Ostrum ASSET MANAGEMENT

# MyStratWeekly
Market views and strategy

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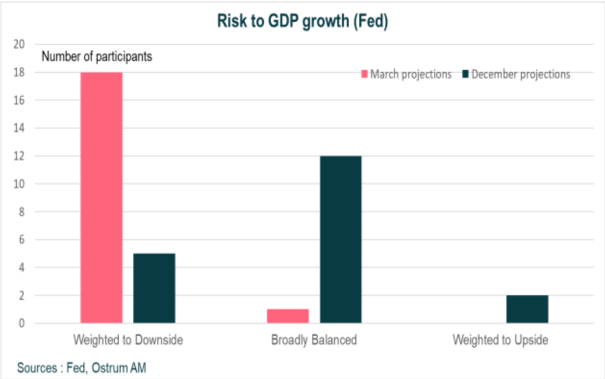
## Topic of the week: Is China on the verge of entering a new era of consumption?
**by Zouhoure Bousbih**

- China is finally tackling its high savings rate (42% of GDP), which is linked to an inadequate social protection system and income inequalities between rural and urban areas stemming from the "Hukou" system;
- The Chinese government has unveiled a 30-point plan aimed at stimulating domestic consumption, which is considered crucial for alleviating external pressures and facilitating the country's structural transition;
- The plan seeks to enhance household incomes and reduce financial burdens by improving social welfare and expanding the service sector to foster "new consumption";
- Reforms have notably accelerated in the realms of social protection and the dismantling of the "Hukou" system ;
- For the first time, artificial intelligence (AI) is positioned at the center of the consumption strategy, emphasizing emerging technologies such as autonomous driving and robotics that have the potential to transform consumer behavior.

## Market review: The Fed Confronts Uncertainty
**by Axel Botte**

- The Fed forecasts slower growth and higher inflation in 2025;
- The Fed keeps rates unchanged but reduces QT;
- Bond market volatility eases as Bund yields fall below 2.80%;
- Credit spreads and equity markets stabilize.

## Chart of the week




During the FOMC meeting on March 19, members clearly mentioned the significant uncertainty induced by the chaotic approach of the new U.S. administration regarding growth and inflation.

As a result, the downside risks to growth have increased considerably since the December FOMC meeting. The Fed has also significantly revised its GDP growth forecast down to 1.7%, compared to the previous estimate of 2.1% in December. Its inflation forecasts have also risen by 2 basis points to 2.7%.

The Fed clearly indicates that its next move will likely be a rate cut, possibly as early as June.

## Figure of the week

**350**

The central bank of Turkey implemented a cumulative increase of 350 basis points in its key interest rates to defend its currency following the arrest of the main opposition candidate for the 2028 presidential election.
Source: Bloomberg

## Topic of the week

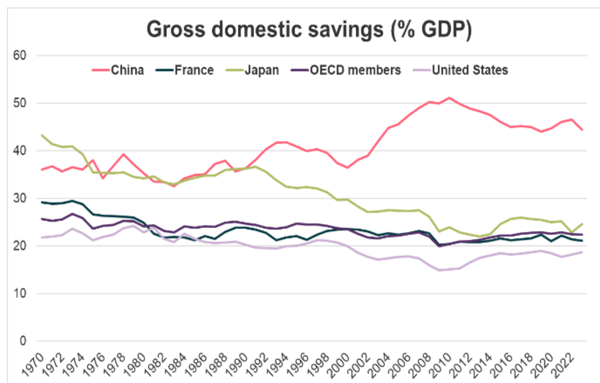
# Is China on the verge of entering a new era of consumption?

**One week after the National People's Congress meeting on March 5, which called for "broadening domestic demand on all fronts," the State Council released a 30-point plan to stimulate consumption. Consumption has become a priority for the government, with targets set for 2025. Chinese authorities are banking on domestic consumption to mitigate the effects of external pressures while facilitating the country's structural transition.**

## Consumption: The Main Constraint on Chinese Growth

### A Very High Savings Rate

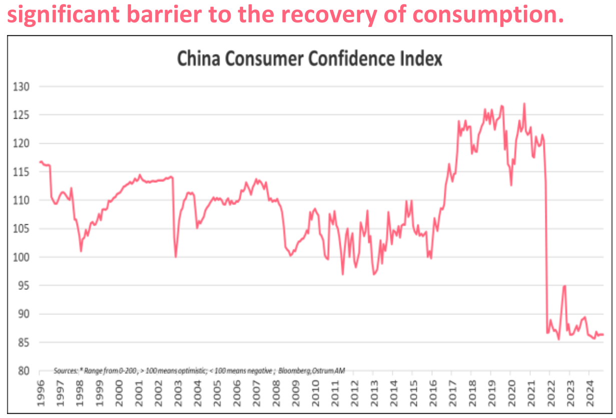
Consumption in China accounts for 40.7 % of GDP (2023), which is low compared to 72% in the United States and 50% to 70% in OECD member countries. This weakness is linked to two significant structural factors. First, the economic model is focused on investment in infrastructure and industry rather than on domestic consumption. Secondly, there is an inadequate social protection system. Concerns related to health, education, and retirement lead households to save more rather than spend.




Additionally, income inequalities between rural and urban areas create a consumption imbalance. The "Hukou" system, which registers households, restricts worker mobility and their access to social services in cities where they are not registered. Despite their income, migrant workers do not enjoy the same consumption capacity as permanent residents. As a result, China has a high savings rate of over 40% compared to industrialized countries.

*China is finally addressing its high savings rate, which represents 42% of its GDP?!*

### Consumer confidence also remains a significant barrier to the recovery of consumption.




The real estate crisis and the deterioration of the labor market following the crackdown on the private sector in 2021 have severely impacted Chinese consumer confidence, which has stabilized at historically low levels despite recent signs of stabilization in the real estate sector. Restoring consumer confidence is crucial for a sustainable recovery in consumption.

*Without confidence, there is no sustainable recovery of consumption.*

# A "Special" Action Plan for Sustainable Consumption Recovery

## Increasing Income, Social Welfare, and "New Consumption"

The "special" action plan includes 30 initiatives focused on demand by intensifying political efforts to promote household income growth and reduce financial burdens (through improved social welfare) for sustainable consumption growth. It can be summarized as follows:

*External pressures have accelerated structural reforms: removing 'Hukou' requirements and improvement of social protection.*

| Action Plan | Measures |
|---|---|
| Consumption Capacity | - Increase urban and rural household incomes.<br>- Call for "reasonable wage growth" and improvements to the minimum wage.<br>- Support for employment, skills training, and enhancement of unemployment insurance. |
| Wealth Effect | - Measures to support the stock market and increase bond market products for individual investors.<br>- Stabilization of the real estate market, which is important for household balance sheets. |
| Willingness to Consume (Purchasing Power) | - Improvement of guarantees in various areas (student aid, pensions, health insurance).<br>- Development of the service sector (childcare, elderly care, lifestyle services, health, tourism). |
| Consumption Environment | - Reform of the leave system to encourage consumption.<br>- Support for the creation of quality brands and "new consumption" strategies. |

*The focus is on social welfare to stimulate the consumption of services.*

For the first time, the government is integrating the wealth effect associated with real estate and stock markets into its consumption support strategy.

The plan also emphasizes social welfare, particularly by removing "Hukou" requirements to provide a basic pension and health insurance for temporary workers, often employed on digital platforms. This marks a first step towards reforming the "Hukou" system, which has long hindered consumption by exacerbating income inequalities between rural and urban areas.

Furthermore, service development is also a priority. The strict enforcement of paid leave, the prohibition of illegal extensions of working hours, and the introduction of spring and autumn holidays in primary and secondary schools are initiatives aimed at stimulating "new consumption" in services.

## Implementation of the Plan

Ministries and local governments will be responsible for its implementation. The State Council plans to introduce tax subsidies for personal consumption loans and interest rate subsidies, in addition to expanded programs for the repurchase of old goods such as household appliances and used vehicles.

*Fiscal and credit support from the government and the PBOC will be implemented to stimulate consumption.*

The People's Bank of China (PBOC) will support financial institutions in developing asset securitization activities using consumer loans and auto loans as underlying assets. The goal is to increase the granting of loans and broaden the diversity of bond investments. The central bank will also actively support financial institutions in issuing consumption-related financial bonds, with an experimental program planned for densely populated cities. Consumer loans currently account for barely a quarter of household loans, with the majority being mortgage loans.

Finally, local governments will be able to allocate more budgetary resources to areas such as education, healthcare for the elderly, childcare, vocational training, culture, sports, and tourism.

## AI at the Heart of the Consumption Recovery Strategy

***AI and augmented reality will influence the consumption habits of Chinese households.***

For the first time, China has placed artificial intelligence (AI) at the center of its consumption plan, accelerating the development and application of new technologies and products such as autonomous driving, connected devices, ultra-high-definition video, brain-computer interfaces, robotics, and additive manufacturing.

With a population of 1.4 billion and 1.1 billion internet users, China's consumption transformation through AI is poised to accelerate rapidly. Consumers are already reaping the tangible benefits of AI through innovations like autonomous vehicles and effective chatbots that address problems seamlessly.

China is distinguishing itself in the tech landscape by developing applications that cater to consumer demands while generating significant economic value for the industry. In the pharmaceutical sector, where drug development can take up to 10 years and cost $1 billion, AI has the potential to drive considerable profits.

These emerging technologies are likely to change and stimulate consumption habits. Just as color televisions were considered luxury items by Chinese households in the 1990s and mobile phones later, these emerging technologies could quickly become commonplace consumer products.

## Conclusion

**Is China on the verge of entering a new era of consumption? It certainly appears to be on that path. The new consumption plan aims to increase household incomes while reducing their burdens (through improvements in social welfare) to achieve sustainable consumption growth. In response to external pressures, reforms have accelerated, particularly in social protection and the "Hukou" system (household registration). Substantial resources have been deployed, including fiscal and financial support from the government, and the central bank to revive the growth of consumer credit. For the first time, artificial intelligence is at the core of this new plan to influence and stimulate consumption. Additionally, the National Bureau of Statistics has introduced a new economic indicator: the industrial output of "service robots." Will robots soon invade the homes of Chinese households?**

**Zouhoure Bousbih**

## Market review

# The Fed Confronts Uncertainty

**The Fed's monetary status quo reflects the high level of uncertainty regarding growth and inflation in the United States. However, markets are factoring in the dovish bias reaffirmed by the reduction in quantitative tightening (QT). Interest rates have stabilized, and equities appear directionless. Gold continues to serve as a safe haven.**

The Federal Reserve has revised its expected growth for the year to the fourth quarter of 2025 down from 2.1% to 1.7%. Core inflation is projected to rise to 2.8%, up from 2.5% in December. The increase in tariffs is weighing on demand while simultaneously fuelling households' inflation expectations. Breakeven inflation rates do not show a divergence comparable to consumer surveys, but members of the FOMC are increasingly concerned about the risk of an inflationary spiral. The Fed anticipates two rate cuts this year, with the monetary status quo likely to persist until June, when a 25 bp reduction seems feasible. In the meantime, Donald Trump is expected to make a decision on tariff reciprocity, further intensifying the trade war, with an announcement anticipated on April 2. Despite unchanged rates, the Fed has eased its policy by slowing the pace of QT. The Treasury holdings on the balance sheet will decrease by $5 billion each month starting in April, down from the previous $25 billion. The MBS reinvestment policy remains unchanged, resulting in an amortization of approximately $25 billion per month. Once the debt ceiling constraint is lifted, the Treasury will need to quickly rebuild its cash reserves to avoid liquidity tensions. The slowdown in QT is a risk management strategy.

The easing of monetary policy in the U.S. has stabilized the 10-year T-note yield around 4.25%. The bias within the FOMC remains towards easing. Any deterioration in economic activity and unemployment would accelerate the timeline for rate cuts. There is a slight upward pressure on the curve's steepening, particularly on the 10-30 year spread (+4 bps over the week). In the Eurozone, following the shock from investment plans in Germany, the Bund is trading again below 2.80% (-11 bps last week). German long-term rates are becoming attractive to long-term investors, especially as the ECB appears committed to continuing easing towards 2%. Sovereign spreads continue to overlook volatility in the underlying risk-free rates. The 10-year OAT widens by 1 bp to 70 bps, while the BTP tightens by 1 bp (111 bps). Meanwhile, credit spreads are hovering around 85 bps against swaps. Flows into the asset class are slowing as the quarter-end approaches. European high-yield spreads have eased by 5 bps (311 bps against swaps). Valuations for B-rated and lower securities remain expensive, but flows are stabilizing. Equity markets have responded positively to the Fed's quantitative easing, and volatility is subsiding (VIX below 20%). Nevertheless, participants are taking profits on European cyclicals. Banks remain well-positioned, and utilities are outperforming amid the calm in long-term rates.

**Axel Botte**

## Main market indicators

| G4 Government Bonds | 24-Mar-25 | 1wk (bp) | 1m (bp) | 2025 (bp) |
|---|---|---|---|---|
| EUR Bunds 2y | 2.13% | -6 | +4 | +5 |
| EUR Bunds 10y | 2.77% | -5 | +29 | +40 |
| EUR Bunds 2s10s | 63.4 bp | +1 | +25 | +35 |
| USD Treasuries 2y | 3.98% | -7 | -20 | -26 |
| USD Treasuries 10y | 4.28% | -2 | -12 | -29 |
| USD Treasuries 2s10s | 29.7 bp | +5 | +7 | -3 |
| GBP Gilt 10y | 4.67% | +3 | +11 | +10 |
| JPY JGB 10y | 1.55% | +3 | +4 | +17 |
| **€ Sovereign Spreads (10y)** | 24-Mar-25 | 1wk (bp) | 1m (bp) | 2025 (bp) |
| France | 69 bp | +2 | -5 | -14 |
| Italy | 110 bp | 0 | -4 | -6 |
| Spain | 63 bp | +1 | -1 | -6 |
| **Inflation Break-evens (10y)** | 24-Mar-25 | 1wk (bp) | 1m (bp) | 2025 (bp) |
| EUR 10y Inflation Swap | 2.04% | -3 | +6 | +11 |
| USD 10y Inflation Swap | 2.47% | +4 | -9 | +1 |
| GBP 10y Inflation Swap | 3.42% | +3 | -10 | -10 |
| **EUR Credit Indices** | 24-Mar-25 | 1wk (bp) | 1m (bp) | 2025 (bp) |
| EUR Corporate Credit OAS | 92 bp | +0 | +5 | -10 |
| EUR Agencies OAS | 49 bp | +0 | -3 | -13 |
| EUR Securitized - Covered OAS | 45 bp | +1 | -3 | -11 |
| EUR Pan-European High Yield OAS | 320 bp | -5 | +26 | +2 |
| **EUR/USD CDS Indices 5y** | 24-Mar-25 | 1wk (bp) | 1m (bp) | 2025 (bp) |
| iTraxx IG | 59 bp | +3 | +6 | +1 |
| iTraxx Crossover | 310 bp | +6 | +24 | -3 |
| CDX IG | 60 bp | +6 | +11 | +10 |
| CDX High Yield | 349 bp | +5 | +48 | +38 |
| **Emerging Markets** | 24-Mar-25 | 1wk (bp) | 1m (bp) | 2025 (bp) |
| JPM EMBI Global Div. Spread | 334 bp | +3 | +14 | +8 |
| **Currencies** | 24-Mar-25 | 1wk (%) | 1m (%) | 2025 (%) |
| EUR/USD | $1.085 | -0.605 | 3.581 | 4.8 |
| GBP/USD | $1.296 | -0.262 | 2.508 | 3.5 |
| USD/JPY | JPY 150 | -0.381 | 0.013 | 5.2 |
| **Commodity Futures** | 24-Mar-25 | -1wk ($) | -1m ($) | 2025 (%) |
| Crude Brent | $72.0 | $0.9 | -$2.3 | -2.5 |
| Gold | $3 027.8 | $29.9 | $84.4 | 15.4 |
| **Equity Market Indices** | 24-Mar-25 | -1wk (%) | -1m (%) | 2025 (%) |
| S&P 500 | 5 668 | 0.51 | -5.28 | -3.6 |
| EuroStoxx 50 | 5 453 | 0.14 | -0.01 | 11.4 |
| CAC 40 | 8 081 | 0.09 | -0.12 | 9.5 |
| Nikkei 225 | 37 608 | 1.50 | -3.01 | -5.7 |
| Shanghai Composite | 3 370 | -1.64 | -0.09 | 0.5 |
| VIX - Implied Volatility Index | 18.92 | -7.75 | -0.32 | 9.0 |

Source: Bloomberg, Ostrum AM

# Additional notes

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