Weekly Macro and Markets View

18 September 2023

Highlights and View

China's economic growth is starting to pick up steam, though the property market remains in the doldrums

We expect more support measures to be introduced as several major policy meetings are scheduled before the year end, including the October Politburo meeting, the National Finance Work Conference and the Third Plenum.

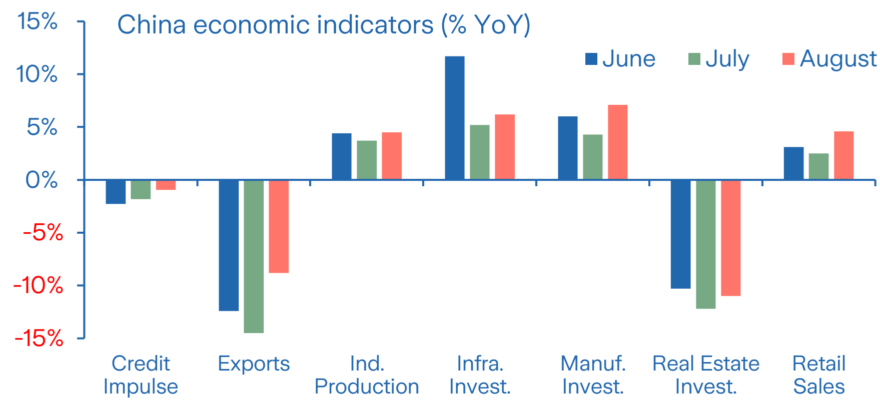
The ECB delivers a further rate hike, but signals that a pause is now warranted

While no further rate hikes are expected from the ECB, rates are likely to stay high for longer as Eurozone inflation remains sticky.

UK macro data surprise to the downside, with falling GDP and rising unemployment in July, while wage growth stays elevated

The economic outlook is deteriorating but the BoE is expected to maintain its hawkish stance for now as inflation and wage pressures remain troubling.

A glimmer of hope



Source: NBS, Bloomberg

Following better than expected August credit data and a return, albeit minor, to CPI inflation, several August economic activity data points came in above consensus expectations last week and are showing a bottoming out of the economy. Nominal retail sales were up 4.6% YoY, versus 2.5% in July, while industrial production growth improved to 4.5% YoY, from 3.7% in July, amid stabilising exports. The service sector grew 6.8% YoY, versus a prior 5.7%, driven by travel and entertainment. Fixed asset investment data for August remain a mixed bag. Though up to 2% YoY from 1.2% in July, investment growth remained below the Q2 average of 3.4%. Growth drivers were once again infrastructure and manufacturing investment, both mainly driven by government support, while property investment keeps contracting and remains the weak link in China's economic performance. We do not envisage a broad recovery unless the property sector at least stabilises. The PBoC cut the Reserve Requirement Rate (RRR) for financial institutions by 25bps, the second cut this year, releasing RMB 550bn of long-term funding to the banking system. This follows various measures by the authorities to support home owners and potential buyers, including massive easing of home-loan restrictions, cutting mortgage rates for first-home buyers effective next Monday, easing mortgage payment rules, and cutting the minimum down-payment ratio by ten percentage points.

US

Mixed data and choppy markets prior to Fed meeting

Last week's economic data were somewhat ambiguous, requiring investors to look into the detail, but ultimately left stocks flat for the week. The much anticipated CPI and PPI inflation readings were elevated, dominated by the rise in energy prices, with oil up 30% since June and now close to 10% higher this year. Headline CPI jumped from 3.2% YoY to 3.7%, while the core reading eased back to 4.3%, though still up a higher than the expected 0.3% on the month. Gasoline prices played a big part in the headline, while the rise in the core was impacted by a spike in airfares, which tend to be volatile. Home rental prices were more encouraging and we see an improving outlook in the months ahead as rent growth eases. Retail sales were also flattered by higher gasoline prices and although in aggregate they remain decent, there were revisions lowering June and July numbers and, when adjusted for inflation, sales are now down YoY. In addition, with industrial production better and consumer confidence worse near term, the Fed has a difficult task this week. We view the current level of rates as appropriate.

Eurozone

A final hike from the ECB

The ECB delivered a dovish hike last week, raising the policy rate by 25bps to 4%. The inflation forecasts for 2023 and 2024 were bumped up, likely partially reflecting higher oil prices, while both headline and core inflation were left above 2% for 2026. This justified another hike despite a meaningful cut to the growth outlook. The decision was not unanimous, with some committee members preferring a pause. Importantly, the policy statement introduced a new sentence stating that rates 'had reached levels that, if maintained for a sufficiently long duration, would make a substantial contribution to the timely return of inflation to target'. While this does not close the door to further tightening, another hike would likely require meaningful upside data surprises, including a reacceleration in core inflation. Bund yields fell on the decision but later recovered, leaving them slightly up on the week. Looking forward, we expect this to have been the ECBs last hike, but anticipate rates will be left on hold for longer.

Japan

A Cabinet reshuffle and signs of slower growth

Japan's PM Kishida reshuffled his Cabinet and key LDP executive positions. While the proportional representation of political factions remains roughly unchanged, we note that number of ministries headed by women increased from two to five, including the foreign ministry and one of the top leadership positions. PM Kishida needs to improve his public poll ratings, which have deteriorated markedly, in order to be able to call snap elections either this autumn or next year. Meanwhile, more investors are now anticipating an end of the Bank of Japan's negative interest rate policy (NIRP) and yield curve control (YCC) following vague remarks by Governor Ueda. On the economic front, the surge in both the manufacturing and non-manufacturing components of the Reuters Tankan in August has been evaporating in September. We note strong sentiment in the auto sector, but high pessimism in the tech industries. Machinery orders fell in July. We concur with the Cabinet Office that 'the recovery appears at a standstill'.

Brazil

IPCA inflation accelerates for the second consecutive month after reaching the minimum last June

In August, Brazil's Extended National Consumer Price Index (IPCA) showed an increase of 0.23% MoM, up from 0.12% MoM in July but slightly below the 0.28% MoM that had been anticipated by the market. Year on year inflation increased to 4.61%, up from 3.99% YoY the previous month. Within the components, food and beverages continued to decelerate to 1.08% YoY from 2.2% the previous month. In contrast, electricity, new vehicle, and gasoline prices contributed positively. Electricity prices had a 4.59% MoM increase, mainly driven by Petrobras' announcement, which meant a 16% increase in the wholesale price of gasoline. This impact was offset by a new drop in food prices , down -0.85% in the month with -18 bps contribution to the total. Based on this data, we maintain our expectation of a 50bp cut in the next meeting, which would leave room for two additional 50bp cuts in 2023.

US ABS

Delinquencies and defaults rise while student loan payments loom

US ABS was soft last week, underperforming the broader credit market. Weakness in the secondary market was likely driven by a record weekly issuance volume of USD 16 billion. As seen during most of this year, activity was again dominated by auto ABS deals, with 11 transactions totalling USD 10 billion. In a warning sign, however, the latest ABS performance reports show a rise in delinquencies and defaults despite the strong labour market and an expected US recession that has yet to materialise. We expect this trend to persist as banks are tightening their lending standards and households face more pressure from high inflation and the rising cost of debt. In a few weeks, student loan payments are expected to restart, which will be an additional headwind for millions of borrowers who haven't paid any instalments on their student loans for the past three years. The most vulnerable segments of borrowers could find that the resumption of loan payments may force them to cut spending and lower their ability to service other debt, such auto loans, credit cards and other unsecured loans.

What to Watch

- The Flash PMIs for major economies will show whether growth continued to slow in September.
- While US existing home sales and PMI readings are important and expected to have improved, it will be the Fed rate decision on Wednesday and subsequent press conference that will dominate US activity this week.
- In Europe, the BoE and the SNB are expected to hike rates.
- In APAC, we expect the central banks of Japan, China, Taiwan, Indonesia and the Philippines to keep policy rates unchanged. September PMIs will be reported for Japan and Australia. Japan will release CPI and export statistics for August. Taiwan, Korea, Singapore, Malaysia and Thailand will report export data. Taiwan will publish industrial production and August labour market data.
- As Brazil's economy has remained resilient and inflation near the inflation target range, we anticipate that the Central Bank will cut the Selic rate by 50bps at its policy meeting this week, leaving it at 12.75%.

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