18 September 2019

# Macro Insight

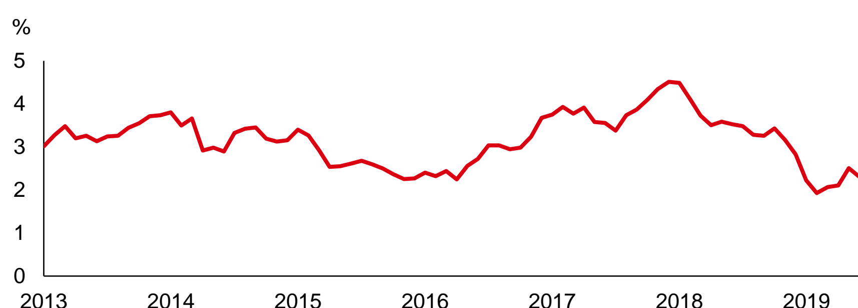
# The value of Nowcast analysis

## Since January 2018, our global Nowcast has steadily declined

Our global Nowcast, a "big data" measure of economic activity, has steadily declined since the beginning of 2018, from a peak of 4.6% annualised growth in January 2018 to 2.2% in July 2019 (Figure 1).

Recent weakness in economic data - combined with volatile stock markets and a temporary inversion of the yield curve - has raised concerns among investors about the risk of a US or global recession. Indeed, the current global growth rate is at about the same level as during 2016 when recession fears last flared up.

**Figure 1: Global Nowcast (annualised growth rates)**

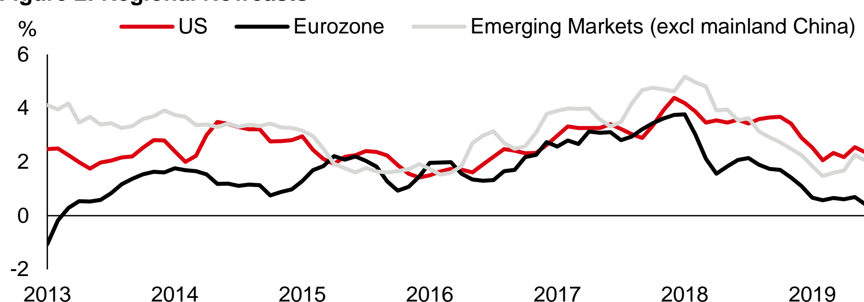



*Source: HSBC Global Asset Management, data as at 10 September 2019.*

## All major regions have trended lower, but the US has outperformed

This slowdown has been borne out by all major regions, albeit with variations. Figure 2 shows the history of the Nowcasts for the eurozone, the US and emerging markets (EM) excluding mainland China. The eurozone Nowcast has fallen the most, while the US has held up relatively well. The performance of EM economies has been somewhere in the middle.

**Figure 2: Regional Nowcasts**




*Source: HSBC Global Asset Management, data as at 10 September 2019.*

**Where does this weakness come from, and what explains the regional differences?**

To answer these questions, it helps to look at the underlying data that feed into our Nowcast model. Here, we focus on two particular groups; on the one hand economic indicators of the services and consumer sector, and on the other those that report on industrial activity and international trade (which almost always means trade in goods excluding services).

While there are many more indicators in our database outside these sectors, for this exercise we focus just on these two broadly defined groups. We take the averages of the data in each group. The resulting data are depicted in Figure 3.

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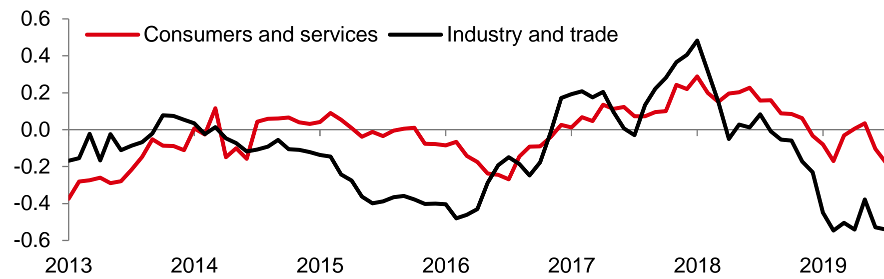
Industrial and trade sector activity has fallen sharply, to below the last trough in 2016

**Figure 3: Performance by sector (standard deviation from mean)**




*Source: HSBC Global Asset Management, data as at 10 September 2019.*

We note that industrial and trade sector activity has deteriorated precipitously from its peak at the end of 2017, to below the last trough seen in 2016. The consumer and services sector (which accounts for a larger share of the global economy) has followed a similar trajectory, but not to the same extent - activity remains slightly stronger than the 2016 cyclical low.

The industrial sector is softening for two reasons. Firstly, it is in a structural decline, as an ever larger share of global consumption is directed to services. Secondly, there are cyclical headwinds affecting the industrial sector, most notably global trade tensions and geopolitical uncertainty impacting supply chains and demand for investment goods (e.g. machinery and equipment).

Services and consumer sector activity is steadier

The services sector, on the other hand, is more stable by nature. It is less susceptible to the corporate investment cycle and global trade disputes. It is more geared towards the domestic economy and hence more sensitive to monetary policy and financial conditions, which have been supportive in many economies this year.

Overall, this may explain the performance gap between the US and the eurozone: the former is a relatively closed economy based on domestic consumption, while the latter has a large export sector and industrial base.

**Where do we go from here?**

Recession fears flared up in 2015/16. A slowdown in China reverberated through the global economy and corporate profits came under pressure stoking fears of a downturn. However, the recession did not materialise, and instead what followed was a two-year period of a synchronised global upswing, dubbed the “goldilocks” economy.

It is not clear if we will experience a similar outturn this time around. Compared to 2016, the global economy is at a more advanced stage of the business cycle; the unemployment rate is lower and inflation is higher than in early 2016, both suggesting less spare capacity. But lower government debt and bond yields suggest governments have capacity to ease fiscal conditions in case of a downturn.

**Where does this leave us with investments?**

We maintain our overweight equities position

Given the current weakness of the business cycle and the uncertainties about the economic outlook it may be tempting to reduce our allocation to risky assets. However, perceived “safe” assets - in particular government bonds - have rallied recently based on the expectation that central banks will ease monetary policy further to support the economy. This has widened the valuation gap between bonds and equities. Hence, equities are attractively priced relative to bonds.

Therefore, we maintain a pro-risk stance in our portfolios; overweight global equities and underweight government bonds[1]. But given the vulnerabilities around the industrial cycle that we discussed above, we advocate a cautious use of our risk budgets on a tactical basis.

**Marcus Sonntag, Macro & Investment Strategist**

[1] In emerging markets, we prefer local-currency government bonds over equities.

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