

Weekly Macro & Markets View

Highlights and View

- **The US and China have agreed to halt the imposition of new tariffs for 90 days**

The path to a final agreement is not a smooth one and there is still the risk that tensions rise again but the ceasefire is a welcome relief for financial markets and removes one of the near-term risks.

- **A dovish Fed lifts investors' spirits**

The latest Fed signals were more dovish and open up the possibility that the FOMC may soon be willing to pause the hiking cycle until the impact of past hikes becomes more visible.

- **China's PMIs give mixed signals with a negative tilt**

While the G20 ceasefire agreed over the weekend may improve the outlook for exports, weak lending data suggest a difficult Q1

Equities rebound as clouds disperse



Source: Bloomberg

The S&P 500 gained 4.85% last week, the best weekly performance since December 2011. Investors' optimism was lifted by dovish Fed signals and early indications that the US and China might agree on some sort of a ceasefire at the G20 summit. While remarks made by Fed Chair Powell back in October caused worries about the Fed tightening too much, the latest signals were more dovish and left open the possibility that the FOMC may soon be willing to pause the hiking cycle until the impact of past hikes becomes more visible. 10yr Treasury yields dipped below 3% for the first time since September while equity markets all over the world soared.

The positive sentiment has carried over into the current week with the US and China having agreed to halt the imposition of new tariffs for 90 days, signalling a willingness to keep the trade dispute from escalating further. The path to a final agreement is not a smooth one and there is still the risk that tensions may rise again, but the ceasefire is a welcome relief for financial markets and removes one of the near-term risks. Economic data in the US was in line with solid but softening momentum. The Conference Board Consumer Confidence index ticked down to 135.7 in November from 137.9 the month before. Importantly, the PCE Core inflation measure fell to 1.8% YoY in October from a revised down 1.9%, confirming our view that inflation remains contained for now.

China: Despite the G20 truce, the economy will struggle in Q1

Both China's official NBS and the Caixin manufacturing PMI for November were not too far away from the October reading, hovering around the 50 level. The sub-indicators gave mixed signals, while the NBS non-manufacturing index decreased by half a point to 53.4, mainly driven by weaker construction activities. The truce reached between Presidents Trump and Xi at the G20 meeting over the weekend may improve sentiment for exporters, but we believe the next few months will be difficult in the aftermath of the much weaker aggregate

financing data. We would not be surprised to even see prints below the boom/bust line of 50 for the manufacturing PMIs or their sub-components. However, that does not mean that the economy will contract, but rather show slower growth. We stick to our 6.2% GDP growth forecast for 2019, which is now more in line with consensus. It will be important that lending to private SMEs picks up again, which is now obviously a target set by China's administration.

Eurozone: Data mixed, but risk appetite firmer

The German ifo survey disappointed last week, especially the expectations component. However, the European Commission Business and Consumer Confidence survey fell less than expected and is still consistent with an above trend pace of growth in the Eurozone. In addition, the latest lending data for October show that lending to households was unchanged at 3.2% YoY, while lending to non-financial corporations dipped but was still decent at 3.9% YoY versus 4.3% YoY in September. Taken together, the data suggest that underlying growth is running slightly

above trend, but that the recovery is fragile and susceptible to any further external or internal shocks. Italian government bond spreads were tighter and Eurozone equities firmer last week as various Italian government ministers reiterated their recent shift in stance that the 2019 budget deficit target could be lower than 2.4% of GDP. Finally, ECB President Mario Draghi recognised that recent data had been weaker than expected, but indicated that the ECB was still on track to end QE asset purchases this year.

Switzerland: Growth falling from a high level, but GDP likely overstate Q3 weakness

Third quarter GDP was much weaker than anticipated, at -0.2% QoQ, down from +0.7% in Q2. This reduces the YoY growth rate from 3.5% to 2.4% and reflects broad-based weakness, with sluggish consumption, unchanged construction and a large contraction in equipment investment. Exports and imports fell sharply and net trade was a large drag on GDP. There was also a sizable inventory build-up so underlying demand growth was even weaker. Leading indicators have signalled a sharp deceleration in the economy since September but they still imply

positive growth. With some temporary factors likely to wane, GDP growth should rebound in Q4, though not to the levels seen earlier this year. The more timely data also show signs of stabilisation in November, with the KOF remaining broadly flat while the manufacturing PMI picked up slightly. With a sharp slowdown in growth and inflation well below target, this supports our view that the SNB is unlikely to tighten policy any time soon.

Japan: Q4 should see a revival of growth following a dismal Q3

Even though Japan's Manufacturing PMI for November fell to a 2018 low, we are encouraged by strong industrial production data for October. It was clear that production would recover following the negative impact of a series of natural disasters that caused disruptions to Japan's supply chain, but the recovery was stronger than consensus had expected. More importantly, production plans for November and December are encouraging, as they suggest a 4% QoQ increase in output in Q4. Even though we have to incorporate the fact that companies

tend to be too optimistic in their forecasts, the recovery still shows strong momentum. Retail sales also recovered in October, obviously driven by domestic demand rather than by higher department store spending by Chinese and Korean tourists. We are not too concerned about the weak MoF corporate survey for Q3 reported today, as it may be distorted due to the natural disasters. We expect a downward revision for Q3 GDP and take note of the steep drop in manufacturing profits, but expect a recovery in Q4.

Credit: Unicredit debt deal says it all

Credit continued to underperform equities last week, with cash credit markets being significantly weaker even though equities rebounded strongly on seemingly dovish comments from the Fed and hopes of constructive trade talks. Encouragingly, primary markets roared to life although issuers paid a price with elevated new issue concessions. Both US and European markets saw a significant uptick in volumes from the previous week, causing the secondary market to weaken. Most sectors continued to see outflows. The event that we find most

interesting though is the repricing that European bank issuers are facing amid higher peripheral yields and other fragilities such as exposure to EMs. Unicredit, which is exposed to both EMs and Italy, issued USD 3bn five-year senior non-preferred bonds in a deal to PIMCO, which was the sole investor. The pricing of the deal at around 420bps over the euro swap rate is a substantial jump versus the 70bps paid on a similar bond in January. To us, this seems like write-down risk being priced into new bail-in-able senior debt.

What to Watch

- In the US, the ISM Manufacturing and Non-Manufacturing indices are expected to show solid but softening economic momentum while labour market data is likely to remain healthy.
- In Germany, the CDU will elect its new leader and likely eventual replacement for Angela Merkel as Chancellor at the end of the week.
- We expect both Australia's RBA and India's RBI to stand pat when their monetary policy councils convene this week. Several Asian countries will release export and CPI data for November. In Japan, the focus will be on wages and household spending data for October and the Services PMI for November. In Australia, GDP for Q3 and PMIs for November will be published.

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