Macro views

World
- We expect global growth to accelerate to +3.9% in 2018, marginally faster than 2017 which was the fastest in a decade, with the improvement led by the US and emerging markets. We expect the Eurozone to continue growing above potential, but do not anticipate any further acceleration. In China, we expect growth to slow, and are more worried about inflation and financial risks than consensus.
- This remains a very robust and broad-based economic backdrop. However, 2018 should mark the peak of the current cyclical expansion, and growth should decelerate from 2019.
- Growth to accelerate in 2018 to +2.7%, the fastest pace since 2015, boosted around 0.3-0.4pp by Trump’s tax reform. We note upside risks to this estimate given the potential for increased fiscal spending if Congress ends up raising its spending caps in the FY2018 budget.
- Growth momentum remains very strong. Fourth quarter 2017 GDP printed below our expectations, but the miss was attributable to inventories and we expect growth to compensate this quarter.
- Dollar weakness (7% depreciation on a trade-weighted basis in 2017) should add a few tenths of a percentage point to both inflation and growth this year.

Eurozone
- Eurozone growth has risen to the fastest pace in a decade. We forecast +2.3% growth for 2018, in line with consensus. We expect growth to decelerate in the second half of the year as tailwinds fade.
- The current pace of growth is far above our estimate of potential growth, which is around +1.0%. Cyclical momentum will naturally decline as output gaps close; financial conditions will tighten as the ECB withdraws accommodation; the boost from net exports will fade as Asia decelerates; and the stronger euro will drag on growth.
- German wage negotiations point to wage rises at the high-end of the range which should boost policymakers’ confidence that tightening labour markets will lead to higher inflation.
- The political agenda remains busy, with Germany’s government formation, Brexit negotiations, the Italian election and the debate on EU reform. On all fronts, though, our baseline scenario is for little fundamental change or macro impact.

China
- China’s economy to continue decelerating in 2018. We forecast +6.3% growth vs. +6.9% for 2017. We see risks balanced on both sides. Fiscal and monetary policies will remain tight and investment will continue to slow. This will be partially balanced by strong wage growth and consumer spending.
- Assuring growth decelerates as we expect, PBoC should ease monetary policy in H2 (we see two RRR cuts) to prop up growth again.
- We expect the renminbi to remain roughly stable versus the PBoC’s trade-weighted basket, and strengthen vs. the dollar. Capital controls are also tighter than we expect.
- We see two major risks to our base case. The first is inflation: core inflation reached a 6-year high in 2017 and could rise further this quarter; this could prompt PBoC to raise rates (in the past we have seen hikes when CPI reached +3.0%). The second is financial stability on the back of high leverage in the financial sector. The system has grown more complex, credit quality has deteriorated, and IMF stress tests showed potential capital shortfalls.

Emerging Markets
- EM growth to remain broadly positive in 2018, but regional cycles becoming more differentiated: Latin America in a more favourable cyclical position than most of EM Asia and, to a lesser extent, CEEMEA.
- Robust fundamentals of strong momentum, favourable external environment will continue supporting continued portfolio inflows. A weaker dollar offsets rising US rates.
- The key negative challenge is one of political risk escalation, given a charged event calendar this year.

Monetary Policy
- **Fed**: expect 4 rate hikes in 2018, more than FOMC guidance (3) and than market pricing (2.5).
- **ECB**: slow exit to continue. No new measures until mid-year; QE to end in 2018, first hike in mid-2019.
- **BoJ**: not under pressure to act, no change expected in target short rate or yield curve control policy.
- **BoE**: no policy change through 2018; risk is earlier tightening, with May hike possible.
- **PBoC**: policy steady through H1-2018, followed by 100 bps of RRR cuts as growth slows in H2. Risk of policy tightening if inflation surprises to the upside.
- **EM**: regional divergence – tightening in Asia contrasts with room for rate cuts in LatAm.
The House View: Snapshot (Continued)
7 February 2018

Key downside risks
- Higher than expected inflation: prompts fast monetary policy tightening, disrupts markets.
- Global growth disruption: global equity correction weighs on sentiment / wealth, triggers a recession.
- China slowdown: higher inflation, a policy mistake, or financial stress leads to sharp growth slowdown, with global ramifications though trade, financial channels.
- Financial stability: tighter policy / slower growth causes financial sector instability, especially where leverage is high.

Key themes
- A healthy pullback: sell-off in risk assets was healthy and was long overdue. But fundamentals remain supportive and magnitude appears overdone.
- Return of market volatility: as typified by the recent episode, pullbacks and volatility will become more common as investors adjust to rising interest rates and capital is allocated out of risk assets and into higher-yielding fixed income. But overall volatility will remain low.
- Cyclical recovery reaches its peak: global growth will accelerate in 2018, but for many countries growth will plateau or decelerate in 2018. As such this year should mark the peak of the current cyclical expansion, and growth should decelerate from 2019.
- Steady inflationary pressures: we expect inflation to start picking up more noticeably this year, as output gaps close. Leading indicators suggest prices will accelerate from Q2 in the US; we expect similar dynamics in Europe. In EM, energy and food prices may rise, partially attributable to positive base effects, pressuring headline inflation.
- The end of QE: 2018 (almost) the last year of QE. ECB purchases should end in Q4; the BoJ’s volume of purchases has slowed amid its YCC framework; the Fed will continue to let its balance sheet runoff accelerate. The end of QE will significant, given the its earlier impact on term premia and risk assets.

Key macro and markets forecasts

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<tr>
<th>GDP growth (%)</th>
<th>Central Bank policy rate (%)</th>
<th>Key market metrics</th>
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<td></td>
<td>Current</td>
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<td>China</td>
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<tr>
<td>Oil</td>
<td>Oil WTI (USD/bbl)</td>
<td>63.4</td>
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Recent publications
- The House View: A healthy pullback, 7-Feb-2018
- The House View: Happy holidays, 11-Dec-2017
- The House View: Back to school, 17-Sep-2017