Vontobel

Weekly Flash

Global monetary tightening, easing in China

MARKET PERFORMANCES (as of December 10, 2021 – 15:20 CET)

	CURRENT	CHANGE 1 WEEK	CHANGE YTD		CURRENT	CHANGE 1 WEEK	CHANGE YTD
S&P 500 Index	4'667.45	1.97%	24.26%	**Gold**	1'783.59	0.05%	-6.01%
S&P/Toronto Stock	20'925.49	1.42%	20.03%	**Silver**	22.15	-1.47%	-16.04%
EuroStoxx 50	4'213.62	3.27%	18.61%	**Oil WTI**	71.80	8.36%	47.98%
SMI Index	12'615.17	3.61%	17.86%	**EUR/USD**	1.1282	-0.23%	-7.62%
DAX Index	15'667.33	3.28%	14.20%	**EUR/CHF**	1.0414	-0.39%	3.74%
Nikkei Index	28'437.77	1.46%	3.62%	**USD/CHF**	0.9231	-0.76%	4.18%
Emerging Market Index	71'016.49	1.71%	-0.94%	**USD/JPY**	113.47	-0.66%	9.09%
Yield 10Y US Treasuries	1.473	0.1288	0.5587	**CAD/USD**	0.7874	-1.23%	-0.28%
Yield 10Y German Bund	-0.357	0.0362	0.2178	**USD/CNY**	6.3689	0.11%	-2.47%

[Source: Bloomberg]

Summary

- China switches to a more accommodative monetary policy stance to support the property sector and stimulate economic activity.
- Eurozone growth was strong in the third quarter, but headwinds from rising infections and mobility restrictions in several countries start to build.
- Early data suggest that the Omicron strain is much more transmissible but less harmful compared to previous Covid variants.

China shifts to policy easing

The December Chinese Politburo meeting put emphasis on supporting the housing market and stabilizing growth in light of the material property market slowdown and GDP growth significantly below trend. Supporting this easing stance, the People's Bank of China (PBoC) cut its reserve requirement ratio (RRR) by 0.5% to strengthen the real economy and in particular small and medium enterprises. Without monetary policy easing, extremely weak housing activity threatens to persist through next year and potentially thereafter, further slowing growth expectations for the Chinese economy. On the other hand, policymakers don't want to over-stimulate the economy for not provoking further excesses, which ultimately led to the default of Evergrande Group, China's largest and the world's most indebted property developer. Thus, policymakers seem to be willing to do just enough to manage the balance between supporting growth and forcing structural reforms. As expected, China has now shifted to easing, while the rest of the world switched to a tightening mode. This should stabilize the economy over the coming months. However, the risk of a more significant property market contraction needs to be carefully monitored.

Eurozone rebound continues

According to official data, Eurozone third quarter real GDP rose by 2.2% from the previous three months. With an increase of 4.1% quarter-on-quarter, private consumption was the biggest contributor to Euro area growth, as the region reopened following broad lockdowns. The recent surge in Covid infections is now threatening to impact the recovery on renewed mobility restrictions. German industrial production increased by 2.8% in October, which was well above expectations and mainly driven by capital goods. The gap between factory orders and production – resulting from supply-chain disruptions – narrowed on the back of a decline in foreign machinery and equipment demand. Strong orders point to a continuation of industrial production growth well into 2022, with the resurgence of Covid representing a near-term headwind.

All eyes on Omicron

As of today, the world does not know much about the new Covid variant, simply because there is still lack of a broad and reliable statistical database. Early medical data from small groups of infected people suggest that the rate of spread is much higher for Omicron than for Delta. This either points to higher transmissibility or significant erosion of immunity acquired from prior infection or vaccination. So far, the severity of Omicron looks more benign compared to delta. Most experts currently anticipate significant vaccine protection against severe progression and hospitalization, especially after booster shots. Rising Omicron cases could push the recovery of virus-hit service sectors further into next year. However, we currently do not expect the strong global economic recovery to be challenged.

Conclusion

Chinese November broad credit growth slowed by more than expected from October. Loan growth slowed despite the PBoC's guidance on normalizing credit support to the property sector. The recent RRR cut should lower funding costs for banks and provide support for the economy. Rising Covid cases in many countries certainly represent a headwind for economic growth. This could make central banks rethink their current stance towards tightening.