Weekly Flash

Getting closer to tapering

MARKET PERFORMANCES (as of August 20, 2021 – 15:15 CET)

	CURRENT	CHANGE 1 WEEK	CHANGE YTD		CURRENT	CHANGE 1 WEEK	CHANGE YTD
S&P 500 Index	4'405.80	-1.23%	17.30%	Gold	1'781.94	0.15%	-6.10%
S&P/Toronto Stock	20'215.36	-1.48%	15.96%	Silver	23.16	-2.37%	-12.22%
EuroStoxx 50	4'131.29	-2.33%	16.29%	Oil WTI	63.03	-7.90%	29.91%
SMI Index	12'381.29	-0.67%	15.68%	EUR/USD	1.1676	-0.98%	-4.39%
DAX Index	15'736.37	-1.51%	14.71%	EUR/CHF	1.0714	0.76%	0.83%
Nikkei Index	27'013.25	-3.45%	-1.57%	USD/CHF	0.9176	-0.31%	3.61%
Emerging Market Index	69'824.13	-3.26%	-2.61%	USD/JPY	109.82	-0.26%	6.07%
Yield 10Y US Treasuries	1.243	-0.0334	0.3293	CAD/USD	0.7759	2.95%	1.20%
Yield 10Y German Bund	-0.490	-0.0201	0.0854	USD/CNY	6.5006	-0.37%	-0.39%

[Source: Bloomberg]

Summary

- Several indicators point to a likely normalization of the currently strong economic expansion in the U.S. over the coming months.
- FOMC members seem to view the economic environment as strong enough to justify an earlier-than-expected reduction of asset purchases.

U.S. retail sales decline

Retail sales decreased by 1.1% in July and core retail sales fell by 1.0% compared to the previous month. This was more than expected and largely reflects high consumer prices, rising virus cases due to the delta variant, and a reversion to more normal spending habits. The composition of retail sales reflected a broad-based pullback, with a sharp drop in auto sales and non-store retailers. The details of the spending report indicate a higher pace of consumption in the second quarter and a likely drop back towards the pre-pandemic trend during the second half of the year. Roughly two-thirds of overall consumer spending in GDP comprises services categories not covered in the retail sales report, including housing, and health care. The University of Michigan's preliminary sentiment index fell to the lowest level since 2011 in August and confirms our view that U.S. growth likely peaked during the second quarter of 2021.

Earnings reports continue to be strong

With more than 90% of larger companies in the U.S. and the Euro area having reported, it is fair to say that the earnings season for the second quarter was again a very strong one. In the U.S., 85% of S&P 500 members reported earnings above expectations and the average earnings surprise was 17%. In the Eurozone, 67% of reported earnings came in above expectations with an average earnings surprise of 33%. Earnings reports were particularly strong in the Health Care, Technology, Consumer Discretionary, and Financials sectors. Strong earnings reports usually lead to rising future consensus earnings estimates. As earnings are the single most important driver of stock returns, this development should be incrementally supportive for the overall stock market.

FOMC minutes slightly more dovish

The minutes to the July meeting of the Federal Open Market Committee (FOMC) raise odds of a taper announcement in November. The majority of participants judged that enough progress had been made toward their inflation goal, while gains had been made toward their inflation objective. Thus, it could be appropriate to start reducing the pace of asset purchases this year if the economy evolves in line with expectations. A potentially earlier-than-expected start to tapering could be accompanied by a slower pace of tapering. However, several participants indicated that an earlier start to tapering should largely depend on the economic impact of the new virus strains. While the recent surge in consumer prices has grabbed policy makers' attention, several participants were still worried that inflation could slump back into the pre-pandemic trend of running below the 2% target. Officials saw progress on the labor front, but uncertainty related to the near- and medium-term labor market slack remained, given the job destruction tied to the pandemic.

Conclusion

Declining retail sales from elevated levels and a weaker consumer sentiment point to a likely deceleration of U.S. growth over the coming months. We still believe that tapering will be announced in the fourth quarter of the current year and be implemented during the first quarter of 2022. As the reduction of asset purchases to zero requires some time, a hike of the policy rate before 2023 is highly unlikely in our view.