

Danske Daily

Germany may ease fiscal policy but (unfortunately) not now

Market movers today

- Today, we have a light calendar where we mainly look out for **the final euro area inflation figures** at 11:00 CEST. The flash estimates showed overall HICP inflation at 1.1% y/y and core inflation at 0.9% y/y in July and we expect no revision of the data.
- **Markets will continue to carefully watch tweets and communication from the US and China** and, most recently, following Donald Trump's upbeat tweet this weekend.
- **Later this week**, we have the important US manufacturing PMI, which we expect to tick below 50 (however, we note upside risks from strong regional PMIs last week). We also have minutes from both the Fed and ECB meetings in July and the Jackson Hole Conference (Powell speaks on Friday). We also get euro area PMIs.
- **In the Nordic area, Swedish unemployment figures and the Norwegian investment survey are the most important items this week.**
- The ECB is widely expected to announce a tiering system while cutting rates at the next meeting in September. We have taken a closer look, see *ECB: Mitigating side effects – gauging the tiering premium*, 16 August.

Selected market news

Risk appetite has improved this morning. Many Asian stock indices, the US S&P500 futures, oil and US 10-year Treasury yield are all up. **Yesterday, US President Trump tweeted that “We are doing very well with China, and talking”.** It seems like investors have to accept that Trump is going to intervene in the trade war by tweeting from time to time. Apparently, more US-China teleconferences are planned over the next two weeks. Still, we are having a hard time seeing a trade deal on this side of the presidential elections.

In Germany, Finance Minister Ola Scholz hinted at a EUR50bn (~1.5% of German nominal GDP) fiscal spending package in case of recession, although it is not imminent, see *Bloomberg*. The German government is under heavy pressure by many to ease fiscal policy, as the German economy is struggling (contracted in Q2) and there is a lack of safe assets (bonds) in the market. See also *Harr's view: Why Germany should ease fiscal policy*, 18 August. Unfortunately, the fact that Scholz says a package is not imminent also highlights the time lag problem with fiscal policy: It takes time for politicians to recognise the need for fiscal easing and vote in favour of a specific package, and hence when it has an impact on real activity.

The Iranian supertanker that was detained last month, has left Gibraltar waters despite the US's objections.

Ahead of Boris Johnson's visit to Angela Merkel and Emmanuel Macron, a government report on the worst-case impact on the British economy in case of a no deal Brexit was leaked to the press yesterday. It is grim reading suggesting the UK is definitely not ready for a no deal Brexit, see *BBC*. While the government says that is why it is stepping up no deal preparations, it also highlights the risk of the new government's strategy.

Selected reading from Danske Bank

- *Harr's view: Why Germany should ease fiscal policy*
- *ECB: Mitigating side effects – gauging the tiering premium*
- *FOMC research - New Fed call: Five more from Fed*
- *Norges Bank Review: Keeping the tightening bias, but increasing downside risk*
- *Flash Comment Emerging markets: forget Argentina; focus on Fed, Trump and China*

Follow us on *Twitter* :



@Danske_Research



Video
Danske Bank research playlist

Read more in Danske Bank's recent forecasts and publications

- *Nordic Outlook*
- *Yield Outlook*
- *FX Forecast Update*
- *Weekly Focus*

Senior Analyst
Mikael Olai Milhøj
+45 45 12 76 07
milh@danskebank.dk

Scandi markets

No important Scandi releases today.

Fixed income markets

After a strong FI rally earlier in the week, **US yields** edged higher into Friday's close as risk appetite got a boost from the news that the US-China talks will proceed as planned and not least as it was revealed that the US Treasury was seeking feedback on ultra-long issuance. The 10-30y bear steepened by 3bp and 30Y Treasury yields rose to 2.04% after trading as low as 1.91% the day before.

This week, the **EGB market** will also focus on the long end as the German Finanzagentur comes to the market with a new 30Y bund on Wednesday. We take a closer look at the new 30Y in *Government Bonds Weekly*. We recommend going long the new 30Y bund versus swaps as the 30Y segment is the only segment of the German curve relative to the swap-curve. A fair pricing for the new 30Y Bund is a spread of 3-4bp to Bund 1.25% 08/48 or 29-30bp to mid-swaps (based on pricing on Friday afternoon).

Note that on Friday we updated our Fed call. We now expect five consecutive rate cuts and that 10Y US treasury yields will drop to 1% over the next six months, *see FOMC research: New Fed call: Five more from Fed*, 16 August.

Please see our comprehensive note on an ECB tiering system, *see ECB: Mitigating side effects – gauging the tiering premium*, 16 August.

FX markets

EUR/USD declined last week and ended the week below the 1.11 mark - and we see no obvious triggers for a rebound near term. Preliminary PMIs this week will probably only have limited impact and ECB and FOMC minutes are not likely to put their mark on the market for long. First, we think the current ECB pricing, the likely 'tiered ECB cut', is too aggressive. Second, although our new Fed call suggests five more cuts (slightly more aggressive than market pricing), the Fed looks unlikely to accommodate the market's call for larger rate cuts and we will likely need to get deeper into the easing cycle before we see a more broad-based USD weakness. Meanwhile, speculation over whether the Trump administration could look to FX intervention remains after the recent labelling of China as a currency manipulator: China has said it will not use the **CNY** as a tool in the trade war, and given further Fed easing down the road, we do not see any arguments for the US to officially abandon the strong dollar policy at this stage. **USD/JPY** and **EUR/CHF** have settled at their newfound lows but we would not rule out further drops as the global economic cycle will likely take another turn lower near term.

EUR/GBP has come off its post-Johnson highs but it is, in our view, too early for a firm rebound in the GBP; until we get closer to the 31 October Brexit deadline, the market is unlikely to get its hopes up too high for an extension to avert a 'no deal'.

In the Scandies, global risk sentiment is likely to remain in the driver's seat. Last week's Norges Bank meeting was no game changer for the **NOK** as the hiking bias remained amid rising worries over the global picture. This week's oil investment survey will probably confirm that the sector is set to continue to boost the economy this year and next – but it is unlikely to prove a turning point for the battered NOK that much in the current fragile global environment. We keep a neutral view on EUR/NOK for now. For the **SEK**, we believe it is only a matter of time before the Riksbank decides to postpone the next hike well into next year - a shift it could make already at the September meeting. However, in light of the already relatively soft pricing on the Riksbank, which in our view is justified, such a decision may not lead to any significant rally in EUR/SEK.

Key figures and events

Monday, August 19, 2019				Period	Danske Bank	Consensus	Previous
1:50	JPY	Exports	y/y (%)	Jul		0.0	-0.1
1:50	JPY	Import	y/y (%)	Jul		0.0	-0.1
1:50	JPY	Trade balance, s.a.	JPY bn	Jul		-150.8	-14.4
10:00	EUR	Current account	EUR bn	Jun			29.7
11:00	EUR	HICP inflation	m/m y/y	Jul		-0.4% 1.1%	0.2% 1.3%
11:00	EUR	HICP - core inflation, final	y/y	Jul		0.9%	0.9%

Source: Bloomberg, Danske Bank

Disclosures

This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of the research report is detailed on the front page.

Analyst certification

Each research analyst responsible for the content of this research report certifies that the views expressed in the research report accurately reflect the research analyst's personal view about the financial instruments and issuers covered by the research report. Each responsible research analyst further certifies that no part of the compensation of the research analyst was, is or will be, directly or indirectly, related to the specific recommendations expressed in the research report.

Regulation

Danske Bank is authorised and subject to regulation by the Danish Financial Supervisory Authority and is subject to the rules and regulation of the relevant regulators in all other jurisdictions where it conducts business. Danske Bank is subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority (UK). Details on the extent of the regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available from Danske Bank on request.

Danske Bank's research reports are prepared in accordance with the recommendations of the Danish Securities Dealers Association.

Conflicts of interest

Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high-quality research based on research objectivity and independence. These procedures are documented in Danske Bank's research policies. Employees within Danske Bank's Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and the Compliance Department. Danske Bank's Research Departments are organised independently from and do not report to other business areas within Danske Bank.

Research analysts are remunerated in part based on the overall profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.

Financial models and/or methodology used in this research report

Calculations and presentations in this research report are based on standard econometric tools and methodology as well as publicly available statistics for each individual security, issuer and/or country. Documentation can be obtained from the authors on request.

Risk warning

Major risks connected with recommendations or opinions in this research report, including as sensitivity analysis of relevant assumptions, are stated throughout the text.

Expected updates

Each working day.

Date of first publication

See the front page of this research report for the date of first publication.

General disclaimer

This research report has been prepared by Danske Bank (a division of Danske Bank A/S). It is provided for informational purposes only. It does not constitute or form part of, and shall under no circumstances be considered as, an offer to sell or a solicitation of an offer to purchase or sell any relevant financial instruments (i.e. financial instruments mentioned herein or other financial instruments of any issuer mentioned herein and/or options, warrants, rights or other interests with respect to any such financial instruments) ('Relevant Financial Instruments').

The research report has been prepared independently and solely on the basis of publicly available information that Danske Bank considers to be reliable. While reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation is made as to its accuracy or completeness and Danske Bank, its affiliates and subsidiaries accept no liability whatsoever for any direct or consequential loss, including without limitation any loss of profits, arising from reliance on this research report.

The opinions expressed herein are the opinions of the research analysts responsible for the research report and reflect their judgement as of the date hereof. These opinions are subject to change and Danske Bank does not undertake to notify any recipient of this research report of any such change nor of any other changes related to the information provided herein.

This research report is not intended for, and may not be redistributed to, retail customers in the United Kingdom or the United States.

This research report is protected by copyright and is intended solely for the designated addressee. It may not be reproduced or distributed, in whole or in part, by any recipient for any purpose without Danske Bank's prior written consent.

Disclaimer related to distribution in the United States

This research report was created by Danske Bank A/S and is distributed in the United States by Danske Markets Inc., a U.S. registered broker-dealer and subsidiary of Danske Bank A/A, pursuant to SEC Rule 15a-6 and related interpretations issued by the U.S. Securities and Exchange Commission. The research report is intended for distribution in the United States solely to 'U.S. institutional investors' as defined in SEC Rule 15a-6. Danske Markets Inc. accepts responsibility for this research report in connection with distribution in the United States solely to 'U.S. institutional investors'.

Danske Bank is not subject to U.S. rules with regard to the preparation of research reports and the independence of research analysts. In addition, the research analysts of Danske Bank who have prepared this research report are not registered or qualified as research analysts with the NYSE or FINRA but satisfy the applicable requirements of a non-U.S. jurisdiction.

Any U.S. investor recipient of this research report who wishes to purchase or sell any Relevant Financial Instrument may do so only by contacting Danske Markets Inc. directly and should be aware that investing in non-U.S. financial instruments may entail certain risks. Financial instruments of non-U.S. issuers may not be registered with the U.S. Securities and Exchange Commission and may not be subject to the reporting and auditing standards of the U.S. Securities and Exchange Commission.

Report completed: 19 August 2019, 06:30 CEST

Report first disseminated: 19 August 2019, 07:00 CEST