

THE BIG PICTURE OF GLOBAL ECONOMICS

GLOBAL CIO WEEKLY BY GARY DUGAN



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Staying With a Positive Tone

- **Global markets lurch from nervous to ecstatic. We expect the more to positive tone to persist**
- **We see equities benefiting as a mix of good global growth, peaking inflation and somewhat modest monetary tightening keeps the risk-on sentiment intact**
- **This week's Fed meeting, could see the Fed announce a tapering of its bond purchases and indicate interest rates increases from the mid-2022**
- **China seems to be in a better place. Economic data, while not too encouraging, suggests the economy may be past its worst**
- **We continue to like Vietnamese equities for a re-opening of the economy**

You might also like our [Its No Longer Transitory](#) and [The Omicron Edition](#). Click [here](#) to read them for free.

Markets are in the midst of a strange phase. At times, investor nervousness has been palpable as the news flow on the Omicron variant has led to downside risks and talks of a significant unwind of what many see as bubble-like conditions in part of the markets. Yet, on other occasions, the market rebounds have been sharp and seemingly pulled in more retail money. As these conditions prevail, it makes sense to cut through the emotional rollercoaster and look at the current global economic momentum.

1. Despite some occasional wobbles, global growth appears to be re-accelerating. Economic data has come in broadly ahead of expectations over the past six months.
2. Central bankers will continue to tighten monetary policy. Still, they remain hesitant on pushing on too quickly on fears of the impact of the new variant on growth.
3. We see inflation fears peaking in the near term. The recent drop in energy prices will likely take some steam out of headline inflation. However, we believe inflation will hang around at uncomfortably high levels in 2022.
4. China appears to be finally stabilising with policymakers providing support in easing monetary conditions and a possible increase in government spending.

Good growth, potentially peaking inflation and modest monetary tightening will support further near-term gains for risk assets. Equities may remain the asset class of choice as we turn the year.

Although last week's US inflation report showed headline inflation hitting a 30-year high, the markets saw it as a positive that it came in broadly in line with expectations. US bonds sold off on the week, and US equities rallied. The number of S&P 500 constituents that ended the week above their 10-day moving average has increased to 89% from 5% in just five trading sessions. The US 10-year bond yield rose 14bps to the 1.50% mark, the middle of the three-month trading range of yields. Government bond yields in Europe and Asia remain near their recent lows. Credit performed well, with a rally in US high yield.

Central banks worldwide are gradually picking up pace on the path to monetary tightening. Last week the tone of the Bank of Canada and the Reserve Bank of Australia turned more hawkish. Economists expect Canada's central bank to raise rates in the first half of 2022. The Australian central bank will likely cut back its quantitative easing and raise rates in late 2022.

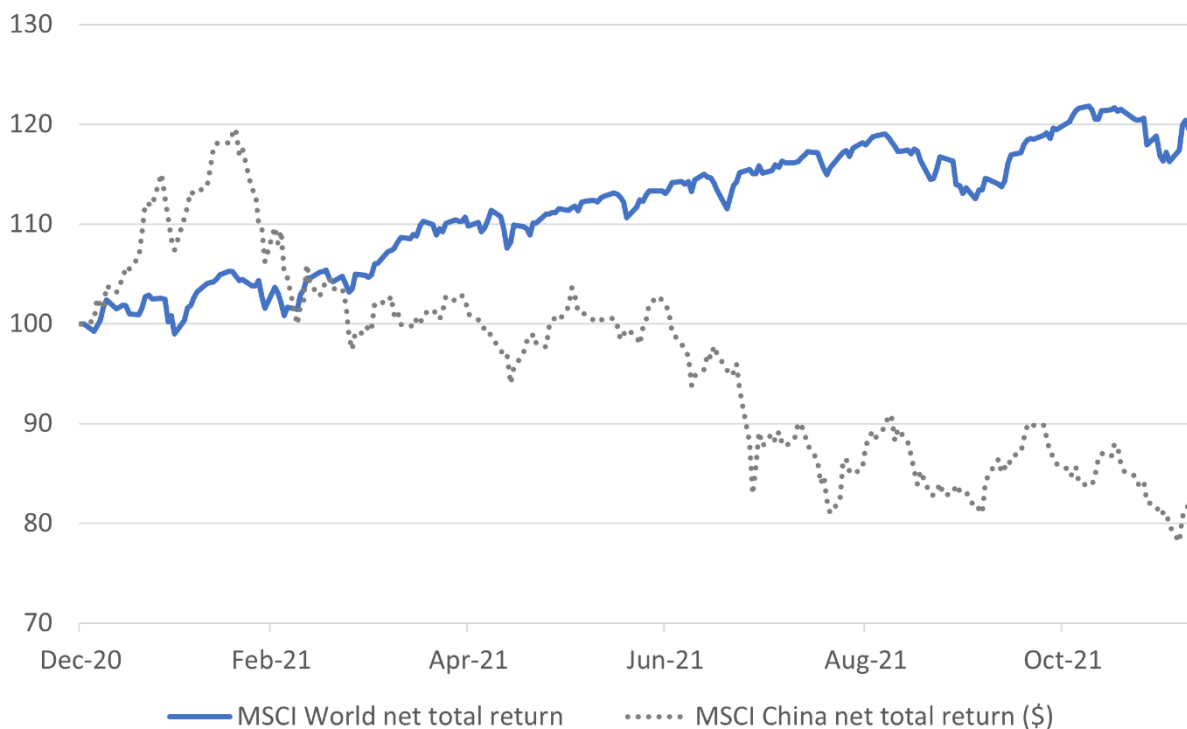
This week the market's focus will be on 22 central bank meetings with the key ones in the US, Eurozone and Japan. The Fed meeting should be rich in content. The market expects the Fed to accelerate its tapering of quantitative easing and to indicate that it could be increasing interest rates from the middle of 2022. Such a shift would bring the US central bank's perspective in line with what the market has come to expect of late. The pace and scale of interest rate increases the Fed envisages in the coming years will be of interest to Economists and markets alike. We still sense the Fed's views will in part be coloured by the ongoing challenges of the new variant. Another factor that may hold them back from signaling a greater pace of tightening is that they've only just moved from the 'transitory' narrative when framing the inflation risk.

Any rate increase from the ECB seems at least a year away. However, they may announce a trimming of future asset purchases this week. We expect both the ECB and the Bank of Japan to signal that policy will remain accommodative in the near term due to concerns about the impact of Omicron on their respective economies.

We get a sense that international investors are keen to move back into Chinese equities at the margin. There are positives. Economic data was profoundly poor at the start of the year, but it gradually turned better through the middle of the year. While the latest data points do not suggest a renewal of good growth, they signal that the economy may be beyond its worst point. The Citigroup economic surprise index that measures the degree to which economic data comes in above or below consensus, hit -80 in October and has subsequently recovered to +19. There is also a sense that policymakers are seeking to more proactively stabilise the economy after it was rocked by the implications of government policies aimed at 'shared prosperity' and the collapse of real estate developer Evergrande. Last week's 50bps reduction in the banking sector's reserve requirements came as a positive surprise. Also, there is a sense that the government is seeking more proactively a path for the orderly unwinding of the problems Evergrande has created.

Chart 1: Chinese equities marked underperformance

Rebased to Dec 2020=100



Source: Bloomberg

We note that Vietnam equities, one of our preferred markets for the past 12 months, continue to perform well. The market is up over 30% since the start of the year.

Encouragingly, after a long period of lockdowns, the government announced that it would allow flights from nine select cities including Beijing, Tokyo, Singapore, Bangkok, and Los

Angeles, from December 15th. We see Vietnam as one of the key beneficiaries of the Regional Comprehensive Economic Partnership agreement that comes into force on January 1st. The deal is one of the largest free trade deals ever implemented, accounting for approximately 30% of the world's population and 30% of the global gross domestic product. Analysts expected the countries to remove tariffs on more than 90% of goods traded in the region. The agreement is between China, South Korea, Japan, Australia, New Zealand and the 10 Association of Southeast Asian Nations members – Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam.

Chart 2: Vietnamese equities marked outperformance

Rebased to Dec 2020=100



Source: Bloomberg

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