

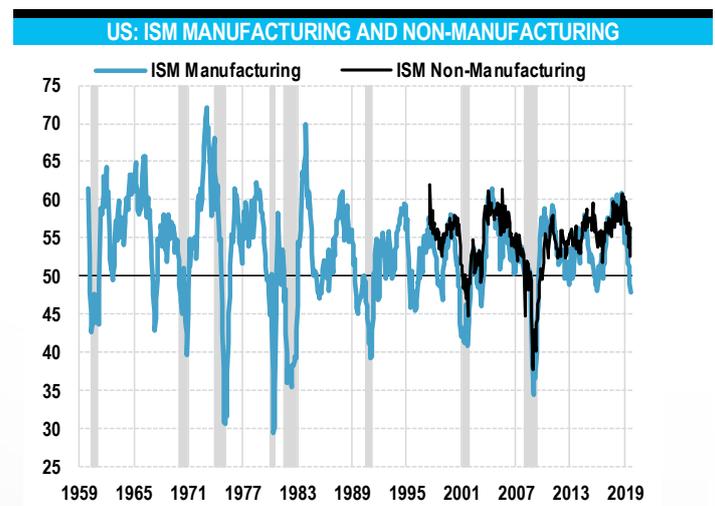
# ECOWEEK

No. 19-36, 04 October 2019

## US: from big growth scare to relief

■ The manufacturing purchasing managers' index of the Institute for Supply Management (ISM) has continued its decline in September, reaching 47.8%. The non-manufacturing ISM has registered a big drop of 3.8 percentage points and is now at 52.6% — a very low print for a non-recessionary period ■ Against this background, bond yields have declined significantly reflecting increasing worries about recession risk, rising expectations about additional Fed easing and a greater flight to safe havens ■ The labour market data for September however brought some relief. Nevertheless, we expect the Fed to continue to cut rates.

How many pieces of bad news does it take to become convinced that the cyclical environment has definitely changed? Difficult question to answer but what is clear is that a big growth scare has developed this week. Typically, it manifests itself through a drop in US treasury yields, as investors — faced with poor economic data — flee to safety. This pretty well summarises this week's experience. It started with the Institute for Supply Management's purchasing managers' index for the manufacturing sector which, for the month of September, dropped 1.3 percentage points to 47.8 percent. This puts the index firmly in recession territory as far as the manufacturing sector is concerned. The new export orders index declined 2.3 percentage points to reach a very low 41 percent reminding us that the slowdown taking place in the rest of the world is increasingly impacting the US. Until recently, one could argue that the services sector was quite resilient but the 3.8 percentage points decline in the non-manufacturing ISM index forces us to reassess this belief. The index is now at 52.6 percent which—as shown in the chart—is quite low, outside of recession periods. In combination with the very weak manufacturing ISM, this points towards a clear slowdown in GDP growth. Corporate investment is the weaker link here, given its sensitivity to uncertainty about where the economy is headed, and of course to worries about how the confrontation with China on trade will evolve. For the household sector, the labour market plays a key role in shaping confidence and expectations about the evolution of income. Household consumption is a key variable for growth, given its weight in GDP (70%) but also considering the



Source: Institute for Supply Management, BNP Paribas

pressure on exports and the subdued outlook for corporate investment. Against this background, the labour market report provided some welcome relief to the market and observers as 136,000 jobs were added in September and the unemployment rate declined to 3.5% from 3.7%. Nevertheless, we think that the US economy will continue to slow in the coming quarters, forcing the Fed to cut rates further

William De Vijlder

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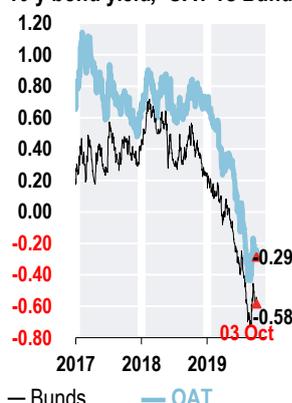
## Markets overview

### The essentials

Week 27-9 19 > 3-10-19

➤ CAC 40	5 641	▶ 5 439	-3.6 %
➤ S&P 500	2 962	▶ 2 911	-1.7 %
➤ Volatility (VIX)	17.2	▶ 19.1	+1.9 pb
➤ Euribor 3M (%)	-0.41	▶ -0.43	-1.3 bp
➤ Libor \$ 3M (%)	2.10	▶ 2.06	-4.2 bp
➤ OAT 10y (%)	-0.27	▶ -0.29	-1.3 bp
➤ Bund 10y (%)	-0.58	▶ -0.58	-0.7 bp
➤ US Tr. 10y (%)	1.67	▶ 1.54	-13.8 bp
➤ Euro vs dollar	1.09	▶ 1.10	+0.3 %
➤ Gold (ounce, \$)	1 492	▶ 1 510	+1.2 %
➤ Oil (Brent, \$)	62.4	▶ 57.4	-8.0 %

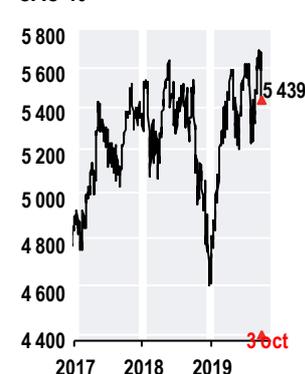
10 y bond yield, OAT vs Bund



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	-0.47 at 07/06	-0.47 at 03/10
Euribor 3M	-0.43 at 24/01	-0.45 at 03/09
Euribor 12M	-0.33 at 06/02	-0.40 at 21/08
\$ FED	2.50 at 01/01	2.00 at 19/09
Libor 3M	2.06 at 01/01	2.06 at 02/10
Libor 12M	1.96 at 21/01	1.89 at 05/09
£ BoE	0.75 at 01/01	0.75 at 01/01
Libor 3M	0.77 at 29/01	0.75 at 29/08
Libor 12M	0.91 at 11/01	0.81 at 03/09

At 3-10-19

Yield (%)	highest' 19	lowest' 19
€ AVG 5-7y	-0.23 at 09/01	-0.36 at 03/09
Bund 2y	-0.78 at 05/03	-0.92 at 02/09
Bund 10y	-0.58 at 01/01	-0.72 at 28/08
OAT 10y	-0.29 at 08/01	-0.44 at 28/08
Corp. BBB	0.80 at 08/01	0.64 at 30/08
\$ Treas. 2y	1.39 at 18/01	1.39 at 03/10
Treas. 10y	1.54 at 18/01	1.46 at 04/09
Corp. BBB	3.18 at 01/01	3.15 at 04/09
£ Treas. 2y	0.37 at 27/02	0.32 at 03/09
Treas. 10y	0.48 at 18/01	0.33 at 03/09

At 3-10-19

10y bond yield & spreads

1.70%	Greece	228 pb
0.83%	Italy	141 pb
0.15%	Portugal	73 pb
0.15%	Spain	73 pb
-0.25%	Belgium	33 pb
-0.28%	Ireland	30 pb
-0.29%	France	29 pb
-0.32%	Finland	26 pb
-0.33%	Austria	25 pb
-0.45%	Netherland	13 pb
-0.58%	Germany	

### Commodities

Spot price in dollars	lowest' 19	2019(€)
Oil, Brent	53.1 at 01/01	+12.4%
Gold (ounce)	1 268 at 02/05	+22.6%
Metals, LMEX	2 774 at 07/08	+3.1%
Copper (ton)	5 628 at 03/09	-1.5%
CRB Foods	312 at 11/09	+4.4%
wheat (ton)	166 at 30/08	-8.2%
Corn (ton)	128 at 24/04	+13.1%

At 3-10-19

Variations

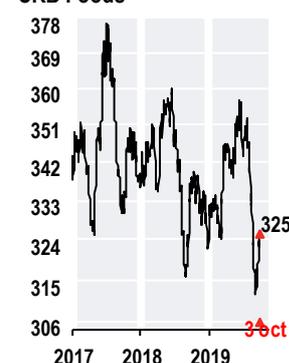
Oil (Brent, \$)



Gold (Ounce, \$)



CRB Foods



### Exchange Rates

€ =	highest' 19	lowest' 19	2019
USD	1.15 at 10/01	1.09 at 30/09	-3.9%
GBP	0.93 at 12/08	0.85 at 14/03	-1.3%
CHF	1.14 at 23/04	1.08 at 04/09	-2.8%
JPY	127.43 at 01/03	116.08 at 03/09	-6.6%
AUD	1.66 at 07/08	1.57 at 18/04	+0.3%
CNY	7.96 at 27/08	7.51 at 25/04	-0.1%
BRL	4.63 at 27/08	4.18 at 31/01	+1.5%
RUB	79.30 at 01/01	70.22 at 24/09	-9.6%
INR	82.00 at 04/02	76.37 at 01/08	-2.5%

At 3-10-19

Variations

### Equity indices

Index	highest' 19	lowest' 19	2019	2019(€)
CAC 40	5 691 at 20/09	4 611 at 03/01	+15.0%	+15.0%
S&P500	3 026 at 26/07	2 448 at 03/01	+16.1%	+20.8%
DAX	12 630 at 04/07	10 417 at 03/01	+12.9%	+12.9%
Nikkei	22 308 at 25/04	19 562 at 04/01	+6.6%	+14.1%
China*	86 at 09/04	68 at 03/01	+6.2%	+10.2%
India*	555 at 03/06	526 at 22/08	+1.0%	+3.6%
Brazil*	2 354 at 10/07	1 862 at 17/05	+12.4%	+10.8%
Russia*	688 at 04/07	572 at 01/01	+14.1%	+25.1%

At 3-10-19

Variations

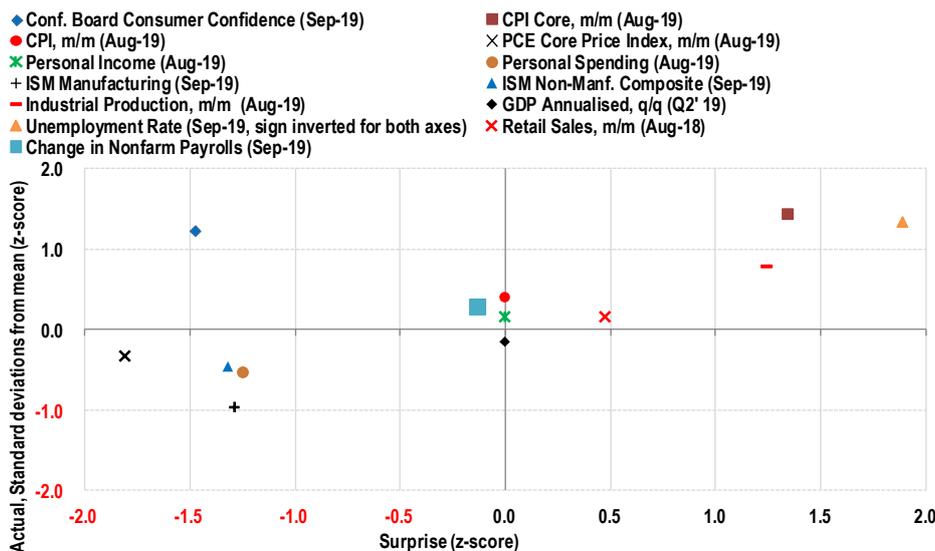
\* MSCI index



## Pulse

### United States : key data send conflicting signals

Although August industrial production and retail sales beat expectations, key data with respect to September have sent conflicting signals. Both the manufacturing and non-manufacturing ISM came in below expectations, creating a lot of nervousness in the run-up to the release of the all-important labour market data. They brought relief with 136.000 jobs having been added in September (versus a Bloomberg consensus of 145.000) and, in particular, an unemployment rate of 3.5%, which is well below the consensus of 3.7%. The labour market is of particular importance for household spending, even more so considering that the Conference Board consumer confidence index has also disappointed in September. The ambiguous signal coming from the recent data releases complicates the task of economic forecasters in assessing the pace of slowdown of the US economy. It is also a challenge for the Federal Reserve in deciding whether to ease policy further. In our view, the FOMC will proceed with further rate cuts.



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,  $\mu$ : mean,  $\sigma$ : standard deviation. On the X-axis,  $x$  corresponds at the last known surprise for each indicator represented on the graph,  $\mu$  and  $\sigma$  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 a

t the last known value of indicator,  $\mu$  and  $\sigma$  corresponds respectively to the mean and the standard deviation for this indicator since 2000 (for China since 2011).

### Indicators preview

Important releases next week are the Caixin PMI in China, the Banque de France industrial sentiment index and, in the US, the sentiment index of the University of Michigan. In Japan, attention will focus on the leading indicator, the Eco Watchers survey as well as machine orders. In the US we will have producer and consumer prices. Of particular importance is the publication of the minutes of the latest FOMC meeting, given the disagreement about the decision to cut the policy rate.

Date	Country/Region	Event	Period	Survey	Prior
10/07/2019	Japan	Leading indicator CI	Aug.	--	93.7
10/08/2019	China	PMI Composite (Caixin)	Sep.	--	51.6
10/08/2019	China	PMI Services (Caixin)	Sep.	52.0	52.1
10/08/2019	Germany	Industrial production CVS MoM	Aug.	--	-0.6%
10/08/2019	USA	NFIB Small Business Optimism	Sep.	102.5	103,1
10/08/2019	USA	PPI Ex Food and Energy MoM	Sep.	0.2%	0.3%
10/08/2019	Japan	CVS Eco watchers survey	Sep..	--	42.8
10/09/2019	Japan	Machine orders y/y	Sep.	--	-37.0%
10/09/2019	France	Industrial sentiment index (Banque de France)	Sep.	--	99
10/09/2019	USA	Minutes of FOMC meeting	Sep.18	--	--
10/09/2019	China	Total financing CNY	Sep.	1.8e+12	1.98e+12
10/10/2019	Japan	Core Machinery Orders MoM	Aug.	--	-6.6%
10/10/2019	Japan	Core Machinery Orders YoY	Aug.	--	0.3%
10/10/2019	Germany	Exports CVS MoM	Aug.	--	0.7%
10/10/2019	France	Industrial production MoM	Aug.	--	0.3%
10/10/2019	United Kingdom	GDP MoM	Aug.	--	0.3%
10/10/2019	USA	CPI MoM	Sep.	0.1%	0.1%
10/11/2019	Germany	CPI EU Harmonized MoM GM	Sep.	--	-0.1%
10/11/2019	USA	University of Michigan sentiment	Oct.	92.3	93.2

Source: Bloomberg, BNP Paribas



## Economic scenario

### UNITED STATES

- Growth is slowing and this trend is expected to continue under the influence of corporate investment (slower profits growth, uncertainty) and housing (declining trend of affordability). Consumer spending should be more resilient. The trade dispute with China acts as an additional drag. Inflation is expected to decline, due to softer growth and weaker oil prices.
- We expect one more Fed Funds target rate cut of 25bp this year and two additional cuts in 2020.

### CHINA

- Economic growth continues to slow and our GDP forecasts have been revised down since June. Industrial activity and exports have been hard hit by US tariff hikes. Domestic demand has also decelerated.
- The central bank is easing liquidity and credit conditions, though the reduction in financial-instability risks should remain a priority and banks seem to remain prudent. Fiscal policy is 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 have some success in supporting consumer spending.

### EUROZONE

- The economic slowdown is continuing in the eurozone, especially in Germany, due to notably international environment uncertainties and a slowdown of the Chinese economy. Activity in the manufacturing sector continues to decline but services still show resilience.
- 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.
- Faced with an outlook of subdued inflation, the Governing Council has eased policy at its meeting on 12 September. This very accommodative environment will be maintained as long as inflation hasn't converged sufficiently, in a convincing and lasting way, towards the ECB's objective.

### 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 its official rate in December in reaction to a slowing economy, moderate inflation and heightened uncertainty. 2020 should see two more cuts. Treasury yields are to decline further in the coming months. Eventually, in the course of 2020 they should move up again in anticipation of a pick-up in growth.
- In the eurozone, the ECB's state-dependent forward guidance and the sluggishness of the inflation process imply that the very accommodative environment will remain in place for a long time. This will exert downward pressure on bond yields.
- No policy rate change expected in Japan.
- With the Fed in easing mode and given the very accommodative ECB policy, we expect little change in EUR/USD even though euro's fair value is quite higher than current pricing. The yen should strengthen on the back of stable BoJ policy and high market volatility.

%	GDP Growth			Inflation		
	2018	2019 e	2020 e	2018	2019 e	2020 e
<b>Advanced</b>	<b>2.2</b>	<b>1.6</b>	<b>1.0</b>	<b>2.1</b>	<b>1.4</b>	<b>1.3</b>
United-States	2.9	2.2	1.5	2.4	1.8	1.8
Japan	0.8	1.2	0.2	1.0	0.6	0.3
United-Kingdom	1.4	1.1	0.6	2.5	1.9	1.8
<b>Euro Area</b>	<b>1.9</b>	<b>1.1</b>	<b>0.7</b>	<b>1.8</b>	<b>1.1</b>	<b>0.8</b>
Germany	1.4	0.4	0.2	1.9	1.4	1.0
France	1.7	1.2	1.0	2.1	1.2	1.0
Italy	0.7	0.1	0.0	1.2	0.6	0.5
Spain	2.6	2.2	1.6	1.7	0.8	0.7
<b>Emerging</b>	<b>4.4</b>	<b>3.8</b>	<b>4.2</b>	<b>4.7</b>	<b>4.8</b>	<b>4.5</b>
China	6.6	5.9	5.6	2.1	2.4	2.8
India*	6.8	6.5	6.3	2.9	3.0	3.3
Brazil	1.1	0.5	2.0	3.7	3.7	3.5
Russia	2.3	1.2	2.0	2.9	4.8	3.8

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
	Q1	Q2	Q3e	Q4e			
<b>US</b>							
Fed Funds	2.50	2.50	2.00	1.75	2.50	1.75	1.25
Libor 3m \$	2.60	2.32	1.90	1.70	2.81	1.70	1.25
T-Notes 10y	2.42	2.00	1.35	1.00	2.69	1.00	1.50
<b>Ezone</b>							
Deposit rate (%)	-0.40	-0.40	-0.50	-0.60	-0.40	-0.60	-0.60
Bund 10y	-0.07	-0.32	-0.50	-0.80	0.25	-0.80	-0.50
OAT 10y	0.26	-0.01	-0.20	-0.55	0.71	-0.55	-0.30
<b>UK</b>							
Base rate	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Gilts 10y	1.00	0.84	0.75	0.55	1.27	0.55	0.75
<b>Japan</b>							
BoJ Rate	-0.06	-0.08	-0.10	-0.10	-0.07	-0.10	-0.10
JGB 10y	-0.09	-0.16	-0.30	-0.40	0.00	-0.40	-0.25

Source : BNP Paribas GlobalMarkets (e: Forecasts)

Exchange Rates	2019				2018	2019e	2020e
	Q1	Q2	Q3e	Q4e			
<b>USD</b>							
EUR / USD	1.12	1.14	1.10	1.11	1.14	1.11	1.14
USD / JPY	111	108	105	102	110	102	96
GBP / USD	1.30	1.27	1.20	1.23	1.27	1.23	1.36
USD / CHF	1.00	0.98	0.99	0.99	0.99	0.99	1.00
<b>EUR</b>							
EUR / GBP	0.85	0.89	0.92	0.90	0.90	0.90	0.84
EUR / CHF	1.12	1.11	1.09	1.10	1.13	1.10	1.14
EUR / JPY	124	123	116	113	125	113	109

Source : BNP Paribas GlobalMarkets (e: Forecasts)



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