

# Weekly Macro and Markets View

15 May 2023



## Highlights and View

### US headline inflation falls to 4.9% YoY in April while core inflation ticks down to 5.5% YoY

Despite elevated monthly rates, the trend is reassuring while producer prices and business price plans point to a further easing of price pressure in the economy.

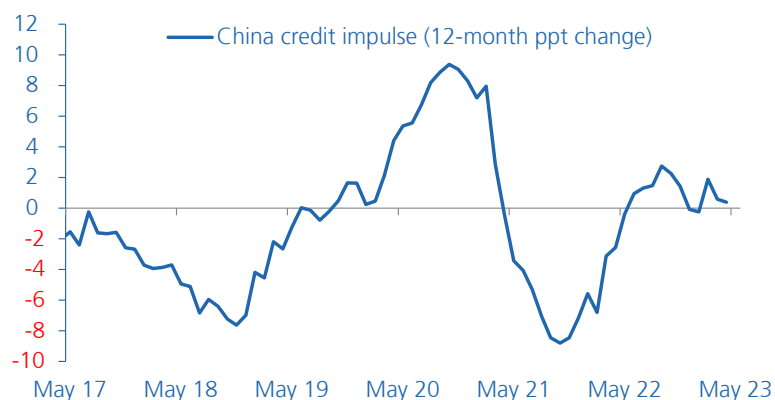
### The BoE lifts the Bank Rate by 25bps to 4.5%, the highest since 2008

Despite still very high inflation and a tight labour market the vote was not unanimous, but the MPC is keeping the door open for further rate hikes.

### The latest bank lending surveys show tightening standards for corporates amid collapsing demand

The surveys from the Fed and ECB confirm our fears that the risk of a credit crunch has increased amid bank stresses and also confirm our expectation that corporate defaults are set to rise further.

## China's reopening boom is starting to show some cracks



Source: Bloomberg

Renewed weakness in the property market is obviously behind China's disappointing economic indicators published last week. Aggregate financing data for April came in far below consensus expectations, mainly due to sharply lower household loans, while long-term corporate loans, mainly to state-owned enterprises, continued to expand. Following the reopening rising home sales were predominantly a bounce-back, not a stable trend towards firmer demand. The Covid years have clearly left their mark in household finances and confidence, and we now believe it may take longer for home sales to recover firmly. Early indications for May confirm that private property demand remains soft. Surveys also reveal that outbound tourism, though firm, is unlikely to recover to pre-Covid levels this year. Weaker domestic demand has also been confirmed by the far higher than expected drop in imports in April, driven by weaker commodity and auto imports. Meanwhile, April exports fell on a sequential basis following the surge in March, while export orders are contracting and both the NBS and Caixin Manufacturing PMIs fell below the 50 boom/bust line. Subdued CPI inflation and increasing PPI deflation confirm the disappointing set of economic indicators. We will be watching whether the remaining April statistics, published tomorrow, will confirm the softer economic conditions. Some monetary easing seems to be needed to support demand.

## US

Headline inflation falls to the lowest in two years

Headline CPI inflation ticked down to an annual rate of 4.9% in April, the lowest in two years. Core inflation also slowed marginally to 5.5% from 5.6% the month before. While the trend is going in the right direction, the monthly rate of 0.4% for both headline and core inflation is still too high for the Fed to be convinced that inflation is under control. However, other indicators are also pointing at further declines in price pressure. Producer price inflation slowed to an annual rate of 2.3% from 2.7%, the slowest pace since January 2021 and not far above the

pre-Covid average. Similarly, small business price plans also fell back to pre-Covid levels, signalling a normalisation. A further slowdown in compensation plans is also reassuring from an inflation perspective while overall small business sentiment is now at the lowest level in more than a decade, mirroring the deteriorating economic outlook. Investors took the mixed economic message with caution with the S&P falling modestly last week.

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## UK

The BoE lifts the Bank Rate to the highest since 2008

As expected, the Bank of England lifted the Bank Rate by 25bps to 4.5% at its meeting last week, the highest level since 2008. The vote was not unanimous as two members of the Monetary Policy Committee voted to keep rates unchanged. Guidance was left unchanged keeping the door open for further rate hikes in the future, which currently looks more likely than not given high inflation rates and a tight labour market. In addition, the BoE lifted its growth forecast for the coming years and is not predicting a recession in 2023 anymore. At the same

time, the Bank also revised up its inflation forecast expecting CPI to be 5.1% in the final quarter of this year, to a large degree driven by higher food inflation. Meanwhile, economic growth in Q1 was in line with expectations, with GDP expanding a very modest 0.1%, the same as in Q4 last year. Business investment was an important driver of growth while consumer spending was flat as falling real wages remain a significant headwind for households.

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## Australia

The 2023-24 budget projects a fiscal surplus and a moderate fiscal expansion

A budget surplus of AUD 4.2bn (0.2% of GDP) is anticipated for 2022-23, a significant turnaround from the earlier forecast of an AUD 36.9bn deficit (-1.5% of GDP), supported by strong growth and robust commodity prices last year. This surplus will allow for an increase of AUD 12bn in fiscal expenses for 2023-24, primarily focused on social welfare and cost-of-living relief measures for low-income households and SMEs. The issuance of government bonds is likely to decline moderately with gross government debt

expected to fall from 37.3% to 34.9% of GDP. However, while supportive fiscal measures may alleviate inflation pressures for households in the short term, they risk offsetting some of the impact from the tighter monetary policy that was aimed at curbing inflation. Meanwhile, economic data show a deteriorating macro environment, with a 4.3% MoM decline in spending intentions in April, along with still weak business confidence and well-below-trend building approvals.

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## LatAm

The Central Bank of Chile remains hawkish

In Chile, annual inflation continued to decelerate, reaching 9.9% in April. Although annual inflation decelerated in all sectors, most of the improvement comes from the volatile components, with core inflation remaining uncomfortable, reaching 10.3%. The Central Bank kept the policy rate on hold at 11.25%. The board considers it appropriate to maintain the current rate until the state of the macroeconomy indicates that inflation has converged to the 3% target. We expect the Central Bank will start the easing cycle in September. In Brazil, annual

headline inflation exceeded expectations, reaching 4.2%, with service prices still under pressure. The negative surprise was mainly driven by the increase in fresh food prices, partially compensated for by the fall in fuel prices as the impact of tax hikes is phasing out. Industrial production rebounded in March, growing 1.1% MoM, explained by the 6.3% growth in capital goods production. Despite the positive surprise, we expect restrictive financial conditions will continue to impact industrial activity.

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## Credit

Lending standards forebode rising defaults

The much anticipated ECB's Bank Lending Standards Survey and the Fed's Senior Loan Officers Survey showed that lending standards tightened further. Typically, tight standards lead default rates of High Yield companies by four quarters. Banks are likely to slow lending amid an uncertain economic environment, continuing deposit outflows and volatility in bank stocks. What was even more concerning in the surveys was that demand for loans from companies collapsed to levels last seen during the financial crisis. Debt capital markets are also lacklustre this

year, although High Yield primary market activity saw some uptick last week. Stress in the US banking sector continued with the KBW Regional Bank declining by over 6% last week, while PacWest Bancorp dropped by 20% after reports surfaced that it lost nearly 10% of deposits during the previous week. More broadly, credit spreads stabilised after the weakness of the previous weeks, while primary activity picked up notably in Europe. However, given the still negative trends around credit fundamentals, vulnerabilities still likely remain.

## What to Watch

- The focus in the US will be on retail sales and the latest batch of housing data.
- In the Eurozone, various data releases such as industrial production and the second estimate of Q1 GDP will be closely scrutinised to better understand the state of the economy.
- In APAC, the focus will be on the G7 meeting in Hiroshima, starting on Friday. Japan will report Q1 GDP, April foreign trade and CPI data. Australia will release Q1 wages as well as April labour market and May consumer confidence data. The Philippines' central bank, BSP, is expected to pause in its rate hiking cycle. April export data will be reported in Indonesia, Malaysia and Singapore. Markets will be closed in Indonesia on Thursday.
- In Chile, we expect to see positive growth in economic activity for Q. In Mexico, the central bank will likely stay on hold. In Brazil, several activity indicators will be released.

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