January 25, 2021

ZURICH®

Weekly Macro & Markets View

Highlights and View

- **US stocks reach a record high on President Biden's inauguration day**

  The absence of violent protests on inauguration day and the prospect of further fiscal stimulus measures lift investors' mood.

- **At its monetary policy meeting the ECB stated it may not use its 1.85 trillion PEPP envelope in full**

  The statement by the ECB unsettled periphery bond markets, but we still expect a substantial amount of monetary support and asset purchases during 2021.

- **Macro data show that industrial and trade momentum remain firm, bolstered by solid demand for IT related equipment**

  The global economy appears resilient as extended policy measures support sentiment and spending, offsetting headwinds from renewed lockdowns on services activity.

S&P 500 reaches an all-time high on President Biden's inauguration

Source: Bloomberg

Investor sentiment was lifted on President Biden's inauguration day as fears about nationwide violent protests, which led to the mobilization of more than 25'000 national guard troops, did not materialise. Through a number of executive orders President Biden reversed various Trump policies on his first day in office. Actions included re-joining the Paris climate accord and stopping the withdrawal from the WHO. On the economic front, Biden implemented further support measures including an extension of the pause in federal student loan repayments and an extension of the federal eviction moratorium. With initial jobless claims still at 900'000 last week these measures are crucial in bridging the gap until the economy fully reopens. Meanwhile, other economic data published last week are more reassuring given the continuing challenge of COVID-19. Markit's Composite PMI rose to 58 in January, signaling a solid start into 2021. The expansion in business activity was driven both by manufacturing and services. The housing market ended last year on a strong note with December building permits and housing starts rising to the highest level since 2006. Finally, the stock market also got an impetus from a decent start to the corporate earnings season with earnings beats and an overall positive guidance providing support.

Eurozone: Flash PMIs decline and BTPs sell off

Italian government bonds (BTPs) sold off last week, with 10yr yields rising 14bps despite Italian Prime Minister Giuseppe Conte surviving a confidence vote in parliament. Indeed, Conte only survived because Matteo Renzi's party (Italia Viva) abstained. Further votes could still see the government defeated and Conte come under pressure to resign. Even if this were to occur it remains unlikely that fresh elections would be called, the formation of a new government is the more probable scenario.

Periphery bond markets were not helped by the ECB statement at its monetary policy meeting that it might not use its EUR 1.85tn PEPP envelope in full. The Eurozone Composite Flash PMI declined by 1.6 points to 47.5 in January, with services again worse affected than manufacturing. Nevertheless, the decline was much less than when the first lockdowns were announced in March/April 2020. Although it is likely that the region will see a double-dip recession with negative Q4 and Q1 GDP growth, we still expect a strong rebound this year from Q2 onwards.

msme@zurich.com

UK: Service activity hit by another lockdown

The latest data show that the third lockdown is affecting the economy more severely than the second back in November (though not as hard as the first one). The Composite PMI fell back to a modest 40.6 in January from 50.4 the month before, indicating that the economy is contracting again at the beginning of the year. Momentum in the manufacturing sector slowed down, but the service sector is again being hit particularly hard by the lockdown measures with the Services PMI tumbling to 38.8 from 49.4. While the near-term outlook is lackluster, longer-term business expectations rose from an already elevated level with positive sentiment reaching its highest since April 2014, indicating that firms do see a light at the end of the tunnel. Households are also feeling the renewed headwinds with consumer confidence ticking down in January. Retail sales recovered only modestly in December following the lockdown-induced drop in November, but they were still a solid 6.4% higher than a year ago.

China: New COVID-19 infection cases may hit services consumption

About a year after the outbreak of COVID-19 in Wuhan, new infection cases in the range of 100-150 per day have been reported in the province of Hebei that surrounds Beijing and Tianjin, followed by the provinces of Heilongjiang and Jilin in the North-East of China. A few cases have also been reported in Beijing and Shanghai. We believe strict measures taken by the authorities including tight lockdowns and mass testing will contain the spreading of the virus. However, consumers are likely to be more cautious, negatively impacting services consumption (particularly in catering), recreation and travel. Authorities have requested that people avoid gatherings and limit travel around the Lunar New Year in early February, which may intensify the slowdown. However, as many migrant workers are likely to keep working in their factories, manufacturing production may benefit. The PBoC issued guidelines to curtail the market share of dominant non-bank payment providers in line with the government's anti-trust measures. Ant's Alipay and Tencent's WeChat Pay dominate the market with a share of about 95%.

Asia: Exports remain buoyant

The latest Asian export data remain strong, particularly for semiconductors and electronics. Taiwan's export orders surged 38.3% YoY in December, even stronger than optimistic consensus expectations. South Korea's exports for the first twenty days of January jumped 10.6% YoY on a working day adjusted basis, driven by surging wireless communication equipment, including the launch of a new mobile phone model, as well as strong semiconductor and car exports. In Japan, electric machinery exports were up 6.6% YoY in December, even though overall export volumes slowed somewhat. However, exports to Asia remained strong. Exports from Singapore and Thailand improved firmly in December, driven by the robustness of semiconductor shipments. Singapore non-oil exports rose by 6.8% YoY, with integrated circuits expanding by 15.7%, while volatile pharmaceutical shipments contracted further. Thailand's exports were up 4.7% YoY, driven by electronics and electrical appliances. Car exports remain volatile with a slight contraction in December.

Credit: Softer but internal dynamics still resilient

In contrast to the price action seen since the beginning of 2021, corporate bond markets were softer while CDS spreads rallied last week. That said, the internal dynamics of credit markets remain resilient as investors continued to pour funds into credit while issuers were able to offer bonds with minimal new issue concessions. Indeed, US investment grade credit funds saw the fourth largest inflow on record during the previous week. Despite the initial surge investment grade supply levels seem to have now moderated with last week's issuance being dominated by financial issuers. However, high yield markets, especially in the US, continue to see robust debt issuance and the month could become the strongest January on record. US Bank earnings indicated strong trading revenues and reserve releases as delinquencies on loan books remain lower than previously feared. In Europe, however, banks' prospects may not be as bright. The ECB's Bank Lending Survey for Q4 2020 showed a continuation of tight lending standards for corporate loans, with SMEs being worse affected than large companies.

What to Watch

- In the US, the corporate earnings season is gathering steam while the first estimate for Q4 GDP will show how much momentum the US economy lost in the final quarter of last year.
- Various economic data, including Q4 GDP for some countries, are likely to show a hit to growth from the lockdown measures.
- In APAC, several countries will report Q4 GDP as well as December export, industrial production and CPI data. Japan will release most of its relevant December data and Tokyo's CPI for January. On Sunday, China will report its NBS PMIs for January. In Australia, the focus will be on Q4 CPI as well as business confidence and private sector credit data for December.

Zurich Insurance Company Ltd
Investment Management
Mythenquai 2
8002 Zurich

173001566 (01/16) TCL

ZURICH®