WEEKLY UPDATE

A Chilly Winter Ahead

In recent days, IHS Markit has published the results of its monthly business confidence surveys, the Purchasing Managers Indices (PMIs). These have come as the second wave of coronavirus infections in Europe – and the third in the US – appears to have crested, and investors are looking forward to mass vaccination programmes in 2021. What will all this mean for economies and markets over the next year?

As shown on the left-hand chart below, daily numbers of new COVID-19 cases have begun to ease lower in Europe but still remain above the highs registered last spring. The scale of the pandemic has put severe pressure on the health system, forcing governments to reinstate lockdowns, which appear to be achieving their aim. In the US on the other hand, the number of new cases continues to hit new highs – with almost 38 cases per 10,000 inhabitants over the last seven days, the US has been hit harder than other countries (Germany and France are at 16 and 11 per 10,000 respectively).

The lockdowns have depressed business confidence across Europe. The composite PMI for the euro zone in November fell almost 5 points to 45.3 (50 points marks the dividing line between expansion and contraction of activity). This masks sharp divergence between countries and sectors. For example, the composite PMI for Germany remains in expansion territory at 51.7 points while France's plummeted to 40.6. Moreover, the euro zone's manufacturing PMI for November was 53.8 while confidence in services (the bulk of GDP in advanced economies) tumbled to 41.7.

The divergence between industry and services is quite logical, given that lockdowns tend to target service activities such as retail or hospitality. The divergence between France and Germany is rather more surprising – weaker confidence in services can be explained by France's more draconian restrictions, but the decline in the manufacturing PMI there stands in stark contrast to resilience in Germany. Moreover, actual industrial output has actually been stronger in France than in Germany this year as illustrated by the right-hand chart. The explanation may lie in Germany's heavy dependence on Asian demand – the prospect of a less confrontational Biden administration on trade tariffs would be good news for German exporters. Future output data will show if their confidence is misplaced.

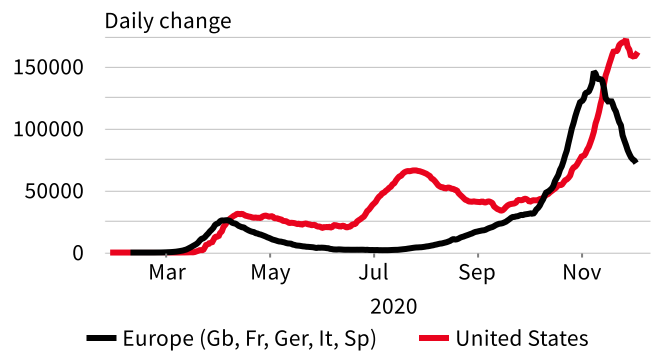
In the US, the lockdowns have been less severe and business confidence remains robust in both manufacturing and services. Indeed, the composite PMI reached its highest point in the last three years at 58.6 points. There are, however, some signs of difficult trading conditions – there have been 740,000 new weekly jobless claims on average over the past month, well above the pre-coronavirus record of 695'000 in 1984.

China on the other hand continues to power ahead. Industrial production expanded 6.9% year-on-year (YoY) in October, in line with the average pace of growth in the pre-pandemic years, while retail sales are recovering strongly (+4.3% YoY in October). Moreover, November's composite PMI came out at 55.7 points, the highest level since March 2012. According to the International Monetary Fund's latest World Economic Outlook, China is the only major economy expected to generate growth this year (+1.9%). And next year should see further outperformance, +8.2% versus the global average of +5.2%.

Bottom line. With many European countries preparing to ease restrictions in the runup to year-end, we cannot rule out the possibility of further waves of COVID-19 infections before the vaccination programmes can help populations build up sufficient levels of immunity. However, the vaccines should thereafter enable households and businesses to resume more normal levels of activity. We expect financial markets to continue to look beyond today's double-dip recession in Europe and towards a cyclical recovery in H2 2021.

New US infections remain high

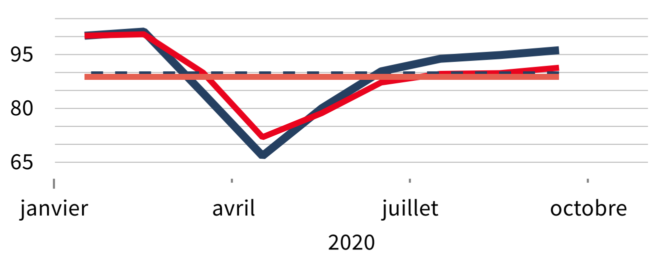
Daily change in new COVID-19 cases



Sources: SGPB, Macrobond, data as of 04/12/2020

Industrial production in France has outperformed

*Industrial production ex construction (France **black**, Germany **red**)*



Sources: SGPB, Macrobond,,Riches-Flores, data as of 04/12/2020

Past performance should not be seen as a guarantee of future returns.

OUR MACRO COMMENTS

This week and next

EUROZONE

- The final PMI figures for November confirm our scenario of a double-dip recession. The composite PMI tumbled to 45.3 from 50.0, driven by weak confidence in services, the area hardest hit by lockdowns.
- Headline consumer price inflation continued to decline, down -0.3% YoY in November on initial estimates, the same pace as in October. Core inflation also remains very low at +0.3% YoY.
- October's unemployment rate hit 8.4%, slightly below September's upwardly revised 8.5%.

Next week's key events		*Per.*	*Prev.*	*Cons.*
08 Dec	GDP QoQ final	Q3	-11.8%	12.6%
10 Dec	ECB deposit rate	-	-0.5%	-0.5%

UNITED KINGDOM

- Final manufacturing PMI figures beat expectations at 55.6, up form 53.7 as businesses increased inventories and order books ahead of Brexit. Services PMI hit 47.6 points, above initial estimates but still well below October's 51.4.
- Nationwide's house price index rose 0.9% MoM in November, taking the YoY trend to 6.5%.
- The M4 broad money aggregate rose 12.9% YoY in October thanks to a sharp increase in mortgage lending. Mortgage approvals reached 97,500 in October, well above forecasts.

Next week's key events		*Per.*	*Prev.*	*Cons.*
10 Dec	Manufacturing production MoM	Oct	0.2%	0.5%
10 Dec	Visible trade balance	Oct	-£9.3bn	-£9.6bn

UNITED STATES

- Initial jobless claims for the week ending November 21 fell to 712,000, well below expectations for 775'000. Continuing claims also fell from 6.1m to 5.5m.
- Confidence in manufacturing remains strong. The ISM survey hit 57.5 points (from 59.3 in October) while Markit's final PMI rose to 56.7. ISM's non-manufacturing survey was also robust at 55.9, as was the Markit services PMI at 58.4.
- Pending home sales decreased -1.1% MoM in October after -2.0% the previous month.

Next week's key events		*Per.*	*Prev.*	*Cons.*
10 Dec	Headline CPI YoY	Nov	1.2%	1.1%
11 Dec	Michigan consumer conf.	Dec	76.9	76.0

ASIA & EMERGING

- China's November PMI surveys confirm optimism about growth. The NBS series for manufacturing reached its best level since September 2017 while non-manufacturing confidence was the strongest since June 2012. The Caixin composite PMI hit a three-year high at 57.5
- In Japan, capital spending fell -10.6% YoY in Q3, better than forecasts and Q2.
- Brazil saw Q3 GDP bounce 7.7% QoQ, but activity was still down -3.9% YoY.

Next week's key events		*Per.*	*Prev.*	*Cons.*
8 Dec	Japan core machinery orders YoY	Oct	-11.5%	-11.2%
9 Dec	China M2 YoY	Nov	10.5%	-10.5%

Sources: DataStream, Bloomberg, 20 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	1.21	1.21
GBP/USD	1.35	1.35
EUR/CHF	1.08	1.09
USD/JPY	103.8	**104.0**
Brent	$48.8	$45.0
Gold (oz.)	$1827	$1800

NB See new changes to our 3-month targets this week.

Forecast figures are not a reliable indicator of future performance.

THIS WEEK'S Q&A

What is the outlook for the Swiss franc against EUR and USD?

The Swiss franc has historically benefited from a number of supportive factors. The country has enjoyed a lower inflation rate than its neighbours over recent decades, which pushes the purchasing power of francs higher. Swiss companies in areas such as healthcare, chemicals, precision engineering, luxury goods etc have shown themselves to be very competitive globally and their strong export performance has translated into sizeable trade surpluses. Switzerland's multi-tier democracy is characterised by tightly controlled budgets and low levels of debt – according to the IMF, gross debt in Switzerland should reach 48.7% of gross domestic product (GDP) in 2020 versus 101.1% for the euro zone and 141.2% for the G7 nations. Finally, the stability of Switzerland's economic and political systems has resulted in the country being viewed as a safe haven, generating substantial capital inflows, particularly in times of crisis.

These factors have generally pushed the franc higher against other currencies over recent decades, which from time to time has caused problems for Swiss businesses when surges in the exchange rate happened faster than companies' abilities to restructure and innovate. In recent years, the formation of the euro zone has created a large currency bloc within the European Union, Switzerland's largest trading partner, which has become the main focus for Swiss policy makers.

Given inflation differentials, the Swiss National Bank (SNB) has been able to fix key interest rates at levels well below those of most other advanced economies. This has had the additional objective of attempting to discourage hot money inflows into Swiss francs. However, these attempts have not always been successful and the SNB has resorted to various types of currency intervention. For example, in September 2011, the central bank introduced a floor for the EUR/CHF exchange rate at 1.20 and set its interventions in order to prevent the franc breaking through that level, thereby building up substantial reserves in euros. The floor finally broke in January 2015 as selling pressure on the euro (which had fallen from 1.40 to 1.15 against the US dollar) proved impossible to resist.

Since then, the SNB has continued to intervene but without signalling a particular level to the markets. The resulting purchases of foreign currencies have been used to purchase assets in those currencies, both high quality bonds and equities. At the end of October, the SNB's balance sheet reached a total of CHF 861 bn (almost 150% of Swiss gross domestic product), of which 93% is in foreign currency assets, 6% in gold and less than 0.5% in Swiss franc bonds.

The SNB has had to step up interventions this year, as pandemic-induced uncertainty has revived safe-haven buying of Swiss francs, with the apparent intention of preventing the EUR/CHF rate dropping below 1.05. These operations appear to have been largely successful and the Swiss franc began to ease modestly lower from late spring onwards, reaching 1.07 against the euro in late October.

Bottom line. The Swiss franc then shot lower on November 9 as the first successful vaccine trials raised hopes that the pandemic could come under control, reducing the need for safe havens. As a result, the Swiss National Bank has been able to step away from currency intervention for now with the euro back above CHF 1.08. We continue to expect further modest franc weakness over the next year. Our 3-month EUR/CHF target is 1.09 and 1.12 on a one-year horizon. We expect the USD/CHF exchange rate to remain broadly stable over the next year.

MARKET PERFORMANCE

Interest rates

Interest rates	Last	1wk		3mth	YTD	12mth
EONIA (EUR)	-0.47 %	0 bp	➡	-1 bp	-3 bp	-2 bp
3mth Euribor (EUR)	-0.53 %	0 bp	➡	-5 bp	-14 bp	-13 bp
3mth Libor (USD)	0.23 %	0 bp	➡	-2 bp	-168 bp	-167 bp
3mth Libor (GBP)	0.04 %	0 bp	➡	-4 bp	-75 bp	-75 bp
10-year US Treasury bond	0.92 %	4 bp	⬆	30 bp	-99 bp	-79 bp
10-year German bond	-0.55 %	4 bp	⬆	-6 bp	-36 bp	-20 bp
10-year French bond	-0.31 %	4 bp	⬆	-12 bp	-44 bp	-27 bp
10-year UK bond	0.32 %	4 bp	⬆	9 bp	-50 bp	-35 bp

Credit

Credit	1wk		3mth	YTD	12mth
BAML EURO Corp. IG	-0.1%	➡	1.6 %	2.5 %	2.4 %
BAML EURO Corp HY	0.6%	⬆	3.9 %	2.4 %	3.5 %
BAML GBP Corp IG	-0.1%	⬇	1.7 %	7.4 %	7.2 %
BAML US IG	0.4%	⬆	1.2 %	9.2 %	9.2 %
BAML US HY	0.8%	⬆	3.9 %	4.8 %	7.2 %
BAML Global EM Sov. External Plus	1.0%	⬆	2.6 %	4.4 %	7.8 %

Exchange rates

Exchange rates	Last	1wk		3mth	YTD	12mth
EUR/USD	1.21	1.9 %	⬆	2.5 %	8.3 %	9.6%
EUR/CHF	1.08	0.2 %	⬆	0.4 %	-0.3 %	-1.1%
GBP/USD	1.35	0.7 %	⬆	1.3 %	1.5 %	3.5%
USD/JPY	103.8	-0.4 %	⬇	-2.2 %	-4.4 %	-4.4%
USD/BRL	5.15	-3.5 %	⬇	-2.7 %	28.2 %	22.5%
USD/CNY	6.54	-0.5 %	⬇	-4.4 %	-6.0 %	-7.3%
USD/RUB	74.5	-1.6 %	⬇	-1.1 %	20.3 %	16.2%

Government bonds*

Government bonds*	1wk		3mth	YTD	12mth
United States (3-7yr)	0.0 %	➡	-0.5 %	6.7 %	6.2 %
United Kingdom (3-7yr)	-0.1 %	➡	-0.4 %	2.7 %	2.2 %
Germany (3-7yr)	-0.1 %	⬇	0.0 %	0.7 %	0.1 %
Japan (3-7yr)	-0.1 %	➡	0.0 %	-0.1 %	-0.2 %

Equities*

Equities*	Last	1wk		3mth	YTD	12mth
MSCI AC World	628	1.2 %	⬆	9.0 %	13.5 %	18.9 %
Eurostoxx 50	3 517	0.2 %	⬆	6.7 %	-3.6 %	0.0 %
DAX	13 253	-0.3 %	⬇	1.5 %	0.0 %	2.0 %
CAC 40	5 574	0.2 %	⬆	11.6 %	-4.7 %	-0.5 %
S&P 500	3 667	1.1 %	⬆	6.6 %	15.5 %	20.8 %
FTSE 100	6 490	2.0 %	⬆	11.5 %	-11.3 %	-6.4 %
SMI	10 343	-1.5 %	⬇	1.4 %	0.8 %	4.6 %
Topix	1 775	-0.2 %	⬇	9.8 %	5.5 %	6.6 %
IBOV Brazil	112 292	1.9 %	⬆	11.5 %	-2.9 %	3.1 %
MICEX Russia *	3 163	0.8 %	⬆	7.9 %	3.8 %	9.7 %
MSCI EM	1 239	0.8 %	⬆	12.1 %	13.7 %	22.5 %
SENSEX 30 India	44 633	0.8 %	⬆	14.7 %	9.5 %	11.0 %
Hang Seng (H-K)	26 729	-0.3 %	⬇	7.3 %	-2.1 %	4.5 %
Shanghaï Composite	3 442	2.1 %	⬆	1.7 %	12.9 %	19.3 %

Commodities

Commodities	Last	1wk		3mth	YTD	12mth
Brent	$48.8	2.2 %	⬆	10.7 %	-26.4 %	-20.2 %
Gold	$1 827	1.0 %	⬆	-5.6 %	20.2 %	23.6 %
Copper	$7 669	3.8 %	⬆	16.6 %	24.7 %	32.5 %

Source: DataStream, on 3 December 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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