March 29, 2021

Weekly Macro & Markets View

Highlights and View

- **Eurozone business surveys jump sharply in March, though they were conducted before the latest extensions to lockdowns**

  The surveys indicate a lot of pent-up demand and set the stage for a strong rebound in Eurozone economic activity later this year.

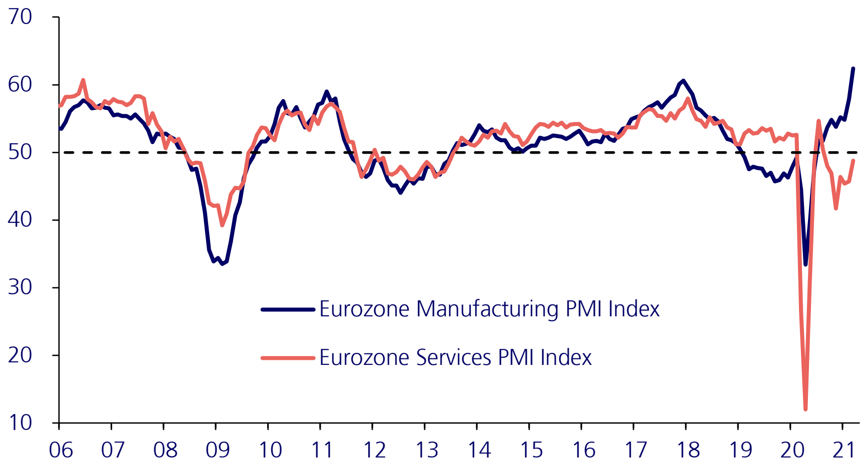
- **The blocking of the Suez Canal will be disruptive for global supply chains and trade**

  Disruptions should be manageable for the global economy as long as they are relatively short lived, but may amplify efforts to reduce vulnerability over long and complex supply chains.

- **Corporates keep coming forward with debt sales, USD high yield issuance reaches quarterly record**

  Rating agencies will keep watching how newly issued debt is deployed as Oracle's downgrade demonstrates.

Eurozone business confidence surges in March



Source: Bloomberg

Various surveys of business confidence in the Eurozone jumped last week, suggesting actual economic activity should rebound sharply in the next few months or at the latest by the second half of the year, with the Eurozone then likely to join other regions such as the US and parts of Asia that are currently seeing very strong growth. Last week, the Eurozone Manufacturing PMI rose to a record high of 62.4 in March from 57.9 in February with subcomponents in the index such as new orders, output and employment also increasing sharply. National business surveys such as the German ifo also confirmed the surge in manufacturing sentiment. The Eurozone Services PMI also rose by around three points to 48.8, though still below the 50 line separating expansion from contraction. While we still expect Eurozone GDP growth in Q1 to be negative, meaning that the region is currently in a technical recession, we expect a surge in growth from late Q2 or at the latest in the second half of the year. Admittedly, these surveys were conducted before the latest extensions to lockdown restrictions in various countries were announced. Confidence could therefore fall back a bit over the next couple of months. However, they indicate a lot of pent-up demand. The key point is that as long as these new restrictions do not last too long, Eurozone economic activity should be able to rebound sharply in the coming months and quarters.

Trade: Strong global trade momentum will be dented by the Suez Canal blockage

World trade has staged a remarkable recovery and the level of global goods trade has now more than fully recovered to its pre-crisis level, led by buoyant trade activity in Asia. The latest flash PMIs suggest that the trend is broadening with Eurozone new export orders at an all-time high in March. Leading Asian trade data, including Taiwan export orders and preliminary Korean exports, also remain elevated. Given strong trade momentum amid ongoing border restrictions and transportation challenges, it is not surprising that supply chains have come under pressure with surging shipping rates and a shortage of semiconductors. Further issues should be expected given the unfortunate blocking of the Suez Canal, amplifying near term pressures. Disruptions are likely to be relatively short-lived though, given efforts to re-float the vessel, and should be manageable for the global economy. That said, the event may amplify efforts triggered by the COVID crisis to reduce vulnerability over long and complex supply chains, including running slightly higher inventories and sourcing additional supply channels for critical components.

US: Personal spending softer ahead of the next wave of fiscal stimulus

The S&P 500 ended the week with a 1.6% gain thanks to a surge during the final trading hours on Friday. Small caps were again lagging the broader market with the Russell 2000 shedding 2.9%. Economic data were mixed last week. Personal spending fell by 1% MoM in February as income dropped by more than 7%. These numbers do not reflect the real underlying trend, however, as they fall between two tranches of fiscal stimulus. Similarly, durable goods orders fell by more than 1% MoM in February following a strong pickup in January.

The latest Markit PMI survey gives a timelier picture of the expected acceleration in business activity. Fuelled by looser COVID-19 restrictions, service providers recorded the steepest increase in new business in almost three years. The overall rate of input cost inflation accelerated to the fastest on record driven by stronger demand and persistent supply chain disruptions. Finally, new home sales fell by more than 18% MoM in February, distorted by bad weather conditions in a number of regions.

UK: Business expectations soar as the end of the lockdown approaches

Business activity accelerated markedly in March with the Composite PMI rising to 56.6 from 49.6 in February and a particularly solid improvement in the service sector. Reflecting the growing optimism regarding the re-opening of the economy, business expectations for the year ahead picked up for the third month in a row and were the strongest since the index began in July 2012. Retail sales rebounded in February following the setback in January, although levels were still 3.7% below the same month last year. The unemployment rate ticked down to 5% in January though that number does not reflect the true state of the labour market with underlying weakness in employment growth and a persistently depressed number of vacancies. Finally, inflation was weaker than expected in February, distorted by the timing of the current lockdown as prices normally rise following the expiry of Christmas discounts. However, inflation rates are likely to accelerate once shops reopen in the coming months.

Chile: The government announces a new fiscal package, S&P cuts sovereign rating

Although Chile has already vaccinated ~35% of the population with at least one dose (of which 50% already have the two doses), the pandemic has worsened, forcing the government to issue stricter lockdowns, which will affect more than 85% of the population, and to postpone the April elections for five weeks. The President announced a new fiscal stimulus of USD 6bn, equivalent to more than 2% of GDP, to compensate for the economic effect of the restrictions. This latest stimulus will extend family income protection until June. It will also strengthen support for the middle class, employment protection, and SMEs and the health system. Meanwhile, S&P cut the country's sovereign rating from A+ to A and changed its outlook from negative to stable. The erosion of public finances over the last ten years, which are expected to stabilise at a weaker level once the pandemic is finally contained, was the basis for their decision. Furthermore, the rating agency noted that the persistent political pressure to boost social spending is likely to weigh on public finance over the next two to three years.

Credit: Issuance undeterred but rating agencies are watching

Primary market activity was undeterred last week. Even if already flush with cash after the 2020 heavy issuance many companies are coming forward with deals, lured by the current low borrowing costs. Rating agencies are watching, mindful of already high corporate leverage. Oracle, after its USD 15bn deal on March 22, which the company may use in part to fund stock buybacks and dividends, was downgraded by Moody’s and Fitch to BBB and BBB+, respectively. In USD high yield, weekly sales pushed Q1 issuance to the largest quarterly number on record.

Cruise operator Royal Caribbean came forward with its first sale since June to refinance debt and raise more cash. Refinancing early, however, does not come for free. Companies are making the educated guess that they will be better off refinancing early in order to lock in low borrowing costs even if that means paying hefty call premiums, instead of waiting with the risk of facing much higher costs or, even worse, finding that the primary market is altogether shut for them.

What to Watch

- In the US, the ISM surveys are expected to reflect stronger business activity while the labour market should also show signs of further improvement.
- The European Commission business and consumer confidence surveys are likely to confirm the resilience of sentiment, especially in the manufacturing sector.
- In Japan, the focus will be on the BoJ Tankan Survey for Q1 and several indicators for February. South Korea will release export and CPI data for March and industrial production statistics for February. China’s NBS and Caixin March PMIs will be reported as well as Hong Kong’s retail sales data and Thailand’s production data for February. Australia will report foreign trade, retail sales, building approvals and private sector credit data for February as well as house prices for March. India’s financial markets are closed today due to the Holi Festival.

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