

# Weekly Macro & Markets View

## Highlights and View

- **Black Friday sales bode well for US retailers, as the holiday season kicks off on a strong note**

Although in-store traffic is no longer what it once was, our view has been that consumer sentiment would drive purchases higher, particularly online.

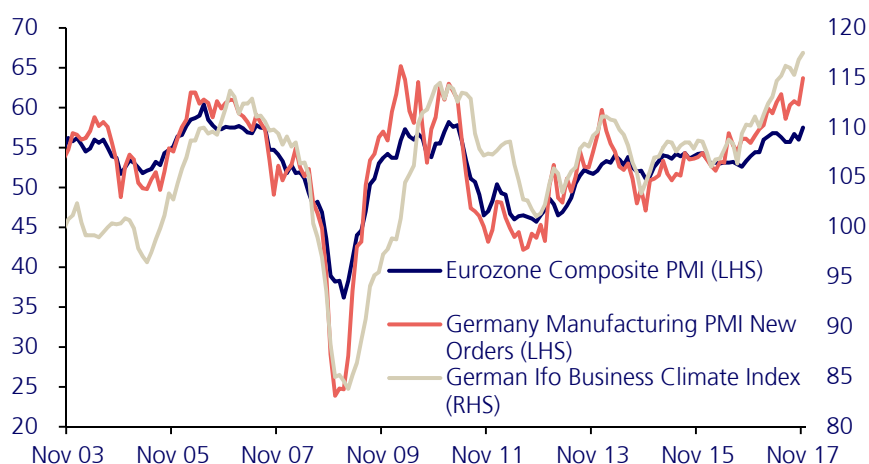
- **G3 flash PMIs strong, further acceleration in the Eurozone and Japan, activity steady in the US**

The global cycle remains solid, and there are signs of renewed vigour in manufacturing activity.

- **German ifo Business Climate Index hits fresh record high**

Surging business confidence in Germany and the rest of the Eurozone, with few signs of a slowdown, suggests upside risks to growth in Q4 and early 2018.

## Surge in business confidence points to upside risk to Eurozone growth



Source: Bloomberg

Business confidence in the Eurozone surged in November, hitting fresh record highs on some measures and suggesting upside risks to growth both in late 2017 and early 2018. The overall Eurozone composite market PMI rose one point to 57.6, its highest levels since 2011. Growth was broad-based at the country level. The composite PMI jumped one point in Germany to 57.7 and by 2.8 points in France to 60.2. Forward-looking components, such as new orders, were also strong, especially in the manufacturing sector. The German manufacturing new orders index jumped to 63.7 in November from 60.4 in October, with market commenting that companies are "inundated with new orders", but that capacity is coming under pressure and supply chains stretched. The Ifo survey of 7,000 German companies corroborated the findings from the market PMI survey with the overall business climate index hitting a fresh record high in November. The strength of the data suggests we will eventually see higher bond yields in the Eurozone and should also be supportive of corporate earnings and thus equity markets.

On the political front in Germany, the news flow has also improved. It looks increasingly likely that another round of elections will be avoided and that another grand coalition will be formed between the CDU and SPD instead. Whilst the SPD had initially rejected this, political pressure to avoid fresh elections, led by the German president, is increasing.

## US: Thanksgiving brings much to cheer

In a holiday shortened trading week there was good reason to give thanks, as stocks pushed further into record territory and economic readings remained supportive of above trend growth. As we suspected last week, the market wobble of a couple of weeks ago did indeed prove transitory. The usual tech stalwarts led the charge and lifted the NASDAQ index 1.5% on the week, to a gain of 28% for the year. Certainly it is the online retailers that are benefiting most as the holiday shopping season kicks off in earnest, though the more traditional outlets are

adapting and now challenging online outlets more successfully in the cyber space. On that note, consumer sentiment remained elevated, while existing home sales jumped higher in October, supporting the string of robust readings from the sector. Initial jobless claims moderated as we had hoped following a couple of weeks of higher readings, while durable goods orders were one of the few areas of weakness, though we would caution against reading too much into this highly volatile series.

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## UK: Chancellor's budget supports housing and reduces austerity

The highlights from Chancellor Philip Hammond's budget were less fiscal austerity, more support for the housing market on both the demand and supply side, and a significant downgrade to both potential growth and actual growth expected by the OBR over the medium term. There will be around one percentage point of GDP less fiscal austerity over the next five years, with most of the easing in austerity front-loaded. Instead, there will be increased spending on the National Health Service, tax breaks for first-time home buyers, and additional spending to support

house building. The reaction from markets was relatively muted, with sterling moved more by the latest developments in the ongoing Brexit negotiations, with increasing signs that progress is being made on agreeing the so-called "divorce bill" supporting the currency, though many other issues remain to be resolved.

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## China: Don't mix up a blip with a blow

How can it be that China featured both the best and the worst performance rank among major Asian equity markets last week? China's 'H'-shares, which are traded in Hong Kong, gained 2.6%, while domestically traded 'A'-shares fell 1.6% in Shenzhen and 0.9% in Shanghai. Guess which market made it to the headlines? Of course the 3% drop of 'A'-shares on Thursday. However, commentators failed to note that these stocks had rallied nearly 5% from the Monday low to the Wednesday high, before a brief pullback occurred. Institutional investors tend to focus

on the MSCI China instead, which again has a different index composition. Thursday's minor loss in this index turned out to be just a blip and not worth a headline at all. We admit that rising domestic yields, reflecting tighter control of credit leverage, are causing stress. At least 21 bonds have defaulted this year, as 10yr yields have risen by nearly 100 bps to 4%. This is causing frictions, some intended, some unintended. Yes, the road to more focus on qualitative growth will be bumpy, but is not avoidable.

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## Global Trade: Doing fine

World trade was flat in September, following strong growth in the prior months. More timely Asian data show a rebound in October, spurred by the global capex recovery. In Japan, exports continue to outperform imports, with machinery, transport equipment and precision instruments contributing to growth. Thailand, which is highly integrated in global supply chains, sees solid performance, and exports are up close to 20% YoY in Singapore and Indonesia, with broad-based strength. Taiwan export orders rebounded in October, following softer data

in the prior two months, and South Korean exports for the first 20 days in November were solid, underpinned by semiconductors and autos. The strong trade cycle is also visible outside of Asia. In Germany, the manufacturing PMI spiked on a surge in new orders in November and, in Switzerland, foreign machinery orders were up over 17% YoY in Q3. While the level of growth is likely to moderate going forward, we anticipate trade to end 2017 on a strong footing.

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## Credit: US Bank profitability outlook darkens, although ABS should remain resilient

Over the last few weeks, US bank equities have been underperforming broader US equities, although credit markets have not taken much notice. US banks have strong balance sheets, but at the margin a flatter US Treasury curve and rising delinquencies imply profitability pressures could emerge in the coming quarters. An interesting conundrum is the rising delinquencies despite the benign economic environment and low interest rates, which is leading to a tightening of lending standards across several categories of credit such as credit cards, auto loans and

commercial real estate. The latest mortgage delinquency data have also showed an uptick, although this may be transient and perhaps hurricane related. That said, these warning signals often forebode the end of the cycle and warrant continued monitoring by investors. One area that should remain more resilient is ABS, as larger cushions protect senior investors, but the same is not true for bank credit.

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## What to Watch

- In the US, the incoming Fed Chair, Jerome Powell, has his confirmation hearing, while personal income and spending data, along with the Fed's favoured PCE inflation readings, are potentially market moving.
- Most Asian November PMIs will be published, including the NBS and Caixin PMIs for China, and many important economic indicators in Japan and Korea. On Thursday, Bank of Korea's MPC will convene. We believe a policy rate hike of 25bps to 1.5% is probable.
- Lending data and European Commission business and consumer confidence surveys likely to provide further evidence of robust growth in the Eurozone.
- In Switzerland, the manufacturing PMI, the KOF leading indicator and Q3 GDP data are expected to show that the economy is growing steadily.

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