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Group Economics

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Will tailwinds offset headwinds on time?

- **If a US-China trade deal becomes real, the number one risk for the global economy eases**
- **The more dovish monetary policy stance of the main central banks takes time to filter through, but is expected to gradually give economies tailwind later this year**
- **Meanwhile trade distortions are starting to hit manufacturing export orders sharply, …**
- **… hurting European export-driven economies most**
- **Tight labor markets, rising wages and low unemployment keep consumers spending and most economies resilient, …**
- **… but for how long will they hold?**

At the start of the week, on Sunday evening, US President Trump galvanized markets with a tweet announcing a delay of the US increase in tariffs scheduled for March 1st. If negotiations keep making further headway, he said, this could lead to an agreement in Trumps' Mar al Lago Resort 'soon'. Secretary Mnuchin mentioned a tentative planning for this meeting late March. Chinese stocks rallied immediately after. Could there be light at the end of the trade war tunnel?
Reinforcing the good news on trade are a number of key events such as the likely delay of Article 50 on Brexit, the dovish shift of known hawks Weidmann and Knot at the ECB, and the more accommodating stance of central banks globally.

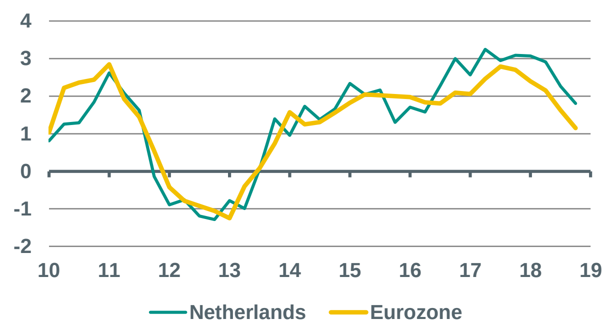
Although these events ease the downside risks to the global economy, we feel that it is not yet enough to provide a significant tailwind in the next few quarters. The political good news is highly uncertain, and policy shifts take time to feed through.

Meanwhile, trade distortions between China and the US, ongoing political uncertainty surrounding Brexit and slower growth in China's and many other emerging Asian economies reflecting past tightening of financial conditions are causing a sharp downward revision of growth expectations, especially in the most export driven European economies of Germany and The Netherlands.

Steeply declining manufacturers export orders expectations (such as in China's manufacturing PMI for February), are the main drivers of the decline. The Eurozone manufacturing PMI dropped below 50 for the first time in nearly six years in February.

Economic growth has decelerated sharply

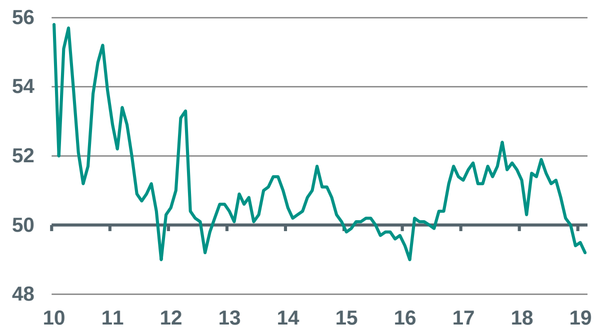
GDP, % yoy



Source: Thomson Reuters Datastream

China: PMI mfg

Index, 50=neutral



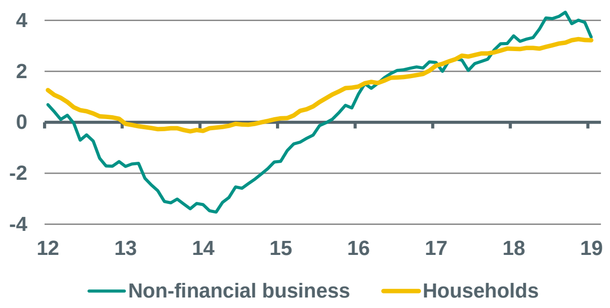
Source: Bloomberg

Fears of protectionism creeping into economic data

The slowdown in global growth and uncertainty about trade policy has led companied to scale back their investment plans. This leads to lower demand for bank loans over time. Data published this week saw bank lending growth losing momentum.

Lending growth in the Eurozone

% yoy, adjusted for securisation and asset sales



Source: Bloomberg

As we expect the growth of European economies to stay below trend at least until the summer, lending growth to non-financial businesses is set to decrease further, strengthening the case for a new round of cheap TLTRO funding provided by the ECB (read more on this here).

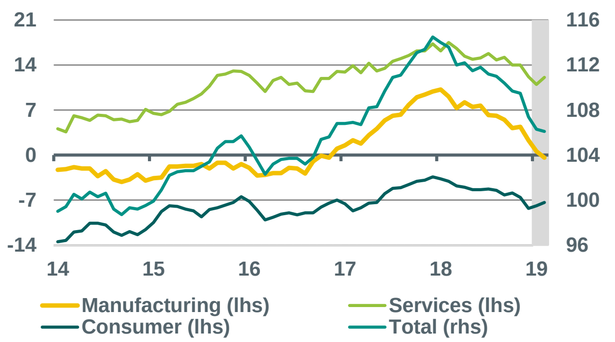
While TLTRO brings stable and reliable funding in times of market turbulence, there are also risks to keep in mind. Lenders might for instance signal credit weakness if funding through TLTRO is being perceived as reflecting an inability to get funding elsewhere at reasonable interest rates.

Thus far, domestic resilience has prevented worse

Given the sharp slowdown in global trade, why is GDP in the advanced economies still moderately expanding? Part of the answer can be found in domestic resilience that is coming from the services industry and from consumers, who have been feeling rather secure in strong labor markets, with low unemployment and wage increases. A breakdown of this weeks' economic sentiment data on the Eurozone shows that the negative economic sentiment is almost solely driven by negative manufacturing sentiments. The service industries and consumers have proven to be resilient if not upbeat in their judgement of their own and overall economic prospects. The same holds for Germany and the US, as Nick Kounis wrote in our previous macro weekly.

Eurozone sentiment

% yoy, adjusted for securisation and asset sales



Source: Bloomberg

In the US, consumers have proven particularly important in keeping economic growth in pace. After a very long government shutdown, which left us guessing on part of the US and the global picture, we finally received the GDP data on the US in Q4 this Thursday. While the annualized growth pace of 2.6 percent in the last quarter was less than previous quarters, it does generate an annual growth rate of 2.9 percent, which is just below the target of the American president and our own forecast.

GDP growth

	18Q1	18Q2	18Q3	18Q4
Real GDP (% yoy)	2.6	2.9	3.0	3.1
% qoq, SAAR				
Real GDP	2.2	4.2	3.4	2.6
Consumer spending	0.5	3.8	3.5	2.8
Government spending	1.5	2.5	2.6	0.4
Private Investments	9.6	-0.5	15.2	4.6
Exports	3.6	9.3	-4.9	1.6
Imports	3.0	-0.6	9.3	2.7

Source: Bloomberg SAAR = seasonal adjusted annual rate

This table shows how crucial American consumers have become in times when trade is faltering.

The big questions

Will accommodating policies feed through on time? Will trade issues be resolved before consumers stop spending? If policy is not providing sufficient tailwind, and consumers decide to start saving for bad times, it is time for politicians to think about fiscal measures to be taken.

Main economic/financial forecasts

GDP growth (%)	2017	2018e	2019e	2020e	3M interbank rate	21/02/2019	28/02/2019	+3M	2019e	2020e
United States	2.2	2.9	2.7	1.7	United States	2.65	2.62	2.60	2.60	2.50
Eurozone	2.5	1.8	0.8	1.3	Eurozone	-0.31	-0.31	-0.30	-0.30	-0.20
Japan	1.9	0.7	0.9	0.7	Japan	0.07	0.07	-0.10	-0.10	-0.10
United Kingdom	1.8	1.4	1.1	1.8	United Kingdom	0.86	0.85	0.80	1.00	1.25
China	6.9	6.6	6.3	6.0						
World	3.8	3.6	3.4	3.3						
Inflation (%)	**2017**	**2018e**	**2019e**	**2020e**	**10Y interest rate**	**21/02/2019**	**28/02/2019**	**+3M**	**2019e**	**2020e**
United States	2.1	2.4	1.6	2.0	US Treasury	2.69	2.71	2.6	2.60	2.50
Eurozone	1.5	1.7	1.0	1.3	German Bund	0.13	0.19	0.0	0.20	0.50
Japan	0.5	0.9	1.1	1.6	Euro swap rate	0.66	0.71	0.6	0.80	1.10
United Kingdom	2.7	2.5	1.4	1.8	Japanese gov. bonds	-0.04	-0.02	0.0	0.10	0.30
China	1.6	2.1	2.5	2.5	UK gilts	1.20	1.30	1.5	1.50	1.80
World	3.0	3.5	3.8	3.3						
Key policy rate	**28/02/2019**	**+3M**	**2019e**	**2020e**	**Currencies**	**21/02/2019**	**28/02/2019**	**+3M**	**2019e**	**2020e**
Federal Reserve	2.50	2.50	2.50	2.50	EUR/USD	1.13	1.14	1.10	1.16	1.25
European Central Bank	-0.40	-0.40	-0.40	-0.30	USD/JPY	110.7	111.4	111	108	105
Bank of Japan	-0.10	-0.10	-0.10	-0.10	GBP/USD	1.31	1.33	1.28	1.35	1.45
Bank of England	0.75	0.75	0.75	1.00	EUR/GBP	0.87	0.86	0.86	0.86	0.86
People's Bank of China	4.35	4.35	4.35	4.35	USD/CNY	6.72	6.69	6.70	6.60	6.60

Source: Thomson Reuters Datastream, ABN AMRO Group Economics.

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