WEEKLY UPDATE

On Tenterhooks

In our recent Market Update on the US elections (see The Final Countdown), we outlined a scenario which may well be playing out – a narrow Biden victory with the Republicans retaining majority control of the Senate. This stands in stark contrast to the pre-election consensus from opinion pollsters and online prediction markets which foresaw a blue (i.e, Democratic) wave sweeping Congress and the White House. With those expectations dashed, what is the outlook for the US economy and markets?

At the time of writing, the actual outcome remains deeply uncertain. In five states, the race could go either way. And the President has already called for a recount in Wisconsin where Biden leads by only 49.4% to 48.8% with over 98% of votes counted. And further challenges are likely, for example in Pennsylvania and Georgia where the current gaps between the two are only 5,597 votes and 1,097 respectively. The uncertainty could last weeks – the deadline for conclusion of any legal challenges and selection of electors by each State is December 8 and the formal vote by the electoral college will be held on December 14.

In the weeks running up to the election, the perceived probability of a blue wave saw investors focus on the impact of Biden's massive $2 trillion 4-year investment plan. This was expected to boost long-term growth but also to spark higher inflation, encouraging "reflation trades" on higher bond yields (see chart) and a swing to more cyclical sectors. Between early August and election day, the S&P Industrials index gained 11.9% versus 2.5% for Technology. Curiously, US stocks rallied by 3.0% on Monday and Tuesday on blue wave hopes and then by a further 4.2% on Wednesday and Thursday as those hopes were disappointed!

If we are correct in judging that Joe Biden will indeed be inaugurated as President with the Senate remaining under Republican control, the new administration could find itself stymied. As we wrote in the Market Update, this scenario "would make policy implementation difficult, keeping Trump's tax cuts in place. Such a period of stalemate would not be bad for markets, but it could hamper plans of near-term fiscal stimulus". This would mean no long-term improvement in US growth potential, although we still expect the worsening pandemic to trigger bipartisan support for a new stimulus package in coming months.

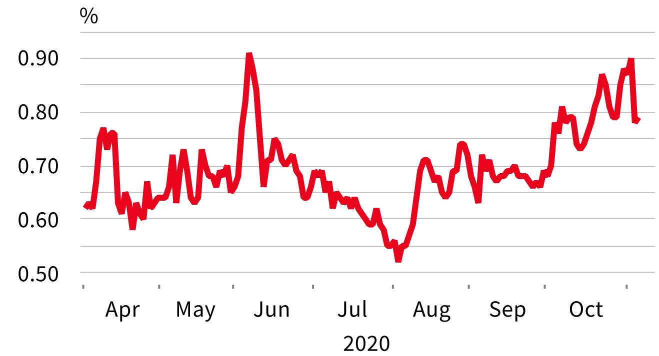
The President does have more room for manoeuvre in areas like foreign policy, suggesting a less confrontational stance with allies like the EU and Japan in order to build a coalition to keep pressure on China. Joe Biden has also promised to rejoin the Paris climate agreement on becoming President, which could provide an incentive to boost US research & development of green technologies. Biden would also be likely to adopt a more constructive approach to engagement with multilateral institutions like the United Nations, the World Trade Organisation and so on.

On Thursday, we had the latest central bank policy meetings in Washington and London. The Federal Reserve (Fed) left policy unchanged as expected – key rates remain at 0-0.25% and the Fed will continue bond purchases at around $120bn per month. Chair Jerome Powell also reiterated his call for more fiscal support for the economy. The surprise came from the Bank of England – rates were left at 0.1% but asset purchases were boosted by £150bn rather than the expected £50-100bn. This reflects the central bank's worries about the COVID-19 induced drop in consumer spending and expectations that hold-ups for exports at the border will slow recovery after Brexit becomes effective next year.

Bottom line. Looking ahead, we expect that overindebtedness and high unemployment will keep inflation low and key US rates close to zero with Fed purchases capping upside pressure on Treasury yields. As post-election uncertainty fades, we expect safe-haven flows into dollars to ebb, with the euro resuming its recovery in 2021. Regarding equity markets, policy gridlock has often proved quite supportive given that it provides great visibility to investors and businesses alike. Moreover, fiscal and monetary policy are set to remain supportive for years to come.

US Treasury yields have corrected earlier this week

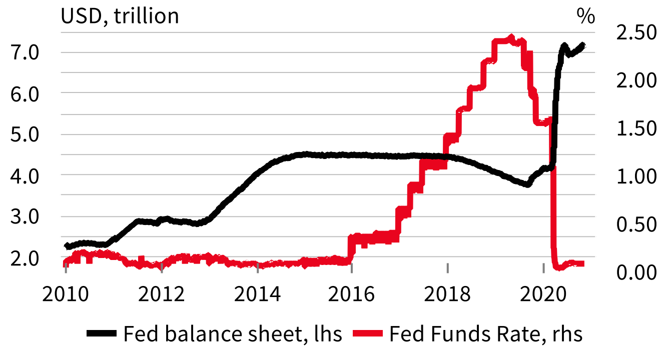
10-year US Treasury yield (in %)



Sources: SGPB, Macrobond, data as of 06/11/2020

The Federal Reserve continues its dovish stance

Fed Funds Rate and the Fed balance sheet (in USD)



Sources: SGPB, Macrobond, data as of 06/11/2020

OUR MACRO COMMENTS

This week and next

EUROZONE

- Manufacturing PMI rose to 54.8 in October, from 53.7 in September. On the other hand, services PMI fell to 46.9 from 48.0, and new restrictions due to COVID-19 may hit again economic activity.
- Retail sales fell 2.0% MoM in September after +4.4% in August, suggesting that the recovery had started to ease before the new restrictions on activity. On an annual basis, sales rose 2.2% in September.
- In Germany, industrial orders and production rose +0.5% MoM and +1.6% MoM respectively in September.

Next week's key events		*Per.*	*Prev.*	*Cons.*
12 Nov	Industrial production YoY	Sep	-7.2%	-5.5%
13 Nov	GDP growth YoY	Q3	-14.7%	-4.3%

UNITED KINGDOM

- Manufacturing PMI came in at 53.7 in October, down from 54.1 in September, suggesting that economic recovery has started to ease. At the same time, services PMI fell from 56.1 to 51.4.
- The Bank of England maintained its main lending rate at 0.1% and also voted to expand its target stock of asset purchases by £150 billion to £895 billion ($1.2 trillion).
- According to Halifax, house prices rose 0.3% MoM in October, following +1.6% the previous month.

Next week's key events		*Per.*	*Prev.*	*Cons.*
10 Nov	Unemployment rate	Sep	-4.7%	4.5%
12 Nov	GDP growth YoY	Sep	-9.3%	--

UNITED STATES

- ISM manufacturing PMI rose sharply to 59.3 in October from 55.4 in September, highlighting a solid economic recovery despite the spread of the virus. Non-manufacturing fell from 57.8 to 56.6 but remained solidly in expansion territory.
- The US Federal Reserve kept its benchmark interest rate unchanged at 0.25% in its first scheduled meeting after the US election.
- Initial jobless claims came in at 751k for the week ended October 31, down slightly from 758k the previous week.

Next week's key events		*Per.*	*Prev.*	*Cons.*
12 Nov	Inflation rate YoY	Oct	1.4%	--
13 Nov	U Mich consumer confidence	Nov	81.8	82.0

ASIA & EMERGING

- In China, Caixin's manufacturing PMI rose to 53.6 in October, from 53.0 in September. At the same time, their services PMI jumped from 54.8 to 56.8.
- In Japan, household spending rose 3.8% MoM in September after +1.7% the previous month. However, on an annual basis. It was down 10.2%.

Next week's key events		*Per.*	*Prev.*	*Cons.*
10 Nov	China: inflation rate YoY	Oct	1.7%	0.8%
19 Oct	Japan: machinery orders YoY	Sep	-15.2%	-11.6%

Sources: DataStream, Bloomberg, 06 November 2020. Note: YoY = year-on-year; QoQ = quarter-on-quarter; MoM = month-on-month, P = preliminary figure, A = advanced figure, F = final figure, seasonally adjusted, PMI = Purchasing Manager's Index.

Our 3-month targets for currencies and commodities

	Thursday close	3mth target
EUR/USD	1.18	1.18
GBP/USD	1.31	1.27
EUR/CHF	1.07	1.08
USD/JPY	103.5	**106.0**
Brent	$41.0	$42.5
Gold (oz.)	$1949	$1900

NB No changes to our 3-month targets this week.

Forecast figures are not a reliable indicator of future performance.

MARKET PERFORMANCE

Interest rates

Interest rates	Last	1wk		3mth	YTD	12mth
EONIA (EUR)	-0,47 %	-1 bp	→	-1 bp	-3 bp	-2 bp
3mth Euribor (EUR)	-0,52 %	0 bp	→	-5 bp	-13 bp	-11 bp
3mth Libor (USD)	0,21 %	0 bp	→	-3 bp	-170 bp	-168 bp
3mth Libor (GBP)	0,05 %	0 bp	→	-3 bp	-75 bp	-76 bp
10-year US Treasury bond	0,78 %	-6 bp	↓	24 bp	-113 bp	-109 bp
10-year German bond	-0,63 %	0 bp	→	-13 bp	-45 bp	-31 bp
10-year French bond	-0,36 %	-1 bp	→	-16 bp	-48 bp	-34 bp
10-year UK bond	0,24 %	1 bp	↑	11 bp	-59 bp	-54 bp

Credit

Credit	1wk		3mth	YTD	12mth
BAML EURO Corp. IG	0,3%	↑	1,7 %	1,9 %	1,7 %
BAML EURO Corp HY	1,4%	↑	2,2 %	-0,9 %	0,7 %
BAML GBP Corp IG	0,2%	↑	0,7 %	6,1 %	6,9 %
BAML US IG	1,2%	↑	-0,5 %	7,9 %	9,4 %
BAML US HY	2,2%	↑	2,1 %	2,4 %	4,5 %
BAML Global EM Sov. External Plus	2,7%	↑	1,1 %	1,8 %	4,1 %

Exchange rates

Exchange rates	Last	1wk		3mth	YTD	12mth
EUR/USD	1,18	1,3 %	↑	-0,3 %	5,4 %	6,8%
EUR/CHF	1,07	0,1 %	→	-0,8 %	-1,5 %	-2,7%
GBP/USD	1,31	1,7 %	↑	0,2 %	-0,9 %	2,0%
USD/JPY	103,5	-1,1 %	↓	-2,0 %	-4,7 %	-5,2%
USD/BRL	5,53	-4,4 %	↓	4,4 %	37,5 %	38,3%
USD/CNY	6,61	-1,6 %	↓	-4,8 %	-5,1 %	-5,8%
USD/RUB	76,9	-2,7 %	↓	5,2 %	24,1 %	21,1%

Government bonds*

Government bonds*	1wk		3mth	YTD	12mth
United States (3-7yr)	0,2 %	↑	-0,3 %	7,0 %	7,2 %
United Kingdom (3-7yr)	-0,1 %	→	-0,2 %	3,0 %	2,7 %
Germany (3-7yr)	-0,1 %	↓	0,4 %	1,0 %	0,4 %
Japan (3-7yr)	0,0 %	→	-0,1 %	-0,1 %	-0,8 %

Equities*

Equities*	Last	1wk		3mth	YTD	12mth
MSCI AC World	591	6,1 %	↑	5,3 %	6,6 %	11,6 %
Eurostoxx 50	3 216	8,7 %	↑	-1,3 %	-11,9 %	-10,1 %
DAX	12 568	8,4 %	↑	-0,7 %	-5,1 %	-4,4 %
CAC 40	4 984	9,1 %	↑	1,2 %	-14,8 %	-12,8 %
S&P 500	3 510	6,1 %	↑	5,9 %	10,4 %	16,4 %
FTSE 100	5 906	5,9 %	↑	-2,3 %	-19,5 %	-17,3 %
SMI	10 306	7,9 %	↑	2,1 %	0,3 %	3,7 %
Topix	1 650	2,4 %	↑	7,0 %	-2,0 %	-0,2 %
IBOV Brazil	100 751	4,3 %	↑	-2,0 %	-12,9 %	-7,3 %
MICEX Russia *	2 861	5,6 %	↑	-4,4 %	-6,1 %	-3,0 %
MSCI EM	1 166	4,1 %	↑	6,2 %	6,9 %	11,7 %
SENSEX 30 India	41 340	4,0 %	↑	10,1 %	1,4 %	3,9 %
Hang Seng (H-K)	25 696	4,5 %	↑	3,0 %	-6,0 %	-4,2 %
Shanghaï Composite	3 320	1,4 %	↑	-1,7 %	8,9 %	11,0 %

Commodities

Commodities	Last	1wk		3mth	YTD	12mth
Brent	$41,0	8,2 %	↑	-9,6 %	-38,2 %	-34,9 %
Gold	$1 949	4,1 %	↑	-4,8 %	28,2 %	31,2 %
Copper	$6 843	1,9 %	↑	5,3 %	11,3 %	15,7 %

Source: DataStream, on 06 November 2020.

1wk = 1-week change, 3mth = 3-month change, 12mth = 12-month change, YTD = year-to-date change, YoY = year-on-year change, BAML = Bank of America Merrill Lynch, JPM = JP Morgan, IG = Investment Grade, EM = emerging markets. * Price return for MICEX equity index. Equities; total return in local currency. Government bonds = 3-7-year returns. Figures are rounded.

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