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Weekly Macro and Markets View

24 April 2023

Highlights and View

China's growth surpasses expectations in Q1, driven by services and consumer spending

China's recovery is in full swing thanks to a consumption surge. The spending spree is likely to persist, and services should remain the key pillar of growth

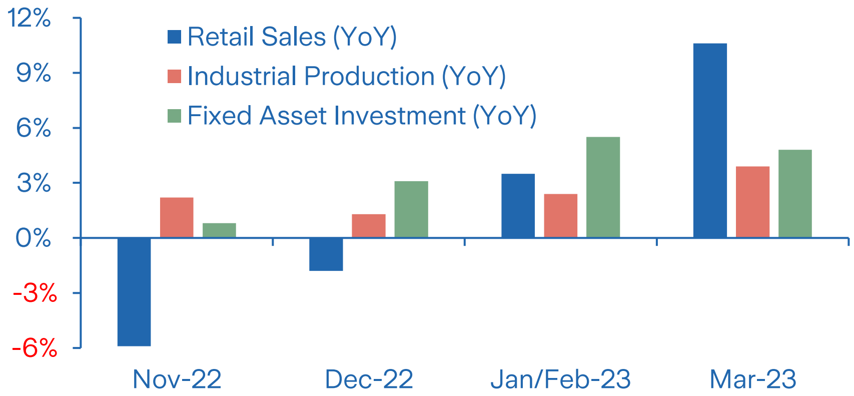
Asian trade and global manufacturing data remain weak, with little positive impact from China's reopening so far

Economic activity is unusually divergent, with subdued manufacturing and trade despite booming services, showing vulnerability to the rate hike cycle

In the UK, inflation remains above 10% for the seventh month in a row

Stubbornly high inflation and elevated wage growth are likely to force the BoE to further tighten its policy in the near term

China's growth in the spotlight



Source: NBS, ZIG

China's economy is experiencing a remarkable resurgence, after being under lockdown for almost three years, with Q1 GDP growing by 4.5% YoY versus forecasts of 4%. The reopening has fuelled a surge in consumer spending, particularly in the services sector, including hospitality and catering, which has shown a notable recovery. In March, retail sales jumped 10.6% YoY, materially beating market expectations of 7.5%, and high-frequency data suggest momentum continues to be strong.

On the industrial front, the picture is decent but not as rosy. Industrial production grew at 3.9% YoY, falling short of expectations of 4.4% in March. Fixed asset investment rose 4.8% YoY, slowing from the previous two months' average, with growth in both manufacturing and infrastructure moderating. Property investment remains subdued, but new home sales have shown signs of a rebound as the reopening has bolstered demand. In the job market, however, visible scarring persists, with joblessness among young people around a record level, although the unemployment rate for the overall population is trending lower.

All told, services and consumption will likely be the growth engine of China's ongoing recovery, with the spending spree having further to run.

US

Leading indicators are now in recession territory

The S&P 500 switched from gains to losses multiple times to finally end the week with a minor loss of 0.1%. The Nasdaq fared only slightly worse, with a loss of 0.4%. Economic data that mostly reflected a further growth deceleration as well as a number of mixed earnings reports left investors on the sidelines. The Conference Board's leading indicator fell another 1.2% MoM in March leaving it a substantial 7.8% lower than a year ago, a level that is usually only seen in or shortly ahead of a recession. The same can be said about the Philadelphia Fed's Business Outlook Survey which dropped to the lowest level since May 2020. Meanwhile, building permits, housing starts and existing home sales all fell in March while home builder sentiment remained subdued in April. There were more signs that the labour market is also easing. Initial jobless claims ticked up to 245'000, while continuing claims are rising steadily, reaching the highest level since November 2021. The subdued economic picture was brightened by the latest set of PMI surveys which show a modest improvement in both manufacturing and services in April.

UK

Inflation remains above 10% for the seventh month in a row

Headline inflation has receded slightly in March though remains elevated at 10.1% YoY after 10.4% in February. Core CPI inflation was stable at 6.2% YoY. Food inflation was an important driver behind the stubbornly high inflation numbers but price pressure remains relatively broad based. At the same time, the labour market is still very tight although a pick-up in jobless claims and a slightly higher unemployment rate are pointing to some moderation at the margin. Nevertheless, at 6.6% YoY wage growth remains uncomfortably high and is likely to force the Bank of England to keep tightening policy at its meeting in May. Meanwhile, the economy seems to have entered the second quarter with decent momentum. While the manufacturing sector has moved further into contractionary territory, with the related PMI falling to 46.6, service activity has picked up to 54.9 in April according to the latest PMI survey. The slightly better picture is confirmed by an improvement in consumer confidence, despite the ongoing pressure on real wages.

Eurozone

Services PMI jumps, but other indicators are less optimistic

The Eurozone flash composite PMI increased more than expected in April, to 54.4 from 53.7 in March, driven by a much larger than expected jump in service sector confidence. This suggests that growth early in Q2 was decent. However, forward-looking indicators are less rosy. We have already noted that bank lending growth has been decelerating for a while. In addition, despite the strong services data, last week saw further declines in the manufacturing PMI, to 45.5 in April from 47.3 in March, and manufacturing tends to lead services by a few months. In addition, the German ZEW economic expectations indicator fell for a second consecutive month.

Overall, while the jump in service sector activity is a welcome development near term, we remain concerned that growth will weaken again over the course of the year, especially as the ECB seems determined to continue tightening monetary policy. Indeed, there was a raft of generally hawkish comments from various ECB policymakers again last week.

Global Trade

Divergent outlook, with trade and manufacturing remaining weak

Last week's leading trade data from Asia suggest that trade activity has stagnated. Although Japan's exports posted a 4.3% YoY increase and MoM export growth in Singapore surprised to the upside with rising shipments to China, other data for the region are still extremely weak. Korea's 20-day exports and Taiwan's export orders showed deep contractions in April, down by 11% and 25.7% YoY respectively. Commodity exporters, including Indonesia and Malaysia, also saw weak shipments. While China's reopening has offered hope that Asian trade might improve, data are yet to show a meaningful rebound. The weakness in trade is mirrored in subdued global manufacturing activity. Last week's flash PMIs show a lack of recovery for the sector, with soft output and new orders data indicating weak demand, despite China reopening. By contrast, services activity is booming, boosted by travel and strong consumption. Such divergence is unusual, and we anticipate the gap to narrow in the months ahead as policy tightening weighs on demand and activity in key regions.

US ABS

Delinquencies to rise further as funding costs bite

Households' funding costs continue to rise, as existing and rollover financing face higher interest rates driven by both higher risk free rates and credit risk premiums. Indeed, interest rates charged on credit cards, auto loans and personal loans now stand at nearly 21%, 7.5% and 11.5% respectively. We expect these higher costs to translate into higher delinquencies and losses as real incomes remain under pressure due to inflation, while unemployment is likely to pick up, especially in the US. These trends were also evident in the recent earnings reports of US banks, which showed better net interest income but increased their credit loss provisions. That said, we don't expect delinquencies to reach levels seen during the financial crisis given better underwriting processes since then. However, credit conditions for consumers are still expected to tighten, given the recent banking sector stress and deposit outflows. The latest lending standards survey to be released in early May will be critically important to assess the potential of a credit crunch.

What to Watch

- In the Eurozone, various business surveys and the first estimate of Q1 GDP growth will give more clues as to the state of the economy.
- Bank of Japan's meeting is in focus. Key data including jobs, industrial production, retail sales and housing starts will be published in Japan. Q1 GDP and March industrial production for Korea and Taiwan as well as Australia's monthly CPI are also key statistics to watch.
- In Mexico, we expect Q1 GDP to accelerate, while the labour market in Chile will likely soften. In Brazil, economic activity figures will be released.

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