Weekly Macro and Markets View

20 March 2023

Highlights and View

Banks continue to roil market sentiment, with a sale of Credit Suisse to UBS announced over the weekend

While we expected volatility to rise in Q1 due to the lagged effect of rate rises, it is important that policymakers remain vigilant towards the banking sector and act swiftly to contain further contagion.

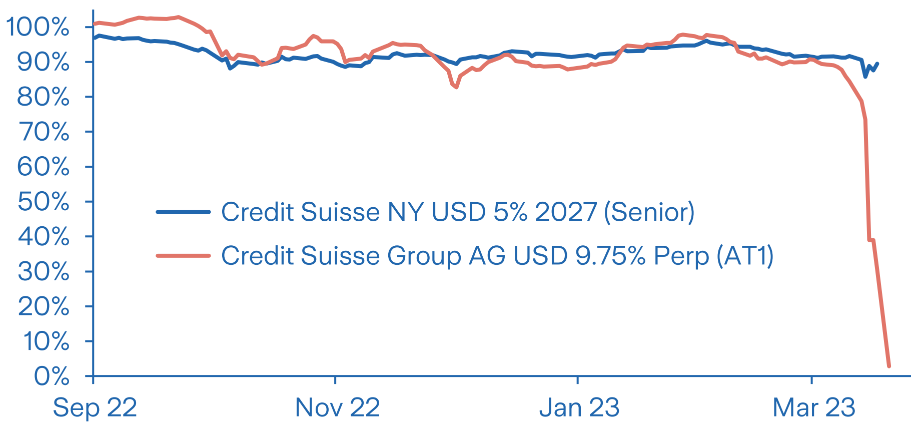
Despite recent financial market turmoil, the ECB raised policy rates by another 50bps last week

If the ECB continues raising interest rates aggressively it could add to financial stresses.

Japan's first round of wage negotiations ('shunto') between employers and labour unions shows a nominal wage rise of 4%, of which base payments increase by 2.3%

These preliminary results are higher than expected as political consensus and labour shortages are playing a larger role than in prior years, though final results may be somewhat lower.

Banks keep investors on an edge



Source: Bloomberg

Investor angst around banks continued to drive wild market moves again last week. Credit Suisse was in the spotlight with its stock price dropping and credit default swap curve widening and inverting to so called distressed levels. This, along with reported deposit outflows led to a sale of the group to UBS over the weekend, which was coordinated by the Swiss authorities. The complete write down of around CHF 16bn junior Additional Tier 1 securities as part of the deal is negatively impacting credit markets this morning. Meanwhile in the US, the stock price of First Republic Bank fell sharply last week, barring a brief reprieve on Thursday when several large US banks pledged to inject deposits totalling USD 30bn into the bank. Furthermore, in another ominous sign, US banks borrowed around USD 165bn from the Fed's discount window and the Fed's newly announced bank term funding program, while US money market funds saw a surge in inflows of around USD 113bn, both of which suggested deposit flight. Risk assets were broadly weak with credit spreads seeing some of the largest daily moves since Covid and the Global Financial Crises while government bond volatility shot up. While we had expected volatility in risk assets to rise in Q1 as the lagged effect of substantial central bank rate hikes manifests itself, it is important that policymakers remain vigilant regarding the banking sector and act swiftly to contain further contagion.

US

Tech stocks benefit from falling bond yields

The S&P 500 and the Nasdaq weathered last week's market turmoil significantly better than most of their peers, rising 1.4% and 4.4% respectively. The massive fall in bond yields and a flight to quality provided a substantial tailwind to the large US tech companies like Apple, Google and Microsoft. Inflation was mostly in line with expectations in February with headline CPI slowing to 6.0% YoY from 6.4% in January. Core CPI inflation ticked down to 5.5% YoY from 5.6%. Price pressure is expected to recede further in the coming months as indicated by the latest set of producer price data, with headline PPI slowing substantially from 5.7%YoY to 4.6%. Retail sales fell slightly in February following the very strong pickup the month before. Deteriorating consumer sentiment, driven by both current conditions and expectations, points at further headwinds for consumer spending in the near term. Finally, small business sentiment remained at rather downbeat levels, with hiring intentions and capex plans indicating that firms are reluctant to spend given an uncertain economic outlook.

Eurozone

The ECB raises rates but drops forward guidance

Despite the financial market turmoil and banking stresses last week, the ECB raised policy rates by another 50bps as it had previously committed to do, taking the deposit rate from 2.5% to 3%. However, it dropped its previous forward guidance commitment to continue raising interest rates, and instead said that it would remain 'data-dependent' taking into account 'incoming economic and financial data, the dynamics of underlying inflation, and the strength of monetary policy transmission.' ECB President Christine Lagarde will talk more about the importance of the monetary policy transmission mechanism later this week, but clearly recent events represent a tightening of financial conditions and therefore arguably take pressure off the ECB to do more. However, we expect that the ECB will still having a tightening bias going forward as it also noted last week that 'inflation is projected to remain too high for too long'. Indeed, the final estimate of inflation in February confirmed core inflation at 5.6% YoY, much too high from the ECB's perspective.

UK

A slowdown in wage growth is a welcome signal for the BoE

While most indicators still point at a tight labour market, wage growth decelerated in January, which is encouraging news ahead of the Bank of England's policy meeting this week. Both headline and core average weekly earnings slowed down to 5.7% YoY and 6.5% YoY, respectively. Although these levels are still elevated, they mask a substantial softening on a monthly basis. Raising labour market participation is one of the measures in the government's spring budget presented by Chancellor Hunt. Additional help with childcare costs for working parents along with reforms to benefits for those who are of working age and more generous pensions tax allowances should help to lift employment. To mitigate the impact of high energy costs on households, the Energy Price Guarantee will be kept in place at the current level of GBP 2'500 for another three months. Finally, a temporary full allowance for qualified business investment will help to support investment in the coming years though the impact on growth is likely to be rather limited.

China

Economic data confirm a solid start into the new year

Combined economic indicators for January/February were solid for retail sales and industrial production as well as investments into infrastructure and manufacturing facilities while property investments remained soft. However, we note that home sales are now starting to improve following a pickup in foot traffic to showrooms. Nationwide, house prices have finally started to inch up by 0.3% MoM following 17 months of falling prices, though there are some provincial disparities and new home prices are still down 1.9% YoY. Following the NPC, new Premier Li Qiang focused on high-quality growth, re-opening after the end of the Zero-Covid policy and reform. The PBoC will cut its reserve requirement ratio (RRR) for large and mid-sized banks by 25bps as of March 27 to improve liquidity conditions. In equities, the MSCI China is stabilising just below its flat 200-day moving average, following a six-week long retreat from its prior rally. Meanwhile, Evergrande, the indebted property giant, is preparing a restructuring agreement for the end of this quarter.

Australia

The labour market remains tight despite tentative signs of loosening

The unemployment rate returned to 3.5% in February following an unexpected rise to 3.7% in January, largely driven by seasonality. The participation rate increased slightly from 66.5% to 66.6% while employment rose by 64.6k, compensating for the preceding two months' decline. Over a three-month period, employment growth was approximately 12k on average, weaker than the trend growth of above 20k per month while job vacancy continues to decline. Given that, we believe the job market is in the process of loosening. Meanwhile, consumer confidence remained at a recessionary level of 78.5 in March. Despite still robust business conditions, business sentiment dropped from 6 to -4, indicating firms' growing concerns about the economic outlook. The global banking turmoil has weighed on market sentiment, putting pressure on Australia's stock market, which has a heavy weighting in banks. However, risks of contagion to Australian banks seems contained thus far.

What to Watch

- Investors will closely watch this weeks' central bank meetings, including the Fed, the BoE and the SNB, for any hints regarding a potential pause in the hiking cycle.
- In the Eurozone, the Flash PMIs and ZEW survey will be important to watch to assess the state of the economy.
- In APAC, we expect Taiwan's CBS to stand pat, while the Philippines' central bank seems likely to raise its policy rate by 25bps. PMIs and the Reuters Tankan for March will be released in Japan. Additional upcoming releases are February CPI data in Japan, Hong Kong, Singapore and Malaysia, February export data in Taiwan and Thailand, and February industrial production data in Taiwan and Singapore. Markets will be closed in Japan on Tuesday and in Indonesia on Wednesday and Thursday.
- Retail sales and monthly economic activity for January will be published in Mexico, while 2022 Q4 GDP growth will be released in Argentina. We expect the Central Bank of Brazil to keep monetary policy on hold without indicating any cut to come soon.

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