Deutsche Bank
Research

The House View: Snapshot
The Taps Still Tightening

#PositiveImpact

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Macro views

World

— Our global outlook has been upgraded due to (i) the rapid and successful reopening of China; and (ii) growing evidence that inflation has peaked.

— Inflation seems to have peaked but risks are to the upside, leading to central bank tightening that will slow growth across the key economies.

— Russia's invasion of Ukraine continues to disrupt key commodity markets and supply chains.

United States

— We expect a recession in the beginning of H2 2023 lasting three to four quarters, with overall growth in 2023 at 1%.

— GDP was firm in Q4 2022, but domestic demand growth has slowed and consumer spending remains depressed.

— Inflation has moderated, but there remains risk that it turns up in the near term. Core services ex shelter remains firm. The labour market has momentum and remains historically tight with elevated quit rates.

— The debt ceiling lurks as a key risk in H2 2023, with some combination of FCI tightening/fiscal retrenchment likely.

Europe

— The euro area should just about avoid a recession this winter. We have upgraded our 2023 growth forecast to +0.5% y/y while keeping 2024 unchanged at +1% y/y.

— The rosier outlook comes with (i) the easing of the gas crisis; (ii) the earlier China reopening from Covid in 2023. On the downside, a sharper ECB tightening cycle is a risk to watch.

Germany

— No recession in winter. We have revised 2023 GDP up to 0%.

— Germany's macro outlook has improved markedly thanks to (i) favourable gas storage levels, (ii) the substantial decline in wholesale gas and electricity prices, and (iii) increasing optimism after the rapid change in China's Covid policy.

— Structurally higher energy prices, the US recession in H2 and the increasing impact of the ECB's policy shift are set to weigh on the economic momentum throughout 2023.

China

— China has rebounded from its Omicron exit wave much sooner than expected, and mobility has picked up quickly.

— We see growth to pick up from Q1 onwards, led by the services sector. We expect growth of 6% in 2023 and 6.3% in 2024.

— Inflation rising faster than expected post-reopening is a key risk, as well as an acceleration in technology decoupling that disrupts China's manufacturing sector.

Emerging markets

— EM finds itself in a healthier macro environment. Inflation momentum is slowing in many parts of EM, putting it close to the peak of the policy cycle. EM assets are under owned by global money, and China's rapid reopening is a shot in the arm for EM's demand function.

— Asia – The unexpectedly quick reversal of China's Covid policy is a significant boost for the region in terms of export demand and tourism.

— LatAm – Fundamentals (weaker real economy) are diverging from market drivers (lower dollar, stronger commodities).

— CEEMA – Close to peak of the inflation/rates cycle, but headwinds from Ukraine and large policy uncertainty in Turkey.

Key downside risks

H — High inflation likely to be persistent – Tentative evidence of passing peak inflation but risks are weighted toward more severe recessions being needed to disinflate successfully.

M — Earlier than expected US recession – We expect a US recession in H2 2023, but the risk is that it comes earlier. We still expect the UK economy to fall into a recession – albeit a shallower and shorter one.

M — Elevated geopolitical risks – The Ukraine-Russia conflict will continue in 2023, with risk of escalation. US-China strategic competition may intensify, with further risk of Chinese retaliation against new US controls.

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Market views

Market Sentiment	— Risk assets will struggle in H2 2023 given a US recession, although Treasuries will be supported into late 2023 by the Fed moving to cut rates.
Equities	— In the short-term we see the current bear market rally continuing into Q1. — As the recession begins in Q3, the S&P 500 to bottom at 3250, before recovering into year-end. — A year-end 2023 target of 4500 for the S&P 500.
Rates	— Neutral US front-end, have a mild bearish bias in EUR front-end, expect the UST-Bund spread and Bund ASW to tighten and term premia to rise globally. — 10yr UST at 3.65% by year-end 2023, and 10yr bund at 2.60%.
FX	— The USD has further weakened since the start of 2023, and we expect it to be on a sustained downward trend from here onwards. We see EUR/USD to rise to 1.10 by Q2 and 1.15 by Q4. — The dollar risk premium should further recede as global growth dynamics continue to improve, and the end of the Fed's hiking cycle comes into view.
Credit	— Spreads should widen materially in H2 2023 as a US recession takes hold. — We expect spreads to widen in $IG to 140bps & 465bps by the end of Q1, with more material widening in Q2. — For €IG, we see spreads wider at 160bps in Q2 2023 and €HY widening to 510bps in Q2 2023.
Oil	— We see Brent at $75/bbl for H1 before balances improve in H2 to $80/bbl. — We see recession slowing demand growth, and as China's exit from zero-Covid occurred earlier than expected, there is less scope for a 'slingshot' rebound in Q2.
Monetary Policy	— Fed: 25bps in March and May. Terminal rate at 5.125% in Q2 2023. — ECB: 50ps in March and 25bps in May, reaching terminal 3.25% rate in May 2023. — BoJ: no change in rates. — BoE: 25bps in March, reaching terminal of 4.25% in March 2023. — PBoC: No change in rates.

Key macro & markets forecasts

GDP growth (%)	2023F	2024F
Global	2.7	3.1
US	1.0	0.3
Eurozone	0.5	1.0
Germany	0.0	1.0
Japan	1.0	0.8
UK	-0.5	0.8
China	6.0	6.3

Central bank policy rate (%)	Current	Q1-23	Q4-23
US: federal funds rate	4.625	4.875	4.625
Eurozone: deposit facility rate	2.50	3.00	3.25
Japan: policy balance rate	-0.10	-0.10	-0.10
UK: bank rate	4.00	4.25	4.25
China: MLF 1Y interest rate	2.75	2.75	2.75

Key market forecasts	Current	Q4-23
US 10Y yield (%)	3.65	3.65
EUR 10Y yield (%)	2.29	2.60
EUR/USD	1.07	1.15
USD/JPY	132	120
S&P 500	4111	4500
Gold (USD/oz)	1866	2000
Oil WTI (USD/bbl)	74.46	75
Oil Brent (USD/bbl)	80.56	80

2023 Macro events calendar

March 2023

10	JN	Bank of Japan Decision
16	EZ	ECB Decision
22	US	Federal Reserve Decision
23	UK	BoE Decision
23-24	EU	European Council Meeting

April 2023

10-16		IMF/World Bank Spring Meetings
28	JN	BoJ Decision

May 2023

03	US	Federal Reserve Decision
04	EZ	ECB Decision
11	UK	BoE Decision
19-21		G7 Leaders Summit

Recent editions

- The Taps Still Tightening 9 February 2023
- The Looming Recession 6 December 2022
- Shipwrecked 28 September 2022
- The Gathering Storm 22 June 2022

Analyst Certification

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