Economic Research

April 2021

Market Monitor – United States

Improvements in Labour Market and Consumer Sentiment Further Boost Growth Outlook

Improvements in the labour market and consumer sentiment fuel economic recovery optimism

US employee hiring recovered much faster than expected in February. 379,000 jobs were added to non-farm payrolls during the month, and job gains in January were significantly revised up to 166,000. The unemployment rate edged down further from 6.3% to 6.2%. Most of the job gains in February were in the leisure and hospitality sector, which was hit hardest by the pandemic. The leisure and hospitality sector saw an increase of 355,000 jobs amid a relaxation of dining restrictions in some areas.

The Senate and House of Representatives passed a USD 1.9 trillion relief bill days before the weekly boost to unemployment benefits was set to expire on 14th March. President Biden signed the bill into law on 11th March. The bill will provide a USD 300 per week boost to unemployment benefits through 6th September. This package will also include USD 1,400 checks for individuals making less than USD 75,000 annually. At the same time, Covid-19 vaccinations are also on track. According to Our World in Data, 25.1% of the US population have received at least one dose of vaccine as of 23rd March, up from the 14.9% as of 28th February. Against this backdrop, the consumer sentiment index rose to 84.9 during the month, up from 76.8 the previous month.

Going forward, the US economic outlook will continue to brighten, chiefly due to the new trillion-level stimulus package and vaccination progress. At its policy meeting on 16th to 17th March, the Federal Reserve (Fed) maintained the fed funds rate target at its current level and pledged to continue asset purchases at the current pace until substantial further progress has been made toward the central bank's maximum employment and price stability goals. It also issued an upbeat economic projection, expecting GDP growth in 2021 to accelerate to 6.5%, up from 4.2% as projected in December. Inflation for core personal consumption expenditure in 2021 is projected to be 2.2%, also up from 1.8% in the previous projection. Meanwhile, most Fed officials still expect to maintain interest rates at the current level through 2023.

- **Silver lining for jobs market in February, mainly due to job gains recorded in the leisure and hospitality sector.**
- **Consumer sentiment boosted by new stimulus bill and vaccination progress.**
- **Robust growth outlook pushes Treasury yields higher.**
- **Elevated yields may pose risk for stock and housing markets.**

However, the labour market recovery may be uneven. Tourism-related sectors like leisure & hospitality and aviation may take longer time to recover to pre-pandemic levels, as worldwide vaccination rates are still low. In February, the number of jobs in the leisure & hospitality sector was still about 3.5 million short of its level from a year ago, despite improvements seen during the month.

Treasury yields edge higher as market weighs higher inflation and greater supply of debt

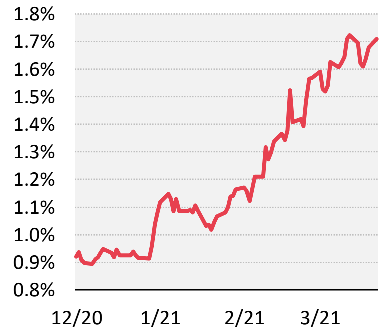
The passage of the USD 1.9 trillion stimulus bill fuelled market expectation that inflation will pick up faster later this year, resulting in lower demand for fixed-income assets. Meanwhile, market participants generally expect that the US government will need to issue more debt in future to finance the stimulus measures, further driving up bond yields. As of 29th March, the 10-year treasury yield closed at 1.71%, about 30 basis points higher than the level at the end of February.

The improved economic outlook and higher treasury yields also prompted speculation that the Fed may reverse its policy stance faster than previously expected, resulting in a stronger US dollar. Although the Fed pledged to maintain low interest rates at its latest meeting, the dot plot showed that four Federal Open Market Committee members were looking for a rate hike in 2022, compared with only one member in the December meeting. Moreover, huge unwinding of positions by Archegos Capital Management, a hedge fund, triggered concern that banks that dealt with the firm could face losses, prompting some risk aversion in the market. As of 29th March, the dollar index stood at 92.944, about 2.3% higher than the level at the end of February.

Benchmark stock indices see diverse performance amid higher yields

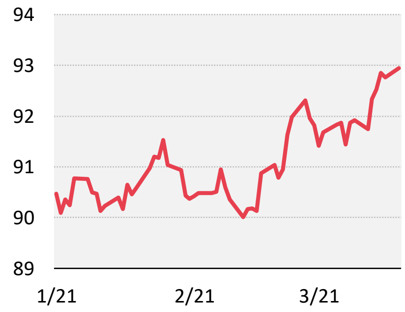
With brighter economic outlook, companies that are sensitive to the economic cycle led the stock market higher. General market expectation is that corporate profits will be boosted later this year by a rebound in consumer spending and stronger economic growth. As of 29th March, the S&P 500 Index registered a 4.2% gain from its level at the end of February, while the Dow Jones Index rose 7.2%. Nonetheless, higher Treasury yields have led to some caution about the expensive valuation of tech stocks. At the same time, investors have also favoured sectors poised to benefit most from the economy reopening. The Nasdaq saw a 1.0% decline over the same horizon.

US 10-year Treasury Yield



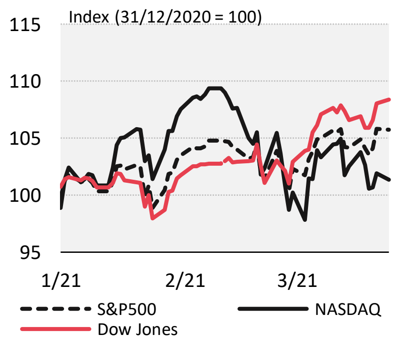
Source: Bloomberg, data as of 29/3/2021

Dollar index



Source: Bloomberg, data as of 29/3/2021

US Equity Indices



Source: Bloomberg, data as of 29/3/2021

Elevated yields may pose risk to asset prices

Looking ahead, treasury yields are projected to stay elevated as the economic outlook keeps improving. This may lead to greater volatility in the stock market, as companies with high valuations could face corrections due to the higher discount rate. In addition, company earnings may also be challenged by a potential corporate tax hike to cover the spending proposed by President Biden.

Mortgage rates may also rise with the 10-year treasury yield. For the week ending 25th March, the US 30-year fixed-rate mortgage rate rose to 3.17% from the historical low of 2.65% on 7th January. Together with the potential end of relief measures for homeowners, buyers may face increased financial pressure amid rising funding costs. This will pose a risk to skyrocketing housing prices, which rose 10.1% in 2020.

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