

ECOWEEK

No. 19-30, 26 July 2019

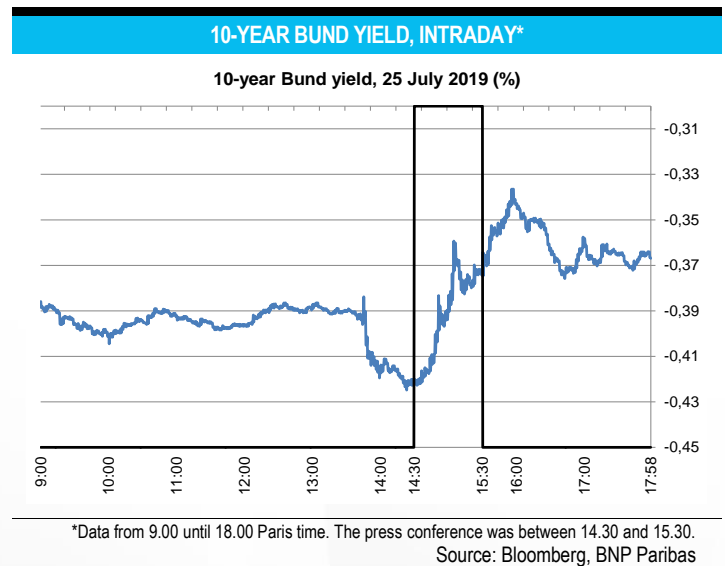
ECB: committed to ease in September, but how much?

■ The Governing Council has tasked Eurosystem committees to examine its monetary policy options ■ Given the insistence on its determination to act, Thursday's meeting outcome was basically a pre-announcement of easing in September ■ Being aware of the importance of maintaining the ECB's inflation targeting credibility, Mario Draghi was very explicit in expressing his dissatisfaction with current inflation and its outlook, adding that a highly accommodative monetary policy is here to stay for a long period of time

Yesterday's press conference of ECB president Mario Draghi was rich in messages, but the most important one was the following: the Governing Council is concerned that inflation will continue to fail to sufficiently converge to its target and hence will do whatever is necessary to achieve its objective. Yet, markets were not impressed and Bund yields rose somewhat as Draghi spoke. This is not a surprise: bond yields had been moving down for weeks after his Sintra speech end June, which suggests some expectation for easing had been priced in. The decision to leave policy unchanged on Thursday triggered some profit taking, despite a message which was nothing less than a pre-announcement of monetary easing at the next meeting on 12 September. By then the relevant Eurosystem committees which have been tasked "with examining options, including ways to reinforce our forward guidance on policy rates, mitigating measures, such as the design of a tiered system for reserve remuneration, and options for the size and composition of potential new net asset purchases" will have come up with their recommendations. New ECB staff projections will also be available on that occasion.

Conscious about the importance to maintain credibility as a central bank, Mario Draghi explained, during the Q&A part of the press conference, in great detail to what extent the message from the Governing Council had changed: 1) the introduction of the easing bias through the introduction of the word "lower" in the forward guidance 2) there was the acknowledgement "that inflation rates, both realised and projected, have been persistently below levels that are in line with our aim" 3) the insistence on being determined to act, hence tasking committees to examine policy options 4) the insistence on the "commitment to symmetry in its inflation aim", which means that getting closer to target would not automatically imply that tightening is imminent.

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ECONOMIC RESEARCH DEPARTMENT



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Eco
WEEK

For the avoidance of doubt, the Introductory Statement says the Governing Council “*therefore stands ready to adjust all of its instruments, as appropriate, to ensure that inflation moves towards its aim in a sustained manner*”. At the moment, the monetary authorities are far from this aim, hence the numerous times Mario Draghi expressed his dissatisfaction about this situation.ⁱⁱ

Whether that will change any time soon will of course depend on how the economy develops. Based on the ECB President’s comments, one can argue that, on the one hand, the risk of a recession is considered to be low thanks to resilience in the labour market, the services sector and the construction sector. In addition, loans to non-financial corporations are growing at a robust pace and those to households see a gradual improvement. On the other hand, recent data point towards weakness of growth extending into the third quarter and the outlook is worsening further in the manufacturing sector. This may end up weighing on services as well. Moreover, risks remain tilted to the downside. Importantly, the pass-through of wage increases into final prices is taking longer than expected. As a consequence, eurozone core inflation remains stubbornly low, market-based indicators of inflation expectations have declined and the same has happened in the Survey of Professional Forecasters.

The inflation dynamics will also depend on the extent of policy easing and its effectiveness. On the latter, the ECB President sounded a word of caution: together with his colleagues, he believes monetary instruments are effective but there may be decreasing returns. However, this should not “*exempt monetary policy from doing what is necessary or what we believe necessary based on the current information*”. Easing on 12 September is a given now. The question is how and how much. We expect a 10 basis points cut in the deposit rate in combination with the introduction of tiered system for reserve remuneration.

William De Vijlder

ⁱ “(...) we decided to keep the key ECB interest rates unchanged. We expect them to remain at their present or lower levels at least through the first half of 2020, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to our aim over the medium term.” Source: ECB, Introductory statement to the press conference on 25 July 2019

ⁱⁱ During the Q&A, there were six, explicit or implicit, references in this respect: “we say we don’t like the current inflation. So, there is no question about accepting lower inflation as we are seeing today”, “we don’t like what we see on the inflation front”, “We don’t accept permanently lower inflation rates”, “on the inflation front we don’t like what we see”, “With the admission – and that’s again very important – with the admission that we don’t like this.”, “1.6% is the inflation rate that we see in 2021 in our projections. That’s something about which the Governing Council said today in the introductory statement: we don’t like it.” Source: ECB, Transcript of the press conference of Mario Draghi and Luis de Guindos on 25 July 2019



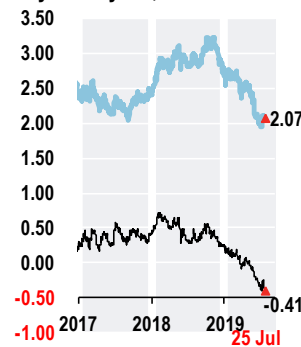
Markets overview

The essentials

Week 19-7-19 > 25-7-19

➔ CAC 40	5 552	➔ 5 578	+0.5 %
➔ S&P 500	2 977	➔ 3 004	+0.9 %
↘ Volatility (VIX)	14.5	➔ 12.7	-1.7 pb
↘ Euribor 3M (%)	-0.38	➔ -0.38	-0.3 bp
➔ Libor \$ 3M (%)	2.26	➔ 2.27	+0.7 bp
↘ OAT 10y (%)	-0.06	➔ -0.10	-3.6 bp
↘ Bund 10y (%)	-0.37	➔ -0.41	-3.9 bp
➔ US Tr. 10y (%)	2.05	➔ 2.07	+2.4 bp
↘ Euro vs dollar	1.12	➔ 1.12	-0.6 %
↘ Gold (ounce, \$)	1 429	➔ 1 419	-0.7 %
➔ Oil (Brent, \$)	62.3	➔ 63.8	+2.4 %

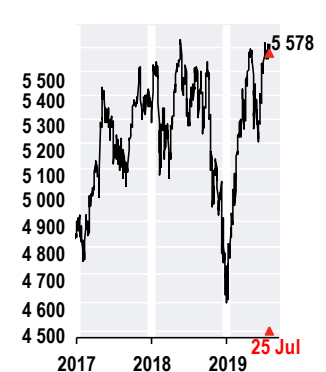
10 y bond yield, OAT vs Bund



Euro-dollar



CAC 40



— Bunds — OAT

Money & Bond Markets

Interest Rates	highest' 19	lowest' 19
€ ECB	0.00	0.00 at 01/01
Eonia	-0.36	-0.25 at 07/06
Euribor 3M	-0.38	-0.31 at 24/01
Euribor 12M	-0.32	-0.11 at 06/02
\$ FED	2.50	2.50 at 01/01
Libor 3M	2.27	2.81 at 01/01
Libor 12M	2.18	3.04 at 21/01
£ BoE	0.75	0.75 at 01/01
Libor 3M	0.78	0.93 at 29/01
Libor 12M	0.86	1.19 at 11/01

At 25-7-19

Yield (%)	highest' 19	lowest' 19
€ AVG 5-7y	-0.11	0.68 at 09/01
Bund 2y	-0.76	-0.53 at 05/03
Bund 10y	-0.41	0.25 at 01/01
OAT 10y	-0.10	0.73 at 08/01
Corp. BBB	0.77	2.15 at 08/01
\$ Treas. 2y	1.86	2.62 at 18/01
Treas. 10y	2.07	2.78 at 18/01
Corp. BBB	3.54	4.65 at 01/01
£ Treas. 2y	0.49	0.83 at 27/02
Treas. 10y	0.71	1.35 at 18/01

At 25-7-19

10y bond yield & spreads

2.70%	Greece	310 pb
1.52%	Italy	192 pb
0.44%	Portugal	84 pb
0.32%	Spain	72 pb
-0.05%	Belgium	35 pb
-0.10%	France	30 pb
-0.15%	Austria	25 pb
-0.18%	Ireland	22 pb
-0.23%	Finland	17 pb
-0.24%	Netherlands	16 pb
-0.41%	Germany	

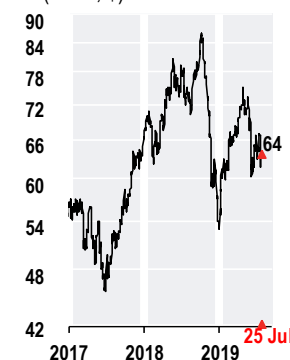
Commodities

Spot price in dollars	lowest' 19	2019(€)
Oil, Brent	63.8	53.1 at 01/01
Gold (ounce)	1 419	1 268 at 02/05
Metals, LMEX	2 847	2 730 at 03/01
Copper (ton)	5 987	5 714 at 03/01
CRB Foods	352	324 at 07/03
wheat (ton)	178	167 at 10/05
Corn (ton)	165	128 at 24/04

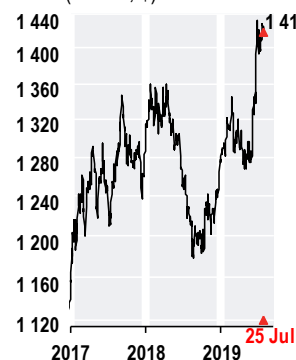
At 25-7-19

Variations

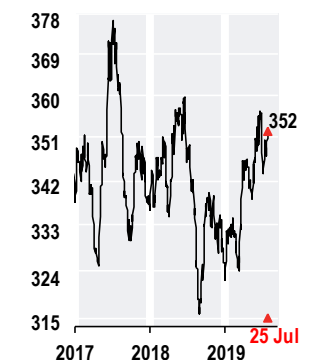
Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



Exchange Rates

1€ =	highest' 19	lowest' 19	2019
USD	1.12	1.15 at 10/01	-2.4%
GBP	0.89	0.90 at 03/01	-0.5%
CHF	1.10	1.14 at 23/04	-2.0%
JPY	121.13	127.43 at 01/03	-3.4%
AUD	1.60	1.64 at 17/06	-1.3%
CNY	7.67	7.87 at 09/01	-2.3%
BRL	4.22	4.59 at 20/05	-4.7%
RUB	70.36	79.30 at 01/01	-11.3%
INR	77.04	82.00 at 04/02	-3.5%

At 25-7-19

Variations

Equity indices

Index	highest' 19	lowest' 19	2019	2019(€)
CAC 40	5 578	5 621 at 04/07	4 611 at 03/01	+17.9%
S&P500	3 004	3 020 at 24/07	2 448 at 03/01	+19.8%
DAX	12 362	12 630 at 04/07	10 417 at 03/01	+17.1%
Nikkei	21 757	22 308 at 25/04	19 562 at 04/01	+8.7%
China*	80	86 at 09/04	68 at 03/01	+12.9%
India*	572	612 at 03/06	530 at 19/02	+1.4%
Brazil*	2 281	2 354 at 10/07	1 862 at 17/05	+14.5%
Russia*	710	747 at 04/07	572 at 01/01	+14.3%

At 25-7-19

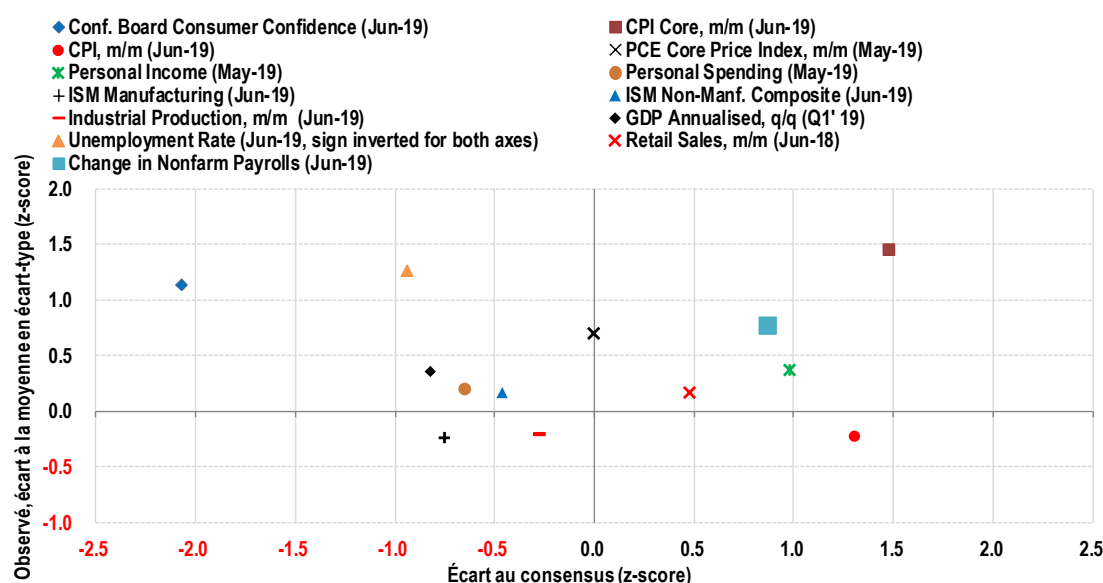
Variations

* MSCI index

Pulse

United States: Slowing growth

According to the recently released Beige Book of the Federal Reserve, the United States should continue to see modest growth. Most indicators are above their long-term average, the manufacturing ISM and industrial production being exceptions. Headline inflation is also below but the opposite holds for core inflation (both CPI and PCE). The labour market continues to perform well, which supports consumer confidence. However, indicators like retail sales, the non-manufacturing ISM and real GDP in Q1 were pretty close to the long-term average. This reflects that growth is cooling, something which also shows up in the number of data which came in below expectations.



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).

Indicators preview

A very heavy schedule next week. Highlights are the FOMC meeting (will the Fed cut its policy rate?) and the US labour market report. The Bank of England and the Bank of Japan also have their policy meeting. As usual at the start of a new month, the purchasing manager indices will be released. We will also have consumer confidence in several countries, second quarter GDP for the eurozone and France as well as inflation in France and Germany.

Date	Country/Region	Event	Period	Survey	Prior
07/30/2019	Japan	Jobless Rate	June	--	2.4%
07/30/2019	France	GDP QoQ	2Q	--	0.3%
07/30/2019	Germany	GfK Consumer Confidence	August	--	9.8
07/30/2019	France	Consumer Spending MoM	June	--	0.4%
07/30/2019	Eurozone	Economic Confidence	July	--	103.3
07/30/2019	Germany	CPI EU Harmonized MoM	July	--	0.3%
07/30/2019	United States	Personal Income	June	0.3%	0.5%
07/30/2019	United States	Personal Spending	June	0.3%	0.4%
07/30/2019	United States	Conf. Board Consumer Confidence	July	124.4	121.5
07/30/2019	Japan	BOJ Policy Balance Rate	July 30	--	-0.100%
07/31/2019	United Kingdom	GfK Consumer Confidence	July	--	-13
07/31/2019	China	Composite PMI	July	--	53.0
07/31/2019	Japan	Consumer Confidence Index	July	--	38.7
07/31/2019	France	CPI EU Harmonized MoM	July	--	0.3%
07/31/2019	Eurozone	Unemployment Rate	June	--	7.5%
07/31/2019	Eurozone	GDP SA QoQ	2Q	--	0.4%
07/31/2019	United States	FOMC Rate Decision (Lower Bound)	July 31	2.00%	2.25%
08/01/2019	China	Caixin China PMI Mfg	July	49.8	49.4
08/01/2019	France	Markit France Manufacturing PMI	July	--	50.0
08/01/2019	Germany	Markit/BME Germany Manufacturing PMI	July	--	43.1
08/01/2019	Eurozone	Markit Eurozone Manufacturing PMI	July	--	46.4



Date	Country/Region	Event	Period	Survey	Prior
08/01/2019	United Kingdom	Bank of England Bank Rate	August 1	0.750%	0.750%
08/01/2019	United States	ISM Manufacturing	July	52.3	51.7
08/02/2019	Eurozone	Retail Sales MoM	June	--	-0.3%
08/02/2019	United States	Change in Nonfarm Payrolls	July	160000	224000
08/02/2019	United States	Unemployment Rate	July	3.6%	3.7%
08/02/2019	United States	University of Michigan Sentiment	July	98.4	98.4
08/05/2019	Japan	Jibun Bank Japan PMI Composite	July	--	51.2
08/05/2019	China	Caixin China PMI Composite	July	--	50.6
08/05/2019	France	Markit France Composite PMI	July	--	51.7
08/05/2019	Germany	Markit/BME Germany Composite PMI	July	--	51.4
08/05/2019	Eurozone	Markit Eurozone Composite PMI	July	--	51.5
08/05/2019	United States	ISM Non-Manufacturing Index	July	55.0	55.1
08/06/2019	Japan	Leading Index CI	June	--	94.9
08/07/2019	Germany	Industrial Production SA MoM	June	--	0.3%
08/08/2019	France	Bank of France Ind. Sentiment	July	--	95
08/08/2019	Eurozone	ECB Publishes Economic Bulletin			
08/08/2019	China	Trade Balance	July	--	5.098e+10
08/09/2019	Japan	GDP Annualized SA QoQ	2Q	--	2.2%
08/09/2019	France	Wages QoQ	2Q	--	0.8%
08/09/2019	France	Private Sector Payrolls QoQ	2Q	--	0.5%
08/09/2019	France	Manufacturing Production MoM	June	--	1.6%
08/09/2019	United Kingdom	GDP QoQ	2Q	--	0.5%
08/09/2019	United States	PPI Final Demand MoM	July	0.2%	0.1%
08/09/2019	China	Aggregate Financing CNY	July	--	2.26e+12
08/13/2019	United Kingdom	ILO Unemployment Rate 3Mths	June	--	3.8%
08/13/2019	United States	NFIB Small Business Optimism	July	--	103.3
08/13/2019	United States	CPI MoM	July	--	0.1%
08/14/2019	Japan	Core Machine Orders MoM	June	--	-7.8%
08/14/2019	France	ILO Unemployment Rate	2Q	--	8.7%
08/14/2019	Germany	GDP SA QoQ	2Q	--	0.4%
08/14/2019	France	CPI EU Harmonized MoM	July	--	--
08/14/2019	Eurozone	Employment QoQ	2Q	--	0.3%
08/14/2019	Eurozone	GDP SA QoQ	2Q	--	--
08/15/2019	United Kingdom	Retail Sales Ex Auto Fuel MoM	July	--	0.9%
08/15/2019	United States	Empire Manufacturing	August	--	4.3
08/15/2019	United States	Philadelphia Fed Business Outlook	August	--	21.8
08/15/2019	United States	Retail Sales Advance MoM	July	--	0.4%
08/15/2019	United States	Industrial Production MoM	July	--	0.0%
08/15/2019	United States	NAHB Housing Market Index	August	--	65
08/16/2019	United States	Housing Starts MoM	July	--	-0.9%
08/16/2019	United States	Building Permits MoM	July	--	-6.1%
08/16/2019	United States	U. of Mich. Sentiment	August	--	--
08/19/2019	Eurozone	CPI MoM	July	--	0.2%
08/19/2019	United Kingdom	CBI Trends Total Orders	August	--	-34
08/21/2019	United States	MBA Mortgage Applications	August 16	--	--
08/21/2019	United States	Existing Home Sales MoM	July	--	-1.7%
08/21/2019	United States	FOMC Meeting Minutes	July 31	--	--
08/22/2019	Japan	Jibun Bank Japan PMI Composite	August	--	--
08/22/2019	France	Markit France Composite PMI	August	--	--
08/22/2019	Eurozone	Markit Eurozone Composite PMI	August	--	--
08/22/2019	United States	Markit US Composite PMI	August	--	--
08/22/2019	United States	Leading Index	July	--	-0.3%
08/22/2019	Eurozone	Consumer Confidence	August	--	--
08/22/2019	United States	Kansas City Fed Manf. Activity	August	--	--
08/23/2019	United States	New Home Sales MoM	July	--	7.0%
08/26/2019	Germany	Ifo Business Climate	August	--	--
08/26/2019	United States	Chicago Fed Nat Activity Index	July	--	-0.02
08/26/2019	United States	Durable Goods Orders	July	--	--

Date	Country/Region	Event	Period	Survey	Prior
08/26/2019	United States	Dallas Fed Manf. Activity	August	--	--
08/27/2019	Germany	GDP SA QoQ	2Q	--	--
08/27/2019	France	Consumer Confidence	August	--	--
08/27/2019	France	Business Confidence	August	--	105
08/27/2019	United States	Richmond Fed Manufact. Index	August	--	-12
08/27/2019	United States	Conf. Board Consumer Confidence	August	--	--
08/27/2019	Germany	Retail Sales MoM	July	--	--
08/28/2019	Germany	GfK Consumer Confidence	Sep	--	--
08/29/2019	France	GDP QoQ	2Q	--	--
08/29/2019	Germany	Unemployment Change (000's)	August	--	--
08/29/2019	Germany	Unemployment Claims Rate SA	August	--	--
08/29/2019	Eurozone	Economic Confidence	August	--	--
08/29/2019	United States	GDP Annualized QoQ	2Q	--	--
08/30/2019	United Kingdom	GfK Consumer Confidence	August	--	--
08/30/2019	Japan	Jobless Rate	July	--	--
08/30/2019	France	CPI EU Harmonized MoM	August	--	--
08/30/2019	Eurozone	Unemployment Rate	July	--	--
08/30/2019	United States	Personal Income	July	--	--
08/30/2019	United States	Personal Spending	July	--	--
08/30/2019	United States	U. of Mich. Sentiment	August	--	--

Source: Bloomberg, BNP Paribas



Economic scenario

UNITED STATES

- Growth picked-up by early 2019 but this was partly due to one-off factors (inventories). The trend in private domestic demand is more subdued. The housing market is softening, corporate investment should slow, as well as exports. Core inflation remains well under control and has eased a bit.
- We believe the Fed Funds target rate will be cut by 2 quarter points in Q3, coming back to 1.75-2% and an additional cut in Q2 2020.

CHINA

- Economic growth continues to slow. Activity rebounded in March 2019 but weakened again afterwards. The recent flare-up in trade tensions with the US has again darkened export prospects.
- 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, exports and private domestic investment should continue to decelerate. Tax measures should support consumer spending.

EUROZONE

- Despite a stronger than expected growth in the 1st quarter of 2019, the economic slowdown is continuing in the eurozone, especially in Germany, due to international environment uncertainties and a slowdown of exports to China. Capacity constraints also play a role and activity in the manufacturing sector continues to decline.
- Inflation is now expected to decrease 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.
- The message from the July meeting of the Governing Council was clear: inflation is expected to remain too low compared to the target, so more easing is necessary. Decisions in this respect should be announced at the meeting on 12 September.

FRANCE

- Growth is slowing although the economy shows 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, we expect the Fed to cut rates twice in the second semester in reaction to a slowing economy, subdued inflation and heightened uncertainty. Bond markets are already pricing in rate cuts, which is why we expect that the decline of the 10 year treasury yield will only be moderate.
- In the eurozone we expect a 10bp cut in the deposit rate (with tiering) to be announced at the Governing Council meeting of 12 September.
- No change expected in Japan.
- We expect the euro to strengthen versus the dollar considering that the latter is expensive on valuation grounds and that the Fed will ease its policy

%	GDP Growth			Inflation		
	2018	2019 e	2020 e	2018	2019 e	2020 e
Advanced	2.2	1.8	1.3	2.0	1.6	1.6
United-States	2.9	2.7	1.8	2.4	2.1	2.0
Japan	0.8	0.6	0.2	1.0	0.6	0.5
United-Kingdom	1.4	1.3	1.4	2.5	1.9	1.9
Euro Area	1.9	1.1	1.0	1.8	1.3	1.3
Germany	1.4	0.6	1.0	1.9	1.5	1.5
France	1.7	1.3	1.2	2.1	1.4	1.5
Italy	0.7	0.3	0.2	1.3	0.9	0.9
Spain	2.6	2.2	1.9	1.7	1.0	1.2
Emerging	4.5	4.2	4.7	4.7	4.8	4.3
China	6.6	6.2	6.0	2.1	2.2	2.6
India*	7.0	7.4	7.6	3.4	3.5	4.2
Brazil	1.1	0.8	2.5	3.7	3.9	3.9
Russia	2.3	1.5	1.7	2.9	5.1	4.1

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

* Fiscal year from April 1st of year n to March 31st of year n+1

Interest rates, %		2019				2018	2019e	2020e
End of period		Q1	Q2e	Q3e	Q4e			
US	Fed Funds	2.50	2.50	2.00	2.00	2.50	2.00	1.75
	Libor 3m \$	2.60	2.45	2.00	2.00	2.81	2.00	1.80
	T-Notes 10y	2.42	2.10	1.95	1.90	2.69	1.90	2.25
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	-0.05	-0.05	0.00	0.25	0.00	0.15
	OAT 10y	0.26	0.30	0.30	0.30	0.71	0.30	0.45
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	-0.10
	JGB 10y	-0.09	-0.03	-0.02	-0.02	0.00	-0.02	-0.05

Source : BNP Paribas GlobalMarkets (e: Forecasts)

Exchange Rates		2019				2018	2019e	2020e
End of period		Q1	Q2e	Q3e	Q4e			
USD	EUR / USD	1.12	1.13	1.16	1.20	1.14	1.20	1.25
	USD / JPY	111.0	108.0	105.0	102.0	110.0	102.0	95.0
	GBP / USD	1.30	1.27	1.32	1.38	1.27	1.38	1.49
	USD / CHF	1.00	1.01	0.99	0.97	0.99	0.97	0.94
EUR	EUR / GBP	0.85	0.89	0.88	0.87	0.90	0.87	0.84
	EUR / CHF	1.12	1.14	1.15	1.16	1.13	1.16	1.18
	EUR / JPY	124.0	122.0	122.0	122.0	125.0	122.0	119.0

Source : BNP Paribas GlobalMarkets (e: Forecasts)

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