ZURICH

Weekly Macro and Markets View

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Highlights and View

US business activity slows further while the employment situation is softening

The ISM Manufacturing survey fell to the lowest since May 2020. Service activity is more resilient for now but is expected to slow down too in the months ahead

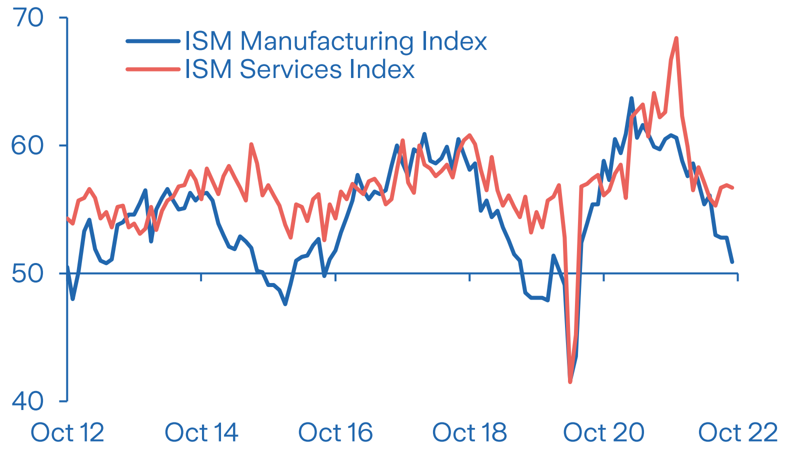
In Australia, the RBA surprised markets with a 25bps rate hike, in contrast to market expectations for a 50bps hike

The RBA becomes the first major central bank to surprise on the dovish side in recent months, as the RBA is keen to monitor the impact of recent rate increases

Credit spread tightening belies underlying fragility

Despite resilient spreads, a lacklustre primary market and persistent fund outflows suggest that sentiment continues to be fragile

US manufacturing activity falls to a post-pandemic low



Source: Bloomberg

The latest batch of economic data in the US brought further evidence of a slowing economy and a deteriorating growth outlook. The ISM Manufacturing survey fell to 50.9 in September, the lowest level since May 2020. At the same time, both new orders and employment dipped into contractionary territory. Service activity is more resilient for now with the ISM Services index ticking down to 56.7, close to the 10-year average, but a further slowdown is expected given the Fed's aggressive stance. The impact of tighter policy is increasingly showing up in a broader range of areas, including the labour market. While the unemployment rate fell back to 3.5% in September, helped by a small drop in the participation rate, most other indicators point at a softer employment situation. 263'000 new payrolls were created in September, the lowest number since April 2021. Annual wage growth slowed to 5% and the latest small business survey is signalling a further slowdown with compensation plans receding to the weakest level since May 2021. In another sign of increasing slack in the labour market, the jobs-hard-to-fill measure fell back to the lowest in 15 months. Finally, job openings dropped by more than 1.1m in August, indicating that the Fed's tightening measures are having an impact.

Australia

The RBA increases the cash rate by only 25bps

The RBA slowed the pace of rate hikes for October, increasing its policy rate by just 25bps, rather than 50bps, to 2.60%. The RBA mentioned that a considerable amount of monetary tightening has already taken place, 250 bps YTD. Concerns over the global economic outlook and recent corrections in the domestic housing market likely contributed to the RBA decision. The RBA is still expected to hike rates by 25 bps at both the November and December meetings, as it will require the cash rate to go well above the neutral rate to moderate the pace of inflation. The dovish surprise by the RBA did contribute to a temporary decline in bond yields, though the move was reversed later in the week. The domestic equity market reacted positively and rallied 4.5% on the week. In other economic data, the Corelogic house price index fell by 1.4% MoM for September, with a 4.3% decline now recorded for Q3. The house price correction will likely continue, as the combination of the high proportion of mortgages with variable interest rates and recent RBA rate hikes adversely impacts sentiment.

Switzerland

Healthy growth and easing inflation in Switzerland

The latest data show a benign macro backdrop in Switzerland, with resilient activity and downward pressure on prices. The manufacturing PMI edged higher in September and, at 57, is consistent with brisk growth in the industrial sector. The employment component is holding up at a near historical high, pointing to a solid job market. This should buffet domestic consumption, despite a slump in sentiment, and help to offset weakening external demand. Consumer prices fell in September, at the fastest monthly pace since end 2020, allowing the YoY rate to tick lower, to 3.3%. This follows a set of negative PPI prints in Q3, confirming that a stronger franc is beginning to weigh on import prices while domestic inflation remains benign. While encouraging, inflation is likely to reaccelerate in early 2023, partly reflecting steeply rising electricity prices. Given this and the resilient growth picture, we expect further SNB rate hikes before year end.

Asian PMIs

Deteriorating export PMIs are a concern

Within the September PMI surveys, a deteriorating new export order component below 50 for many countries suggest that the Asian export success story is taking a hit. Most remarkable is the disappointing 34.2 reading in Taiwan, which is confirmed by the unexpected drop in September exports by 5.3% YoY. Slowing demand from Western markets suggests that a turnaround for the better cannot be expected soon. On a positive note, economies driven by domestic demand like India, Indonesia, and the Philippines, as well as Thailand, are faring better, with headline PMIs in solid territory above 50. In China, we take note of the surprising steep drop of the Caixin Services PMI for September from 55 to 49.3 published over the weekend. Passenger trips during the National Day 'Golden Week' holidays fell 36.4% YoY and 58.1% compared to pre-Covid levels. New Omicron BA-7 outbreaks in various tourist spots are a concern. Travel bans have been imposed in the provinces of Xinjiang and Inner Mongolia.

LatAm

Inflation finally starts to ease in Chile

In Chile, inflation increased by 0.9% MoM in September, mainly driven by the increase in food prices. Annual inflation decelerated for the first time in eighteen months, falling from 14.1% to 13.7%. However, inflation remains widespread, with more than 70% of products posting price increases, and with inflation ex-volatile components, the central bank's preferred core metric, reaching 11.1% YoY, its highest level since 1994. We expect the central bank to hike the policy rate by 50bps this week, maintaining a very restrictive monetary policy stance until inflation pressures decline significantly. In Mexico, domestic demand indicators for July showed mixed results, with private consumption increasing 0.1% MoM and fixed investment falling 1.4% MoM, explained by a decline in imported machinery and non-residential investment. Inflation rose by 0.6%, slightly below market expectations. Nevertheless, price pressures remain strong and widespread, particularly in the core components. Annual headline and core inflation reached 8.7% YoY and 8.3% YoY, respectively.

Credit

Spread tightening belies underlying fragility

Last week, credit markets staged a recovery versus the poor performance of the previous week. IG and HY spreads in the US and Europe tightened on the week, with most of the recovery happening at the beginning of week in line with the rally in US and European equities. However, by Friday spreads had widened again, albeit modestly compared to the harsher drop in equities. In contrast to the secondary market, the primary market was lacklustre. Despite recovering from the abysmal previous week, in the USD IG market new issue volumes were low and new issue concessions (NIC) elevated. USD debt issuers on Thursday paid on average an eye-popping 46bp in NIC, nearly four times the YTD average, mostly driven by the Yankee deal of utility company Enel, which paid as much as 75bps. Fund flows were also lacklustre. For the week ending October 5, outflows were registered across European IG and HY funds (USD 8.2bn and 1.9bn, respectively) and US IG funds (USD 3.54bn). Only US HY funds saw inflows, totalling USD 1.87bn, which only partly reversed the previous week's outflows.

What to Watch

- In the US, investors will focus on the latest set of inflation data as these will have a crucial impact on the Fed's next steps.
- In the Eurozone, industrial production data are likely to confirm that the region`s economy is gradually slowing.
- In Brazil, inflation is expected to decelerate, showing a negative print for the third consecutive month. We expect the Central Bank of Chile to hike the policy rate by 50bps to 11.25%. In Mexico, the focus will be on industrial production and the Banxico meeting minutes.
- In APAC, our focus will be on monetary policy decisions in South Korea and Singapore as well as Japan's Eco Watchers Survey for September and the Reuters Tankan for October. Australia will report business and consumer confidence data. China will release September data for inflation, foreign trade, and monetary aggregates. Singapore will report Q3 GDP data. Markets will be closed on Monday in Japan, Taiwan, South Korea, and Malaysia. Thailand's markets will be closed on Thursday and Friday.

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