

# Week ahead

Enjoy summer doldrums!

US – Labor market remains strong overall

Analyst:

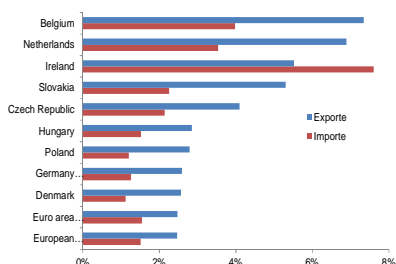
**Rainer Singer**  
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## Major political events in autumn

No potentially market-moving events are scheduled for the upcoming week. So, markets will take their guidance from this week's releases, possibly enhanced by one tweet or another. Periods like this give us the opportunity to look a bit further ahead, and this outlook shows that the current summer doldrums should be enjoyed. For the autumn, major political events lie ahead, with the potential to move markets.

Already this week, markets gave us a taste of the potential of political events. The announcement of a meeting scheduled between the heads of the Italian ruling coalition parties and the finance minister triggered an increase of risk premiums of Italian sovereign bonds. Obviously, markets feared a government crisis or a more expansionary fiscal course of the government. This showed the market's nervousness concerning political events in Italy and that the country could reemerge as a topic on financial markets at any point. In addition, autumn will bring political events that have so far hardly moved markets. Negotiations on Brexit between the UK and EU should be completed in October to provide enough time for member countries to ratify the outcome before March 29, 2019. An extension of the negotiation period is possible, but would require unanimity among EU countries. Due to the long value chains, the impact of a hard Brexit is especially difficult to assess. The EU exports equivalent to 2.4% of GDP to the UK and imports 1.5% of GDP. However, trade with the UK is spread unevenly among EU countries. The chart shows countries with an above-EU average exposure to exports to the UK. So, how might markets react to a hard Brexit? This summer, markets reacted to the discussion about US tariffs on auto imports from the EU already with increased risk perception for the economy. However, the affected volumes would have been clearly below the trade volumes that would be hit by Brexit. More important for the impact on the economy than the actual trade figures would be the accompanying increase of uncertainty among businesses and households. So, markets would price in negative implications for the EU economy from a hard Brexit until proven otherwise.

Trade with the United Kingdom, in % of GDP



Sources: Eurostat, Erste Group Research

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Indications of past performance are no guarantee of a positive performance in the future

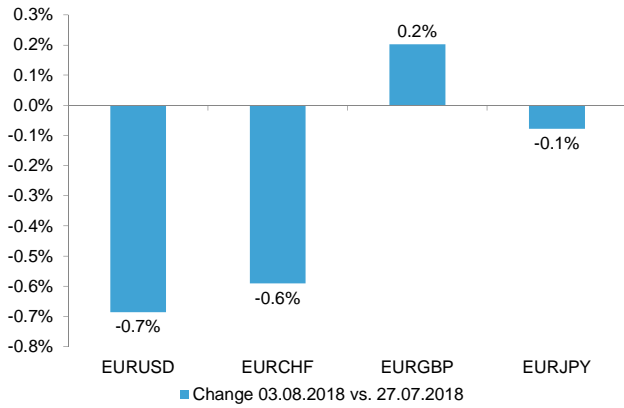
The second foreseeable major political event before year-end is the mid-term elections in the US at the beginning of November. All members of the House of Representatives and a third of senators are up for election. The question is whether the Republicans can hold onto their majorities in both chambers of the US Congress. Should the Democrats gain majorities, the president's scope would be reduced strongly. However, trade policies would hardly be affected, as the president enjoys far-reaching powers here. These powers could be cut by Congress, although this seems unlikely. Majorities by the Democrats would also make it easier to trigger an impeachment procedure regarding the president in the case that more evidence of any ties between Trump's campaign and Russia should emerge. We think that the end to trade conflicts on whatever political grounds would be welcomed by markets.

**US labor market slightly weaker in July, but no trend reversal**

US data showed in total a still strong labor market. However, the July numbers were slightly below market expectations. Non-farm payrolls increased by 157,000, which was 36,000 below the market's estimate. At the same time, the numbers for the previous two years were revised upwards by 59,000 in total. The unemployment rate declined from 4% to 3.9% and matched market estimates. The same can be said for average hourly earnings, which increased by 2.7% y/y, the same rate as in the previous month.

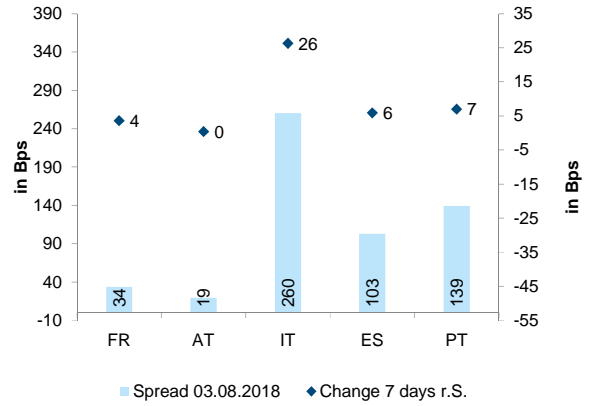
**Forex and government bond markets**

**Exchange rates EUR: USD, CHF, GBP and JPY**  
change last week  
(+ stronger euro / - weaker euro)



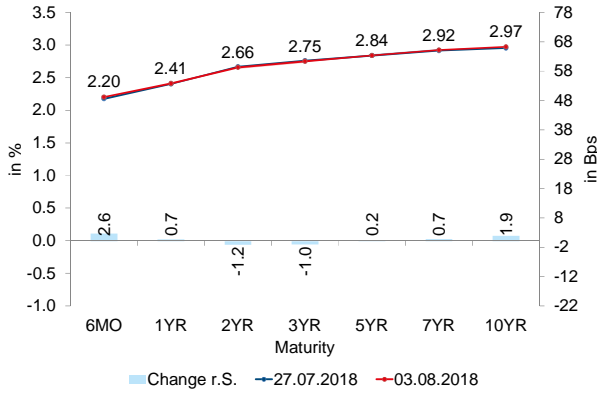
Source: Bloomberg, Erste Group Research

**Eurozone – spreads vs. Germany**  
10Y government bonds



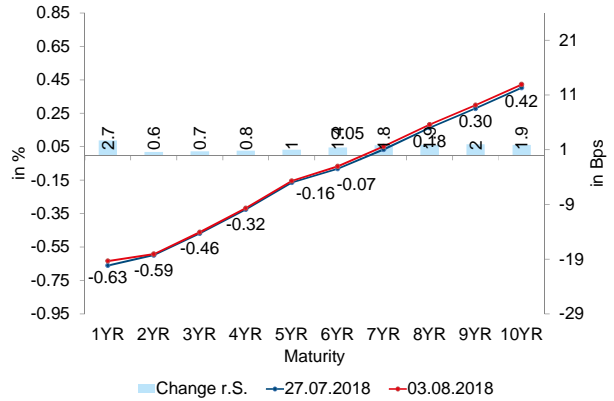
Source: Bloomberg, Erste Group Research

**US Treasuries yield curve**  
change last week



Source: Bloomberg, Erste Group Research

**DE Bund yield curve**  
change last week



Source: Bloomberg, Erste Group Research

**Economic calendar**

| Date          | Time  | Ctry | Release                | Period | Consens    | Prior      |
|---------------|-------|------|------------------------|--------|------------|------------|
| <b>3-Aug</b>  | 10:00 | IT   | Ind. Prod. y/y         | Jun    | 1.9%       | 1.7%       |
|               | 11:00 | EA   | Retail Sales y/y       | Jun    | 1.4%       | 1.2%       |
|               | 14:30 | US   | Wages y/y              | Jul    | 2.7%       | 2.7%       |
|               |       | US   | Trade Balance          | Jun    | -46m       | -43m       |
|               |       | US   | Unempl. Rate           | Jul    | 3.9%       | 4.0%       |
|               |       | US   | Chg. Non-Farm Payrolls | Jul    | 194.2 thd  | 213.0 thd  |
|               | 16:00 | US   | ISM Non-Manufacturing  | Jul    | 58.6 index | 59.1 index |
| <b>7-Aug</b>  | n.a.  | CN   | Forex Reserves         | Jul    | 3107bn     | 3112bn     |
|               | 8:00  | DE   | CA Balance (m)         | Jun    |            | 13 m       |
|               |       | DE   | Trade Balance          | Jun    | 20m        | 20m        |
|               |       | DE   | Ind. Prod. y/y         | Jun    | -0.3%      | 2.6%       |
|               | 8:45  | FR   | Trade Balance          | Jun    | -5359m     | -6005m     |
|               |       | FR   | CA Balance (m)         | Jun    |            | -2917 m    |
| <b>8-Aug</b>  | n.a.  | FR   | Cap Util.              | Jul    |            | 80.1%      |
| <b>9-Aug</b>  | 3:30  | CN   | Inflation y/y          | Jul    | 2.0%       | 1.9%       |
|               |       | CN   | PPI y/y                | Jul    | 4.5%       | 4.7%       |
|               | 14:30 | US   | Jobless Claims         | -      | 219.9 thd  | 218.0 thd  |
|               |       | US   | PPI y/y                | Jul    | 3.4%       | 3.4%       |
| <b>10-Aug</b> | n.a.  | CN   | CNY new loans          | Jul    | 1153bn     | 1840bn     |
|               |       | CN   | M2 yoy                 | Jul    | 8%         | 8%         |
|               | 8:45  | FR   | Ind. Prod. y/y         | Jun    | 1.4%       | -0.9%      |
|               | 10:00 | IT   | Trade Balance          | Jun    |            | 3378m      |
|               | 14:30 | US   | Inflation y/y          | Jul    | 3.0%       | 2.9%       |
|               |       | US   | CPI m/m                | Jul    | 0.2%       | 0.1%       |

Source: Bloomberg, Erste Group Research

**FORECASTS<sup>1)</sup>**

| <b>GDP</b>      | <b>2015</b> | <b>2016</b> | <b>2017</b> | <b>2018</b> | <b>2019</b> |
|-----------------|-------------|-------------|-------------|-------------|-------------|
| <b>Eurozone</b> | 2.0         | 1.8         | 2.4         | 2.3         | 2.2         |
| <b>US</b>       | 2.9         | 1.5         | 2.3         | 2.8         | 2.2         |

| <b>Inflation</b> | <b>2015</b> | <b>2016</b> | <b>2017</b> | <b>2018</b> | <b>2019</b> |
|------------------|-------------|-------------|-------------|-------------|-------------|
| <b>Eurozone</b>  | 0.1         | 0.2         | 1.5         | 1.7         | 1.7         |
| <b>US</b>        | 0.1         | 1.2         | 2.2         | 2.2         | 1.9         |

| <b>Interest rates</b>    | <b>current</b> | <b>Sep.18</b> | <b>Dec.18</b> | <b>Mar.19</b> | <b>Jun.19</b> |
|--------------------------|----------------|---------------|---------------|---------------|---------------|
| <b>ECB MRR</b>           | 0.00           | 0.00          | 0.00          | 0.00          | 0.00          |
| <b>3M Euribor</b>        | -0.32          | -0.30         | -0.30         | -0.30         | -0.30         |
| <b>Germany Govt. 10Y</b> | 0.43           | 0.60          | 0.70          | 0.90          | 1.00          |
| <b>Swap 10Y</b>          | 0.95           | 0.90          | 1.00          | 1.20          | 1.30          |

| <b>Interest rates</b>         | <b>current</b> | <b>Sep.18</b> | <b>Dec.18</b> | <b>Mar.19</b> | <b>Jun.19</b> |
|-------------------------------|----------------|---------------|---------------|---------------|---------------|
| <b>Fed Funds Target Rate*</b> | 1.91           | 2.13          | 2.38          | 2.63          | 2.88          |
| <b>3M Libor</b>               | 2.35           | 2.40          | 2.70          | 2.90          | 3.20          |
| <b>US Govt. 10Y</b>           | 2.97           | 3.20          | 3.30          | 3.50          | 3.50          |
| <b>EURUSD</b>                 | 1.16           | 1.14          | 1.13          | 1.15          | 1.16          |

\*Mid of target range

In case of changes to our forecasts compared to the previous issue, arrows show the direction of the change.

Source: Bloomberg, Erste Group Research

<sup>1</sup> By regulations we are obliged to issue the following statement: Forecasts are no reliable indicator for future performance

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03 August 2018

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