Weekly Macro and Markets View

5 December 2022

Highlights and View

The ISM Manufacturing Index falls into contractionary territory for the first time since the pandemic

Business activity slowed further in November with an increasing number of factors signaling a looming recession in the coming quarters.

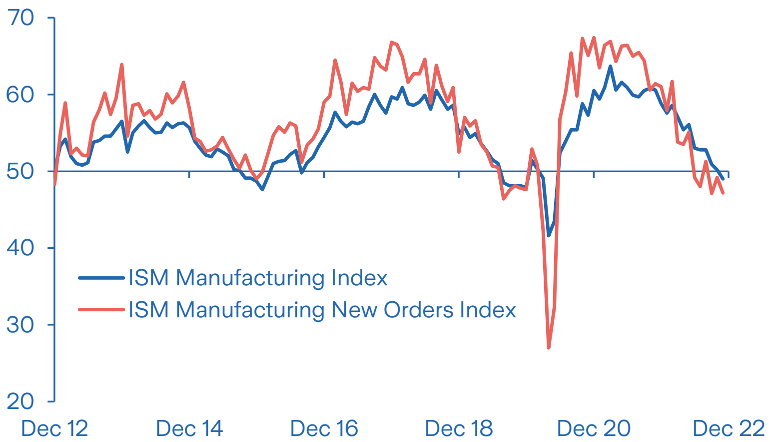
Headline inflation in the Eurozone falls back in November for the first time in many months

The fall in headline inflation is welcome and means the ECB will probably raise rates by 50bps rather than 75bps in December, but core inflation remains very high.

The Global Manufacturing PMI edges lower in November, with new orders in contraction while inventories creep higher

Global growth remains on a downward trajectory, with the global industrial sector in recession and services resilience weakening.

The US is heading for recession



Source: Bloomberg

The ISM Manufacturing Index has moved into contractionary territory for the first time since the pandemic, falling from 50.2 to 49 in November. New orders are signalling a further deceleration, adding to the rising number of indicators suggesting that the US economy is heading for recession in the first quarter of 2023. On a positive note, business prices have fallen significantly, underlining that price pressure is fading rapidly. Wages, on the other hand, keep rising with growth in average hourly earnings accelerating to 0.6% MoM, lifting the annual rate from 4.9% to 5.1% in November. Despite weakening over the past few months, the employment situation remains robust with the number of new payrolls falling from 284'000 to 263'000. Painting a similar picture, the number of job openings dropped from 10.7mn to 10.3mn in October. The quits rate, a leading indicator for future wage pressure, ticked down to 2.6%, the lowest level since May 2021 though it is still above pre-pandemic levels. Caught between stubbornly high inflation and a deteriorating outlook, consumer sentiment weakened again. Equity markets kicked off the week on the backfoot before Fed Chair Powell's relatively dovish speech lifted spirits. Based on his remarks, a 50bp rate hike in December is now all but certain while the FOMC is likely to modestly lift its projected terminal rate.

Eurozone

Headline inflation is peaking, but core is likely to remain sticky

For the first time in many months, headline inflation in the Eurozone fell in November, to 10.0% YoY from 10.6% YoY in October. The main impetus was a fall in energy inflation from around 42% YoY in October to 35% YoY in November. Further falls in headline inflation are likely over the coming months as favourable base effects in terms of energy inflation finally kick in, though the data will remain volatile due to the many interventions at the national level in gas and electricity markets. While the fall in headline inflation will be welcomed by the ECB, the headline rate is still way too high from their perspective. Core inflation also remains extremely high and was unchanged in November at 5.0% YoY. Generous wage deals in recent months, such as the one the German metal workers union, IG Metall, recently negotiated with employers, will also be a concern for the ECB. The upshot is that the ECB will likely raise rates again when it meets to decide monetary policy on December 15, but probably by 50bps rather than the 75bp increment it has been employing in recent hikes.

Switzerland

Brisk domestic demand and stable inflation

GDP grew by 0.2% QoQ in Q3 and Q2 data were revised down. This was weaker than expected but underlying growth was brisk, with a 0.6% QoQ expansion in final domestic demand and solid exports. Weakness came from construction investment, which is in contraction, and a large inventory drawdown. Looking forward, PMI data indicate that the economy will continue to expand, with the Manufacturing PMI at 53.9, which is still consistent with growth, and similarly for services. Consumer prices were unchanged in November, leaving the annual CPI rate flat at 3% and core CPI below 2%. Inflation should pick up in early 2023 due to rising electricity prices but peaking thereafter. The latest nominal wage data also show annual wage growth slowing sharply from 2% in the first half of 2022 to 1.1% in Q3, confirming that domestic price pressures remain contained. The SNB is set to maintain its hawkish bias with further rate hikes expected both in the December meeting and into 2023.

Japan

Consumer confidence tumbles while capex remains strong

While Japan's labour market remains solid, consumption indicators paint a mixed picture. October nominal retail sales growth softened a bit, but mainly because fuel prices fell, whereas apparel sales were brisk. However, consumer confidence fell further in November, with the index for households having lost more than 10 points this year to 28.6. All four subcomponents retreated, with the willingness to buy durable goods falling to an 18-year low. We attribute this to the eighth wave of Covid-infections and high inflation not experienced in the last 40 years (excl. consumption tax hikes). With Japan's soccer team moving to the round of the last 16 at the world championship in Qatar, sentiment may get a boost. Following a 14% surge from May to August, industrial production has slowed since then, and corporate forecasts suggest that a major reversal for the better seems unlikely until year end. Meanwhile, the Q3 MoF survey shows rapid profit growth for manufacturing companies due to the weaker yen, but only shallow growth for non-manufacturing companies, while capex remains solid.

Australia

Weaker economic data, highlighted by a decline in retail sales

Economic data in Australia continue to highlight the broad slowdown of the economy as recent weakness in consumer confidence translated into a decline in retail sales. Retail sales fell by 0.2% MoM in October, worse than the market forecast of a 0.5% increase. House prices also declined further in Australia, with Core Logic house prices falling by 1.1% in November, and the cumulative six-month decline in house price reaching 7.2%. The recent increase in the cash rate has had a significant impact on sentiment for the Australian housing market as variable home loans dominate the mortgage market. October inflation data also came in below market expectations, with YoY inflation at 5.3%, lower than the market forecast of 5.7%. Softer economic data resulted in a decline in the Australian bond yield of 24bps during the week to 3.02%. Despite the lower inflation print for October, we still expect the RBA to increase its cash rate by 25bps to 3.10% in December as further tightening will be needed to bring inflation within the target range.

LatAm

Economic activity is decelerating in Brazil while Chile will likely enter a recession

In Brazil, the fall in the Manufacturing PMI from 50.8 to 44 and the weakening conditions in the labour market suggest that economic activity is decelerating. Furthermore, Q3 GDP disappointed, growing 0.4% QoQ. Private consumption and fixed investment remain solid, but the drag comes from the external sector due to high import growth. In Chile, monthly economic activity surprised to the upside, growing 0.5% MoM in October, driven by the mining sector. Nevertheless, non-mining activity contracted 0.4% MoM and 1.8% YoY. Business confidence showed that expectations remain low, and the non-mining component declined from 36.1 to 35.5, staying in contractionary territory for ten consecutive months. We expect November economic activity to be negatively affected by the trucker strike, which partially blocked main highways for eight days, and the economy will likely enter recession in Q4 2022. In Mexico, the labour market remains tight, with a low unemployment rate and an increasing participation rate. Furthermore, remittances continue to surprise to the upside.

What to Watch

- In the US, the ISM Services Index is expected to have weakened further while PPI numbers are likely to reveal a slowdown in price pressure.
- In the Eurozone, German factory orders and industrial production data for October will be important to watch given the weakness in recent business surveys.
- Australia will release Q3 GDP, current account statistics, and October export data, while the RBA is expected to hike its cash rate by 25bps to 3.1%. India's RBI is likely to hike its repo rate by 25bps. Japan to release its September household spending survey. November CPI data will be reported in China, Taiwan, Thailand and the Philippines, November export data in China and Taiwan. China will publish November aggregate financing data. Philippine markets will be closed on Thursday, Thai markets on Monday.
- The Central Bank of Chile is expected to keep the policy rate on hold with a less hawkish statement as inflation will likely continue to decelerate. Inflation will also likely continue to decelerate in Brazil and Mexico.

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