

Weekly Flash

Inflation not a concern

MARKET PERFORMANCES (as of February 26, 2021 – 14:55 CET)

	CURRENT	CHANGE 1 WEEK	CHANGE YTD		CURRENT	CHANGE 1 WEEK	CHANGE YTD
S&P 500 Index	3'829.34	-2.16%	1.95%	Gold	1'762.34	-1.20%	-7.13%
S&P/Toronto Stock	18'223.54	-0.87%	4.53%	Silver	26.82	-1.62%	1.67%
EuroStoxx 50	3'651.28	-1.67%	2.78%	Oil WTI	62.33	5.22%	28.46%
SMI Index	10'615.81	-0.83%	-0.82%	EUR/USD	1.2117	0.01%	-0.78%
DAX Index	13'812.91	-1.29%	0.69%	EUR/CHF	1.0984	-1.19%	-1.64%
Nikkei Index	28'966.01	-4.20%	5.55%	USD/CHF	0.9065	-1.20%	2.43%
Emerging Market Index	77'156.47	-3.10%	7.62%	USD/JPY	106.32	-0.88%	2.98%
Yield 10Y US Treasuries	1.465	0.1278	0.5510	CAD/USD	0.7911	0.16%	-0.75%
Yield 10Y German Bund	-0.263	0.0457	0.3121	USD/CNY	6.464	-0.13%	-0.96%

[Source: Bloomberg]

Summary

- According to FED officials, rising inflation numbers are only a temporary risk, as the U.S. economy is still far away from full recovery.
- After an initial increase in the second quarter due to base effects, inflation pressure will likely abate during 2021.

FED continues buying bonds

During Tuesday's speech to the Senate Banking Committee, Jerome Powell signalled that the central bank would keep short-term interest rates pinned near zero and continue to purchase bonds "until substantial further progress" had been made towards the main goals of maximum employment and 2% inflation. The FED is currently purchasing \$120bln of assets per month, split into \$80bln of Treasuries and \$40bln of mortgage-backed debt. He played down concerns of rising inflation as a result of another big stimulus package or an unleashing of pent-up demand once the virus threat eases as a growing number of the U.S. population is vaccinated. Asked about the prospects for the economy, Powell responded that the U.S. started into 2021 on a strong note and that GDP growth could be as high as 6% after a contraction of 2.5% in 2020. In our view, inflation will likely pick up during the coming months due to base effects, as current price levels are compared to depressed readings a year ago. However, this effect will only be temporary and inflation likely moderate thereafter. Industrial capacity utilization is currently way below normal levels and there is plenty of slack in the labor market. We may not see price pressure, either from the demand side or from the supply side. Thus, the FED will likely keep its accommodative monetary policy stance at least until 2023.

President Lagarde stressed in a speech this week that the European Central Bank (ECB) will closely monitor the trend of longer-term bond yields. In our view this is a first sign, that the ECB may be uncomfortable with rising interest rates. Given the Governing Council's determination to keep financing conditions favourable, the EBC may very well step up government bond purchases in the coming weeks. Eurozone core inflation rebounded from 0.2% in December to 1.4% currently, partly

driven by the end of the VAT rate cut in Germany. During the coming months, Eurozone inflation will likely rise further, driven by base effects. In our view, this increase is not sustainable, as it will take several years before capacity utilization and slack in the labor market will have fully recovered. We expect underlying price pressures to remain subdued in the medium term, further supporting the ECB's dovish monetary policy regime.

EU speeds up vaccine deployment

Thanks to new supply pacts and increased production, the European Union (EU) is finally catching up in securing vaccine supplies and seems to be on track to immunize its population faster than expected. According to European Commission President Ursula von der Leyen, 300 million vaccine doses will be delivered in the second quarter after an estimated 18 million in January, 33 million in February and 55 million in March. On its vaccination path, the EU is currently way behind countries, such as the U.S., the U.K. and Israel. Large drug makers are now expanding their manufacturing capacities. Sanofi is converting German and French facilities to produce the products of Pfizer and Johnson & Johnson. Novartis also agreed to produce the Pfizer vaccine. According to London-based research firm Airfinity, the EU may be able to vaccinate 75% of its adult population by the end of August based on a positive roll-out scenario. If EU countries succeed in solving their logistical issues, they may finally narrow the gap to other countries in their effort to slow the propagation of the virus. Moderna reported plans to develop new vaccines in order to combat new variants of the virus, such as the strain now prevalent in South Africa. These vaccines could be used as an additional shot or in combination with existing vaccines. Vaccines based on mRNA technology are expected to be more versatile regarding their adaptability to mutations of the virus.

Conclusion

Due to base effects, inflation will temporarily rise during the next few months. Current low industrial capacity utilization and slack in the labor market speak against the sustainability of price pressures. Central banks will most likely look through short-term price increases and keep rates at record lows.

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