Month in Review

Fed says US economy favours 2015 rate rise

FT, 15 Jul 2015

Eurozone economy in best health for four years - despite Greece

The Telegraph, 3 July 2015

Greece: a bad deal for everyone

The Conversation, 14 Jul 2015

Oil price drops sharply on surprise rise in reserves

The Week, 23 July 2015

China crash hits commodity prices

FT Adviser, 13 Jul 2015

China Stocks Sink Most Since 2007 as State-Induced Calm Shatters

Bloomberg, 27 Jul 2015

Weak U.S. retail sales hint at slower economic growth

Reuters, 14 Jul 2015

Fed Officials Finally See U.S. Housing Sector on the Upswing

WSJ, 08 Jul 2015

China rolls out emergency measures to prevent stock market crash

Reuters, 05 Jul 2015

Gold price falls again to new five-year low

The Telegraph, 24 Jul 2015

U.S. Earnings Season: Low Bar, High Hopes

WSJ, 05 Jul 2015

Landmark deal reached on Iran nuclear program

CNN, 15 Jul 2015

Greece votes ‘No’, ‘Grexit’ now looms

The BRICS post, 7 July 2015
Greece, the sell-offs in China equities and in commodities dominated market attention in recent weeks and months. Greece is no longer in focus. The deal with Europe put an end to months of brinkmanship, and the risk of Grexit has receded for now – even if Greek political dynamics remain a risk in the next 3-6 months.

The negative price action in China equities and commodities continues. Idiosyncratic factors can help explain it in part. The rally in China had been spectacular, comparable to that of the Nasdaq in the late 1990s, and was vulnerable to a change in sentiment; a correction was justified for many commodities given weak fundamentals. But the sell-offs also seem to reflect lingering concerns over China and global growth. Growth momentum does remain weak across EM, but is robust in the eurozone and has bottomed out in the US. We expect stronger growth in the second half of the year, especially in developed markets, backed by improving credit conditions that support private domestic demand.

Global inflation remains low but has likely bottomed earlier this year. The fall in commodity prices certainly presents downside risks but does not change our expectation of gradually rising inflation, as the domestic drivers in key developed markets are improving. As a result, this will allow the Fed to hike rates this year. The exact timing (September, marginally more likely, or December) is less important than the fact that the pace of hikes will be very gradual and should not derail economic momentum.

This environment is generally supportive for risk assets, and sell-offs provide attractive entry points. In rates, we expect US short-end yields to rise as Fed hikes approach while long-term yields drift moderately higher on improving macro data. In FX, improving US data and Fed hikes will lead to further dollar strength, while euro weakness will resume as ECB easing / Fed tightening divergence comes back into play; commodity currencies will remain under pressure.

David Folkerts-Landau, Group Chief Economist
We expect growth to pick-up in the second half of the year, on a US rebound and eurozone strength – while EM remain weak

Economic outlook
- Global growth of 3.2% (just below 2014). EM slowdown offsets recovery in Eurozone and Japan. 2016 at 3.7%
- US growth of 2.3% for 2015 (close to 2014). Data have rebounded from a weak Q1 and fundamentals are solid for growth pick-up into H2-2015 to 3.0%
- Eurozone growth at 1.4-1.6% in 2015-16. Recovery is robust, improving credit conditions offer some upside
- EM growth to slow to 4.2% before rebounding in 2016. Weak growth remains a key issue across EM, but we don’t expect systemic EM crises

Central bank watch
- Fed: expect first hike in 2015; September marginally more likely; hiking cycle to be gradual. Market pricing too slow a pace of hikes
- ECB: fully committed to QE until inflation target is met. Too early to consider change in tone / communication
- BoJ: on hold; more easing only if inflation worsens
- BoE: on hold; first hike in Q2-2016
- PBoC: in easing cycle. Expect further rate cuts in 2015, reducing short-term risk of a sharp slowdown
- EM: easing in Asia contrasts with end of easing / start of tightening cycles in Latin America and CEEMEA

Views on key themes
- Greece: no longer in focus since risk of imminent Grexit receded following deal with Europe, but flare-up in the next 3-6 months is possible
- China equities retreated sharply again after policy response brought brief stabilisation; fundamentals should lead stocks higher after the summer
- Commodity prices: sell-off overdone but weak fundamentals mean any price rebound should be short-lived
- Monetary policy to remain accommodative even as Fed starts hiking

Key downside risks to our view
- Sharp market corrections / volatility episodes, e.g., on the back of the Fed rate hikes
- EM crises, driven by China slowdown, stronger dollar and rising rates, lower commodity prices
- China hard landing: sharper contraction of domestic demand due to fiscal drag, weakening property spend
- Crisis returns to Europe: political risk, Grexit risk returns, spurs significant contagion to other peripheral countries
- Prolonged US slowdown
- Geopolitical risk: rise in tensions derails world economy

Notes: H / M / L indicates estimated probability of risk (High, Medium, Low).
With Greece resolved for now, the key risks come from more episodes of market volatility and weak growth in EM

The House View - Risk Matrix

Downside risks
1. Sharp market corrections / volatility episodes, e.g., re-pricing of central bank action causes sharp market corrections in low market liquidity environment
2. EM crises: driven by China slowdown, stronger dollar and rising rates, low commodity prices
3. China hard landing: sharper contraction of domestic demand due to fiscal drag, weakening property spend
4. Crisis returns to Europe: political risk overshadows ECB QE. Grexit risk returns, spurs significant contagion to other peripheral countries
5. Prolonged US growth slowdown: US economy fails to accelerate; the housing recovery is derailed and investment fails to pick-up
6. Geopolitical risk: rise in tensions derailed world economy

Upside risks
7. Smooth start to Fed tightening
8. Eurozone growth surprises to the upside

Note: Moves represent change in risk outlook over previous month
Source: Deutsche Bank Research
Equities have outperformed YTD, although returns have been flat or negative since June. Rates have delivered nil returns YTD.

Total returns* 2015 YTD and since 1st June 2015

<table>
<thead>
<tr>
<th>%</th>
<th>Equities</th>
<th>Corporate Credit</th>
<th>Sovereign debt</th>
<th>FX**</th>
<th>Commodities**</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>YTD 2015</td>
<td>Since June 1st</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td>23</td>
<td></td>
<td>23</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Milan</td>
<td>18</td>
<td></td>
<td>18</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>17</td>
<td></td>
<td>17</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>CAC-40</td>
<td>17</td>
<td></td>
<td>17</td>
<td>-1</td>
<td>-21</td>
</tr>
<tr>
<td>Russia</td>
<td>14</td>
<td></td>
<td>14</td>
<td>-2</td>
<td>-16</td>
</tr>
<tr>
<td>Micex</td>
<td>13</td>
<td></td>
<td>13</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>Japan</td>
<td>11</td>
<td></td>
<td>11</td>
<td>-12</td>
<td>-16</td>
</tr>
<tr>
<td>Nikkei</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Eurostoxx 50 (E)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>DAX-30</td>
<td></td>
<td>2</td>
<td>0</td>
<td>-8</td>
</tr>
<tr>
<td>Spain</td>
<td>IBEX-35</td>
<td></td>
<td>0</td>
<td>-2</td>
<td>-11</td>
</tr>
<tr>
<td>Italy</td>
<td>FTSE 100</td>
<td></td>
<td>0</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>India</td>
<td>S &amp; P 500</td>
<td></td>
<td>0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Brazil</td>
<td>Bovespa</td>
<td></td>
<td>0</td>
<td></td>
<td>-30</td>
</tr>
<tr>
<td>Emerging Markets</td>
<td>MSCI EM</td>
<td></td>
<td>0</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>US</td>
<td>HY</td>
<td></td>
<td>-2</td>
<td>0</td>
<td>-2</td>
</tr>
<tr>
<td>China</td>
<td>US IG</td>
<td></td>
<td>2</td>
<td>0</td>
<td>-8</td>
</tr>
<tr>
<td>Germany</td>
<td>EU IG</td>
<td></td>
<td>-1</td>
<td>0</td>
<td>-11</td>
</tr>
<tr>
<td>UK</td>
<td>Dollar Index</td>
<td></td>
<td>0</td>
<td>0</td>
<td>-16</td>
</tr>
<tr>
<td>China</td>
<td>GBP</td>
<td></td>
<td>-2</td>
<td>-2</td>
<td>-11</td>
</tr>
<tr>
<td>US</td>
<td>INR</td>
<td></td>
<td>0</td>
<td>-8</td>
<td>-16</td>
</tr>
<tr>
<td>India</td>
<td>RUB</td>
<td></td>
<td>0</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>Japan</td>
<td>EUR</td>
<td></td>
<td>0</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>Australia</td>
<td>AUD</td>
<td></td>
<td>0</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>Canada</td>
<td>CAD</td>
<td></td>
<td>0</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>Turkey</td>
<td>TRY</td>
<td></td>
<td>0</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>Brazil</td>
<td>BRL</td>
<td></td>
<td>0</td>
<td>-11</td>
<td>-16</td>
</tr>
<tr>
<td>Brazil</td>
<td>Soy Beans</td>
<td></td>
<td>0</td>
<td>0</td>
<td>-16</td>
</tr>
<tr>
<td>Brazil</td>
<td>Brent</td>
<td></td>
<td>0</td>
<td>0</td>
<td>-16</td>
</tr>
<tr>
<td>China</td>
<td>Gold</td>
<td></td>
<td>0</td>
<td>0</td>
<td>-16</td>
</tr>
<tr>
<td>Brazil</td>
<td>Commodity Index</td>
<td></td>
<td>0</td>
<td>0</td>
<td>-16</td>
</tr>
<tr>
<td>Brazil</td>
<td>Iron Ore</td>
<td></td>
<td>0</td>
<td>0</td>
<td>-16</td>
</tr>
</tbody>
</table>

Note: (*) Total return accounts for both income (interest or dividends) and capital appreciation. (**) FX, Commodities are spot returns.

Source: Bloomberg Finance LP, Deutsche Bank Research. As of 27 July 2015 except Corporate / Sovereign debt (24 July)

Deutsche Bank
Agreement in Greece put an end to months of brinkmanship, and the risk of Grexit has receded for now

- After months of conflict escalation, Greece’s deal with Europe removes the imminent risk of Grexit
- Negotiations have started on the third bailout*, and should conclude by the end of the summer
  - EUR82-85bn financing needs through 2018 in exchange for fiscal adjustment and reform
  - Programme will include tight oversight from creditor institutions, with aid tied to completion of reforms and fiscal targets
  - Greater focus on structural reform is positive
- Meanwhile Europe is providing bridge financing for the Greek sovereign (e.g., for debt service)...
- ...And the ECB is slowly raising liquidity support for banks – though capital controls will remain in place for months, until Greek banks are recapitalised
- Little has been achieved by the Greek government despite months of brinkmanship
  - Greece is again in recession and capital controls are deepening the pain
  - Terms of agreement are tougher than those rejected by Greeks at the 5-July referendum
  - Debt relief has been on the table since 2012

Key elements of agreement

<table>
<thead>
<tr>
<th>Financing support</th>
<th>EUR82-85bn to 2018, incl. ~EUR35bn for rollover of debt maturities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank recapitalisation</td>
<td>Financing support includes EUR25bn for bank recap</td>
</tr>
<tr>
<td>Fiscal austerity</td>
<td>Aggressive fiscal adjustment including both tax rises &amp; spending cuts. Fiscal targets to be agreed</td>
</tr>
<tr>
<td>Structural reforms</td>
<td>Comprehensive growth enhancing structural reform – inclusion of this is positive</td>
</tr>
<tr>
<td>Privatisation fund</td>
<td>EUR50bn privatisation fund (but target is overly ambitious)</td>
</tr>
<tr>
<td>Creditor monitoring</td>
<td>Tight oversight from creditor institutions</td>
</tr>
<tr>
<td></td>
<td>Aid tied to completion of reforms and fiscal targets</td>
</tr>
<tr>
<td>Debt relief</td>
<td>Debt relief to be discussed. No haircuts, but rather maturity extensions, extension of interest holiday</td>
</tr>
</tbody>
</table>

Debt relief for Greece is necessary in the long-run, but despite huge debt the country’s debt servicing costs (ex. maturities) are low

Note: (***) This bailout programme follows the two previous bailouts agreed in 2010 and 2012. It will be financed via the European Stability Mechanism (ESM), which has EUR450bn of available lending capacity for countries / banks in trouble.

Debt relief for Greece is necessary in the long-run, but despite huge debt the country’s debt servicing costs (ex. maturities) are low

Note: (***) This bailout programme follows the two previous bailouts agreed in 2010 and 2012. It will be financed via the European Stability Mechanism (ESM), which has EUR450bn of available lending capacity for countries / banks in trouble.

Note: (**) Based on interest expense and level of debt, relative to other eurozone countries
Source: European Commission, Haver Analytics, Deutsche Bank Research

Greece update: is the crisis over? – 21 July 2015
Greece: will this time be different? – 13 July 2015
However, this is a tough deal and the issue is not fully resolved – the risk of a flare-up in the next 3-6 months remains

- Grexit has been avoided for now and this is positive – but the risk of a new crisis escalation remains
- It is unlikely, though possible, that bailout talks fail
- Instead, risk lays with programme implementation
  - Terms are harsh and will further depress growth in the short-term
  - Lack of ownership of the programme in Greece (government is clearly hostile to it) raises implementation risk
- Some form of political change in Athens is needed to increase programme ownership, raise chances of success and avoid Grexit
  - Uncertainty around programme implementation, the economy and the banking system will persist until the political picture is resolved
  - A move toward the centre by SYRIZA or early elections may be needed
- However, not all is lost for implementation
  - Grexit no longer inconceivable, providing strong incentive for Greece to stick to the agreement
  - Capital controls will remain until banks receive fresh capital: there is an incentive for Greece to co-operate with creditors and avoid delays

**Next steps: high-level timeline**

| July | Agreement between Europe and Greece | ✔ |
|      | Greek parliament approves initial sets of measures | ✔ |
|      | Europe provides bridge financing, ECB raises ELA | ✔ |
|      | Start of technical negotiations of third bailout | ✔ |
| Early-Aug | Greek parliament to vote further pension, tax measures | |
| Mid-Aug | Expected completion of third bailout programme negotiations – to be followed by country parliamentary approvals (including Germany, Finland, Austria) | |
| 20-Aug | ECB bond maturity (EUR3bn) | |
| Q4 | Greek banks recapitalisation, followed by gradual lifting of capital controls | |
| Q4 / Q1-16 | Discussion of potential debt relief | |

**Greece’s macro outlook is grim. Since SYRIZA came to power in January, growth forecasts have been slashed**

```
<table>
<thead>
<tr>
<th></th>
<th>2015 GDP forecast, %yoy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jul-14</td>
<td>4</td>
</tr>
<tr>
<td>Oct-14</td>
<td>2</td>
</tr>
<tr>
<td>Jan-15</td>
<td>-2</td>
</tr>
<tr>
<td>Apr-15</td>
<td>-4</td>
</tr>
<tr>
<td>Jul-15</td>
<td>-4</td>
</tr>
</tbody>
</table>
```

Note: current forecast for Greece is actually the bailout programme’s assumption

Source: Deutsche Bank Research

Focus Europe: There is a way, but is there a will? – 17 July 2015
The rise and subsequent fall in China equities was spectacular but not unusual

- From mid-2014 to the peak in June 2015 Chinese equities rose about 150%
  - The speed and size of the rally was comparable to the Nasdaq in the late 90s
- Several factors help explain the rally
  - Anticipation of monetary and fiscal policy easing to counter China’s weakening growth prospects
  - Role of retail investors, who own ~20% of market but account for around 80% of turnover – 66m new retail investment accounts just in 2015
  - Sharp rise in leveraged exposure – margin financing increased more than five-fold since mid-2014, with ~10% of market cap held by leveraged players
- Similar rallies are not uncommon in China
  - Five occurrences of 100%+ rallies in less than a year since the early 1990s
- Since June peak, equities fell about 1/3rd as margin financing collapsed
Aggressive policy intervention stabilised prices for some time; China equities should head higher after the summer

- Aggressive policy intervention helped stabilise prices for some time
  - PBoC cut interest rates and RRR*
  - Equity stabilisation fund set up to buy shares
  - More than half of shares suspended trading
  - Large shareholders (>5%) banned from selling
  - China Financial Futures Exchange raised margin requirements for sell orders
  - Recent price action suggests sell-off is not over

- Long-term implications from the equity rally and fall for financial stability, growth and reform are limited

- Equities likely to be range-bound after recent declines, before heading higher after the summer
  - Improving macro outlook: >7% GDP growth with more fiscal stimulus and fixed investment uptick
  - Further monetary policy easing in H2-2015
  - Inflows likely as Chinese fundamentals improve and reforms progress

---

### Long-term implications of recent equity moves should be limited

<table>
<thead>
<tr>
<th>Impact</th>
<th>Rationale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial</td>
<td>M</td>
</tr>
<tr>
<td>Financial</td>
<td></td>
</tr>
<tr>
<td>Economic</td>
<td>L</td>
</tr>
<tr>
<td>Economic</td>
<td>M</td>
</tr>
<tr>
<td>Reform</td>
<td></td>
</tr>
<tr>
<td>Reform</td>
<td></td>
</tr>
<tr>
<td>Reform</td>
<td></td>
</tr>
</tbody>
</table>

### Corporate sales growth should rebound with nominal GDP

- Notes: (*) Reserve requirement ratio for large banks. (**) Wealth management products

The correction in commodity prices in the last months attracted significant attention

- Commodities have seen a sharp correction in the last couple of months
  - Commodities index down 10% since mid-May – back to 2002 levels
  - Iron ore led the decline (25% since mid-June, though has since recovered slightly)
  - Oil, copper, gold all fell 10-15%

- While the sell-off was relatively broad-based, some commodities held up well or even rallied
  - Commodities with tightening fundamentals have been more resilient – e.g., soybeans up over 10% in same period, following weather induced reduction in supply expectations

- The commodity sell-off coincided with the rise in financial market volatility
  - Greece negotiations and rising risk of Grexit
  - China equity market sell-off
The sell-off was overdone and exacerbated by China equities – but any recovery will be short-lived due to weak fundamentals

- The sell-off in commodities was overdone – and was likely exacerbated by falling Chinese equities
  - Sell-offs were simultaneous
  - Commodities likely used as a proxy for shorting equities as China authorities restricted trading
  - Fading concerns over Greece and the temporary stabilisation in China equities provided some brief reprieve
- That said, the sell-off in many cases was justified given weak fundamentals
  - Sell-off most marked in commodities with weak physical and financial fundamentals
  - Oil market oversupplied even without Iran oil
  - China overcapacity dampening demand for industrial metals
  - Fed tightening and strong dollar threaten Gold
- Any price recovery is unlikely to be sustainable as fundamental weakness remains
- As with China equities, commodities sell-off reflects lingering concerns over China and global growth

The commodity sell-off was simultaneous with the sell-off in China equities

Source: Bloomberg Finance LP, Deutsche Bank Research

2014 was the first year of material oversupply since the late 1990s, but won’t be the last

Note: Calculated as global supply minus global demand. Assumes production at 31 mmb/d and US production growth resuming in 2017 at an annual average rate of 0.6mbpd

Source: International Energy Agency, Deutsche Bank Research

Commodities Weekly: Exogenous Shocks – 10 July 2015
Inflation is low but has likely bottomed earlier this year, even if downside risks remain from the recent fall in commodity prices

- Inflation has likely bottomed earlier this year in the US and Europe

- Despite low levels currently, the underlying inflation outlook is more positive than earlier in the recovery
  - Headline inflation only just positive at 0.2% yoy in both US and eurozone
  - US inflation to rise given rising wage inflation, rising rent inflation from a tightening housing market, and steady inflation expectations
  - Euro weakness supports eurozone inflation
  - A more rapid rise in wages in the UK is supporting expectations for domestic inflation

- There are downside risks to inflation…
  - Recent commodity price sell-off could weigh on inflation going forward
  - Dollar strength, which should accelerate with Fed tightening, will weigh on US inflation

- …But overall we expect inflation to rise gradually toward target
  - Inflation at 1% in the eurozone and 1.2% in the US by end-15, rising to 1.7% in both by end-16
Growth momentum remains weak in EM but is robust in the eurozone and has bottomed out in the US

With the notable exception of the eurozone, global growth momentum remains generally weak

The start of the year has been disappointing from a growth point of view
- Weakness in Q1 in the US, China and broader EM
- Growth expectations for the year have been cut in many cases – we no longer expect the global economy to accelerate relative to 2014

While data suggest Q2 was stronger in the main regions, momentum remains generally weak
- PMIs trending down, even if still at healthy levels
- The proportion of countries reporting rising PMIs has fallen to less than 50%

In the US, macro data have rebounded and point to a pick-up in momentum in the second half

Momentum in the eurozone remains robust
Improving credit dynamics should support private domestic demand growth in the US and Europe, and also in China

- **US credit dynamics remain supportive** and should support domestic demand growth at rates 3%+ yoy
  - New borrowing levels remain low and lending standards are not overly loose
  - Trends observed in Fed’s SLO** are supportive
  - The US rate hike cycle has yet to begin
- **In the eurozone**, recent lending surveys suggest the best credit environment for growth since 2006
  - Spain and Italy appear to have the largest supports, with growth in Italy set to accelerate
  - ECB QE and strengthened bank balance sheets are set to support credit dynamics going forward
- **In China**, credit is supportive in the short-term, but longer-term prospects remain difficult
  - Credit impulse was negative in the past 2 years
  - Some lending indicators are stabilising, and credit growth together with policy easing should support growth in Q3
  - But the pace of credit growth must be reduced to achieve more sustainable credit dynamics

The US credit impulse* is positive on average, driving a sustained and robust recovery in domestic demand

Credit growth in China remains too high (over 1.5x nominal GDP growth) and must be reduced

Notes: (*) Credit impulse: Deutsche Bank’s non-consensus view is that it is not credit growth but rather the change in credit growth that is important for domestic demand growth. A slowdown in the pace of deleveraging boosts spending growth, even though credit growth is still negative. (**) Senior Loan Officer Survey. (***) Measure of credit to the real economy.
In the US, data have confirmed a rebound from a weak Q1

1. Data have improved during the quarter, suggesting better growth…

2. …Labour market still tightening…

3. …Housing upswing evident in recent data

- Q2 GDP forecasts rising as rebound from weak Q1 confirmed
  - Atlanta Fed GDPNow up to 2.4% from 0.8% in early June
  - Upward revisions driven primarily by stronger data for consumers and housing

- But uncertainties remain
  - June retail sales disappointed
  - Capex still weak
  - Global growth slow

- Labour market strength continues
  - Economy adding on average 200k+ jobs per month
  - Unemployment at 5.3%, soon below Fed’s NAIRU* estimate
  - Improvement also visible from broader measures of unemployment (U-6**)

- Key measure of wage inflation (ECI***) accelerating, pointing to less spare capacity

- Housing has rebounded recently, after disappointing this recovery
  - Housing starts near post-crisis high, 27% above last year
  - Existing home sales rose to post-crisis high in June

- Credit conditions, though still tight, have loosened and mortgage demand has risen

* NAIRU = non-accelerating inflation rate of unemployment, or full employment.
** U-6 underemployment rate includes people working part-time but would like a full-time job and people that are out of the labour force but want a job, in addition to traditional unemployment.
*** The employment cost index (ECI) is a preferred wage measure of the Fed.
The Fed remains on course to hike rates this year; we expect a gradual pace of hikes after the initial increase

- Recent Fed commentary confirms that 2015 hikes are firmly on the table
  - Data rebound, labour market strength and expectation that inflation will rise support this
  - In a close call, September still appears most likely, though odds of a later hike have risen
- Pace of hikes and terminal rate more important than timing of lift-off – pace should be gradual
  - Fed believes persistent headwinds from the financial crisis continue to restrain growth
  - Gradual hikes lower risk of slowing the economy too much and having to reverse hikes
- Market pricing is broadly in line for the timing of first hike – but there is a bigger gap on the pace of hikes
  - Market almost fully prices a hike in 2015; Fed dots suggest 1-2 hikes in 2015
  - However, by 2017 the market prices 3 hikes less than the Fed’s projections
- Regardless of the exact timing of the first hike, we do not expect economic momentum to be derailed
  - US economy has undergone significant healing during this recovery

Fed commentary from key members continues to signal rate hikes later this year…

“If the economy evolves as we expect, economic conditions likely would make it appropriate at some point this year to raise the federal funds rate target.”
Fed Chair Yellen, 15 July

“I still believe this will be the year for liftoff, and I still believe that waiting too long to raise rates poses its own risks.”
San Francisco Fed President Williams, 8 July

“If the data stays on the same course… I think we are on a trajectory for lift-off this year.”
New York Fed President Dudley , 28 June

…Market almost fully pricing a hike in 2015 and more than 1/3 odds lift-off occurs in September

Source: Bloomberg Finance LP, Deutsche Bank Research
The eurozone’s cyclical recovery continues, and positive credit dynamics provide further support and may offer some upside.

- The **cyclical upswing in the eurozone remains intact**
  - Data suggest upside risks to our 0.4% qoq growth forecast for Q2
- **Growth momentum remains robust**
  - SIREN* momentum peaked in June but remains close to this year’s highs
  - Little evidence of negative impact from Greece saga
- **Domestic demand likely to remain key driver of growth**, supported by credit recovery
  - Domestic demand providing most of Q2 growth
  - Credit conditions continue to improve, supporting further domestic demand growth
    - Easing credit supply conditions and rising demand, for both households and corporates
    - Combined measure of credit conditions near 2006’s historical high
  - Exports still lag, but should pick-up from H2-2015 as the effects of the weaker euro kick-in

---

**DB SIREN**: Current growth momentum near 2015 peak

**DB SIREN* macro momentum index**

Note: (*) Deutsche Bank’s SIREN momentum index captures the underlying growth momentum of the euro area economy in real time.
Source: Deutsche Bank Research

**Easiest credit conditions since 2006 should support domestic demand growth**

**Net balance* (>0 = easing)**

Note: (*) Net balance calculated as average of credit supply and demand for households and corporates
Source: ECB, Haver Analytics, Deutsche Bank Research
Growth momentum across EM remains weak as Fed hikes near and China slows – but the region is less vulnerable than in 2013

- Weak growth remains a key issue across EM
  - Growth momentum has continued to fall and is now the weakest since the crisis
  - Four countries are in recession (Brazil, Russia, Ukraine and Venezuela)
  - Momentum almost everywhere is soft with the exceptions of Mexico, Czech Republic, Hungary
- In coming months, the key risks to EM come from the prospect of Fed hikes and China’s slowdown – though lower commodities offer respite for some
- EM adjustment to Fed rate hikes will not be smooth but we do not expect crises – the region is less vulnerable than ahead of the 2013 taper tantrum
  - Better external resilience thanks to generally cheaper currencies, improved current accounts and increased FX reserves
  - Deterioration clearest in growth outlook
  - Of the fragile 5*, only India has really adjusted – Brazil, South Africa, Turkey remain vulnerable
- Weakening in China is worrying given the country’s increasingly important role as a growth driver in EM

Growth momentum in EM is now the weakest since the crisis

![Graph showing EM Composite PMI, 3mma](image)

Region is slightly less vulnerable than in 2013, with generally improved external resilience – but weak growth a key issue

![Graph showing DB vulnerability index](image)

Note: (*) India, Brazil, Indonesia, Turkey, South Africa were the 5 major EM particularly vulnerable at the time of the 2013 taper tantrum
In US equities, the outlook for earnings growth, which is needed for future returns given high valuations, is challenging

- S&P500 revisited record highs, but with multiples elevated, earnings are key for future returns
- With half of the earnings season completed, earnings growth is tracking slightly negative
  - The recent trend of solid earnings beats (66%) and weak revenue growth continues in Q2
  - But earnings are only beating because analysts revised down expectations into reporting season
- US earnings under pressure from several forces, as confirmed by corporate commentary
  - Strengthening dollar
  - Low (and now falling) commodity prices
  - Slow foreign growth
  - Elevated uncertainty with Greece and Fed rate hikes on the horizon
- Going forward, sectors benefitting from rising yields (e.g. banks) or with secular growth & ties to US economy (e.g. healthcare, tech) should outperform
- Energy, industrials and materials should continue to suffer from low oil prices, slowing Chinese demand

Corporate commentary confirms US earnings face several headwinds. Example: Caterpillar

...currency impacts from a stronger U.S. dollar are causing sales in many countries to translate into fewer dollars than we initially expected. While economic conditions in the United States are modestly positive, the global economy remains relatively stagnant. Continuing economic weakness in China and Brazil, as well as uncertainty in the Eurozone and over Greece, haven’t helped confidence. Prices for commodities like coal, iron ore and oil are not signaling an improvement in the short term.

Caterpillar CEO Doug Oberhelman

EPS growth set to fall in Q2 across various sectors

Source: IBES, Deutsche Bank Research
We see upside risk to European equities, and favour companies exposed to domestic demand

- We see upside risk to our year-end target of 410 for the Stoxx 600
  - Scope for upside surprise to private domestic demand in short-term, given credit improvement
  - However, given the deterioration in the global outlook, we have a clear preference for stocks with a strong exposure to eurozone demand

- Eurozone credit conditions improved in May
  - The pace of easing is only slightly below the strongest ever reading in January 2006
  - Expectations remain strong but indicate a marginal moderation going forward
  - Italy stands out as the pace of easing has accelerated further from record levels in April

- The survey provides substantial support to an optimistic outlook on Eurozone domestic demand
  - The implied range of the credit impulse in Q2 to Q4 suggests private domestic demand growth pacing ahead of consensus expectations
### DB forecasts

#### GDP growth (%)

<table>
<thead>
<tr>
<th></th>
<th>2013</th>
<th>2014</th>
<th>2015F</th>
<th>2016F</th>
</tr>
</thead>
<tbody>
<tr>
<td>Global</td>
<td>3.4</td>
<td>3.4</td>
<td>3.2</td>
<td>3.7</td>
</tr>
<tr>
<td>US</td>
<td>2.2</td>
<td>2.4</td>
<td>2.3</td>
<td>3.0</td>
</tr>
<tr>
<td>Eurozone</td>
<td>-0.4</td>
<td>0.9</td>
<td>1.4</td>
<td>1.6</td>
</tr>
<tr>
<td>Germany</td>
<td>0.1</td>
<td>1.6</td>
<td>1.6</td>
<td>1.7</td>
</tr>
<tr>
<td>Japan</td>
<td>1.6</td>
<td>-0.1</td>
<td>1.1</td>
<td>1.8</td>
</tr>
<tr>
<td>UK</td>
<td>1.7</td>
<td>3.0</td>
<td>2.5</td>
<td>2.3</td>
</tr>
<tr>
<td>China</td>
<td>7.7</td>
<td>7.4</td>
<td>7.0</td>
<td>6.7</td>
</tr>
<tr>
<td>India</td>
<td>6.9</td>
<td>7.1</td>
<td>7.5</td>
<td>7.5</td>
</tr>
<tr>
<td>EM (Asia)</td>
<td>6.5</td>
<td>6.4</td>
<td>6.3</td>
<td>6.2</td>
</tr>
<tr>
<td>EM (LatAm)</td>
<td>2.7</td>
<td>0.8</td>
<td>0.0</td>
<td>1.8</td>
</tr>
<tr>
<td>EM (CEEMEA)</td>
<td>2.6</td>
<td>2.4</td>
<td>1.2</td>
<td>2.2</td>
</tr>
<tr>
<td>EM</td>
<td>5.0</td>
<td>4.6</td>
<td>4.2</td>
<td>4.7</td>
</tr>
<tr>
<td>DM</td>
<td>1.3</td>
<td>1.7</td>
<td>1.9</td>
<td>2.3</td>
</tr>
</tbody>
</table>

#### CPI inflation, YoY* (%)

<table>
<thead>
<tr>
<th></th>
<th>2013</th>
<th>2014</th>
<th>2015F</th>
<th>2016F</th>
</tr>
</thead>
<tbody>
<tr>
<td>US</td>
<td>1.5</td>
<td>1.6</td>
<td>0.4</td>
<td>2.6</td>
</tr>
<tr>
<td>Eurozone</td>
<td>1.4</td>
<td>0.4</td>
<td>0.3</td>
<td>1.4</td>
</tr>
<tr>
<td>Japan</td>
<td>0.4</td>
<td>2.7</td>
<td>0.9</td>
<td>1.0</td>
</tr>
<tr>
<td>UK</td>
<td>2.6</td>
<td>1.5</td>
<td>0.5</td>
<td>1.6</td>
</tr>
<tr>
<td>China</td>
<td>2.6</td>
<td>2.0</td>
<td>1.6</td>
<td>2.7</td>
</tr>
<tr>
<td>India</td>
<td>10.7</td>
<td>6.7</td>
<td>5.3</td>
<td>5.7</td>
</tr>
</tbody>
</table>

* CPI (%) forecasts are period averages

**CEEMEA:** Czech Rep., Hungary, Poland, Russia, Turkey, South Africa, Israel, Romania, Kazakhstan, Ukraine, Egypt, Saudi Arabia and UAE

**LATAM:** Argentina, Brazil, Chile, Colombia, Mexico, Peru, Venezuela

### Key market metrics

<table>
<thead>
<tr>
<th></th>
<th>Current</th>
<th>Q4-15</th>
<th>Q4-16</th>
</tr>
</thead>
<tbody>
<tr>
<td>US 10Y yield (%)</td>
<td>2.23</td>
<td>2.45</td>
<td>3.00</td>
</tr>
<tr>
<td>EUR 10Y yield (%)</td>
<td>0.69</td>
<td>1.00</td>
<td>1.50</td>
</tr>
<tr>
<td>EUR/USD</td>
<td>1.111</td>
<td>1.00</td>
<td>0.90</td>
</tr>
<tr>
<td>USD/JPY</td>
<td>123</td>
<td>126</td>
<td>130</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>2,070</td>
<td>2,150</td>
<td>2,300</td>
</tr>
<tr>
<td>Stoxx 600</td>
<td>386</td>
<td>410</td>
<td></td>
</tr>
<tr>
<td>Oil WTI (USD/bbl)</td>
<td>47.6</td>
<td>58</td>
<td>67</td>
</tr>
<tr>
<td>Oil Brent (USD/bbl)</td>
<td>53.7</td>
<td>63</td>
<td>72</td>
</tr>
</tbody>
</table>

Current prices as of 27-Jul UK market close

### Central Bank policy rate (%)

<table>
<thead>
<tr>
<th></th>
<th>Current</th>
<th>Q4-15</th>
<th>Q4-16</th>
</tr>
</thead>
<tbody>
<tr>
<td>US</td>
<td>0-0.25</td>
<td>0.50-0.75</td>
<td>1-1.25</td>
</tr>
<tr>
<td>Eurozone</td>
<td>0.05</td>
<td>0.05</td>
<td>0.05</td>
</tr>
<tr>
<td>Japan</td>
<td>0-0.1</td>
<td>0-0.1</td>
<td>0-0.1</td>
</tr>
<tr>
<td>UK</td>
<td>0.50</td>
<td>0.50</td>
<td>1.25</td>
</tr>
<tr>
<td>China</td>
<td>2.00</td>
<td>1.75</td>
<td>1.75</td>
</tr>
<tr>
<td>India</td>
<td>7.25</td>
<td>7.00</td>
<td>7.00</td>
</tr>
</tbody>
</table>

**ASIA:** China, HK, India, Indonesia, Korea, Malaysia, Philippines, Singapore, Sri Lanka, Taiwan, Thailand, Vietnam

**DM:** US, Japan, Eurozone, UK, Denmark, Norway, Sweden, Canada, Australia, New Zealand, Switzerland

Source: Deutsche Bank Research
Appendix 1
Important Disclosures
Additional Information Available upon Request

*Prices are current as of the end of the previous trading session unless otherwise indicated and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Other information is sourced from Deutsche Bank, subject companies, and other sources. For disclosures pertaining to recommendations or estimates made on securities other than the primary subject of this research, please see the most recently published company report or visit our global disclosure look-up page on our website at http://gm.db.com/ger/disclosure/DisclosureDirectory.eqsr

Analyst Certification

This report covers more than one security and was contributed to by more than one analyst. The views expressed in this report accurately reflect the views of each contributor to this compendium report. In addition, each contributor has not and will not receive any compensation for providing a specific recommendation or view in this compendium report. Marcos Arana/Wolf-von Rotberg

Attribution

The Authors wish to acknowledge the contributions made by Shakun Guleria in the preparation of this report.
Regulatory Disclosures

1. Important Additional Conflict Disclosures
Aside from within this report, important conflict disclosures can also be found at https://gm.db.com/equities under the “Disclosures Lookup” and “Legal” tabs. Investors are strongly encouraged to review this information before investing.

2. Short-Term Trade Ideas
Deutsche Bank equity research analysts sometimes have shorter-term trade ideas (known as SOLAR ideas) that are consistent or inconsistent with Deutsche Bank’s existing longer term ratings. These trade ideas can be found at the SOLAR link at http://gm.db.com.
Additional Information

The information and opinions in this report were prepared by Deutsche Bank AG or one of its affiliates (collectively "Deutsche Bank"). Though the information herein is believed to be reliable and has been obtained from public sources believed to be reliable, Deutsche Bank makes no representation as to its accuracy or completeness.

Deutsche Bank may consider this report in deciding to trade as principal. It may also engage in transactions, for its own account or with customers, in a manner inconsistent with the views taken in this research report. Others within Deutsche Bank, including strategists, sales staff and other analysts, may take views that are inconsistent with those taken in this research report. Deutsche Bank issues a variety of research products, including fundamental analysis, equity-linked analysis, quantitative analysis and trade ideas. Recommendations contained in one type of communication may differ from recommendations contained in others, whether as a result of differing time horizons, methodologies or otherwise.

Analysts are paid in part based on the profitability of Deutsche Bank AG and its affiliates, which includes investment banking revenues.

Opinions, estimates and projections constitute the current judgment of the author as of the date of this report. They do not necessarily reflect the opinions of Deutsche Bank and are subject to change without notice. Deutsche Bank has no obligation to update, modify or amend this report or to otherwise notify a recipient thereof if any opinion, forecast or estimate contained herein changes or subsequently becomes inaccurate. This report is provided for informational purposes only. It is not an offer or a solicitation of an offer to buy or sell any financial instruments or to participate in any particular trading strategy. Target prices are inherently imprecise and a product of the analyst’s judgment. The financial instruments discussed in this report may not be suitable for all investors and investors must make their own informed investment decisions. Prices and availability of financial instruments are subject to change without notice and investment transactions can lead to losses as a result of price fluctuations and other factors. If a financial instrument is denominated in a currency other than an investor’s currency, a change in exchange rates may adversely affect the investment. Past performance is not necessarily indicative of future results. Unless otherwise indicated, prices are current as of the end of the previous trading session, and are sourced from local exchanges via Reuters, Bloomberg and other vendors. Data is sourced from Deutsche Bank, subject companies, and in some cases, other parties.

Macroeconomic fluctuations often account for most of the risks associated with exposures to instruments that promise to pay fixed or variable interest rates. For an investor who is long fixed rate instruments (thus receiving these cash flows), increases in interest rates naturally lift the discount factors applied to the expected cash flows and thus cause a loss. The longer the maturity of a certain cash flow and the higher the move in the discount factor, the higher will be the loss. Upside surprises in inflation, fiscal funding needs, and FX depreciation rates are among the most common adverse macroeconomic shocks to receivers. But counterparty exposure, issuer creditworthiness, client segmentation, regulation (including changes in assets holding limits for different types of investors), changes in tax policies, currency convertibility (which may constrain currency conversion, repatriation of profits and/or the liquidation of positions), and settlement issues related to local clearing houses are also important risk factors to be considered. The sensitivity of fixed income instruments to macroeconomic shocks may be mitigated by indexing the contracted cash flows to inflation, to FX depreciation, or to specified interest rates—these are common in emerging markets. It is important to note that the index fixings may be by construction—lag or mis-measure the actual move in the underlying variables they are intended to track. The choice of the proper fixing (or metric) is particularly important in swaps markets, where floating coupon rates (i.e., coupons indexed to a typically short-dated interest rate reference index) are exchanged for fixed coupons. It is also important to acknowledge that funding in a currency that differs from the currency in which coupons are denominated carries FX risk. Naturally, options on swaps (swaptions) also bear the risks typical to options in addition to the risks related to rates movements.

Derivative transactions involve numerous risks including, among others, market, counterparty default and illiquidity risk. The appropriateness or otherwise of these products for use by investors is dependent on the investors’ own circumstances including their tax position, their regulatory environment and the nature of their other assets and liabilities, and as such, investors should take expert legal and financial advice before entering into any transaction similar to or inspired by the contents of this publication. The risk of loss in futures trading and options, foreign or domestic, can be substantial. As a result of the high degree of leverage available in futures and options trading, losses may be incurred that are greater than the amount of funds initially deposited. Trading in options involves risk and is not suitable for all investors. Prior to buying or selling an option investors must review the “Characteristics and Risks of Standardized Options”, at http://www.optionsclearing.com/about/publications/character-risks.jsp. If you are unable to access the website please contact your Deutsche Bank representative for a copy of this important document.

Participants in foreign exchange transactions may incur risks arising from several factors, including the following: (i) exchange rates can be volatile and are subject to large fluctuations; (ii) the value of currencies may be affected by numerous market factors, including world and national economic, political and regulatory events, events in equity and debt markets and changes in interest rates; and (iii) currencies may be subject to devaluation or government imposed exchange controls which could affect the value of the currency. Investors in securities such as ADRs, whose values are affected by the currency of an underlying security, effectively assume currency risk.

Unless governing law provides otherwise, all transactions should be executed through the Deutsche Bank entity in the investor’s home jurisdiction.

United States: Approved and/or distributed by Deutsche Bank Securities Incorporated, a member of FINRA, NFA and SIPC. Non-U.S. analysts may not be associated persons of Deutsche Bank Securities Incorporated and therefore may not be subject to FINRA regulations concerning communications with subject company, public appearances and securities held by the analysts. Germany: Approved and/or distributed by Deutsche Bank AG, a joint stock corporation with limited liability incorporated in the Federal Republic of Germany with its principal office in Frankfurt am Main. Deutsche Bank AG is authorized under German Banking Law (competent authority: European Central Bank) and is subject to supervision by the European Central Bank and by BaFin, Germany’s Federal Financial Supervisory Authority.

United Kingdom: Approved and/or distributed by Deutsche Bank AG acting through its London Branch at Winchester House, 1 Great Winchester Street, London EC2N 2DB. Deutsche Bank AG in the United Kingdom is authorised by the Prudential Regulation Authority and is subject to limited regulation by the Prudential Regulation Authority and Financial Conduct Authority. Details about the extent of our authorisation and regulation are available on request.

Hong Kong: Distributed by Deutsche Bank AG, Hong Kong Branch.

Korea: Distributed by Deutsche Securities Korea Co.


Singapore: by Deutsche Bank AG, Singapore Branch or Deutsche Securities Asia Limited, Singapore Branch (One Raffles Quay #18-00 South Tower Singapore 048583, +65 6423 8001), which may be contacted in respect of any matters arising from, or in connection with, this report. Where this report is issued or promulgated in Singapore to a person who is not an accredited investor, expert investor or institutional investor (as defined in the applicable Singapore laws and regulations), they accept legal responsibility to such person for its contents.

Japan: Approved and/or distributed by Deutsche Securities Inc.(DSI), registered as a financial instruments dealer by the Head of the Kanto Local Finance Bureau (Kinsho) No. 117. Member of associations: JSDA, Type II Financial Instruments Firms Association, The Financial Futures Association of Japan, and Japan Investment Advisers Association. Commissions and risks involved in stock transactions - for stock transactions, we charge stock commissions and consumption tax by multiplying the transaction amount by the commission rate agreed with each customer. Stock transactions can lead to losses as a result of share price fluctuations and other factors. Transactions in foreign stocks can lead to additional losses stemming from foreign exchange fluctuations. We may also charge commissions and fees for certain categories of investment advice, products and services. Recommended investment strategies, products and services carry the risk of losses to principal and other losses as a result of changes in market and/or economic trends, and/or fluctuations in market value. Before deciding on the purchase of financial products and/or services, customers should carefully read the relevant disclosures, prospectuses and other documentation. Moody’s®, "Standard & Poor’s”, and “Fitch” mentioned in this report are not registered credit rating agencies in Japan unless Japan or “Nippon” is specifically designated in the name of the entity. Reports on Japanese listed companies not written by analysts of DSI are written by Deutsche Bank Group’s analysts with the coverage companies specified by DSI. Some of the foreign securities stated on this report are not disclosed according to the Financial Instruments and Exchange Law of Japan.

Malaysia: Deutsche Bank AG and/or its affiliate(s) may maintain positions in the securities referred to herein and may from time to time offer those securities for purchase or may have an interest to purchase such securities. Deutsche Bank may engage in transactions in a manner inconsistent with the views discussed herein.

Qatar: Deutsche Bank AG in the Qatar Financial Centre (registered no. 00032) is regulated by the Qatar Financial Centre Regulatory Authority. Deutsche Bank AG - QFC Branch may only undertake the financial services activities that fall within the scope of its existing GFCA license. Principal place of business in the QFC: Qatar Financial Centre, Tower, West Bay, Level 5, PO Box 14928, Doha, Qatar. This information has been distributed by Deutsche Bank AG. Related financial products or services are only available to Business Customers, as defined by the Qatar Financial Centre Regulatory Authority.

Russia: This information, interpretation and opinions submitted herein are not in the context of, and do not constitute, any appraisal or evaluation activity requiring a license in the Russian Federation. Kingdom of Saudi Arabia: Deutsche Securities Saudi Arabia LLC Company, (registered no. 07073-37) is regulated by the Capital Market Authority. Deutsche Securities Saudi Arabia may only undertake the financial services activities that fall within the scope of its existing CMA license. Principal place of business in Saudi Arabia: King Fahad Road, Al Olaya District, P.O. Box 301809, Faisaliah Tower - 17th Floor, 11372 Riyadh, Saudi Arabia.

United Arab Emirates: Deutsche Bank AG in the Dubai International Financial Centre (registered no. 00045) is regulated by the Dubai Financial Services Authority. Deutsche Bank AG - DIFC Branch may only undertake the financial services activities that fall within the scope of its existing DFSA license. Principal place of business in the DIFC: Dubai International Financial Centre, The Gate Village, Building 5, PO Box 504902, Dubai, U.A.E. This information has been distributed by Deutsche Bank AG. Related financial products or services are only available to Professional Clients, as defined by the Dubai Financial Services Authority.

Australia: Retail clients should obtain a copy of a Product Disclosure Statement (PDS) relating to any financial product referred to in this report and consider the PDS before making any decision about whether to acquire the product. Please refer to Australian specific research disclosures and related information at https://australia.db.com/australia/content/research-information.html

Australia and New Zealand: This research, and any access to it, is intended only for “wholesale clients” within the meaning of the Australian Corporations Act and New Zealand Financial Advisors Act respectively. Additional information relative to securities, other financial products or issuers discussed in this report is available upon request. This report may not be reproduced, distributed or published by any person for any purpose without Deutsche Bank’s prior written consent. Please cite source when quoting.