

# Weekly Macro & Markets View

## Highlights and View

- **The Q1 earnings season for S&P 500 companies pans out better than expected**

An earnings recession is likely to be avoided for now but the outlook remains uncertain given the slowdown in the economy and the risk of further trade disputes.

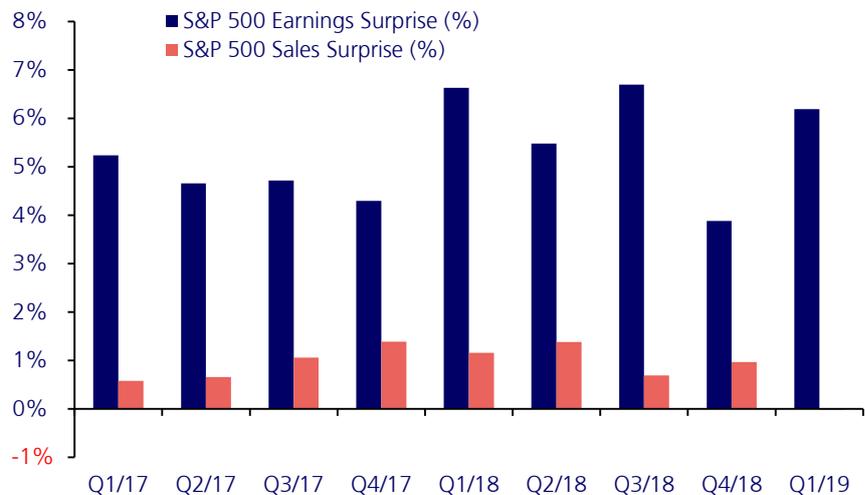
- **Eurozone Q1 GDP growth comes in stronger than expected**

While it is encouraging to see stronger hard data, business surveys suggest that underlying growth in the Eurozone is somewhat weaker than the Q1 GDP outturn indicates.

- **US President Trump threatens to increase tariffs on Chinese imports as of Friday, criticising China's re-negotiation tactics**

We still believe a solution to the US-China trade dispute will be found, but that non-trade related issues, including cybersecurity and China's global commercial expansion, will prevail over the next few years.

## Positive earnings surprise, but an uncertain outlook



Source: Bloomberg

After crossing the no-change threshold a number of times, the S&P 500 ended the week in slightly positive territory, rising 0.20%. Futures point to a negative start into the new week, however, caused by President Trump's threat to increase tariffs on Chinese imports. With more than three quarters of S&P 500 companies having reported their Q1 results, the average earnings surprise stands at 6.2% and sales growth came in almost as expected (-0.01%). While the better earnings picture helps to support equities, economic fundamentals continue to point to a slowdown. At 55.5, the ISM Non-Manufacturing Index indicates that the service sector keeps expanding, though it is down from 56.1 the month before. The ISM Manufacturing Index has weakened more substantially, however, falling from 55.3 to 52.8 in April, the lowest level since October 2016. New orders fell to 51.7, indicating weakening momentum, with new export orders even contracting. Meanwhile, the labour market remains very healthy, with 263'000 new nonfarm payrolls in April. The unemployment rate dropped to 3.6%, the lowest since 1969, a consequence of a falling participation rate. This is reflected in the underemployment rate remaining at 7.3%, the same as in March. Average hourly earnings continued to grow at an annual rate of 3.2%, not very far from the post-recession high reached in February.

## China: Responding with a RRR cut to Trump's tariff hike threat

US President Trump threatened in a tweet to increase tariffs from 10% to 25% on USD 200bn of goods imported from China as of Friday, and, in addition, to impose 25% tariffs on about USD 325bn of untaxed goods. Equity markets reacted in panic, with China's domestic 'A'-shares down nearly 6%, China's 'H'-shares down 3% and the S&P 500 futures losing 2% in pre-trading. Markets had priced in a solution to the US-China trade dispute within the next weeks and have now been caught wrong-footed. China is considering postponing Vice Premier Liu He's trip to the

US, which was scheduled for Wednesday, as Trump criticized China's stalling tactics. The US request to China to change its Cybersecurity Law to allow US firms to transfer data on China to the US is a critical issue that is hampering a solution. Today, China's PBoC announced a RRR cut of up to 3.5 percentage points to 8% for small and medium-sized regional banks to inject permanent liquidity. We think this measure would have been taken anyway, but it was announced during regular trading hours, obviously to support domestic markets.

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## Eurozone: Q1 GDP stronger than expected, but business confidence remains weak

There was a mixed set of data from the Eurozone last week. Italy emerged from recession and overall Eurozone Q1 GDP growth was stronger than expected at 0.4% QoQ versus expectations of 0.3% QoQ. Lending data from the ECB also suggest the economy continues to grow at a decent pace while manufacturing confidence in some periphery economies such as Italy and Spain was also better than expected. However, the European Commission Economic Sentiment Indicator declined for the eleventh consecutive month in April, led by the

industrial sector. Indeed, the Q1 Eurozone GDP outturn is somewhat above the pace of growth suggested by various business confidence surveys. Overall, we think the Eurozone economy is still only growing at around a trend-like pace of 0.2-0.3% QoQ, and that Q2 GDP growth will probably fall back a bit relative to Q1. Nevertheless, it is encouraging that some of the hard data in the Eurozone have improved, though weak business confidence is still a concern.

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## Switzerland: Slowing growth, but sentiment remains positive

The latest macro data show that the Swiss economy is now being impacted by the Eurozone slowdown and the sluggish global growth environment. The manufacturing PMI fell further in April, dipping below the 50 threshold for the first time since 2015, and is consistent with contraction in the industrial sector. The KOF leading indicator also slipped, led by weakness in construction and manufacturing, and remains well below its long-run average. Consumer confidence ticked down, though it is still at a decent level, helped by favourable labour markets

and offering some near-term support for the economy. CPI inflation appears to be stabilising at around 0.7% YoY, following a few firm monthly readings. While much stronger than the SNB's forecast for 2019 of only 0.3%, inflation is still weak, justifying a dovish monetary policy stance. The franc also remains vulnerable to appreciation with the US-China trade conflict back in the spotlight.

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## Australia: Housing market remains shaky

April data for Australia's housing market were weak again, with home prices down 9.7% from their September 2017 high in eight capital cities, marking the biggest downturn for decades in YoY terms. Price falls were broad-based on a sequential MoM basis across all major cities with the exception of Canberra. Prices in Sydney were down 14.5% from their high in July 2017, suffering more than average, as foreign demand, which to some extent was speculative, has dried up. We believe that house prices will fall further, though at a slower pace. Fortunately, we have

not yet seen any forced selling, despite tightening lending standards. At some point, policy rate cuts will help. Following weak inflation prints, the RBA has scope to begin cutting this week, despite the still strong labour market, but we believe the MPC will refrain from cutting before the general election. Building approvals plunged again in March, down 15% MoM, reversing last month's sudden and surprising spike of 19%, which had been driven by large project approvals in Sydney and Melbourne and thereby distorted the downtrend.

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## Asia: PMIs a mixed bag

Asian manufacturing PMIs for April revealed a mixed picture across countries, with some signs of stabilisation, though no indication of a solid rebound yet. China's two PMI versions, the NBS and the Caixin PMI, both fell, but remained just above the 50 mark, which in the case of China does not separate between growth and contraction, but rather between strong and weak growth. Taiwan's PMI fell again following last month's rebound, and remained below 50 for the seventh month in a row, confirming the steep drop in industrial production. On a more positive note, Korea's

PMI finally inched back up above the 50 line to a six-month high. This is in line with an improvement in the inventory-to-shipment ratios for both semiconductors and autos. The combined ASEAN manufacturing PMI remained roughly stable at 50.4, but we take note of an improvement in the new export order measure by one point to 50.1. India's PMI fell to 51.8, a typical pattern during a general election. We also note a slight uptick in inflation across the region looking at both consumer prices as well as input and output prices within the PMI reports.

## What to Watch

- The MPCs of several APAC central banks will convene this week. We expect the Bank of Thailand to keep its policy rate unchanged, while Australia's RBA, Malaysia's Bank Negara and the Philippine's BSP have scope to cut, though they may prefer to wait.
- It will be a busy week in terms of Asian economic data releases. Export data will be published in China, Taiwan and the Philippines, industrial production statistics in Malaysia and India, CPI data in China, Taiwan and the Philippines and finally Q1 GDP data in Indonesia and the Philippines. In Japan, Tuesday will be the first working day in the new Reiwa era following an extended Golden Week.
- In the Eurozone, industrial production and factory orders data from various countries should give further indications as to the strength of the recovery.

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