

Weekly Macro and Markets View

30 October 2023



Highlights and View

The ECB shifts their focus to the concerning growth outlook despite above target inflation

There has been positive news on inflation while a mild European recession looks likely. Incoming data are bottoming out at poor levels but, crucially, are not getting worse.

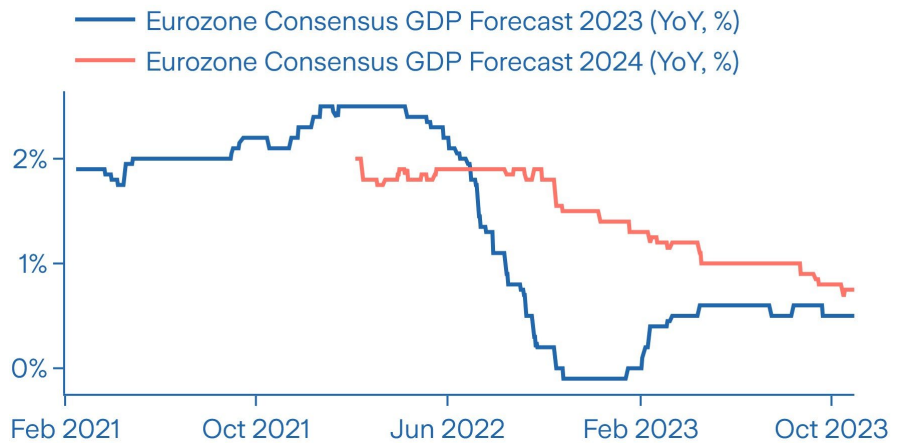
With the earnings season in full swing, mixed results point at rising headwinds to growth

Robust results from Microsoft, Meta and Amazon are encouraging, but Alphabet missed as did economically sensitive UPS and Mastercard, implying a weakening economy.

China enables local governments to spend more on infrastructure while more monetary stimulus seems to be in the offing

We applaud these measures and will keep a close eye on the outcome of the National Financial Work Conference this week as well as the Central Committee's Third Plenum in November.

The ECB's dilemma grows as the economy doesn't



Source: Bloomberg

Last week was busy for Eurozone markets, with significant data releases and an ECB meeting. The ECB is slowly adjusting their framework to place more emphasis on the weaker growth outlook despite above target inflation. They held the deposit rate at 4% and pushed back any discussion on further balance sheet reduction to subsequent meetings.

Overall, the data releases further confirm our view of growth stagnation and a minor recession in coming quarters. Flash PMI numbers were released for Germany, France and the Eurozone overall. All of the numbers printed below the crucial 50 line, indicating contraction. The Eurozone Composite PMI fell to 46.5 from 47.2 in September. Negative surprises were clearest in French Manufacturing, which fell further to 42.6, and German Services, which fell to 48 from 50.2. Meanwhile, the French Service indicator rose to 46.1 from a shockingly poor 44 in September. We also had some closely watched sentiment measures: German GfK Consumer Confidence Index fell further than expected, although it remains above the 2022 lows. On a more positive note, the German ifo Business Climate Index rose from the previous month in both the current assessment and the future outlook. The French INSEE consumer confidence survey also ticked up from the lows, despite the market's expectation for a further fall.

US

Solid growth in Q3; a more modest pace ahead

GDP grew at an annualised rate of 4.9% in the third quarter, driven by a solid rebound in consumer spending. The growth picture looks less benign going forward, however. The S&P Composite PMI ticked up to 51.0 in October from 50.2 the month before, signalling a modest expansion in business activity. Many firms reported that high interest rates and challenging economic conditions weighed on client demand. Meanwhile, input cost inflation fell sharply to the lowest since October 2020 while average selling prices for goods and

services posted the smallest monthly rise since June 2020. PCE Core inflation slowed further to 3.7% YoY, the lowest since May 2021. Interestingly, while initial jobless claims only ticked up to 210'000, continuing claims kept rising at a marked pace to reach the highest level since May, potentially signalling a more challenging employment situation. Finally, new home sales picked up more than expected while durable goods orders grew at a solid pace in September.

China

Fiscal and monetary measures are likely to improve China's economic outlook

China's NPC Standing Committee authorised the Ministry of Finance to issue RMB 1tn in government bonds, scrapping the 3% limit and increasing the budget to 3.8% of GDP. Local governments will thus be able to expand infrastructure investments. The committee also approved the frontloading of next year's special local government bond quota. We applaud these stimulus measures, though we note that local governments have already lost RMB 3tn in land sales revenue due to the property crisis, and we expect additional liquidity

support from the PBoC. President Xi's PBoC visit may be hinting at more monetary stimulus to come. Meanwhile, China's Central Huijin Investment, part of the 'National Team', bought ETFs and bank stocks to stabilise the A-share market, which has fallen 15% since early August. Since the purchases, the market has recovered 3%. We will also watch the planned meeting between President Xi and US President Biden at the APEC meeting next month.

Chile

The Central Bank cuts the MPR by less than the market anticipates

The Central Bank of Chile unanimously cut the Monetary Policy Rate by 50bps, less than market expectations of 75bps. The decision occurs in the context of volatile international markets, upward trending US Treasury rates, surging geopolitical risks and increasing oil prices, and U.S. dollar appreciation. While economic activity in Chile has continued to show signs of weakening, and inflation has decreased further, the recent Chilean peso depreciation has increased inflationary risks. As a result, the Central Bank has decided to pause the

International Reserve replacement program, which aimed to raise the country's international reserves. Finally, we anticipate that the Central Bank will continue its cutting cycle, although the pace of cuts is likely to be reduced and will depend both on the evolution of the international factors that have driven risk aversion, as well as local factors such as the closing of the Constituent Assembly in December.

Equities

Results season offers little cheer as the S&P 500 enters correction territory

Another miserable week for equity investors saw the S&P 500 give up 2.5%, taking it into correction territory, down over 10% from July's high. Other markets fared a bit better with the Euro Stoxx 600 off 1%, and the MSCI China Index actually up 2.5%. While some equity markets may be a bit oversold in the short-term, we still see risks to the downside as fundamentals continue to deteriorate. With earnings season in full swing, robust results from Microsoft, Meta and Amazon were encouraging and showed the resilience of good business models, but

Alphabet missed as did economically sensitive UPS and Mastercard, implying a weakening economy and opaque outlook. Investors are becoming more concerned about the longer-term impact of higher rates and signs that margins are coming under pressure. While Eurozone stocks were only off modestly last week, having previously lagged the US markets, disappointing earnings from Mercedes and Volkswagen underlined the challenges that the manufacturing and export dependent sectors are facing.

Credit

Resilience unlikely to last

Credit spreads were remarkably resilient last week despite continued volatility in stock markets. While some of the resilience could be explained by tentative stability returning to bond markets, credit is unlikely to remain stable if stock market jitters continue. The VIX has been steadily rising since early September, which suggests that volatility could remain persistent for some time. Furthermore, other broader gauges of demand were weak last week. Supply dropped precipitously to a trickle in both the US and Europe, and fund outflows were also

seen across the board in the US and Europe. Elevated geopolitical risk and investors' lacklustre response to the earnings season have also been compounding factors. Last but not the least, KBW US Bank Index is now below the lows for the year seen last March. All in all, with the relative income share of credit spreads in corporate bond yields being the lowest since the financial crisis, spreads currently offer little risk premium.

What to Watch

- In the US, the Fed is expected to keep rates on hold while the ISM surveys, consumer confidence and labour market data are expected to reflect growing headwinds for the economy.
- Preliminary October inflation data will be released in Europe with Eurozone HICP Inflation predicted to fall to 3.1% YoY. Q3 GDP, for which we see downside risks to the 0% consensus, will also be released as will German labour market data.
- In APAC, we will see Japan's BoJ meeting, the Cabinet's economic stimulus package and the usual month-end economic indicators. China and India will report October PMIs. Australia will publish foreign trade, retail sales and building approval data for September as well as October house prices. Bank Negara Malaysia is expected to keep policy rates unchanged. Taiwan and Hong Kong will report Q3 GDP data. South Korea will release September industrial production and October export data.
- In Latin America, the Central Bank of Brazil will announce its monetary policy decision. We anticipate a cut of 50bps, leaving the rate at 12.25%.

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Investment Management
Mythenquai 2
8002 Zurich