Deutsche Bank
Research

The House View

Snapshot

Macro views

World

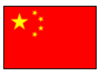
- Global growth is undeniably slowing and risks have risen. Central banks are set to respond with policy support across developed and emerging market economies, but we are not certain how successful their efforts will be.
- The main risk to the global economy is the trade war. It is extremely hard to predict what will happen, which raises uncertainty and results in an adverse economic impact regardless of how conditions evolve. We now think the Fed, ECB, and PBoC will be forced to respond to these elevated risks with more policy accommodation.

United States

- The US economy is still growing, but the trend is undeniably slowing. We forecast full-year 2019 and 2020 growth at 2.2% and 1.5%, respectively. That represents a downgrade from our prior forecasts and is principally a result of the escalating trade war.
- Trade tensions are weighing on manufacturing and capital spending by businesses. This will present a material drag on growth over the next several quarters. We are already seeing these dynamics appear in the data, with the ISM manufacturing survey below 50 and forward-looking sub-indexes suggesting further slowdown to come.
- Consumer fundamentals remain solid, excluding the trade war effects, but we are beginning to see spillovers into the services sector and labour market. Headline job growth and hours worked have both slowed, though wages continue to rise.
- Inflation is set to remain below the Fed’s target; there are limited price pressures in the economy and expectations are still down substantially from their pre-2014 levels.
- The principle risks to our view, on both the upside and downside, come from the trade war. A resolution could unlock new capital spending while further escalation could tip the economy into recession.

Eurozone

- European growth has slowed and risks are elevated. With full-year 2019 growth forecast at 1.1%, there is limited scope to absorb a negative shock without tipping into recession.
- Risks are elevated, as Brexit uncertainty lingers and the trade war continues. There is still the threat that the US could apply tariffs to EU auto exports.
- Manufacturing, especially in Germany, remains in decline and there are no signs of a turnaround. On the other hand, the labour market remains strong and financial conditions are still supportive for growth.



China

- Growth in China is decelerating, though there is still scope for moderate policy support. We forecast 2019 growth at 6.2%, falling to 5.9% in 2020.
- As growth slows, imports will fall faster than exports, which will end up supporting headline growth via stronger net exports. Household consumption remains strong and the outlook is positive.
- The PBoC is set to provide further policy support, but fiscal policy space is constrained until next April. There are positive risks if easing ends up being more substantial than expected, boosting asset prices and consumer confidence.
- The trade war remains a major risk, as tariffs affect the export economy. An even bigger risk would be escalation beyond tariffs, toward financial or technology arenas, which would likely result in an even more adverse impact on economic growth.

Emerging Markets

- Growth is slowing across emerging markets, with the trade war a major risk. A de-escalation would end up being largely positive.
- Across Asia, central banks are deploying rate cuts and policy support to counteract the slowdown and to keep pace with cuts by the Fed and PBoC.
- In LatAm, slower growth exposes larger countries to shocks.
- In CEEMEA, growth is proving to be resilient, albeit at a lower level.

Monetary Policy

- Fed: Four more cuts (Sep, Oct, Dec, and Jan)
- ECB: 10bps deposit rate cut in September and December, tiering in September, QE a close call
- BoJ: On hold, no changes in target yields on YCC, possibly well into 2020
- BoE: No hike this year, one hike in Aug 2020
- PBoC: To cut OMO rates by 10-50bps by year-end
- EM: Expect cuts across a series of EM central banks

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Key downside risks	▪ Crash Brexit: No-deal Brexit risks are rising, as are the risks of a fresh general election. The timeline is tight between now and 31 October deadline ▪ Trade war: Escalation in US-China trade war, and an extension of tariffs to Europe (auto tariff) would disrupt global trade activity and hit global growth hard ▪ Recession: Prolonged and accelerated weakness in Chinese & European growth & associated global recession / sharp correction in financial markets ▪ Geopolitical risks: Rising tensions between US-Iran, UK-Iran can spark volatility and dent market sentiment
Key themes	▪ Monetary easing: Major central banks are set to engage in simultaneous policy easing this fall to limit slowing growth momentum. Rate cuts likely in the US, Europe, China, and several other EM economies ▪ Trade war: Some de-escalation recently on US-China trade front, but no signs of a deal as yet. EU auto tariff risk also remains on the table. Truce may be temporary ▪ Brexit: Our base case remains a general election this year. We raise our no-deal Brexit indicative probability to 50%, higher than consensus.
Market views	
Market sentiment	▪ We believe that central bank easing will arrest the current slowdown in growth, prolonging the current economic expansion ▪ Near term, there are risks given current valuations and positioning
Equities	▪ We expect growth to continue, as central bank easing counteracts political and trade headwinds ▪ However, we are cautious in the near term given elevated positioning risks
Rates	▪ We prefer treasuries to bunds, given valuations and the scope for deeper cuts by the Fed compared to the ECB ▪ We prefer positioning for relative value trades within the European sovereign complex
FX	▪ Fundamentals are mixed, as scope for dollar weakness versus current account-surplus countries is offset by dollar strength versus emerging market currencies ▪ In the medium term, the dollar should weaken as Fed has more space to cut rates and it is near the top of its historical valuation range
Credit	▪ The likely upcoming accommodative actions from central banks should be supportive for credit, but heightened risks and high valuations make us cautious ▪ We expect mild widening this year before more substantive widening in 2020
EM	▪ Extended accommodation provides supportive backdrop, but slow growth and idiosyncratic risks limit scope for high performance to carry ▪ We turn less bearish on EM currencies, but are still selective within the asset class
Oil	▪ On a fundamental level, there is a bit of scope for prices to rise over the near term ▪ We are cautious, however, as political developments are having outsized effects on markets in the current climate

Key macro and markets forecasts

GDP growth (%)

	2018	2019F	2020F
Global	3.8	3.1	3.2
US	2.9	2.2	1.5
Eurozone	1.9	1.1	1.0
Germany	1.5	0.3	0.7
Japan	0.8	0.9	-0.1
UK	1.4	1.2	1.3
China	6.6	6.2	5.9

Central Bank policy rate (%)

	Current	2019F	2020F
US	1.88	1.38	1.13
Eurozone	-0.50	-0.60	-0.60
Japan	-0.10	-0.10	-0.10
UK	0.75	0.75	1.00
China	3.30	3.00	
India	5.40	4.90	4.75

Key market metrics

	Current	Q3-19	Q4-19
US 10Y yield (%)	1.73	2.05	2.15
EUR 10Y yield (%)	-0.56	-0.35	-0.30
EUR/USD	1.10	1.10	1.13
USD/JPY	108	108	105
S&P 500	2989	3175	3250
Gold (USD/oz)	1494	1488	1488
Oil WTI (USD/bbl)	56.1	62.0	60.0
Oil Brent (USD/bbl)	61.1	70.0	68.0

Current prices as of Sep 11, 2019

Recent publications

- The House View: Cushioning downside risks 10 September 2019
- The House View: Global monetary medicine on the way 23 July 2019
- The House View: Surveying slower growth, 20 June 2019
- The House View: Trade war heat is on, 16 May 2019