May 3, 2021

Weekly Macro & Markets View

Highlights and View

- **Biden's American Families Plan would provide about USD 1.8tn over ten years in new benefit spending and tax credits**

  The proposal includes spending on childcare, universal preschool, paid leave, free community college and intends to reverse long-term trends of rising inequality in the US.

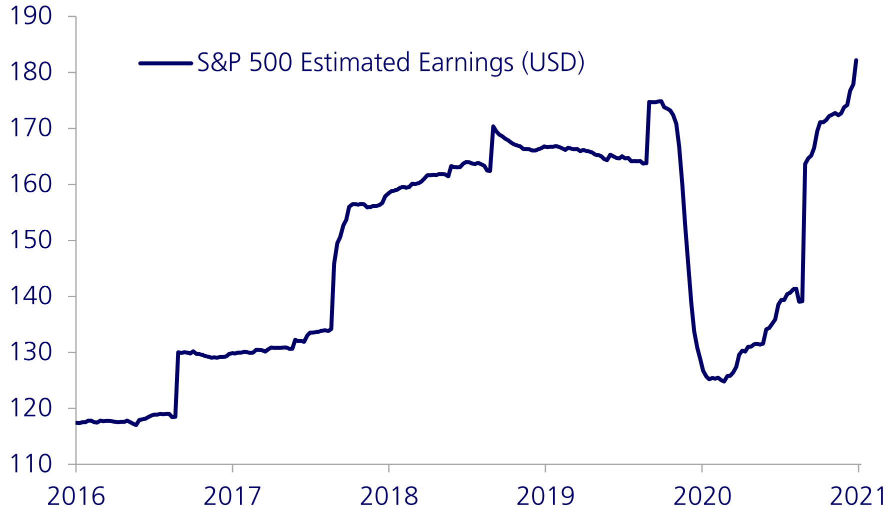
- **Eurozone GDP data show it experienced a double-dip recession**

  Growth is likely to rebound sharply in the coming months, while government spending plans under the Next Gen EU initiative will support the economy in 2022/23 as well.

- **The latest wave of COVID-19 intensifies in India and several emerging markets in Asia**

  Surging infections are causing a public health crisis in India. The struggle to contain the pandemic is likely to widen the economic performance gap between EMs and DMs this year.

US corporate earnings rebound



Source: Bloomberg

The S&P 500 reached a fresh record high last week before falling back and ending the week basically unchanged while both the Nasdaq 100 and the Russell 2000 were slightly lower. Investor focus was mostly on the US earnings season with more than 60% of the companies in the S&P 500 having reported their Q1 figures so far, a third of them last week. Overall, the current earnings season reflects the strong economic rebound in the US with a very high beat-miss-ratio of 87% and an average earnings surprise of more than 20%. Nevertheless, despite the outstanding quarter, the market reaction was relatively muted. Investors seem to be focusing more on potential headwinds and the fact that stellar growth rates will have to slow going forward. Economic data published last week were decent with only a few weak spots. Durable goods orders rose less than expected in March following the dip in February and although consumer confidence jumped in April the improvement was almost exclusively driven by the current situation while expectations ticked up only slightly. PCE core inflation accelerated to 1.8% YoY while the employment cost index rose at the fastest pace since 2007 in Q1. Meanwhile, the Fed reiterated its stance of focussing on the labour market as it considers the expected pickup in inflation to be transitory.

Eurozone: GDP data show double-dip recession, but markets are forward looking

The first estimate for 2021 Q1 GDP in the Eurozone showed that the region experienced a double-dip recession. GDP declined by -0.6% QoQ in Q1, after declining by -0.7% QoQ in Q4 2020. This followed the sharp contraction in the economy in H1 2020. However, investors were, correctly in our view, unfazed by the GDP numbers, preferring to focus on forward-looking business surveys and improving vaccination roll-out news, which are pointing to a very sharp rebound in the economy over the next few months and quarters, especially as lockdown restrictions are eased. Indeed, last week, the EC economic sentiment indicator for May jumped to its highest level since 2018. Looking further ahead, various EU governments have presented their spending plans under the EUR 750 bn Next Gen EU initiative. The extra spending should help support a period of strong growth in the Eurozone in 2022 and 2023 as well. Italy's plans for stimulating growth and reforming the economy are particularly ambitious and even if only partially implemented should also help to improve long-term trend growth.

Switzerland: Data beat great expectations

Economic data were already strong, but the latest batch strengthened further and surprised to the upside. The Manufacturing PMI accelerated to a new high of almost 70 in April, as an overwhelming majority of firms saw improving conditions. Capacity pressures are on the rise with increases in delivery times, backlogged orders, and input prices. The only component that did not post a rise was employment, suggesting that the latest improvement in activity is partly viewed as temporary, reflecting restocking and pent-up demand. The KOF leading indicator, which proxies whole-economy growth, greatly exceeded expectations in April. It surpassed the previous high from the post-financial crisis recovery in 2010, led by broad-based strength, with the key exception being accommodation and food services. Retail sales finally rose by over 20% MoM in March as shops opened up again while cross-border shopping remains limited. Though pent-up demand should ease going forward, the data paint a rosy picture, confirming strong growth for 2021.

Japan: Mixed economic data and a multi-year low for Japanese versus global equities

The Bank of Japan kept policy unchanged but revised down its core inflation outlook for the current fiscal year due to the reduction in mobile phone charges. Its new forecast for FY 2023 projects core inflation ex fresh food at only 1%, clearly below its 2% target. Meanwhile, most of the relevant economic indicators for March have been released, painting a mixed picture. Retail sales have been brisk, but consumer confidence is retreating again due to the current pandemic wave that triggered new state-of-emergencies in Tokyo and the Kansai region around Osaka. Industrial production surprised to the upside, driven by the recovery in auto production and firm output from materials related sectors, while machinery suffered from supply chain disruptions. The unemployment rate fell markedly, but this was driven by a steeper fall in the labour force than in employment as some unemployed have given up seeking a job. Finally, we note the recovery in housing starts far above consensus expectations. The good news did not help Japanese equities, however, with the MSCI Japan falling to a multi-year low relative to the MSCI World.

India & ASEAN: A record-breaking number of new infections

Just a month ago, the prevailing mood regarding the outlook for India's economy was one of optimism. However, the situation quickly took a turn for the worse as a second wave of COVID-19 struck. Last week, India continued to report a world record-breaking number of new daily cases. While the vaccine rollout has gathered pace, it has been difficult to keep up with the rapid spread of the virus. The 'double mutant' virus variant has complicated the situation further, with hospitals now under enormous stress. Both infection and death rates have soared. We expect the second wave will slow the ongoing recovery of India's economy significantly in Q2. The picture was also bleak in several ASEAN emerging economies. Malaysia, Thailand, and the Philippines are now battling new waves of infections. Although the speed of inoculation has picked up, most ASEAN countries have only vaccinated between 2-5% of their population so far, except for Singapore. We expect the ability to contain the pandemic will remain key to the economic outlook for the region this year.

US Municipal Credit: Rich valuations likely to be become richer

US municipal bonds continue to perform strongly and have significantly outperformed Treasuries in 2021 thus far. Valuations are now becoming expensive with ratios between tax-exempt and Treasury yields at historically low levels. However, we expect strength to continue as technicals remain supportive with strong inflows into mutual funds amid heavy redemptions and coupon flows back to investors. The recent bold initiatives suggested by President Biden should also support US munis, both on the supply and the demand sides. The infrastructure plan should lead to higher supply, especially if there is a new version of the Build America Bonds (BAB) program, allowing subsidies from federal funds to back local investment projects. At the same time, the more recently unveiled American Families Plan is expected to be funded through tax rate increases for wealthier households. This should boost demand for tax-exempt securities from retail investors. Fundamentals also remain strong with recent data showing that tax collections remained resilient for state and local governments.

What to Watch

- In the US, the ISM Manufacturing Index is expected to keep signalling a strong expansion in manufacturing activity while the number of new payrolls is likely to have risen substantially in April.
- Both Japan's and China's financial markets will re-open on Thursday following the 'Golden Week' holidays. Korea's markets will be closed on Wednesday. Japan will report wage data for March while China will release foreign trade statistics and the Caixin Services PMI for April. The central banks of Australia, Thailand and Malaysia are expected to keep their policy rates unchanged. Indonesia's GDP for Q1 is likely to show a further rebound in activity. Australia's housing and trade data as well as inflation data in various Asian countries are also key to watch.
- Inflation data for several LatAm countries will be published this week. In Brazil, we expect the BCB to hike the Selic rate by 75bps, while industrial production and retail sales should be affected by the pandemic. In Chile, we expect monthly economic activity to accelerate.

Disclaimer and cautionary statement

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