ECOWEEK

No. 19-15, 12 April 2019

US: Three different messages from Washington DC

■ President Trump has argued that the US economy would get a boost if the Federal Reserve were to cut rates ■ The minutes of the FOMC show the members are confident about the growth outlook. The outlook for inflation, against a background of global uncertainties, allows them to be patient in terms of policy ■ The IMF in its latest Global Financial Stability Report expresses concern about how high debt levels weigh on the resilience when faced with significantly slower growth or higher borrowing costs ■ This implies that Fed policy will not only be confidently patient but also patiently vigilant

Recent comments and analyses about the US show that the perspective drives the messages. Hence the messages are different, not to say conflicting. President Trump argued last week that the economy would climb like a rocket ship if the Fed would cut rates, adding that the central bank had slowed down the economy. Considering that next year is an election year, it doesn't come as a surprise that politicians closely monitor the health of the economy. It is reminiscent of the famous line *"it's the economy stupid"* from Bill Clinton's successful campaign against George Bush sr. for the 1992 presidential elections.

From the perspective of the Federal Reserve, the focus is on meeting the policy objectives. The minutes of the March meeting show that the committee members are quite relaxed about the economic outlook with their projections pointing towards ongoing good growth (slightly above potential), a low rate of unemployment and inflation which remains under control. Compared to December, their uncertainty about the outlook hasn't really changed although the risks of a pick-up of the unemployment rate and a decline of inflation have increased, but only slightly so (charts on next page). The minutes also show that the Fed staff is confident about the outlook: the first quarter slowdown should be transitory and growth is expected to bounce back solidly in the second quarter. Moreover, it considers uncertainty around its projections to be in line with the historical average, whereas risks to the outlook are roughly balanced. All in all, this leads to a central bank which is confidently patient: confident about the growth outlook but waiting patiently before contemplating any new action on official rates. Why hurry when inflation is stubbornly close to target and foreign headwinds haven't disappeared?

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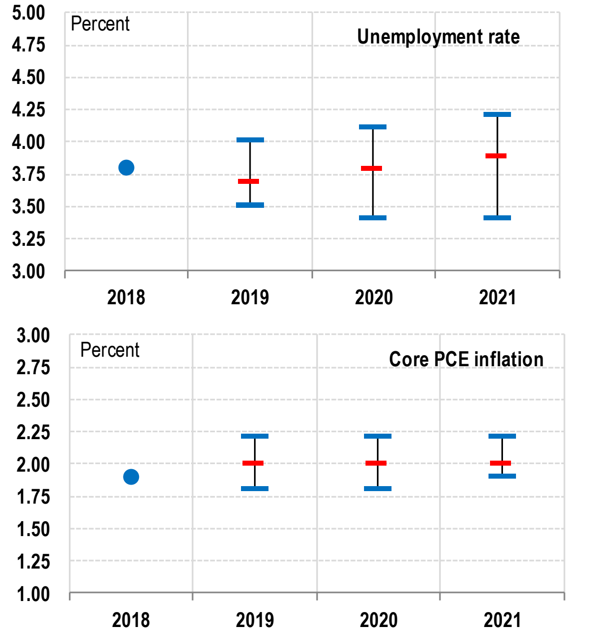
PROJECTIONS OF THE FOMC MEMBERS



Source: Federal Reserve, Minutes of the March meeting of the FOMC, BNP Paribas

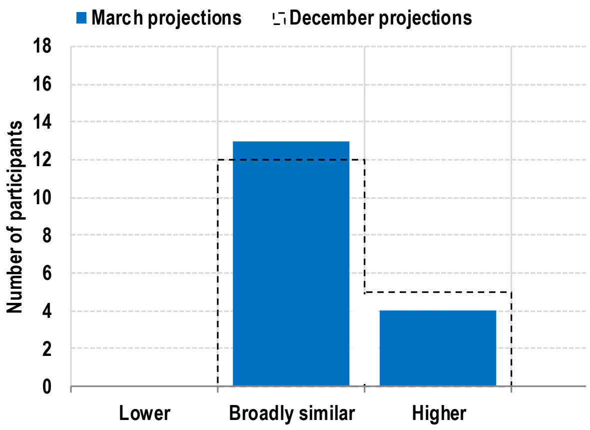
Eco WEEK

ECONOMIC RESEARCH DEPARTMENT

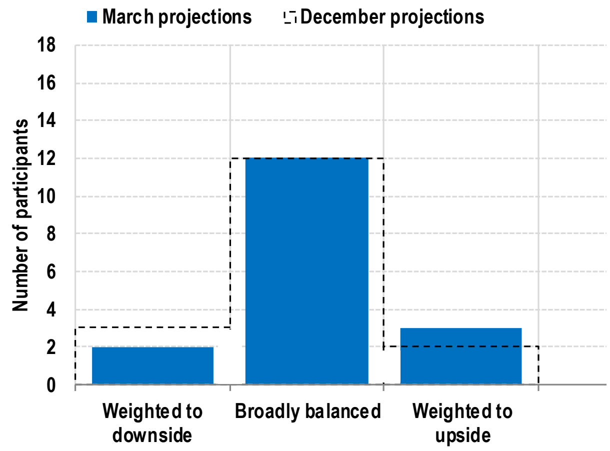
The minutes report that "*A few participants observed that the appropriate path for policy, insofar as it implied lower interest rates for longer periods of time, could lead to greater financial stability risks. However, a couple of these participants noted that such financial stability risks could be addressed through appropriate use of countercyclical macroprudential policy tools or other supervisory or regulatory tools.*" Moreover, "*a few participants observed that an economic deterioration in the United States, if it occurred, might be amplified by significant debt service burdens for many firms.*" A link can easily be made with the IMF's new Global Financial Stability Report, "*Vulnerabilities in a Maturing Credit Cycle*". In this report the authors point towards a US corporate credit cycle which appears to be at its highest point in recent history (though lower than in some other countries); corporate debt is skewed towards lower-rated issuers; leverage is at cyclical highs in most ratings buckets. This has happened, quite logically, against the background of prolonged monetary accommodation and a global expansion. However, when these cyclical support factors turn into headwinds, the implications of reduced resilience should manifest themselves: increased sensitivity to lower earnings or to an increase in interest rates, following a rise in the corporate spread versus treasuries if recession risks were to mount. The extent of the downturn then becomes particularly important: "*Although corporate balance sheets are strong enough to sustain a moderate economic slowdown or a gradual tightening of financial conditions, a significant deceleration in earnings growth or a sharp tightening of financial conditions could lead to a notable deterioration in corporate credit quality.*" One should also be concerned about contagion effects starting from lower-rated issuers, which will suffer more from a deterioration in the macro environment. This may end up impacting higher quality corporates as well, via their business with financially constrained firms and a deterioration in their own funding conditions, with banks and investors turning more cautious across the board. The lagged effects of monetary easing to counter such a tide, create a two-fold challenge for the Fed: avoiding to tighten too much when the environment still looks good and making sure to ease sufficiently quickly when the outlook worsens. The policy is not only confidently patient, it will also be patiently vigilant.

William De Vijlder

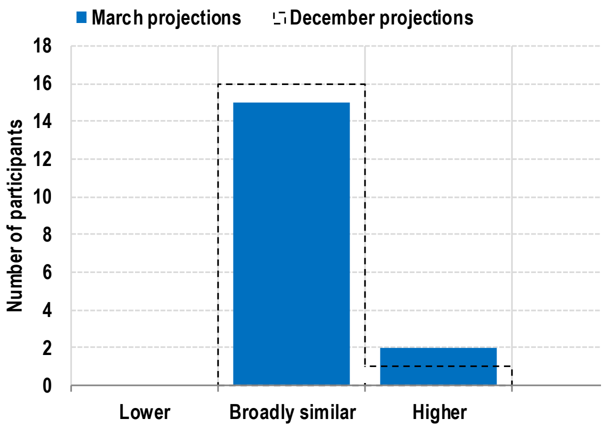
UNCERTAINTY ABOUT THE UNEMPLOYMENT RATE



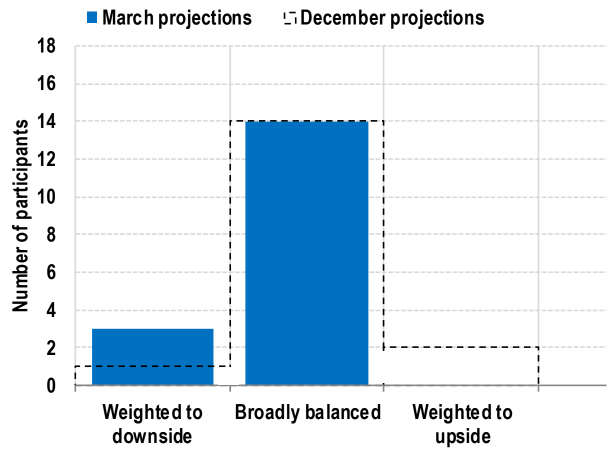
RISKS TO THE UNEMPLOYMENT RATE



UNCERTAINTY ABOUT PCE INFLATION



RISKS TO CORE PCE INFLATION



Source: Federal Reserve, Minutes of the March meeting of the FOMC, BNP Paribas

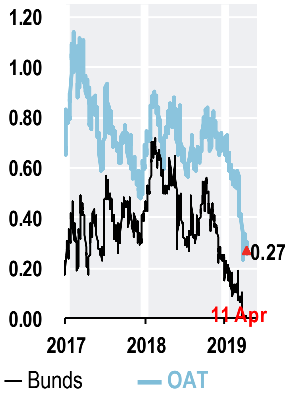
Markets overview

The essentials

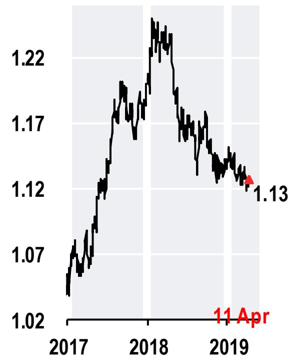
Week 5-4 19 > 11-4-19

↗ **CAC 40**	5 476	▸	**5 486**	**+0.2**	%
↘ **S&P 500**	2 893	▸	**2 888**	**-0.2**	%
↗ Volatility (VIX)	12.8	▸	13.0	+0.2	pb
↗ **Euribor 3M (%)**	-0.31	▸	**-0.31**	**+0.0**	bp
↗ Libor $ 3M (%)	2.59	▸	2.60	+1.1	bp
↘ OAT 10y (%)	0.30	▸	0.27	-2.5	bp
↘ Bund 10y (%)	0.00	▸	-0.01	-0.9	bp
↗ US Tr. 10y (%)	2.50	▸	2.51	+0.5	bp
↗ **Euro vs dollar**	1.12	▸	**1.13**	**+0.4**	%
↗ Gold (ounce, $)	1 292	▸	1 296	+0.3	%
↗ **Oil (Brent, $)**	69.9	▸	**71.4**	**+2.2**	%

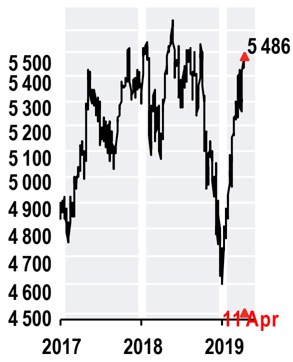
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



Money & Bond Markets

Interest Rates		highest' 19		lowest' 19	
€ ECB	**0.00**	0.00	at 01/01	0.00	at 01/01
Eonia	**-0.37**	-0.36	at 01/01	-0.37	at 26/02
Euribor 3M	**-0.31**	-0.31	at 24/01	-0.31	at 28/03
Euribor 12M	**-0.11**	-0.11	at 06/02	-0.12	at 02/01
$ FED	**2.50**	2.50	at 01/01	2.50	at 01/01
Libor 3M	**2.60**	2.81	at 01/01	2.58	at 09/04
Libor 12M	**2.74**	3.04	at 21/01	2.68	at 27/03
£ BoE	**0.75**	0.75	at 01/01	0.75	at 01/01
Libor 3M	**0.82**	0.93	at 29/01	0.82	at 08/04
Libor 12M	**1.08**	1.19	at 11/01	1.05	at 02/04

At 11-4-19

Yield (%)			highest' 19		lowest' 19	
€	AVG 5-7y	**0.38**	0.68	at 09/01	0.38	at 11/04
	Bund 2y	**-0.58**	-0.53	at 05/03	-0.63	at 27/03
	Bund 10y	**-0.01**	0.25	at 01/01	-0.08	at 27/03
	OAT 10y	**0.27**	0.73	at 08/01	0.24	at 27/03
	Corp. BBB	**1.40**	2.15	at 08/01	1.40	at 10/04
$	Treas. 2y	**2.37**	2.62	at 18/01	2.22	at 27/03
	Treas. 10y	**2.51**	2.78	at 18/01	2.37	at 27/03
	Corp. BBB	**4.01**	4.65	at 01/01	3.98	at 27/03
£	Treas. 2y	**0.74**	0.83	at 27/02	0.63	at 02/04
	Treas. 10y	**1.15**	1.35	at 18/01	0.99	at 25/03

At 11-4-19

10y bond yield & spreads

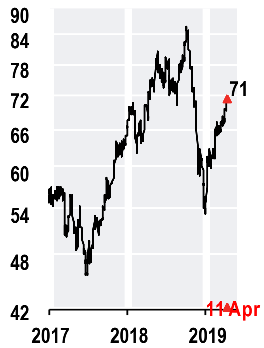
3.82%	Greece	382 pb
2.37%	Italy	237 pb
1.14%	Portugal	114 pb
1.00%	Spain	100 pb
0.44%	Belgium	44 pb
0.28%	Austria	28 pb
0.27%	France	27 pb
0.20%	Finland	20 pb
0.17%	Netherland	17 pb
0.16%	Ireland	16 pb
-0.01%	Germany	

Commodities

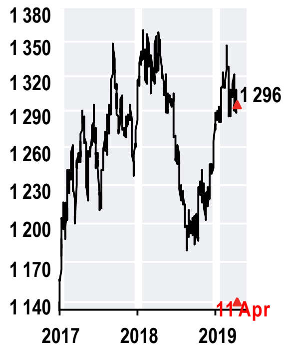
Spot price in dollars		lowest' 19			2019(€)
Oil, Brent	**71.4**	53.1	at	01/01	**+36.3%**
Gold (ounce)	**1 296**	1 281	at	21/01	**+2.5%**
Metals, LMEX	**2 998**	2 730	at	03/01	**+8.5%**
Copper (ton)	**6 391**	5 714	at	03/01	**+8.9%**
CRB Foods	**345**	324	at	07/03	**+8.0%**
wheat (ton)	**182**	168	at	11/03	**-6.5%**
Corn (ton)	**133**	130	at	29/03	**-0.9%**

At 11-4-19 *Variations*

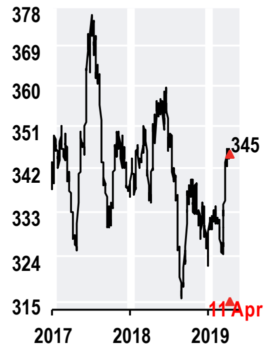
Oil (Brent, $)



Gold (Ounce, $)



CRB Foods



Exchange Rates

1€ =		highest' 19			lowest' 19			2019
USD	**1.13**	1.15	at	10/01	1.12	at	02/04	**-1.4%**
GBP	**0.86**	0.90	at	03/01	0.85	at	14/03	-4.0%
CHF	**1.13**	1.14	at	05/02	1.12	at	02/04	+0.3%
JPY	**125.67**	127.43	at	01/03	122.54	at	03/01	+0.2%
AUD	**1.58**	1.63	at	03/01	1.57	at	31/01	-2.8%
CNY	**7.57**	7.87	at	09/01	7.52	at	02/04	-3.5%
BRL	**4.32**	4.46	at	28/03	4.18	at	31/01	-2.5%
RUB	**72.64**	79.30	at	01/01	72.45	at	21/03	-8.4%
INR	**77.68**	82.00	at	04/02	76.84	at	03/04	-2.7%

At 11-4-19 *Variations*

Equity indices

	Index	highest' 19			lowest' 19			2019	2019(€)
CAC 40	**5 486**	5 486	at	11/04	4 611	at	03/01	+16.0%	**+16.0%**
S&P500	**2 888**	2 896	at	08/04	2 448	at	03/01	+15.2%	**+16.8%**
DAX	**11 935**	12 010	at	05/04	10 417	at	03/01	+13.0%	**+13.0%**
Nikkei	**21 711**	21 822	at	04/03	19 562	at	04/01	+8.5%	**+8.3%**
China*	**85**	86	at	09/04	68	at	03/01	+21.4%	**+23.0%**
India*	**599**	606	at	02/04	530	at	19/02	+6.0%	**+8.9%**
Brazil*	**2 097**	2 304	at	04/02	1 944	at	01/01	+6.7%	**+9.4%**
Russia*	**665**	674	at	10/04	572	at	01/01	+9.0%	**+17.8%**

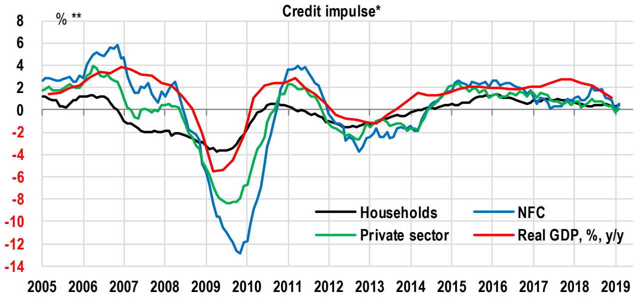
At 11-4-19 *Variations*

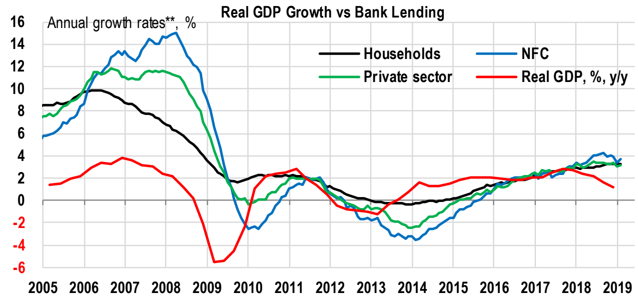
* MSCI index

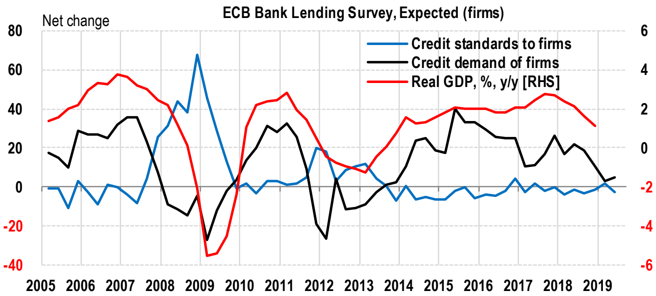
Pulse

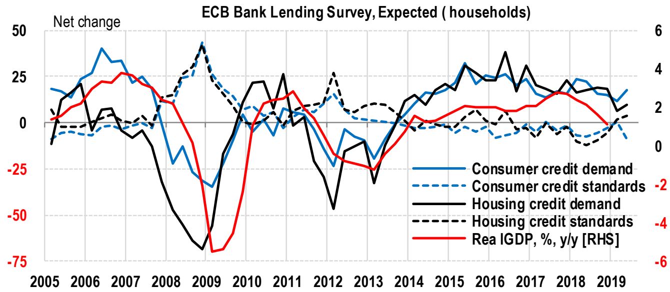
Eurozone: credit impulse

After contracting in January, the credit impulse picked up very slightly in February 2019. This trend is due almost exclusively to lending to non-financial companies, whereas the credit impulse has remained relatively flat for households since November 2018. Demand is expected to increase in second-quarter 2019 for all loan categories, stimulated by the easing of financing conditions, except for home loans, for which lending conditions are expected to tighten slightly.









*Credit impulse is measured as the annual change of the annual growth rate of MFI loans   ** Adjusted for securitizations

Source: ECB, ECB survey on the distribution of credit, BLS, BNP Paribas calculations

Indicators preview

Next week is rather light on data. We have inflation numbers in the eurozone and the UK and, in the US, industrial production, retail sales, housing starts and building permits. The Philadelphia Fed business outlook will provide a first flavour of how April is doing. The Federal Reserve will publish its Beige Book with the usual regional granularity on US economic developments.

Date	Country	Event	Period	Surv(M)	Prior
04/16/19	United States	Industrial Production MoM	March	0.3%	0.1%
04/17/19	United Kingdom	CPI MoM	March	--	0.5%
04/17/19	Eurozone	CPI MoM	March	--	0.3%
04/17/19	United States	U.S. Federal Reserve Releases Beige Book			
04/18/19	United Kingdom	Retail Sales Ex Auto Fuel MoM	March	--	0.2%
04/18/19	United States	Retail Sales Advance MoM	March	0.9%	-0.2%
04/18/19	United States	Philadelphia Fed Business Outlook	April	10.0	13.7
04/19/19	United States	Housing Starts MoM	March	6.2%	-8.7%
04/19/19	United States	Building Permits MoM	March	0.6%	-1.6%

Source: Bloomberg, BNP Paribas

Economic scenario

UNITED STATES

- Growth is expected to slow to 2.3% this year. Trade war uncertainty acts as a drag, the housing market is softening, corporate investment should slow, as well as exports in reaction to the past strengthening of the dollar against a broad range of currencies.
- Core inflation remains well under control and has eased a bit.
- Following the dovish message from the January FOMC meeting, markets are pricing in a policy easing in the course of 2020.

CHINA

- Economic growth continues to slow, with an export outlook severely darkened by US tariff hikes.
- The central bank is easing liquidity and credit conditions, though the reduction in financial-instability risks via regulatory tightening should remain a priority. Fiscal policy has also turned expansionary through increased infrastructure spending and a rising number of household/corporate tax cuts.
- In the short term, private domestic demand should be affected by the knock-on effect of weakening exports and the continued moderation in the property market. Fiscal measures should support consumer spending.

EUROZONE

- The slowdown is becoming increasingly evident, especially in the German economy, which has suffered from one-off factors but also from a slowdown of exports to China. Capacity constraints also play a role. Business climate in the manufacturing sector continues to decline. Italy has now entered a technical recession with quarterly growth negative in the third and fourth quarter of 2018.
- Inflation is now expected to decrease following the past drop in the oil price, while core CPI is hardly moving. The activity slowdown also implies that the pick-up in core inflation should be slower than expected until recently. We do not expect the ECB to move rates this year (see below).

FRANCE

- Growth is slowing although the economy should show some resilience. 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, the Fed has announced to be patient before deciding on any change in its policy. We expect key rates to stay on hold. We have changed the forecast for 10 year treasury yields and now expect a yield of 2.80% by mid-year and 2.70% at the end of the year.
- As the ECB confirmed that key rates won't change this year, the forecast for 10 year Bund yields and now expect a yield of 0.30% by mid-year and 0.40% at the end of the year.
- No change expected in Japan.
- The prospect of a 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).

	GDP Growth			Inflation		
%	2018	2019	2020 e	2018	2019 e	2020 e
Advanced	**2.2**	**1.5**	**1.3**	**2.0**	**1.4**	**1.6**
United-States	2.9	2.3	1.8	2.4	1.7	2.0
Japan	0.8	0.2	0.3	1.0	0.5	0.5
United-Kingdom	1.4	1.1	1.5	2.5	2.0	1.9
Euro Area	**1.8**	**0.9**	**1.0**	**1.8**	**1.2**	**1.4**
Germany	1.4	0.7	0.9	1.9	1.4	1.7
France	1.5	1.2	1.2	2.1	1.2	1.7
Italy	0.8	0.0	0.5	1.3	0.9	1.2
Spain	2.5	2.1	1.7	1.7	1.0	1.4
Emerging	**5.9**	**5.8**	**5.8**	**2.6**	**2.5**	**2.8**
China	6.6	6.2	6.0	2.1	1.6	2.0
India	7.4	7.6	7.8	3.4	3.3	4.1
Brazil	1.1	2.0	3.0	3.7	3.8	3.6
Russia	1.7	1.5	1.8	2.8	5.1	4.1

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

Interest rates, %		2019						
End of period		Q1	Q2e	Q3e	Q4e	2018	2019e	2020e
US	Fed Funds	2.50	2.50	2.50	2.50	2.50	2.50	2.50
	Libor 3m $	2.60	2.60	2.60	2.60	2.81	2.60	2.50
	T-Notes 10y	2.42	2.80	2.75	2.70	2.69	2.70	2.50
Ezone	ECB Refi	0.00	0.00	0.00	0.00	0.00	0.00	0.00
	Euribor 3m	-0.31	-0.30	-0.30	-0.30	-0.31	-0.30	-0.30
	Bund 10y	-0.07	0.30	0.30	0.30	0.25	0.30	0.40
	OAT 10y	0.26	0.65	0.65	0.60	0.71	0.60	0.70
UK	Base rate	0.75	1.00	1.00	1.25	0.75	1.25	1.25
	Gilts 10y	1.00	1.85	2.00	2.10	1.27	2.10	2.10
Japan	BoJ Rate	-0.06	-0.10	-0.10	-0.10	-0.07	-0.10	-0.20
	JGB 10y	-0.09	-0.03	-0.05	-0.05	0.00	-0.05	-0.20

Source : BNP Paribas GlobalMarkets (e: Forecasts)

Exchange Rates		2019						
End of period		Q1	Q2e	Q3e	Q4e	2018	2019e	2020e
USD	EUR / USD	1.12	1.17	1.18	1.20	1.14	1.20	1.25
	USD / JPY	111	108	105	100	110	100	90
	GBP / USD	1.30	1.38	1.40	1.45	1.27	1.45	1.51
	USD / CHF	1.00	0.97	0.97	0.97	0.99	0.97	0.93
EUR	EUR / GBP	0.85	0.85	0.84	0.83	0.90	0.83	0.83
	EUR / CHF	1.12	1.14	1.15	1.16	1.13	1.16	1.16
	EUR / JPY	124	126	124	120	125	120	113

Source : BNP Paribas GlobalMarkets (e: Forecasts)

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ECOTV WEEK

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