

Week Ahead

Focus: Brexit vote, recession in Germany?

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What does Brexit Plan B look like?

The vote in the British Parliament on the divorce package with the EU, originally scheduled for December 11, will take place on Tuesday next week. The starting position is clear. Nobody expects the package to get a majority, so all attention will be focused on the British government's Plan B. The government has three days to present this, according to a parliamentary decision this week. The next deadline is therefore January 21.

The market reaction will probably depend on the extent of the expected defeat. A narrow defeat could raise hopes of getting a majority in further votes, while a clear rebuff would probably put new elections on the agenda, which could take place within 25 days at the earliest. Should the defeat take place to the expected extent, the attention of the markets will shift relatively quickly to January 21. The market reaction will then depend on what Plan B looks like. Since we rule out the possibility of renegotiation with the EU, we see only two realistic alternatives, namely a hard Brexit or new referendum. The latter is clearly more likely, and the EU should also be prepared to postpone the withdrawal date. A referendum could no longer be held before March 29. The prospect of a new referendum would probably be well received by the markets, as there would at least be a chance that the UK would remain in the EU. If, on the other hand, the British government does not provide a credible alternative to the divorce package by January 21 and loses more time, the markets would increasingly prepare for a hard Brexit. This means uncertainty in a number of areas. First, contingency plans would be used to avoid the worst effects of an abrupt break. While both the EU and UK have readied such plans, it can only be discovered after March 29 whether everything has been considered. The second uncertainty relates to the impact on the economy. Uncertainty would probably be drawn into the real economy and thus lead to temporary negative impact. All in all, this would trigger a prolonged period of low yields on government bonds and would probably weigh on the euro exchange rate against the dollar.

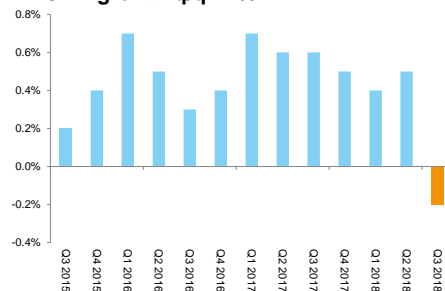
Is Germany threatened by a recession?

Due to the importance of foreign trade, Germany's economy is particularly susceptible to the current phase of global trade weakness. Already in 3Q18, Germany's GDP shrank by 0.2% q/q, triggered by falling exports and shrinking private consumption. In addition, negative one-off effects (new registration procedures weighed on car production and low water levels dampened transport capacity in inland navigation) weighed on growth. As things stand at present, however, the passenger car sector does not seem to have completely overcome the problems with the new registration procedures. If Germany's GDP fell further in 4Q18, Germany would technically be in recession. Therefore, next week (January 15), the focus will be on the publication of a first estimate of GDP growth for 2018 as a whole.

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Note: Past performance is not necessarily indicative of future results.

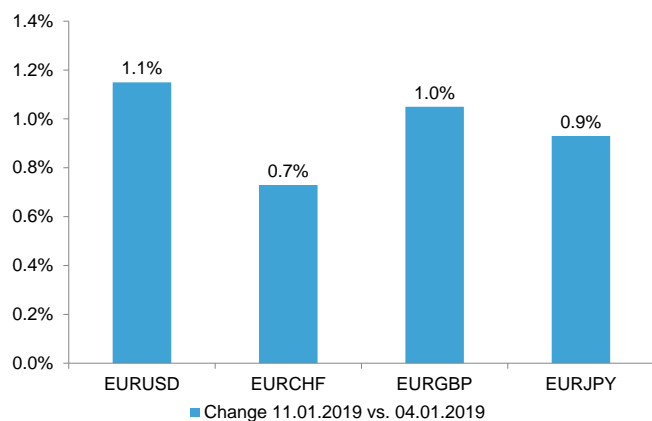
DE GDP-growth q/q in %

Leading indicators developed in a mixed manner in 4Q18. For example, based on the average data for October and November, Germany's industrial production shrank by 1.7% compared with the average for the third quarter. On the other hand, retail sales (October/November), supported by a sharp fall in energy prices from November onwards, increased by an average of 0.6% compared to 3Q. Against this backdrop, we expect Germany's GDP to have grown slightly in 4Q, although a further decline (should the problems in the automotive sector persist unchanged, for example) cannot be entirely ruled out. We assume that growth in Germany and the Eurozone will weaken in 2019 (see [Economic Outlook](#)) in the direction of potential growth (approx. 1.5%), due to a lack of impetus from foreign trade.

Source: Eurostat, Erste Group Research

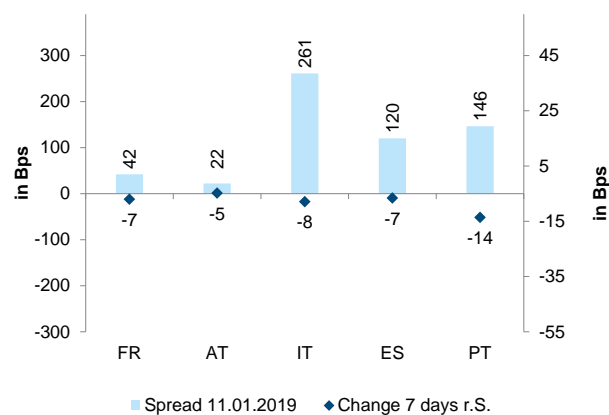
Forex and government bond markets

Exchange rates EUR: USD, CHF, GBP and JPY Changes compared to last week



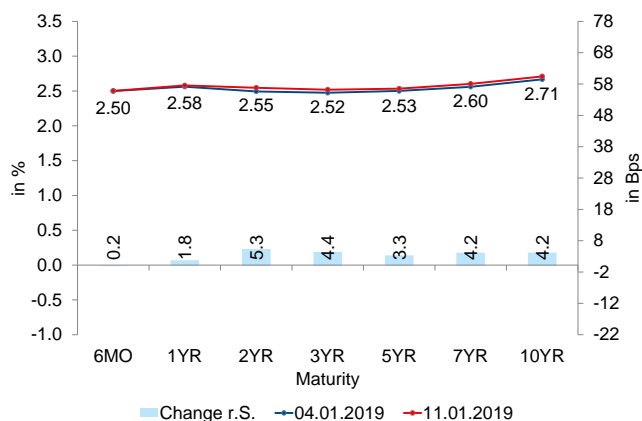
Source: Bloomberg, Erste Group Research

Eurozone-spreads vs. Germany 10Y government bonds



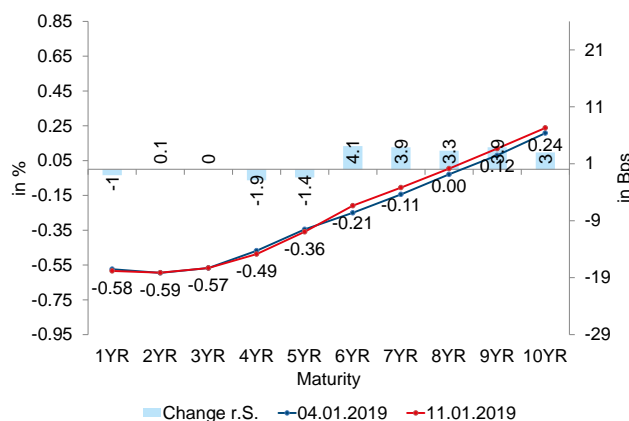
Source: Bloomberg, Erste Group Research

US Treasuries yield curve Changes compared to last week



Source: Bloomberg, Erste Group Research

DE Bund yield curve Changes compared to last week



Source: Bloomberg, Erste Group Research

Economic calendar

Date	Time	Ctry	Release	Period	Consens	Prior
11-Jan	n.a.	CN	CNY new loans	Dec	869bn	1250bn
		CN	M2 yoy	Dec	8%	8%
		FR	Cap Util.	Dec		79.7%
	10:00	IT	Ind. Prod. y/y	Nov	0.5%	1.0%
	14:30	US	Inflation y/y	Dec	1.9%	2.2%
		US	CPI m/m	Dec	-0.1%	0.0%
14-Jan	n.a.	US	Durable Goods Orders	Nov F		0.8%
		US	New Home Sales	Nov	568.3 thd	544.0 thd
		US	Trade Balance	Nov	-54m	-55m
	11:00	EA	Ind. Prod. y/y	Nov	-1.7%	1.2%
15-Jan	8:45	FR	CPI m/m	Dec F	0.1%	0.1%
		FR	Inflation y/y	Dec F	1.9%	1.9%
	11:00	EA	Trade Balance	Nov		12486m
	14:30	US	PPI y/y	Dec	2.6%	2.5%
16-Jan	8:00	DE	Inflation y/y	Dec F	1.7%	1.7%
		DE	CPI m/m	Dec F	0.3%	0.3%
	11:00	IT	Inflation y/y	Dec F	1.1%	1.2%
	14:30	US	Retail Sales mom	Dec	0.3%	0.2%
		US	Univ. Michigan Index	Jan P	96.7 index	98.3 index
17-Jan	n.a.	AT	Inflation y/y	Dec		2.3%
		AT	CPI m/m	Dec		0.0%
	10:00	IT	Trade Balance	Nov		3784m
	11:00	EA	CPI m/m	Dec		0.0%
		EA	Inflation y/y	Dec F	1.6%	1.6%
	14:30	US	Jobless Claims	Jan 12	227.5 thd	216.0 thd
18-Jan	n.a.	US	Ind. Prod. y/y	Dec		3.9%
		IT	CA Balance (m)	Nov		6081 m
	10:00	EA	CA Balance (m)	Nov		23 m
		US	Univ. Michigan Index	Jan P	96.7 index	98.3 index

Source: Bloomberg, Erste Group Research

Forecasts¹

GDP	2017	2018	2019	2020
Eurozone	2.4	1.9	1.5	1.4
US	2.3	2.9	2.3	2.1

Inflation	2017	2018	2019	2020
Eurozone	1.5	1.7	1.7 ↓	1.7 ↑
US	2.2	2.4	1.8	1.9

Interest rates	current	Mar.19	Jun.19	Sep.19	Dec.19
ECB MRR	0.00	0.00	0.00	0.00	0.25
3M Euribor	-0.31	-0.30	-0.30	-0.10	0.10
Germany Govt. 10Y	0.24	0.50	0.70	0.80	1.00
Swap 10Y	0.80	0.80	1.00	1.10	1.30

Interest rates	current	Mar.19	Jun.19	Sep.19	Dec.19
Fed Funds Target Rate*	2.40	2.38	2.63	2.88	3.13
3M Libor	2.80	2.70	2.90	3.20	3.40
US Govt. 10Y	2.71	2.90	3.10	3.30	3.50
EURUSD	1.15	1.11	1.12	1.14	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

¹ Note: By regulations we are obliged to issue the following statement: Forecasts are no reliable indicator of future performance.

Erste Group Research

Week Ahead | Major Markets | Eurozone, USA

11. January 2019

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Published by:

Erste Group Bank AG
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1100 Vienna, Austria, Am Belvedere 1
Head Office: Wien
Commercial Register No: FN 33209m
Commercial Court of Vienna

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