

Weekly Macro & Markets View

Highlights and View

- **US nonfarm payrolls rise by a solid 379'000 in February**

More than half a million jobs came back over the last two months. While the recovery is promising, there is still a long way to go until the labour market has fully recovered.

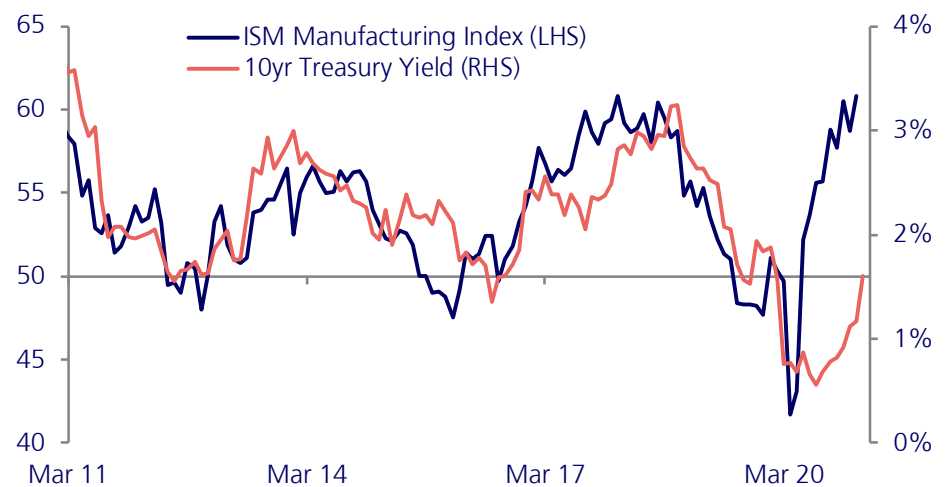
- **The UK government extends fiscal support measures and wants to boost investment**

The extensions are crucial to avoid a cliff edge in spring, particularly in the labour market where the furlough program will now run until the end of September.

- **China's growth target has been set at above 6% for this year**

We believe that this target is politically motivated and does not reflect our and the market's forecast of above 8% growth.

Treasury yields increasingly reflect stronger economic activity



Source: Bloomberg

The S&P 500's modest weekly gain of 0.8% disguises a relatively volatile week with four of five trading days experiencing moves of more than 1.3% in either direction. Yields on 10yr Treasuries have risen another 16bps, the biggest weekly move since the Democrats' double victory in Georgia's Senate runoff at the beginning of the year. The rise in yields was fuelled by another batch of strong economic data published last week. The ISM Manufacturing Index rose to 60.8, matching the 14-year high reached in 2018. Activity in the service sector was more muted but still expanding at a decent pace while the price indices rose to multiyear highs in both sectors, underlining the expected spike in inflation in the coming months. With nonfarm payrolls rising by almost 400'000 in February, following a positively revised 166'000 in January, the labour market also reflects the stronger economic momentum and increased activity. The fact that the unemployment rate has only ticked down slightly despite the substantial payroll gains supports the Fed's view that there remains a significant amount of slack, which makes any discussion on tapering premature. The Senate passed President Biden's USD 1.9tn stimulus plan with only minor changes, clearing another major hurdle. The House of Representatives is expected to pass the Senate's version on Tuesday, which could then be signed by President Biden soon after.

UK: More fiscal support and an expected boost to investment

Chancellor Sunak's budget announcement last week came with two key messages. Firstly, the government will extend most of the support measures implemented during the crisis to avoid a cliff edge in spring when the economy is likely to reopen but will remain fragile until activity is back on a stronger footing. This was particularly important with regard to the furlough programs, which will now continue to support the labour market until the end of September. Secondly, the fiscal support comes with a price tag as the government intends to raise

taxes, particularly for corporates, to bring public finances back on a more sustainable path. Crucially, however, these tax hikes will only come into effect in April 2023 when the economy is expected to have recovered from the COVID-19 shock. An important measure to create a more attractive business environment and boost investment will be the new 'super deduction' that will allow firms to cut their tax bills by 25p for every GBP 1 they invest in qualifying new equipment.

Eurozone: Signs of more fiscal stimulus, but also of inflationary pressures

The final Eurozone PMIs were encouraging in their somewhat upward revisions to the flash estimates. They also showed signs of improvement in the so-called periphery economies, especially in Italy where the Composite PMI jumped to 51.4 in February from 47.2 in January. However, the survey also suggested some inflationary pressures building, with Italy's manufacturing input and output price components increasing to 70.8 and 58.1 respectively, for example. Meanwhile, more fiscal stimulus could be coming in the Eurozone this year. Germany's

Finance Minister, Olaf Scholz, indicated that more stimulus measures were being prepared for the economy. In Italy and Spain, governments appear to be preparing more fiscal stimulus as well. None of these stimulus plans are likely to be on the scale of what we are currently seeing in the US. Nevertheless, combined with the gradual rollout of the Next Gen EU initiative they should provide important support for the Eurozone economy this year and next.

China: The NPC has started

China's 2021 National People's Congress (NPC) has started with Premier Li presenting the Government Work Report (GWR) and economic targets for this year. Although it was considered a possibility that China's political elite may again refrain from issuing a growth target, the announced goal of above 6% YoY will help avoid a spending frenzy by local governments while confirming economic stability to the broader domestic public. We're sticking to our growth forecast of 8.4% for this year, incorporating the beneficial base effect compared to last year's growth slump.

The size of the fiscal package and the special loan quota for local governments came in stronger than consensus had expected, obviously taking into account potential risks from the private consumption and foreign trade fronts, while monetary policy is expected to both support growth but also to rein in risks. In terms of thematic policies, carbon neutrality, technological innovation, rural vitalisation and supporting consumption in smaller cities and rural areas are in focus. NPC Vice-chairman Wang Chen announced plans to change Hong Kong's election law.

Australia: Q4 GDP exceeds expectations

GDP growth of -2.4% YoY for 2020 shows that Australia was one of the most resilient developed economies last year. Q4 GDP growth came in at 3.1% QoQ, exceeding the consensus expectation of 2.5%. Consumption and dwelling investment were the key drivers. Encouragingly, non-dwelling investment rose by 2.2%, signalling that the recovery has already extended beyond the consumer sector. Meanwhile, home prices in capital cities reached a new high in February, and home loans surged by 10.5% MoM in January, far exceeding consensus

expectations. In its March meeting, the RBA noted that 'lending standards remain sound, and it is important that they remain so in an environment of rising housing prices and low interest rates. If the housing frenzy were to continue, the RBA might start worrying about financial stability aspects. For now, however, rising bond yields are interpreted as the result of better economic prospects. Nevertheless, the RBA has ramped up its bond purchases recently to prevent bond yields from rising too far too fast.

Covered Bonds: Issuance boosted by surge in government bonds yields

Last week credit was not immune to the volatility brought by the recent surge in government bond yields, but spread widening remained limited. Higher yields also had a positive side effect on the covered bond primary market. After historically low issuance in February, with only three issuers and less than EUR 2bn of issuance in the Euro Benchmark market, activity resumed last week, which was the busiest since January. Three issuers sold a combined EUR 2.25bn of new bonds, all of which were 10-year maturity notes, getting strong order books as

nowadays this maturity provides investors with minimal positive yield. This is a very positive development and will help to limit the decrease in outstanding covered bond amounts. Given the steady amounts of ECB purchases and investor appetite for this asset class, we expect continuing support for spreads. We don't think the supply surge will last and derail covered bond outperformance as banks continue to focus on regulatory issuance with loss-absorbing bonds.

What to Watch

- In the US, small business optimism is expected to reflect an improving environment while inflation is likely to have accelerated in February
- In the Eurozone, all eyes will be on the ECB meeting this Thursday, when ECB President Christine Lagarde will face the challenge of reassuring bond markets that it stands ready and able to dampen down excessive bond market volatility.
- Japan's BSI corporate survey for Q1, the Eco Watchers survey for February and wage data for January will be in focus. In Australia, RBA Governor Lowe will give a speech on the recovery, investments and monetary policy. China's inflation, money supply and credit data and Taiwan's inflation and foreign trade data for February will be released. India's CPI should hover within the RBI's target zone. The Philippines' export data as well as Malaysia's and India's industrial production statistics for January are worth watching.

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