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Weekly Macro and Markets View

12 February 2024

Highlights and View

China's deflation pressure persists, highlighting weak growth momentum

China witnessed its most significant CPI drop since 2009, with credit growth yet to rebound significantly. However, given policymakers' increased openness to stimulus measures, there is hope for a more meaningful uptick in economic activity.

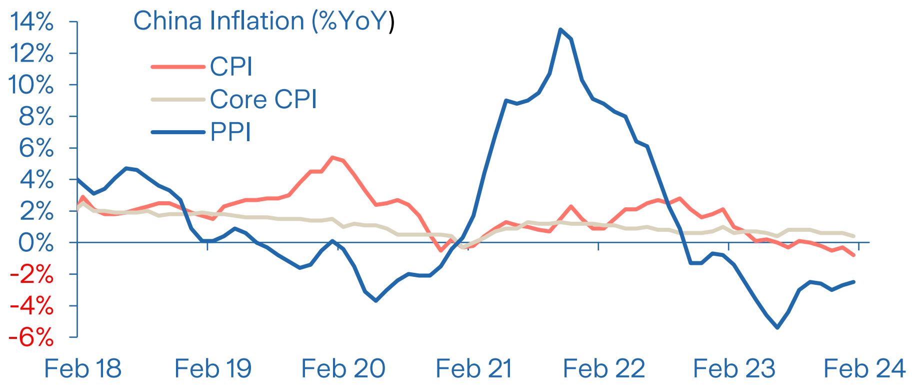
In the US, the ISM Services survey reflects robust activity in the service sector

While new orders indicate solid growth, employment expanded only modestly and prices paid rose at the fastest pace in almost a year.

In Argentina, Milei's government suffered a setback after the Chamber of Deputies did not approve the omnibus law

With the rejection of the omnibus law Milei's government could call for a plebiscite or popular consultation to govern, for which he would likewise need the approval of Congress.

The deflation trend suggests China's growth continues to be weak



Source: NBS

In January, China's CPI deepened further into deflation, dropping from -0.3% YoY in December to -0.8%, marking the sharpest decline since the Global Financial Crisis. The fall was largely driven by reduced food prices, with seasonal adjustments related to the Lunar New Year amplifying the effect. Core inflation also fell from 0.6% YoY to a seven-month low of 0.4%. Meanwhile, PPI deflation improved marginally from -2.7% to -2.5% YoY. Overall, the persistent deflationary pressure on both CPI and PPI underscores the lacklustre growth momentum.

On the credit front, January saw a typical seasonal rise in net credit, resulting in record-high new bank lending. Despite exceeding low consensus expectations, YoY growth in lending and aggregate financing remains sluggish. Growth in outstanding bank loans even slowed slightly from 10.6% YoY to 10.4% in January. Given recent more proactive policy measures, such as a larger-than-expected 50bp rate cut by the People's Bank of China (PBoC) and the government's liquidity injections into major banks, there is hope that credit growth will pick up more markedly going forward. Chinese equities showed a strong rebound last week, but the sustainability of this trend will depend on the ongoing performance of the economy and further meaningful stimulus.

US

Services activity rebounds

Services activity reaccelerated at the beginning of the year as indicated by the latest ISM Services survey. The headline number rose from 50.5 in December to 53.4 in January, with new orders pointing at further strength in the near term while employment expanded modestly. On the flipside, prices paid rose at the strongest pace in almost a year, reflecting the still elevated price pressure. The Fed's latest Senior Loan Officer Survey revealed a slowing pace of credit tightening in the final quarter of last year, which should help to ease the headwind to growth. Once again, several members of the FOMC expressed caution with regard to the recent path of inflation, making a rate cut in March unlikely. Treasury yields rose in the aftermath of the data and Fed comments, but this did not stop the S&P 500 from rising by another 1.4% last week, setting a new all-time high by closing above 5,000 for the first time in history. Smaller companies fared even better, with the Russell 2000 rising by 2.4%.

Eurozone

More 2023 disappointment, but the outlook is improving

This week saw further evidence of data weakness for December 2023, while forward looking sentiment broadly continues a slow grind higher. Eurozone retail sales fell -1.1% on the month of November, continuing a steady decline since mid-2022. German December Industrial Production was similarly disappointing, falling at a pace of -3% YoY. Some positive news came from factory orders, which surged by 8.9% on the month, driven by bulk orders. Italian confidence numbers continued to increase across consumers and businesses, but remain below long-term averages. Sentix investor confidence numbers, too, increased for the fifth month. Various ECB members pushed back on market pricing for cut expectations, with both Isabel Schnabel and Philip Lane emphasising the need for caution before declaring inflation dead. Froth has been taken out of the market, with less than a 50% chance now assigned to an April cut. We continue to see the first move coming in June amid ECB caution, but see this as highly sensitive in both directions to immediate inflation prints.

Australia

The RBA maintains a cautious tone

In its first meeting of the year, the Reserve Bank of Australia (RBA) held the cash rate steady at 4.35%, as was widely expected. It signalled a cautious outlook, predicting inflation might only reach the upper end of the 2-3% target range in 2025, while not ruling out the possibility of further rate hikes. We think the central bank's hawkish tone was intended to counteract the market's optimistic pricing of impending RBA rate cuts. Nevertheless, recent inflation data indicate a sharp decline, with CPI dropping from 5.4% YoY to 4.1% in Q4, lower than both consensus expectations and the RBA's forecast. The monthly CPI also showed a significant decrease from 4.3% YoY to 3.4% in December last year. Overall, should inflation continue to decline at its current rate, it could open the door for the RBA to consider rate cuts in the second half of the year, particularly after the Federal Reserve begins its easing cycle.

LatAm

Inflation maintains its downward trend although temporary price pressures have arisen in Brazil and Mexico

In Brazil, inflation in January showed an increase of 0.42% MoM, above market expectations of 0.34%. The 12-month accumulation was 4.51% and above the market consensus of 4.42%. Pressures on service prices were the main drivers of inflation and if this pressure continues, it could influence the magnitude of the CBB's rate cuts. In Chile, January inflation surprised by showing an increase of 0.7% MoM, after a fall of -0.5% in December, while market expectations had been 0.4%. Annual inflation was 3.8% YoY, above market consensus of 3.5%. The National Institute of Statistics has made changes to the weights in the index that will take effect this month, and which will have varying effects on the CPI. However, when calculating the index with the previous weights, inflation was 3.2% YoY. We expect the Chilean central bank to continue with the cycle of cuts, reducing the MPR by 75bps at the next meeting. In Mexico, inflation showed an increase of 0.89% MoM in January, slightly below market expectations of 0.88%. Non-core components were the main drivers.

Credit

Risk appetite undeterred by bond market volatility

Equities and corporate bonds performed well last week despite government bond yields widening, although CDS lagged. New issuance was strong, exceeding expectations in both Europe and the US. New deals were well received, with small single-digit new issue concessions and healthy oversubscription levels. Positive sentiment was also visible as IG and HY corporate funds continued to see inflows. However, banks, and their exposure to commercial real estate (CRE), continued to cause concern. In the US, New York Community Bank was downgraded to junk by Moody's, following the downgrade to BBB- by Fitch the prior week. In Europe, there were concerns regarding Aareal and Deutsche Pfandbriefbank, two German banks specialized in CRE, and while the broader European credit market was muted, bank hybrid capital underperformed. Finally, the latest release of the Federal Reserve lending survey showed that lending standards for corporate loans tightened at a slower pace in Q4 versus Q3, suggesting that defaults are likely to moderate in 2024.

What to Watch

- In the US, investors will focus on the latest batch of inflation numbers and retail sales data.
- Tuesday brings the latest German ZEW survey where we look for further improvements. On Wednesday we see preliminary 4Q 2023 GDP, employment and industrial production data for the Eurozone, with 0% GDP growth expected on the quarter.
- Japan is set to release January's PPI, Machine Tool Orders, and Q4 GDP data. Australia's job data for January will be closely watched. Export data from several countries including Indonesia and Singapore will be published. Malaysia's Q4 GDP will shed light on the country's economic performance in the final quarter of 2023.

Disclaimer and cautionary statement

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