



### Macro views



#### World

- Global growth remains solid, but has slowed over the last month in Europe, China, and emerging markets. The US remains the bastion of global growth, despite some softer data and tighter financial conditions.
- Even with recent market turbulence, financial conditions remain accommodative, and fiscal policy will remain supportive. As long as Europe and China manage their slowdowns as we expect, the world economy should be able to maintain its steady growth. EM growth has moderated, but not collapsed.
- Aggressive quantitative tightening, political risk ("crash Brexit" or Italy debt vulnerability shocks) and sharp correction in financial market poses key downside risks



#### United States

- In 3Q, US GDP grew at an annualized rate of 3.5%, of which 2.1pp was attributable to inventories while capex contributed only 0.1pp. The outlook still remains strong over the medium-term. Expect growth to accelerate in 2018 to +2.9%, boosted by tax cuts, fiscal spending, rebound in consumer spending, etc.
- There are some downside risks on the horizon in the form of tighter financial conditions due to Fed rate hikes, elevated corporate debt levels, and uncertainty around trade policy.
- Our comprehensive recession model, which uses financial conditions to predict the likelihood of a recession, points to very low risks. Risk are more elevated over longer time period, e.g. over next 2 or 3 years, but this model is historically more liable to "false positives."



#### Eurozone

- The health of the euro area recovery has come under scrutiny in the past 2-3 months. This was reflected in disappointing Q3 GDP of 0.2% qoq, the two-year lows in manufacturing and composite PMIs in Oct, and SIREN Surprise indicator moving back into meaningfully negative territory. This data flow suggests increasing downside risk to near-term growth.
- We lowered German 2019 GDP forecast to 1.3%, from previous 1.7%, reflecting auto distortions but also softer export expectations and sentiment.
- Stronger wage growth and still-easy financial conditions point to domestic resilience. However, with credit flows flat since the start of 2018, bank credit has turned from a support to a challenge for 2019 above-trend consensus growth expectations. We expect 2019 euro area growth of 1.7%.



#### China

- China's Q3 real GDP growth slowed to 6.5% yoy from 6.7% in Q2 (consensus 6.6%, DB estimate 6.5%). This was largely driven by lower industrial output from auto production and weak construction activity.
- Q4 has started on a balanced note, with latest data showing resilience. October exports and industrial production came in stronger than expected, though weakness in auto sales continued. Manufacturing sector investment strengthened further to 9.1% ytd yoy in Oct.
- We think the government may keep the current policy stance in Q4 as growth is on track to achieve the annual growth target. For 2019, we revise down Q1 growth to 6.2% to reflect headwinds from exports and land market. Recently-announced personal income tax cuts, estimated to be ~0.5% of GDP, should boost retail sales and help offset downside risks to growth from the trade war.



#### Emerging Markets

- EM growth fears have been postponed for now. Policy responses in the more important idiosyncratic cases (e.g. Turkey) have been reassuring, but a long - and increasingly risky - adjustment lies ahead.
- The back-loading of recession fears may pave the way for a technical rebound. However, there is no room for complacency as volatility is set to increase and the funding bar is raised.
- Differentiation across cycles is notable. LatAm has brought good and bad news. Brazilian election outcome has opened the door for reforms while news flow in Mexico is concerning. In EMEA, economic activity is softening in Russia (further sanctions from the US) while confidence shock has dented Turkey's growth dynamics. In Asia, policy is prioritizing growth, while officials try to ensure financial stability.

#### Monetary

#### Policy

- Fed:** expect 1 more hike in 2018 and 4 hikes in 2019
- ECB:** QE to end in Dec-2018. First 15bp depo rate hike in Sep-2019
- BoJ:** Discussion in next 2-3 years on changing policy goal from inflation to growth or price level
- BoE:** No more hikes in 2018 as growth and MPC focus now on Brexit developments
- PBoC:** Three reserve requirement ratio cuts in 2019

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- Key downside risks**
- **Crash Brexit:** The publication of the Brexit Withdrawal Agreement between the UK and EU27 generated considerable political volatility in the UK, threatening the ratification process by the UK Parliament resulting in a disorderly Brexit. There is also risk of a leadership challenge for PM May.
  - **Italy:** Continued confrontation between Italy and the European Commission over Italy's fiscal plan could heighten political uncertainties and volatility in European assets and potentially result in a broader eurozone sovereign debt crisis.
  - **Trade conflict:** Failure to secure trade deal between US-China on the sidelines of G20 Summit, imposition of tariffs on remaining China imports, or escalation of conflicts beyond trade and tariff resulting into a full blown economic war.

- Key themes**
- **Brexit:** In line with our baseline view, the UK and EU have reportedly secured a deal on Brexit Withdrawal Agreement. However, more difficult tasks lies ahead of securing UK Parliamentary support for the deal over the coming weeks. The initial political reaction is not encouraging. While not our base case, we believe that the market is materially under-pricing the prospect of a disorderly Brexit.
  - **Italy:** Italy's growth and deficit projections are overly optimistic. The Commission is likely to implement its Excessive Deficit Procedure over the next few weeks, potentially leading to fines. Another eurozone sovereign debt crisis will be likely, unless the confrontational approach by both parties gives way to greater co-operative engagement.
  - **Trade war:** Recent rhetoric on US-China trade conflict have somewhat softened, following a call between the US and Chinese Presidents. We see a 50% likelihood of a deal being reached on Nov 29. A deal may end a battle for now but US-China relations will likely remain tense over the coming years.

**Market views**

- Market sentiment**
- Markets remain supported by strong macro fundamentals.
  - Episodes of higher volatility will be more common as central banks remove extraordinary accommodation.

- Equities**
- **Bullish US equities.** Earnings are strong and underlying growth is robust.
  - Current conditions appear oversold and inconsistent with the macro outlook.

- 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 expect yields to rise as ECB ends QE and macro momentum continues.

- FX**
- **Dollar pressured longer term, near-term balanced.** Our strategic view is for further dollar weakness over the next year against major currencies. However, we expect the dollar to rally further vs. Chinese yuan.
  - **Neutral on euro for now.** Flows have negatively impacted the euro, outweighing other tailwinds. We still expect growth momentum to rebound and for the ECB to tighten policy next year.
  - **Neutral yen.** Flows have not turned yet and the yen is unlikely to break out of recent range for now.

- Credit**
- **Prefer EUR over USD.** USD HY still look expensive relative to our models, while EUR credit looks cheap relative to volatility-implied spreads. Volatility will likely recover, but we expect it to be structurally higher.

- EM**
- **Technical rebound possible.** Policy responses in the more important idiosyncratic EM cases have been reassuring, but a long - and increasingly risky - adjustment lies ahead. We see room for retracement in EM FX and turn tactically more constructive on EM credit. In Local Fixed Income, increased term-premium provides a buffer for performance.

- Oil**
- 2019 oil market is unlikely to show major oversupply, unless demand growth falls below +1.3mmb/day yoy. USD 68/bbl is a reasonable measure of long-term equilibrium based on incentive costs.

**Key macro and markets forecasts**

	GDP growth (%)				Central Bank policy rate (%)				Key market metrics					
	2016	2017	2018F	2019F		Current	2017	2018F	2019F	Current	Q4-18F	Q2-19F	Q4-19F	
Global	3.2	3.8	3.8	3.8	US	2.125	1.375	2.375	3.375	US 10Y yield (%)	3.09	3.50	3.75	3.60
US	1.6	2.2	2.9	2.8	Eurozone	0.00	0.00	0.00	0.00	Germany 10Y yield (%)	0.40	0.70	0.91	1.14
Eurozone	1.9	2.5	2.0	1.7	Japan	-0.10	-0.10	-0.10	-0.10	EUR/USD	1.13	1.13	1.25	1.30
Germany	2.2	2.2	1.6	1.3	UK	0.75	0.50	0.75	1.00	USD/JPY	113	112	103	100
Japan	1.0	1.7	0.9	0.6	China	1.50	1.50	1.50	1.50	S&P 500	2,694	3,000		
UK	1.8	1.7	1.3	1.6						Stoxx 600	357	395		
China	6.7	6.9	6.6	6.3						Oil WTI (USD/bbl)	57.2	72	70	68
										Oil Brent (USD/bbl)	67.3	80	78	76

Current prices as of 15-Nov-2018

- Recent publications**
- [The House View – US keeping solid global growth alive](#), 15-November 2018
  - [The House View – Markets after the recent sell-off](#), 16-October 2018
  - [The House View: Mind the \(political\) hurdles](#), 10- September-2018