

Can Draghi's Europe Catch up With Biden's America?

WATCH LIST

Date		Period	Consensus	Previous
U.S.				
Tue 2/23	FHFA House Price Index	Dec		1% M/M
Tue 2/23	Conference Board Consumer Confidence	Feb	90.0	▲ 89.3
Wed 2/24	New Home Sales	Jan	860K	▲ 842K
Thu 2/25	GDP, annualized (Second Estimate)	4Q20	4.3% Q/Q	▲ 4.0% Q/Q
Thu 2/25	Pending Home Sales	Jan		-0.3% M/M
Fri 2/26	Personal Income	Jan	9.7% M/M	▲ 0.6% M/M
Fri 2/26	Personal Spending	Jan	0.5% M/M	▲ -0.2% M/M
Fri 2/26	Core PCE Deflator	Jan	0.1% M/M	▼ 0.3% M/M
Europe				
Tue 2/23	U.K. Unemployment Rate	Dec	5.2%	▲ 5.0%
Tue 2/23	EZ Consumer Price Index (Final Estimate)	Jan		-0.3% Y/Y
Wed 2/24	Germany GDP (Final Estimate)	4Q20	0.1% Q/Q	- 0.1% Q/Q
Fri 2/26	France GDP (Final Estimate)	4Q20		-1.3% Q/Q
Asia Pacific				
Mon 2/22	PBOC Meeting	Feb	--	--
Mon 2/22	South Korea Exports 20 Days	Feb		10.6% Y/Y
Tue 2/23	Japan Markets Closed for Emperor's Birthday		--	--
Fri 2/26	Japan Industrial Production (Preliminary Estimate)	Jan	3.9% M/M	▲ -1.0% M/M
Fri 2/26	Japan Retail Sales	Jan	-1.4% M/M	▼ -0.8% M/M

Arrows indicate consensus forecast compared to the previous period. Local dates of release.

U.S.

- **Personal income, savings, and spending for January are set to jump** alongside stimulus disbursements. January retail sales figures show consumers are spending their extra cash, but the savings rate will show how much is being stashed away—particularly among the higher-income cohort.
- We watch to see how higher input prices and limited supply impact **house prices and sales**.

Europe

- We will be looking at **the final estimate of EZ CPI for January**. If there is an upward revision, this could spark fears of an inflation reemergence. Base effects and supply constraint in commodities are likely to cause inflation to accelerate further in the next month. While this warrants close monitoring, our baseline, which calls for inflation to remain well below the ECB's target of 2% this year and next, remains unchanged.

Asia Pacific

- **The PBOC is expected to remain on its current path** of a targeted easing of stimulus. While greater restrictions during the Lunar New Year are weighing on activity data, this is seen as temporary.
- Eyes are on **Japan retail sales** for January. Though Japan's domestic demand ended 2020 stronger than expected, renewed restrictions are likely to be a weight in Q1.

Institute's Central Scenario

An impressive rise in U.S. retail sales this week showed that fiscal stimulus is working and keeping shoppers in the driver's seat. U.S. housing market demand remains strong, but concerns surrounding affordability could weigh on the pace of growth, in line with our baseline outlook. In Europe, comparably smaller fiscal support and tighter restrictions have weighed on consumer spending but investment and export growth point to a stronger second half of the year. Japan GDP ended 2020 with a positive beat, aided by robust external demand, better-than-expected internal demand, and private investment. While renewed lockdowns should weigh on Q1 growth, this provides upside to our baseline outlook for Japan. Please see our [Monthly Macro Dashboard](#).

IN REVIEW
Stimulus Boosts U.S. Retail Sales

After a three-month decline, U.S. retail sales surprised greatly to the upside in January, showing that fiscal stimulus works. Retail sales rose 5.3% M/M, bringing them 7.8% above pre-crisis levels. All 13 major categories rose over the month, but most encouraging was the improvement in discretionary categories.



Source: Bloomberg. As of February 18, 2021.

The increase was driven by stimulus checks and enhanced unemployment benefits, as well as improving COVID trends. While the boost from checks will likely prove temporary, another round is increasingly likely to pass.

The promising news may raise concerns about the need for more fiscal support, but Democrats seem determined to pass a large amount of stimulus through the budget reconciliation process. The decision to use this route, rather than a bipartisan bill, means that the total dollar amount of spending passed should be closer to Biden's proposed \$1.9 trillion, with current estimates hovering around \$1.5 trillion. Our baseline scenario calls for additional support this year, which will keep consumers in the driver's seat of the strong 2021 U.S. rebound.

Vaccines, Reform & Taxes Lead Draghi Era 2.0

Mario Draghi is Italy's new prime minister, having obtained the support of all parties in Parliament except one, a first in the country. Judging from the hints he gave, Draghi's first actions will focus on the vaccination program, a thorough tax reform, and restarting public investment in education, logistics and decarbonization. Using the huge resources made available by the European Recovery Fund (€209 billion, 11% of Italy's GDP) to reform and restart productive investment would have certain impact on Italy's productivity and growth.

It will not be smooth sailing, and party support can shift rapidly once the emergency passes, as former PM Mario Monti learned after he was ousted in 2012. There are two major differences to be more optimistic this time, though. First, Monti had to implement a harsh austerity program, while Draghi has the happier task of spending €209 billion of EU money. Second, with such a wide majority, no party is indispensable for Draghi. He has the numbers to govern even if one of the unpredictable parties, Lega or the Five Star Movement, defects and the other supports him. There's a balance to strike, but it's not impossible.

Italy's economic future and the effectiveness of the single currency area depend on his success, and bond markets are betting on it—the first auction of 10-year Italian sovereign bonds received subscriptions 11 times the offered amount.

Rising Prices Could be Weighing on U.S. Housing

U.S. homebuilder confidence remains strong despite a recent surge in input prices that threatens to weigh on the outlook. The NAHB housing market index rose from 83 to 84 in February, including an increase of prospective buyers, suggesting demand remains robust due to low-mortgage rates, millennial market entry, and a move to single-family. Housing permits—a leading indicator of construction—rose at its highest pace since 2006.

However, low inventories and a notable rise in input prices (such as a 48% M/M rise in lumber prices) are reducing affordability and may be weighing on the pace of starts. While housing starts remain elevated historically, they eased more than expected in January, falling 6% at an annualized rate, with single-family down 12.2%. Within the details of the NAHB housing market index, even as traffic of prospective buyers improved, the measure of builder expectations for the next six months fell. Our baseline scenario does not call for this to derail the recovery in housing—particularly as demand remains strong—but it could ease the pace of growth this year.

Encouraging Rebound for Japan GDP

Fourth-quarter GDP showed Japan's economy bettered end-of-year expectations. Despite slowing from the strong Q3 pace, Japan's GDP rose 12.7% Q/Q annualized in 4Q20, compared with consensus expectations for a 10.7% gain. Exports were a growth driver due to strong external demand. While this was largely expected, the positive surprise was in firmer-than-expected domestic demand. Renewed lockdowns and slow vaccine rollout will likely lead to a double-dip in 1Q21, but Japan's economy is starting from a higher level and could be better positioned when restrictions lift.

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KEY FINANCIAL INDICATORS

Rates	Yield	1 W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
Fed Funds	0.25%	0 bps	0 bps	0 bps	0 bps	-150 bps	0 bps
U.S. SOFR	0.06%	0 bps	-2 bps	-3 bps	-4 bps	-152 bps	-1 bps
3 Month USD Libor	0.18%	-2 bps	-4 bps	-5 bps	-9 bps	-151 bps	-6 bps
3 Month Euribor	-0.55%	0 bps	1 bps	-2 bps	-7 bps	-13 bps	0 bps
3 Month U.S. T-Bill	0.05%	0 bps	-4 bps	-4 bps	-5 bps	-153 bps	-3 bps
2-Year U.S. Treasury	0.10%	1 bps	-2 bps	-6 bps	-4 bps	-131 bps	-1 bps
10-Year U.S. Treasury	1.30%	17 bps	21 bps	43 bps	62 bps	-28 bps	38 bps
10-Year German Bund	-0.37%	8 bps	18 bps	19 bps	8 bps	4 bps	21 bps
10-Year U.K. Gilt	0.58%	11 bps	29 bps	25 bps	36 bps	-6 bps	38 bps
10-Year JGB	0.09%	2 bps	7 bps	7 bps	6 bps	12 bps	7 bps
Fixed Income	Yield	OAS	1W Return	1M Return	3M Return	12M Return	YTD Return
Barclays Capital U.S. Government-Treasury	0.75%	N/A	-0.8%	-1.0%	-2.0%	3.5%	-2.1%
Barclays Capital U.S. TIPS	0.90%	N/A	-0.8%	-0.1%	1.6%	8.5%	-0.4%
Barclays Capital U.S. Aggregate	1.30%	34	-0.6%	-0.7%	-0.9%	4.0%	-1.5%
Barclays Capital Global Aggregate	0.98%	33	-0.9%	-1.1%	-0.1%	6.6%	-1.9%
Barclays Capital U.S. ABS	0.41%	28	0.0%	0.1%	0.4%	3.6%	0.1%
Barclays Capital U.S. MBS	1.44%	20	-0.3%	-0.3%	0.0%	2.7%	-0.3%
Barclays Capital U.S. Corporate Investment Grade	1.93%	89	-0.8%	-0.9%	-0.5%	5.0%	-2.0%
BAML Euro Corporate Investment Grade	0.28%	87	-0.3%	-0.4%	0.0%	1.1%	-0.3%
Barclays Capital U.S. Corporate High Yield	3.96%	319	0.0%	1.0%	4.2%	7.3%	1.3%
BAML European Currency High Yield Non-Financial	2.76%	326	0.1%	0.9%	3.2%	3.5%	1.4%
CS U.S. Leveraged Loans	4.73%	447	0.1%	0.4%	3.6%	3.9%	1.8%
CS Western European Leveraged Loans Non-USD	4.26%	419	0.3%	0.7%	2.8%	3.7%	1.5%
JPM CEMBI Broad Diversified	4.15%	307	-0.1%	0.6%	2.5%	5.2%	0.3%
JPM EMBI Global Diversified	4.85%	348	-1.1%	-0.4%	0.4%	1.0%	-1.9%
JPM GBI-EM Global Diversified	4.44%	N/A	-1.0%	-0.4%	2.1%	2.5%	-1.3%
Equities	Price	Div Yield	1W Return	1M Return	3M Return	12M Return	YTD Return
S&P 500	3,931.33	1.43%	0.6%	4.5%	9.4%	18.4%	4.9%
Euro STOXX 600 (Local)	416.10	2.05%	1.6%	2.0%	7.0%	-3.7%	4.3%
U.K. FTSE 100 (Local)	6,710.90	3.43%	2.9%	-0.4%	5.4%	-9.7%	3.9%
Japan Nikkei 225 (Local)	30,292.19	1.37%	2.5%	6.2%	16.4%	28.8%	10.4%
China Shanghai Composite (Local)	3,655.09	1.93%	0.0%	2.5%	9.4%	22.5%	5.2%
MSCI AC World (Local)	682.70	1.73%	0.9%	4.3%	11.8%	18.0%	6.2%
MSCI Emerging Markets (Local)	1,444.93	1.73%	1.6%	6.6%	19.3%	34.6%	12.5%
Commodities/Currencies	Price	1W Change	1M Change	3M Change	6M Change	12M Change	YTD Change
S&P GS Commodity Index	473.15	3.0%	9.6%	27.9%	32.5%	19.4%	15.6%
WTI Crude (\$/bbl)	61.14	4.7%	17.0%	48.3%	42.6%	17.5%	26.5%
Copper (\$/lb)	3.84	1.3%	6.5%	20.0%	32.4%	47.2%	9.2%
Gold (\$/oz)	1,780.70	-3.4%	-3.2%	-5.7%	-9.7%	12.6%	-5.7%
U.S. Dollar Index	90.95	0.6%	0.2%	-1.6%	-2.0%	-8.2%	1.1%
Euro (USD/EUR)	1.20	-0.8%	-0.5%	1.3%	1.4%	11.1%	-1.7%
British Pound (USD/GBP)	1.39	0.1%	2.0%	4.5%	5.8%	6.5%	1.4%
Japanese Yen (Yen/USD)	105.93	1.2%	2.0%	1.6%	-0.1%	-3.7%	2.6%
Chinese Yuan (CNY/USD)	6.44	0.0%	-0.6%	-1.8%	-7.3%	-7.8%	-1.6%

Source: FactSet and Bloomberg. As of February 17, 2021.

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