated, a share that is expected to increase to 90% over the next years. Other non-tariff restrictions will also be tackled in areas such as government procurement, travel, services, e-commerce and intellectual property.

What to Watch

- In the US, retail sales and housing market data for October will indicate whether strong momentum in the household sector continued entering the final quarter of the year.
- In APAC, we believe the central banks of Indonesia, Thailand and the Philippines will keep policy rates unchanged. In Japan, foreign trade data and CPI for October will be reported. Australia will release statistics on Q3 GDP, Q3 wages and labour market data, and retail sales for October. Export data for October will be reported in Taiwan, Singapore and Indonesia.

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