Deutsche Bank
Research

The House View

Snapshot

Macro views

World

- Global growth remains robust with major developed economies growing at above potential rates and perhaps showing signs of peaking. We expect global growth to rise to +3.8% this year as fundamentals remain supportive, but decelerate marginally by the end of next year with risks of slowing EM
- Trade wars remain a key risk to the global economy. There have been some positive signals recently regarding NAFTA and the US-EU relationship, but the conflict with China looks set to continue through at least the next few months
- Italy remain in focus as the new government formulates the 2019 budget, key for its debt sustainability
- Emerging markets have come under recent pressure amid a combination of idiosyncratic risks, tighter US monetary policy, and the aforementioned trade wars. Cognizant of contagion risks for broader EM, and continuing negative trend in trade policy, we have revised down our regional growth forecasts

United States

- Growth to accelerate in 2018 to +2.9%, boosted by tax cuts, fiscal spending etc. Growth momentum is also supported by rebound in consumer spending and solid capital expenditures
- Residential investment spending presents slight downside risks to our near term growth forecasts. Also, downside risks from the potential trade war and from potentially tighter financial conditions remain. Hence, we lowered our 2019 forecastsby a tenth to 2.7%
- Recent wage and price data supports our expectation of upside surprise to inflation this year. Labour markets have tightened and little slack remains, so growth will be increasingly inflationary this year.With inflation already at the Fed’s target, further upside will support the case for further monetary tightening

Eurozone

- We expect the Eurozone economy to grow +2.1% this year, a modest slowdown after 2017’s impressive performance. Above trend growth remains underpinned by solid income growth and easy financial conditions, with potential upside risks if fiscal policy becomes more expansionary than we expect
- There are risks to the European outlook from a more disruptive trade war and from a confrontation between Italy and the European Commission over the 2019 budget. We expect both issues to remain latent risks over the medium term. The risks to euro areag growth from Turkey remains manageable with Turkey representing just 3% of goods exports.
- Brexit negotiations continue and we expect a last-minute deal to be struck. Though the complete future relationship will probably not be settled for now with transition likely to be extended beyond Dec-2020

China

- We expect China’s economic growth to slow down to +6.6% this year, with activity decelerating in the second half of the year. Retail sales, auto sales and home applicances sales all fell in July and infrastructure investment declined further. Property and manufacturing sectors showed positive signs
- The main risk to the outlook is trade policy via further escalation with the US that could derail exports. The impact of measures implemented so far will be manageable, but the risks are clearly to the downside. However, authorities have policy space to support growth if necessary, and we expect easing financials and its stimulative effects on growth to show up by H1 2019
- Monetary policy will likely be eased further to support growth, which will naturally result in a weaker currency due to interest rate differentials. Expect Yuan to weaken further this year and in 2019

Emerging Markets

- We have revised down our EM growth forecasts (to 4.9% in 2018), especially in EMEA and Latin America. Recent developments in Argentina and Turkey, in particular, prompted us to marked down our growth forecasts in both the countries. Meanwhile, a vigorous re-pricing in Brazil due to the worsening electoral outlook has also started threatening to further entrench fear of broad contagion. In addition, South Africa has entered a technical recession and Russia remains vulnerable to further sanctions.
- Overall, differentiation and divergence between EMs is continuing, with domestic politics and policy responses largely determining which countries are the over- and under-performers. Trade war risks remain and can affect EMs broadly, which could result in more pressure on growth moving forward.

Monetary Policy

- Fed: expect 2 more hikes in 2018, i.e. total 4 hikes this year, and 4 hikes in 2019
- ECB: QE to slow to €15bn per month in Q4 and end in Dec 2018; first 20bp depo hike in Sep-2019, contingent upon our macro forecasts for above-potential growth
- BoJ: no changes to our view. Discussion in next 2-3 years on shifting policy goal from inflation to growth
- BoE: no more rate hikes in 2018, but return to hiking cycle next year
- PBoC: one more rate cut this year and three more cuts in 2019
- EM: Increasing divergence across EM central banks

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Key downside risks	▪ Trade conflict escalation US impose 2nd/3rd round tariffs on China and revisits sector-wide tariffs on auto industry, followed by foreign retaliation – all to hurt global supply chains & growth ▪ Brexit and Italiy budget: Political uncertainty in Europe could heighten uncertainties and volatility in European assets and disrupt recovery ▪ US mid-term elections (Nov-6) is a key risk event this autumn. Markets are sensitive to political and policy changes and this can lead to rise in volatility ▪ EM crisis: Escalation of idiosyncratic risks in Turkey/Argentina/Brazil can translate into wider EM crisis ▪ Recession: Sharp correction in financial market can trigger slowdown/recession
Key themes	▪ Trade wars: No signs yet of a de-escalation. We expect the US to implement 25% tariffs on an additional $200bn of Chinese imports soon. Some softening in rhetoric against the EU auto industry and Mexico ▪ Brexit: We expect the UK to reach a deal with the EU by the end of this year which comprises of a withdrawal agreement & a political declaration on a future relationship ▪ Italy: Markets are alert to the impending Italian budget battle, but concerns over fiscal sustainability are longer-term and will lurk in the background until resolved. The immediate focus will be on the deficit target - number around or above 2.3% of GDP might will likely cause negative market reaction ▪ EM slowdown: EM growth outlook has slowed down (clear signs of deceleration in LatAm and EMEA) due to idiosyncratic factors, continued negative trend in trade policy and lack of spill over from DM.

Market views

Market sentiment	▪ Markets remain supported by strong macro fundamentals ▪ We maintain our overarching strategic views, though downside risks around trade, Italy, and emerging markets have intensified recently
Equities	▪ Bullish US equities. Earnings are strong and underlying growth is robust ▪ Cautious in September, but expect a rally to our full-year targets in the 4th quarter
Rates	▪ Strategically bearish. We continue to expect the Fed to tighten policy further, the term premium to rise, pension demand to soften, and inflation to rise further ▪ In Europe, we remain bearish. QE is ending and the growth outlook remains healthy
FX	▪ Near-term risks are balanced, but our strategic view is still for further dollar weakness over the next year given the deteriorating flow outlook ▪ Neutral on euro for now. We expect growth momentum to rebound and for the ECB to continue its tightening process by raising rates next year, which will provide a tailwind to the euro next year ▪ Neutral yen. The Bank of Japan continues its stealth taper but remains largely on autopilot for now
Credit	▪ Credit looks cheap based on our volatility models, but we remain neutral as volatility and risks are set to rise. Dovish ECB guidance supports European credit spreads, though downside risks from trade, more aggressive Fed hiking, and European politics (Italy) remain. Prefer IG over HY and EUR credit over USD
EM	▪ EM stress is still largely idiosyncratic, but the risk of a broader fallout is increasing ▪ The sell-off in August shows clear signs of overshooting and some retracement may be in order. But the underlying trend for trade policy remains negative leaving room for further downward revisions in growth. We expect investors to remain bearish.
Oil	▪ Expect oil prices to rise in the near-term ($80 by YE-18) before global market rebalances ($77 by Q2-19) ▪ The Iran sanctions and subsequent production response will be key, but we expect the US and Saudi Arabia to balance out any Iran-linked disruptions

Key macro and markets forecasts

GDP growth (%)

	2016	2017	2018F	2019F
Global	3.2	3.8	3.8	3.7
US	1.6	2.2	2.9	2.7
Eurozone	1.9	2.5	2.1	1.7
Germany	2.2	2.2	1.9	1.7
Japan	1.0	1.7	0.8	0.6
UK	1.8	1.7	1.3	1.6
China	6.7	6.9	6.6	6.3

Central Bank policy rate (%)

	Current	2017	2018F	2019F
US	1.875	1.375	2.375	3.375
Eurozone	0.00	0.00	0.00	0.25
Japan	-0.10	-0.10	-0.10	-0.10
UK	0.75	0.50	0.75	1.00
China	1.50	1.50	1.50	1.50

Key market metrics

	Current	Q3-18F	Q4-18F	Q2-19F
US 10Y yield (%)	2.96	3.25	3.50	3.60
Germany 10Y yield (%)	0.43	0.45	0.90	1.00
EUR/USD	1.16	1.16	1.17	1.25
USD/JPY	111	111	108	103
S&P 500	2,877		3,000	
Stoxx 600	374		395	
Oil WTI (USD/bbl)	68	74	74	70
Oil Brent (USD/bbl)	78	80	80	77

Current prices as of 11-Sep-2018

Recent publications	▪ The House View: Mind the (political) hurdles, 10- September-2018 ▪ The House View: Central Bank Watch, 08-August-2018 ▪ The House View: Tug of (trade) war, 24-July-2018 ▪ The House View: Trade war tensions, 26-June-201