Weekly Market Brief

AIB Treasury Economic Research Unit

10th-14th December 2018

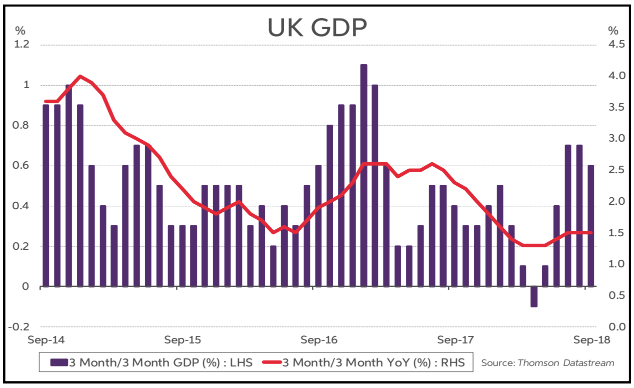
A Wall of Worry

- **The past few days on financial markets have been turbulent. Equity markets came under sharp selling pressure, with Wall Street suffering a fall of over 3% on Tuesday alone.** However, the stress has not just been confined to stocks. Oil prices experienced further falls, while credit spreads widened sharply. At the same time, sovereign bonds benefitted from safe haven appeal, resulting in declining yields. **The US 10 year Treasury yield fell by 20bps in the past week, declining to below 2.9%. Even more noteworthy, the US yield curve inverted as 5 year yields dropped below 2 year yield levels.** An inverted curve has tended to be a forerunner to a downturn in the US economy. However, underlying economic fundamentals (incl. labour market metrics) remain strong in the US and while the economy is likely to slow next year, there are no signs that a recession is imminent.

- Overall, what could be happening is that **markets may be in the process of repricing valuations and risk to more realistic levels** in light of the vast array of threats hovering on the horizon. These include slowing global growth, escalating trade tensions, geopolitical risks, tightening in global monetary policy and Brexit. **If the global economy holds up, investors may return to riskier assets in the New Year** given more attractive valuations following the recent sell-off.

- **The week ahead will bring Brexit risk very much to the front and centre of market attention. The UK Parliament is due to vote on the Withdrawal Agreement on Tuesday.** It is widely expected that the deal will be rejected by Parliament. What happens after that is unclear. Much will depend on the margin by which the vote is lost. A possible Labour party motion of no confidence in the government is not expected to be successful. A second vote on the Brexit deal may occur in the New Year. There is also the possibility of another referendum and, given the turmoil in parliament, a General Election cannot be ruled out. The reaction of markets to the likely defeat of the Brexit deal vote is hard to gauge. It should be largely priced into markets, including sterling. However, if the margin of defeat is very large, it could trigger greater political instability and in turn a sharper market reaction.

- **While market attention will be largely focussed on proceedings in Parliament this week, there is also a bumper UK data calendar. The key release is the GDP estimate for the three months to October.** Growth was relatively stagnant in the last two months of Q3 and leading indicators, such as the PMIs, fell back in October. Therefore, the consensus is for GDP growth to have moderated to 0.4%, from 0.6%, in the period. Meantime, industrial output is expected to have remained flat in October, while the goods trade balance is forecast to have widened in the month. Employment growth has been weak recently and this trend looks to have continued in October, with the unemployment rate seen holding at just 4.1%. The tightness of the labour market will likely result in underlying earnings maintaining their over 3.0% annual growth rate.



- **In the US, a packed diary includes the release of CPI data for November.** Headline inflation is projected to have decelerated to 2.2%, from 2.5%, while the core measure is forecast to have moved up slightly to 2.2%, from 2.1%. November retail sales are projected to rise by 0.2%. A solid monthly increase is pencilled in for the November reading of industrial output. In a timelier update, flash PMIs for December are expected to show that the US economy is continuing to grow strongly.

- **Elsewhere, the highlight of the Eurozone agenda is the ECB meeting.** The central bank is ending its asset purchase programme this month. In terms of interest rates, the Governing Council have been guiding that hikes are on hold "at least through the summer of 2019". Markets will look to the accompanying press conference, meeting statement and updated staff projections for any insight into the implications of financial volatility and recent weaker macro data on the likely future path for rates.

- **Data-wise, flash PMIs for December are also due in the Eurozone. The composite index is expected to have edged upwards in the month.** Meantime, in terms of other noteworthy releases, wage growth is anticipated to have recorded a healthy increase in Q3, while industrial output is projected to have risen slightly in October. Finally, the **Q3 National Accounts are due in Ireland** with growth forecast to have slowed, reflecting base effects from 2017. However, the data remain volatile and are heavily distorted by the activity of a few large multinationals.

Interest Rate Forecasts

	Current	End Q4 2018	End Q1 2019	End Q2 2019
Fed Funds	2.125	2.375	2.625	2.875
ECB Deposit	-0.40	-0.40	-0.40	-0.40
BoE Repo	0.75	0.75	0.75	1.00
BoJ OCR	-0.10	-0.10	-0.10	-0.10

Current Rates Reuters, Forecasts AIB's ERU

Exchange Rate Forecasts (Mid-Point of Range)

	Current	End Q4 2018	End Q1 2019	End Q2 2019
EUR/USD	1.1388	1.14	1.15	1.17
EUR/GBP	0.8929	0.89	0.87	0.86
EUR/JPY	128.30	129	129	130
GBP/USD	1.2751	1.28	1.32	1.36
USD/JPY	112.66	113	112	111

Current Rates Reuters, Forecasts AIB's ERU

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ECONOMIC DIARY

Monday 10th —Friday 14th December 2018

Date	*UK & Irish Time (GMT)*		*Release*	*Previous*	*Forecast*
This Week:	**ECB Speakers:**		de Guindos (Tuesday); de Cos (Wednesday); de Guindos, **Draghi**, Lautenschlager (Friday)		
	EU-27:		EU Leaders' Summit (Thursday to Friday)		
Mon 10th	**JPN:**	00.00	GDP (Q3: Second Reading)	-0.3% / -1.2% s.a.a.r. (p)	-0.5% / -1.9%
	JPN:	05.00	Economy Watchers' Poll (October)	49.5	
	GER:	07.00	Trade Balance (October)	€17.6bn	€17.7bn
			- Exports	-0.8%	+0.5%
	ITA:	09.00	Industrial Output (October)	-0.2%	-0.4%
	UK:	09.30	GDP (3 months to October)	+0.6% (+1.5%)	+0.4% (1.6%)
	UK:	09.30	Industrial Output (October)	+0.0% (+0.0%)	+0.1% (-0.2%)
			- Manufacturing	+0.2% (+0.5%)	+0.0% (+0.0%)
	UK:	09.30	Goods Trade Balance (October)	-£9.73bn	-£10.5bn
			- Non-EU	-£2.34bn	-£3.15bn
	EU-19:	09.30	Sentix Index (December)	8.8	8.3
Tue 11th	**UK:**		Parliamentary Vote on the Withdrawal Agreement		
	UK:	09.30	ILO Unemployment (3 months to October)	4.1%	4.1%
			- Employment	+23,000	+20,000
	UK:	09.30	Average Weekly Earnings (3 months to October)	(+3.0%)	(+3.0%)
			- Ex-Bonus	(+3.2%)	(+3.2%)
	GER:	10.00	ZEW Economic Sentiment (December)	-24.1	-25.0
	US:	11.00	NFIB Business Optimism (November)	107.4	
	IRL:	***11.00***	***Residential Property Prices (October)***	***+0.7% (+8.2%)***	***+0.5% (+8.4%)***
	US:	13.30	PPI (November)	+0.6% (+2.9%)	+0.0% (2.6%)
	JPN:	23.50	Domestic Wholesale Prices (November)	(+2.9%)	(+2.4%)
	JPN:	23.50	Core Machinery Orders (October)	(-7.0%)	(+5.9%)
Wed 12th	**EU-19:**	10.00	Industrial Output (October)	-0.3% (+0.9%)	+0.3% (+0.8%)
	US:	08.50	CPI (November)	(+2.5%)	(+2.2%)
			- Core (Ex-Food & Energy)	(+2.1%)	(+2.2%)
	US:	19.00	Federal Budget (November)	Nov'17: -$139bn	
Thurs 13th	**UK:**	00.01	RICS House Price Survey (November)	-10	
	GER:	07.00	Final HICP (November)	(+2.2%)	(+2.2%)
	FRA:	07.45	Final HICP (November)	(+2.2%)	(+2.2%)
	IRL:	***11.00***	***CPI (November)***	***-0.1% (+0.9%)***	***+0.0% (+1.1%)***
	IRL:	***11.00***	***GDP (Q3)***	***(+9.0%)***	***(+3.5%)***
	EU-19:	12.45	ECB Refi Rate Announcement	0.00%	0.00%
			- Deposit Rate	-0.40%	-0.40%
	EU-19:	13.00	ECB Press Conference		
	US:	13.30	Import / Export Prices (November)	+0.5% / +0.4%	-0.5% / +0.2%
	US:	13.30	Initial Jobless Claims (w/e 3rd December)	231,000	230,000
	JPN:	23.50	Tankan Big Manufacturing Index (Q4)	19	17
			- Non-Manufacturing	22	21
Fri 14th	**CHINA:**	02.00	Industrial Output (November)	(+5.9%)	(+5.9%)
	EU-19:	08.00	Flash Markit Composite PMI (December)	52.7	52.8
			- Manufacturing / Services	51.8 / 53.4	52.0 / 53.5
	FRA:	08.15	Flash Markit Composite PMI (December)	54.2	53.9
	GER:	08.30	Flash Markit Composite PMI (December)	52.3	52.6
	ITA:	09.00	Final HICP	(+1.7%)	(+1.7%)
	EU-19	10.00	Wage Growth (Q3)	(+1.9%)	
	IRL:	***11.00***	***Goods Trade Balance (October)***	***€3.0bn***	***€3.5bn***
	US:	13.30	Retail Sales (November)	+0.8%	+0.2%
			- Ex-Autos	+0.7%	+0.3%
			- Ex-Gas, Autos & Building Materials	+0.3%	+0.4%
	US:	14.15	Industrial Production (November)	+0.1%	+0.3%
			- Capacity Utilisation	78.4%	78.5%
	US:	14.45	Flash Markit Composite PMI (December)	54.7	
			Manufacturing / Services	55.3 / 54.7	55.2 / 55.0

♦ *Month-on-month changes (year-on-year shown in brackets)*
All forecasts AIB ERU, historical data in the Economic Diary derived from publicly available sources