

ECOWEEK

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United States: The Powell put

■ Fed chairman Powell has recently emphasized that the FOMC will be patient given the muted inflation reading and that it is ready to shift the policy stance swiftly if required ■ He also considers that financial markets are pricing in downside risks well ahead of the data. This means that they are too pessimistic on growth ■ Professional forecasters' estimates of the probability of entering into recession in the coming quarters do not display the typical pre-recession dynamics either

At the recent annual meeting of the American Economic Association, New York Times journalist Neil Irwin, the moderator of a panel discussion between Ben Bernanke, Janet Yellen and Jerome Powell, quippingly started by wondering what you get when a lawyer (Jerome Powell) walks into a conference with 13000 economists. Having watched the event on YouTube¹, the answer is "a clear message".

When a central banker wants to influence the near term development of the economy and indeed of financial markets, he can signal a readiness to act should conditions require but he can also manifest a high level of conviction in describing the economic environment. Speaking at the panel, Powell did both things. On policy signalling, he insisted that the FOMC will be patient given muted inflation readings and that it is "always prepared to shift the policy stance and to shift significantly if necessary in order to promote our statutory goals of maximum employment and stable prices". This stance goes back to the Greenspan era, and the liquidity injections following the October 1987 stock market crash. The view that, faced with a bleaker outlook, the Fed would swiftly ease its policy, thereby supporting investor risk appetite, is referred to by commentators as the Greenspan put, Bernanke put, Yellen put and Powell put. Importantly, the current Fed chairman was also very explicit on how his reading of the outlook differs from market signals: "I think the markets are pricing in downside risks and they're obviously well ahead of the data." We concur with this assessment not only based on the recent dataflow and its derived measures², but also when looking at the "anxious index"³. Based on a survey of professional forecasters, this index shows the probability of a decline in real GDP in the quarter after the survey is taken. Its recent trend does not display at all the traditional pre-recession dynamics. In addition, whereas in the run-up to recessions the difference in recession probability 4 quarters ahead versus next quarter declines, it is currently still rising.

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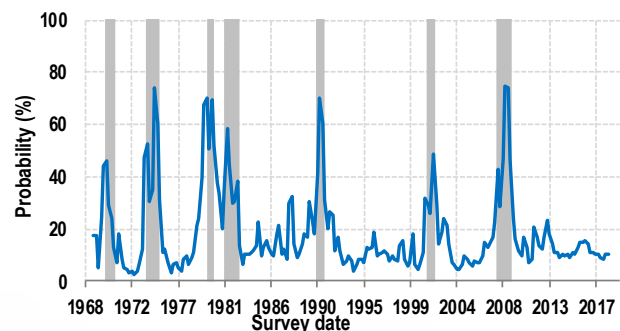
¹ <https://www.youtube.com/watch?v=DH030t70Ho0>

² The derived measures refer to the nowcasts of the Federal Reserve of Atlanta, New York and St Louis. Their respective estimates for real GDP growth (seasonally adjusted annual rate) are 2.8%, 2.5% and 2.6%.

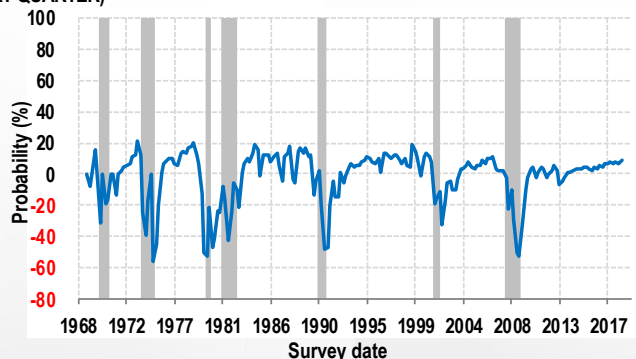
³ www.philadelphiafed.org/research-and-data/real-time-center/survey-of-professional-forecasters/anxious-index

US: THE ANXIOUS INDEX

PROBABILITY OF DECLINE IN REAL GDP NEXT QUARTER (QUARTERLY, 1968 Q4 TO 2018 Q4)



DIFFERENCE IN PROBABILITY OF DECLINE IN REAL GDP (4 QUARTERS AHEAD MINUS NEXT QUARTER)



Source: Federal Reserve Bank of Philadelphia, BNP Paribas

p. 2

Markets Overview

p. 3

Pulse & Calendar

p. 4

Economic scenario

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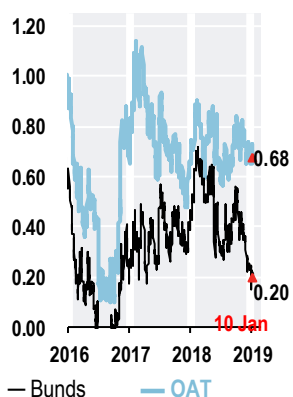
Markets overview

The essentials

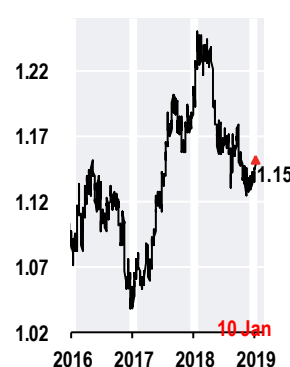
Week 4-1 19 > 10-1-19

➤ CAC 40	4 737	▶ 4 806	+1.4 %
➤ S&P 500	2 532	▶ 2 597	+2.6 %
➤ Volatility (VIX)	21.4	▶ 19.5	-1.9 pb
➤ Euribor 3M (%)	-0.31	▶ -0.31	+0.1 bp
➤ Libor \$ 3M (%)	2.80	▶ 2.80	-0.5 bp
➤ OAT 10y (%)	0.70	▶ 0.68	-2.7 bp
➤ Bund 10y (%)	0.21	▶ 0.20	-1.0 bp
➤ US Tr. 10y (%)	2.66	▶ 2.73	+7.2 bp
➤ Euro vs dollar	1.14	▶ 1.15	+1.0 %
➤ Gold (ounce, \$)	1 283	▶ 1 289	+0.5 %
➤ Oil (Brent, \$)	56.9	▶ 61.5	+8.0 %

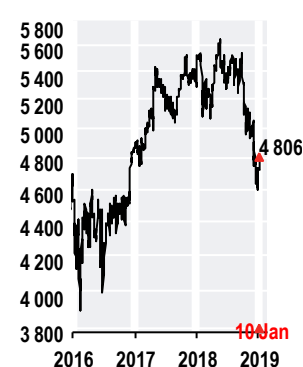
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



Money & Bond Markets

Interest Rates	highest' 19	lowest' 19
€ ECB	0.00 at 01/01	0.00 at 01/01
Eonia	-0.37 at 01/01	-0.37 at 02/01
Euribor 3M	-0.31 at 08/01	-0.31 at 02/01
Euribor 12M	-0.12 at 01/01	-0.12 at 02/01
\$ FED	2.50 at 01/01	2.50 at 01/01
Libor 3M	2.80 at 01/01	2.78 at 08/01
Libor 12M	3.04 at 09/01	2.96 at 04/01
£ BoE	0.75 at 01/01	0.75 at 01/01
Libor 3M	0.90 at 01/01	0.90 at 07/01
Libor 12M	1.18 at 09/01	1.17 at 02/01

At 10-1-19

Yield (%)	highest' 19	lowest' 19
€ AVG 5-7y	0.62 at 09/01	0.58 at 02/01
Bund 2y	-0.59 at 08/01	-0.62 at 03/01
Bund 10y	0.20 at 01/01	0.15 at 03/01
OAT 10y	0.68 at 08/01	0.65 at 03/01
Corp. BBB	2.15 at 08/01	2.03 at 02/01
\$ Treas. 2y	2.59 at 08/01	2.39 at 03/01
Treas. 10y	2.73 at 10/01	2.55 at 03/01
Corp. BBB	4.65 at 01/01	4.57 at 03/01
£ Treas. 2y	0.76 at 10/01	0.68 at 03/01
Treas. 10y	1.28 at 10/01	1.18 at 03/01

At 10-1-19

10y bond yield & spreads

4.90%	Greece	469 pb
2.90%	Italy	269 pb
1.72%	Portugal	152 pb
1.46%	Spain	126 pb
0.73%	Belgium	53 pb
0.68%	France	47 pb
0.57%	Ireland	37 pb
0.51%	Finland	31 pb
0.48%	Austria	28 pb
0.34%	Netherland	14 pb
0.20%	Germany	

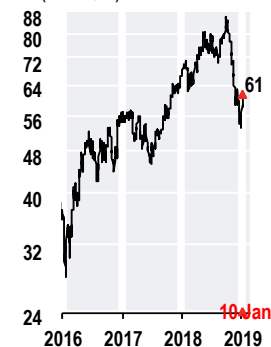
Commodities

Spot price in dollars	lowest' 19	2019(€)
Oil, Brent	53.1 at 01/01	+14.8%
Gold (ounce)	1 281 at 01/01	-0.2%
Metals, LME	2 730 at 03/01	-0.7%
Copper (ton)	5 714 at 03/01	-1.5%
CRB Foods	324 at 01/01	+0.9%
wheat (ton)	197 at 01/01	+0.9%
Corn (ton)	136 at 01/01	+0.4%

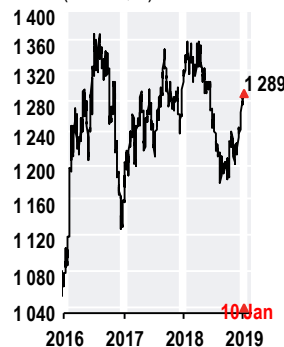
At 10-1-19

Variations

Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



Exchange Rates

€ =	highest' 19	lowest' 19	2019
USD	1.15 at 10/01	1.14 at 02/01	+0.8%
GBP	0.90 at 03/01	0.90 at 04/01	+0.5%
CHF	1.13 at 10/01	1.12 at 02/01	+0.2%
JPY	124.67 at 01/01	122.54 at 03/01	-0.6%
AUD	1.60 at 03/01	1.60 at 10/01	-1.3%
CNY	7.81 at 09/01	7.78 at 02/01	-0.5%
BRL	4.24 at 01/01	4.24 at 09/01	-4.2%
RUB	77.22 at 01/01	76.43 at 07/01	-2.6%
INR	81.17 at 09/01	79.57 at 04/01	+1.7%

At 10-1-19

Variations

Equity indices

Index	highest' 19	lowest' 19	2019	2019(€)
CAC 40	4 814 at 09/01	4 611 at 03/01	+1.6%	+1.6%
S&P500	2 597 at 10/01	2 448 at 03/01	+3.6%	+2.8%
DAX	10 922 at 10/01	10 417 at 03/01	+3.4%	+3.4%
Nikkei	20 164 at 09/01	19 562 at 04/01	+0.7%	+1.3%
China*	73 at 10/01	68 at 03/01	+4.0%	+3.1%
India*	559 at 01/01	545 at 03/01	-0.5%	-2.2%
Brazil*	2 185 at 10/01	1 944 at 01/01	+6.8%	+11.5%
Russia*	609 at 10/01	570 at 01/01	+3.7%	+6.0%

At 10-1-19

Variations

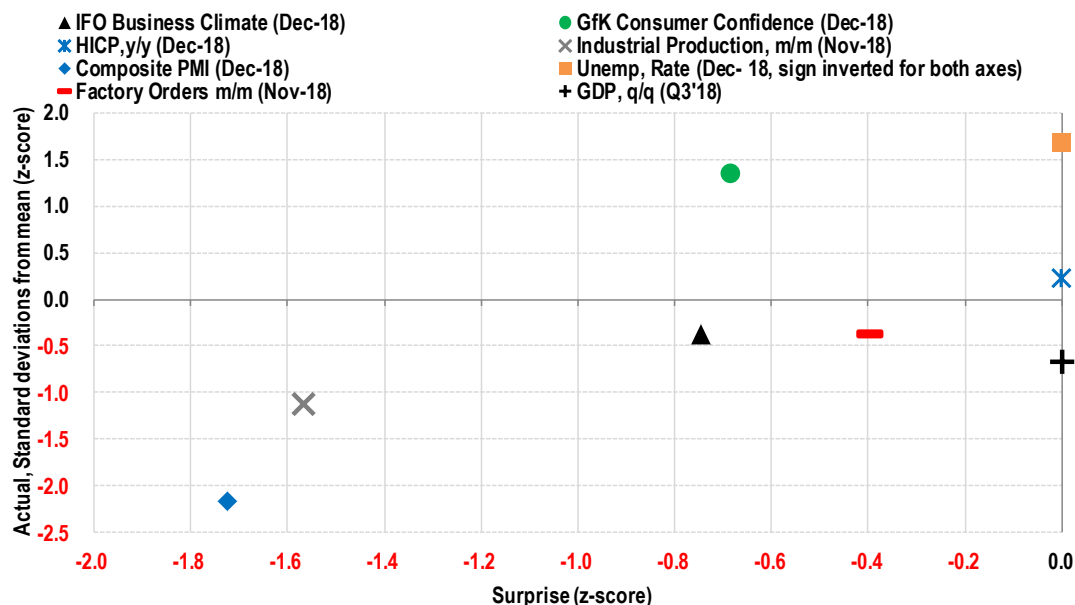
* MSCI index



Pulse

Germany: Rude awakening

For Germany, 2019 started with a hangover. Most indicators that we follow are below their long-term average and all surprised on the downside. In particular, the export-oriented manufacturing sector has been badly affected. Production declined in five months out of the six to November. The further decline in the PMI manufacturing in December to 51.5 does not signal a quick rebound. Nevertheless, household confidence, although weakening, remains well above its long-term average, underpinned by the dynamic labour market, generous pay deals and the loosening fiscal stance.



Note: z-score is a score which indicates how many standard deviations an observation is from the mean: $z=(x-\mu)/\sigma$ where x : observation, μ : mean, σ : standard deviation. On the X-axis, x corresponds at the last known surprise for each indicator represented on the graph, μ and σ corresponds respectively to the mean and the standard deviation of the last 24 value for monthly data and the last 8 quarters for quarterly data. On the Y-axis, x corresponds at the last known value of indicator, μ and σ corresponds respectively to the mean and the standard deviation for this indicator since 2000 (for China since 2011).

Source: Bloomberg, BNP Paribas

Indicators preview

In the US the Beige Book will probably get more attention than normal following the recent weak data and the drop in the stock market. Attention will also go to several housing market indicators, retail sales, University of Michigan household sentiment and to the Philadelphia Fed survey for January. Inflation data will be published for the eurozone, France and the UK.

Date	Country/Region	Event	Period	Surv(M)	Prior
01/15/19	France	CPI EU Harmonized MoM	Dec.	--	--
01/15/19	United States	PPI Ex Food and Energy MoM	Dec.	0.2%	0.3%
01/16/19	Japan	Core Machine Orders MoM	Nov.	--	7.6%
01/16/19	United Kingdom	CPI MoM	Dec.	--	0.2%
01/16/19	United States	Retail Sales Advance MoM	Dec.	0.2%	0.2%
01/16/19	United States	NAHB Housing Market Index	Jan.	--	56
01/16/19	United States	U.S. Federal Reserve Releases Beige Book			
01/17/19	Eurozone	CPI MoM	Dec.	--	-0.2%
01/17/19	United States	Housing Starts MoM	Dec.	0.0%	3.2%
01/17/19	United States	Building Permits MoM	Dec.	-2.1%	5.0%
01/17/19	United States	Philadelphia Fed Business Outlook	Jan.	--	9.4
01/18/19	United Kingdom	Retail Sales Ex Auto Fuel MoM	Dec.	--	1.2%
01/18/19	United States	Industrial Production MoM	Dec.	0.2%	0.6%
01/18/19	United States	University of Michigan Sentiment	Jan.	--	98.3

Source: Bloomberg, BNP Paribas



Economic scenario

UNITED STATES

- Economy is expected to expand at approximately 2.9% this year on the back of tax cuts, booming profits and credit. However, weaker international trade as well as tighter monetary and financial conditions promise a slowdown.
- Inflation has passed its peak, as oil prices are now falling.
- The monetary tightening is coming closer to its end. We forecast the Fed funds target rate to reach 3% in Q2 2019, the stalling.

CHINA

- Economic growth will decelerate in 2018-2019 due to both structural and cyclical reasons. The export outlook is significantly darkened by US tariff hikes. Private domestic demand should be affected by the worsening performance of the export manufacturing sector and the continued moderation in the property market.
- In order to contain the slowdown, the central bank is easing liquidity and credit conditions. At the same time, the reduction in financial instability risks via regulatory tightening should remain a top policy priority. Fiscal policy is also turning expansionary (tax cuts, increased infrastructure spending).

EUROZONE

- The slowdown is becoming increasingly evident, especially in the German economy, which encounters capacity constraint and suffers from reduce demand coming from the EMEs.
- Inflation is now expected to decelerate with falling oil price, while core CPI trend remains subdued. We do not expect the ECB to move rates before 19Q4 (see below)

FRANCE

- Growth slows down but remains above potential. Households' consumption should get a boost from the tax cuts and the jobs recovery but inflation reduces purchasing power gains. Business investment dynamics remain favourable. The global backdrop is less supportive. A slight rise in core inflation is appearing but remains to be confirmed.

INTEREST RATES AND FX RATES

- In the US, ongoing strong growth and a very low unemployment rate point towards more rate hikes. We expect 2 more in the first half of 2019 after which the Fed will want to see how the economy reacts. As a consequence, US treasury yields should increase, although to a limited degree: the market expects that the tightening cycle is already well advanced. The ECB has announced it will stop its net asset purchases at the end of 2018. A first hike of the deposit rate is expected after the summer of 2019. As a consequence, bond yields should increase. No change expected in Japan.
- The narrowing bond yield differential between the US and the eurozone should cause a strengthening of the euro, all the more so considering it is still below its long-term fair value (around 1.34).

SUMMARY

%	GDP Growth			Inflation		
	2018 e	2019 e	2020 e	2018 e	2019 e	2020 e
Advanced	2.2	1.7	1.3	2.0	1.7	1.8
United-States	2.9	2.1	1.5	2.4	1.8	2.0
Japan	0.9	0.7	0.3	1.0	0.6	1.4
United-Kingdom	1.3	1.8	1.6	2.4	2.0	2.0
Euro Area	1.9	1.4	1.2	1.8	1.8	1.5
Germany	1.6	1.5	1.3	1.9	2.2	1.6
France	1.5	1.6	1.3	2.1	1.5	1.6
Italy	1.0	0.6	0.5	1.3	1.5	1.2
Spain	2.5	2.2	2.0	1.8	1.7	1.3
Emerging	5.9	5.9	5.7	2.8	2.7	3.1
China	6.6	6.2	6.0	2.2	1.9	2.5
India	7.4	7.6	7.8	3.8	4.0	4.1
Brazil	1.3	3.0	2.5	3.7	3.8	3.6
Russia	1.8	1.7	1.6	2.8	3.6	4.2

Source : BNP Paribas Group Economic Research (e: Estimates & forecasts)

INTEREST RATES & FX RATES

Interest rates, %	2018	2019					2018e	2019e	2020e
		Q4e	Q1e	Q2e	Q3e	Q4e			
US									
Fed Funds	2.50	2.75	3.00	3.00	3.00	2.50	3.00	3.00	
Libor 3m \$	2.65	2.90	3.05	3.05	3.05	2.65	3.05	2.80	
T-Notes 10y	3.20	3.30	3.40	3.45	3.50	3.20	3.50	3.25	
Ezone									
ECB Refi	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.20	
Euribor 3m	-0.30	-0.30	-0.25	-0.20	-0.15	-0.30	-0.15	0.00	
Bund 10y	0.55	0.55	0.60	0.80	1.00	0.55	1.00	0.90	
OAT 10y	0.90	0.95	1.00	1.10	1.25	0.90	1.25	1.15	
UK									
Base rate	0.75	0.75	1.00	1.00	1.25	0.75	1.25	1.50	
Gilts 10y	1.20	1.70	1.85	2.00	2.10	1.20	2.10	2.10	
Japan									
BoJ Rate	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	
JGB 10y	0.14	0.15	0.15	0.15	0.14	0.14	0.14	0.08	

Source : BNP Paribas GlobalMarkets (e: Estimates & forecasts)

Exchange Rates	End of period	2019					2018e	2019e	2020e
		Q4e	Q1e	Q2e	Q3e	Q4e			
USD									
EUR / USD	1.14	1.15	1.17	1.21	1.25	1.14	1.25	1.34	
USD / JPY	111	110	108	105	100	111	100	90	
GBP / USD	1.27	1.32	1.36	1.41	1.47	1.27	1.47	1.58	
USD / CHF	0.99	1.01	1.00	0.98	0.96	0.99	0.96	0.93	
EUR									
EUR / GBP	0.90	0.87	0.86	0.86	0.85	0.90	0.85	0.85	
EUR / CHF	1.13	1.16	1.17	1.18	1.20	1.13	1.20	1.25	
EUR / JPY	127	127	126	127	125	127	125	121	

Source : BNP Paribas GlobalMarkets (e: Estimates & forecasts)

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