March 1, 2021

Weekly Macro & Markets View

Highlights and View

- **Bond yields continue to surge higher with curves steepening, risk assets fall**

  Expectations of a robust economic recovery and further stimulus have fed inflation fears, though we suspect this will become overdone in the near term.

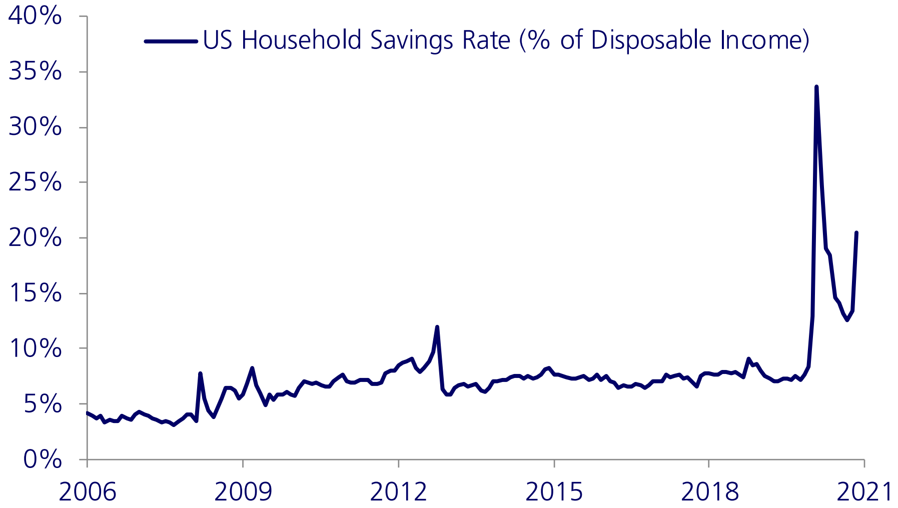
- **Boosted by January's stimulus checks, the US savings rate jumps to more than 20%**

  Consumer spending had already picked up in January, but it is expected to surge once the economy fully reopens.

- **China's February PMIs came in below expectations, even falling below 50 for SMEs and new export orders**

  We are not too concerned as PMIs seem to be distorted by the Lunar New Year and as business expectation components suggest a recovery in March.

A soaring US savings rate reflects substantial pent-up demand



Source: Bloomberg

Economic activity in the US is gaining traction as the vaccination program broadens out, the number of new infections keeps falling, and households begin to look to a brighter future. Personal spending rose a solid 2.4% MoM in January, following drops in the two previous months. Spending was supported by the stimulus checks that were sent out at the beginning of the year, boosting personal income by 10%. Accordingly, the savings rate soared to 20.5%, pointing to substantial reserves to be spent once the economy fully reopens. Consumer confidence improved only slightly in February, however, indicating that there is still a lot of caution among private households. While volatile by nature, the latest fall in initial jobless claims to the lowest since November is a reason for optimism and a signal that hiring is likely to pick up momentum. The housing market continues to show strength with new home sales growing by 4.3% in January, following a rise of 5.5% in December. House prices rose more than 10% YoY in December according to the Case-Shiller Composite Index. With the economic recovery underway, activity is expected to get an additional boost soon through the Democrats' USD 1.9tn fiscal stimulus package, which passed the House of Representatives on Friday and will now be discussed in the Senate.

Markets: Rising bond yields unsettle equity and credit investors

It was the bond markets that took centre stage again last week, with 10yr Treasury yields hitting 1.6% on Thursday before moderating somewhat to close the week at 1.4%. The bond move was global in nature, with Australia's RBA intervening to keep 3yr yields at its target level, while 10yr gilts in the UK are now at 0.8% vs. 0.15% back in January. Surging rates undermined confidence in both credit and equity markets, with the latter seeing the tech heavy Nasdaq Index plunge almost 5%, though banking stocks fared better as they tend to do when rates are rising. Investors are clearly anticipating a robust economic recovery, with fears that further stimulus, particularly in the US, may prove excessive and inflationary. Certainly, economic data are robust, and the Fed emphasised again last week a commitment to maintaining support, but the recent bond moves seems a little too aggressive in the short term. Recovery is still nascent and while there is evidence of rising inflation in some regions, this is partly transitory in nature.

Switzerland: The economy remains resilient, with growth now set to accelerate

The Swiss economy expanded by 0.3% QoQ in 2020 Q4, down from 7.6% in Q3, leaving the annual growth rate in 2020 at -3%. While the contraction was severe, Switzerland fared well compared to most other developed economies, with the economy once again proving to be resilient, helped by highly diversified production, sticky demand for exports, and swift and effective policy measures. Looking forward, leading indicators point to an acceleration in growth over the coming months. An easing of COVID restrictions should boost consumption and services activity, which have been a drag on growth over the past quarter. External demand should remain firm as the global economic cycle improves. This was also confirmed by the Manufacturing PMI, which surprised positively in February, with a pickup in hiring activity and rising new orders supportive of further gains. A weaker currency, particularly against the euro, is also helpful, especially for smaller export businesses. We therefore maintain our above consensus growth forecast, with above trend growth expected for 2021.

North Asia: Weak PMIs in China, mixed data in Japan, BoK buying bonds, Hong Kong budget

China's February PMIs for manufacturing, services and construction inched lower, coming in below consensus expectations, with the NBS Composite PMI falling to a post-COVID low. The subindices for SMEs and new export orders even fell below the boom/bust line of 50. However, we note that business outlook components suggest a swift recovery. In Japan, consumption data remained weak for a third month in a row in January, with the notable exception of strong auto sales. We believe consumption will improve as the state of emergency in several prefectures has been lifted. Industrial production picked up steam in January, but bottlenecks in the auto sector due to supply chain disruptions following the earthquake and semiconductor shortages will take their toll. Meanwhile, the Bank of Korea left policy rates unchanged, as expected, but announced a stabilising bond buying program. February exports remained strong. In Hong Kong, the HKD 120bn stimulus package within the FY 21/22 budget is comprised of various support measures for households and enterprises. The stamp duty hike raised eyebrows.

India: Out of the woods

Q4 GDP came in at 0.4% YoY, a significant jump from -7.3% in Q3. The advanced estimate of annual GDP for the fiscal year between April 2020 and March 2021 stands at -8% YoY, weaker than consensus expectations of -7%. India was among the worst affected economies in Asia during the crisis. Already riddled with a surging poverty rate, the lockdown in Q2 added to the calamity. Supply disruptions moved prices up sharply, putting India among the very few that suffered stagflation during the recession. However, the worst seems to be over. Since September 2020, new COVID-19 cases have declined notably. The vaccine program has begun, although it will take some time before the population receives sufficient doses. Inflation finally fell back to the RBI's target range in January, while consumption improved. The Manufacturing PMI rose from 56.4 to 57.7, one of the highest levels in Asia in January. We expect the economy to keep recovering swiftly this year, bolstered by further vaccination progress.

Brazil: Political and fiscal uncertainty continue to impact the equity market

Financial markets in Brazil were affected by the increase in sovereign rates in the US and uncertainty regarding the fiscal management policy and the reforms process. Congress will probably vote this week on the part of the bill that would allow the government to renew emergency aid payments of BRL 250 per month for the next four months, without breaching the fiscal rules. In addition, the decision of President Bolsonaro to replace Petrobras's CEO, which reflected his disapproval of the current fuel price policy, increased uncertainty in the financial markets. To restore confidence in the reform process, the President announced an acceleration in the privatisation of Electrobras and sent Congress a proposal to privatise Correios (the mail posting SOE). The equity market fell 7.1%, becoming the worst performing in Latin America. The currency depreciated 3.8%, closing at BRL/USD 5.6 while the Central Bank intervened in the spot market, selling USD 3.1bn. According to the BCB Focus Survey, inflation expectations for 2021 increased to 3.8% and are no longer below the target's mid-point.

What to Watch

- In the US, the ISM surveys are expected to show another healthy expansion of business activity while new payrolls are expected to have risen in February.
- UK Chancellor Sunak will present the budget, which is expected to extend most of the support measures but will also signal future tax rises, particularly for corporates.
- Following its acceleration in January Eurozone inflation will be closely watched, alongside retail sales, factory orders and the Services PMI.
- In China, the Chinese People's Political Consultative Conference (CPPCC) will be held on Thursday and the National People's Congress (NPC) will begin on Friday. Foreign trade data for January/February will be released on Sunday. In Japan, the MoF will release its Q4 corporate survey, while labour market data for January will be released as well. In Australia, Q4 GDP as well as foreign trade, retail sales and housing data for January will be published. Both Australia's RBA and Malaysia's BNM are expected to keep policy rates unchanged.

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