

Macro Weekly

Group Economics

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Damaging delay, with green shoots in Eurozone

- **Brexit delay springs hope for softness, but uncertainty keeps damaging**
- **Trade summit US-China delayed until April, but China seems prepared**
- **Inflation expectations in Eurozone springs hope of green shoots**

The recurrent theme in global macro news this week is 'delay'. A probable delay of the US-China summit concerns investors, in that it could reflect a lack of a breakthrough on trade talks. In the UK, a delayed Brexit could lead to a softer Brexit, but also to economic damage from prolonged uncertainty.

Brexit

Brexit has dominated global headlines this week. On Tuesday, a large majority (391 to 242) rejected PM May's second meaningful vote on her tweaked Brexit deal. Wednesday's vote on a 'no deal under any circumstances' was narrowly rejected by 312 to 308 votes. Last night, the House of Commons backed May's plans to request a delay to Brexit, the length of the request conditional on whether her deal passes a third time. If the deal finally passes, 'just' a short delay in Brexit until June 30 would be required. PM May's backing by the House of Commons came amid signs that Eurosceptic opposition is fearing the potential implications of a long delay. A delay that could last up to 2020 or beyond, which would mean the UK will have to take part in European Parliament elections in May.

Which of these outcomes is most likely?

It all depends now on whether at least 75 MPs that had rejected Mays second vote, are going to change their mind on the third vote by Tuesday. (See Bill Diviney's analysis [here](#) for details.) The question thus is whether the long delay brings other options to the table, such as a customs union, the Norway model or even a referendum including remain, that sufficiently horrifies Brexiteer MPs into changing their minds and voting for May's deal.

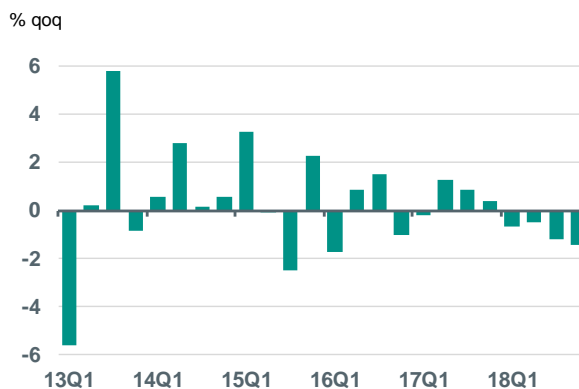
Damaging uncertainty

While Theresa May seems to have regained some control over the Brexit process preventing a most damaging chaotic Brexit, economic uncertainty has not disappeared. In fact, each day of delay causes additional uncertainty that affects business investment, consumer spending decisions and eventually employment. This week Jonathan Haskel, an external member of the Monetary Policy Committee, warned in his first interview since he joined the Committee, that whatever the deal would be, business investment was likely to remain subdued for years. This will at some point start to affect the UK labour market, he

worried. Therefore, his view is to wait for firm evidence of rising inflation before voting to increase interest rates.

Policy makers from the BoE had already lowered their forecast for business investment to -2.75 percent for 2019 compared to previously predicted 2 percent gain when they were still assuming a smooth exit on March 29. Delay, whether short or long, will add to uncertainty and therefore worsen investment appetite, warned the BoE on Thursday.

UK business investment



Source: Bloomberg

Investment demand and approval rates are in decline

Last months' bank lending survey digs a little further in the causes of the decline. The three months forward looking lending dynamics, show that demand for loans is rapidly declining, particularly amongst large private non-financial corporations. On top of declining requests for bank loans, an increasing share of those requests is being rejected.

UK: Demand for lending

Next three months	18Q1	18Q2	18Q3	18Q4
Small businesses	0.0	-2.0	-0.9	-5.8
Medium PNFCs*	11.8	11.3	-0.8	-11.5
Large PNFCs*	9.6	-12.6	-12.5	-22.9

UK: Loan approvals

Next three months	18Q1	18Q2	18Q3	18Q4
Small businesses	0.0	-2.0	0.0	-6.9
Medium PNFCs*	-1.7	-1.9	0.0	-6.3
Large PNFCs*	-0.8	0.0	-1.9	-7.2

Source: Bank of England, 18Q4

* Private Non-Financial Corporation are companies that produce goods and/or provide non-financial services.

Consumers unwilling to make big decisions

British consumers are also calling Brexit uncertainty their main motive for their steeply declining willingness to make big spending decisions, such as homebuying. This Thursday, the RICS housing index had fallen to its lowest since 2011, with 'new buyer inquiries' at -40, far below the initial Brexit 'shock' in June 2016.

UK: Housing market survey new buyers

England and Wales, % net balance index



Source: Bloomberg

Meanwhile on trade from China

With a trade deal on hold until April, China's data releases were somewhat worrying, but not as gloomy as last week's exports figures. On Friday morning, Chinese state media reported "substantive progress" on trade talks and that Beijing had passed a new foreign investment law designed to smooth the way to a new trade deal with the US. The CSI 300 index tracking Shanghai and Shenzhen stocks went up 1.7 per cent after this news. Earlier this week, data on investment in fixed assets were up from 5.9% to 6.1% (yoy) and investments in real estate even jumped from 9.5% to 11.6% (yoy), reflecting that a number of stimulating fiscal policy measures taken by the government might now be paying off. Other indicators did not show improvement this week, such as industrial production (yoy) and retail sales (yoy), which both fell in line with expectations. Less expected was the news on rising Chinese unemployment in non-rural areas that came in this Thursday at 5.3%. Just the day before, Premier Li Keqiang released his 'Employment first strategy' to combat rising unemployment.

Green shoots in the Eurozone

The January industrial production growth rate pick up in the Eurozone of 1.4% mom was well above our expectations, but should be regarded as a fragile green shoot, we feel. This is because the pickup was mainly driven by domestic demand factors such as energy and consumption.

Eurozone core inflation

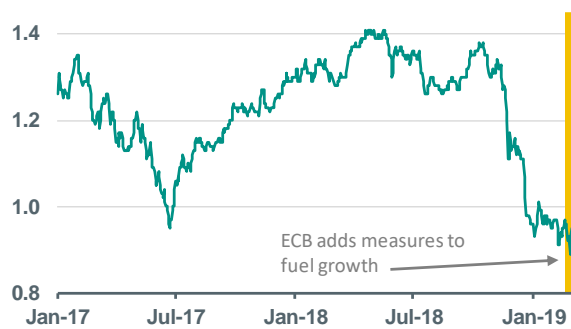
% yoy



Source: Bloomberg

Germany Breakeven 10 Year

%



Source: Bloomberg



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Production of export related goods such as intermediate and capital goods improved only very modestly (see article by Aline Schuiling [here](#)). Indeed, in Germany – the nexus of the manufacturing slowdown – Ifo slashed its growth forecast for 2019 down to 0.6% this week with a rebound to 1.8 % in 2020. For German consumers, there is also good news. The combination of wage growth, tax relief and low inflation leaves them in the sweet spot.

An interesting new green shoot to keep an eye on, is the 10-year German breakeven rate, that reflects investors' expectations of consumer prices in the future. While Eurozone core inflation remains 1.0 % (yoy), inflation expectations are growing. Following the ECB's latest round of accommodative measures taken, investors seem to have grown more confident that the stimulus (or the taking the foot of the brakes) should help the stagnating Eurozone.

Main economic/financial forecasts										
GDP growth (%)	2017	2018e	2019e	2020e	3M interbank rate	07/03/2019	14/03/2019	+3M	2019e	2020e
United States	2.2	2.9	2.3	1.9	United States	2.60	2.61	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	0.8	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	0.84	0.84	1.00	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	07/03/2019	14/03/2019	+3M	2019e	2020e
United States	2.1	2.4	1.6	2.0	US Treasury	2.64	2.63	2.6	2.60	2.50
Eurozone	1.5	1.7	1.0	1.3	German Bund	0.07	0.09	0.0	0.20	0.50
Japan	0.5	0.9	1.1	1.6	Euro swap rate	0.60	0.59	0.6	0.80	1.10
United Kingdom	2.7	2.5	1.4	1.8	Japanese gov. bonds	-0.01	-0.04	0.1	0.10	0.30
China	1.6	2.1	2.5	2.5	UK gilts	1.17	1.23	1.7	1.50	1.80
World	3.0	3.5	3.8	3.3						
Key policy rate	14/03/2019	+3M	2019e	2020e	Currencies	07/03/2019	14/03/2019	+3M	2019e	2020e
Federal Reserve	2.50	2.50	2.50	2.50	EUR/USD	1.12	1.13	1.10	1.16	1.25
European Central Bank	-0.40	-0.40	-0.40	-0.30	USD/JPY	111.6	111.7	110	108	105
Bank of Japan	-0.10	-0.10	-0.10	-0.10	GBP/USD	1.31	1.33	1.30	1.35	1.45
Bank of England	0.75	0.75	0.75	1.00	EUR/GBP	0.86	0.85	0.85	0.86	0.86
People's Bank of China	4.35	4.35	4.35	4.35	USD/CNY	6.72	6.72	6.65	6.60	6.60

Source: Thomson Reuters Datastream, ABN AMRO Group Economics.

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