

## Risk factors

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The table below presents risk factors with judgmental probabilities (i.e. not market based). It also develops the possible market impacts.

Risk # 1	50% probability	<b>Further escalation in trade tensions between the US and China</b>
<p><b>Analysis</b>   Donald Trump increased US tariffs on Chinese imports and announced an additional increase on January 1<sup>st</sup>. China's retaliations have remained moderate. It is likely that Trump's threats (e.g. rise in tariffs on auto imports) are primarily a message sent to his electoral base in the run-up to the mid-term elections (6 November). However we should not rule out a much more severe confrontation between the US and China. Although the probability of an escalation of trade tensions is elevated, that of a chain reaction seems quite limited (25%) for at least two reasons: (1) many sectors in the US would be victims of retaliation which would be counterproductive (strong opposition perceptible in the Republican camp/ boomerang effect); (2) trading partners would be careful not to fall into the trap set and maintain a measured response. That said, we cannot ignore the risk of a clash between China and the US, for at least two other reasons: (1) the moderate camp (favourable to free trade) has almost disappeared from the White House and (2) the strategy pursued by Donald Trump seems to benefit him: his rating approval has increased over the past few weeks, the US economy is close to full employment and the non-manufacturing ISM reached its highest historical level in October (since the index was created in 1997).</p> <p><b>Market impact</b>   Trade tensions have begun to weigh on business climate (especially in the manufacturing sector in Europe) and on the Chinese economy. Subsequently some private-investment projects might be postponed. Even in the absence of a large-scale trade war, global trade, which has started to slow, may thus slow down further. A chain reaction would cause a fall in global trade of goods while exacerbating local inflationary pressures in the short run (mainly in the US), putting central banks in a corner. This would cause a general rise in risk aversion (fear of a global downturn). At the end of the day, a more severe confrontation would only make losers.</p>		
Risk # 2	50% probability	<b>An additional increase in the price of oil</b>
<p><b>Analysis</b>   Oil prices continued to rise over the recent weeks (reaching a peak at US\$ 86 for the Brent on 4 October before sliding to \$83 on 8 October), at its highest level for 4 years. This increase is due mainly to the anticipation of a drop in Iran's oil supply; indeed, the beginning of US sanctions on Iran led, in practice, many countries to stop importing (or to reduce their oil import) from Iran. So far, OPEC countries and Russia have not compensated for the missing supply and US producers are not able to do so (at least not in the short term due to local bottlenecks).</p> <p><b>Market impact</b>   The rise in oil prices weighs on household's purchasing power and on corporate profit margins. Domestic demand in the Eurozone is more at risk than in the US. The emerging economies – those which are net oil importers and which have already been weakened by capital outflows – also see their situation deteriorating. In the short term, the increase in oil prices can increase the inflation risk (base effect) and increase the nervousness of central bankers (the Fed and some Asian CBs). But ultimately, induced inflation should remain transient, with little transmission to core inflation if at the same time GDP growth slows down. In the end, a supply shock would (should) prove more deflationary than inflationary.</p>		
Risk # 3	20% probability	<b>Political instability in Italy with renewed stress on sovereign spreads in the Eurozone</b>
<p><b>Analysis</b>   The government coalition in Italy (between M5S and the League) has obscured the European sky. Relations between the Italian government and other EU countries are very tense, particularly in terms of fiscal policy and migration policy. The Italian government announced an increase in its budget deficit target for 2019-2021. Although its initial proposal (2.4% of GDP on 3 years) was revised in the following days (with a deficit set at 1.8% in 2021), new projections are far away from the commitment of the previous government: -0.8%, 0.0% and + 0.2% of deficit GDP. For the European Commission and for rating agencies, the projected fiscal slippage may not be considered compatible with the medium-term debt sustainability. The good news, however, is that the government remains apparently concerned about containing the debt-to-GDP ratio. Reactions from the European Commission and rating agencies are expected soon. The "arm-wrestling match" with the Commission just starts out.</p> <p><b>Market impact</b>   There is no systemic risk in our opinion. The rise in Italian bond yields has tightened local financial conditions and that will weigh on the ongoing recovery in Italy. And it may even endanger the public-debt sustainability in the medium term. But, at present levels of GDP growth and interest rates, debt is still sustainable. The risk remains domestic since Italian savings are abundant and government-debt securities are mainly held by residents (at 70%): in the short term, they have the ability to absorb the issuance of additional Treasury securities. Moreover, the ECB has anti-contagion tools that it could mobilise to avoid a contagion to other peripheral markets. All of this explains the absence of contagion on peripheral sovereign spreads and on corporate credit spreads.</p>		

Risk # 4

**20%**  
probability

**“Hard Brexit”**

**Analysis** | The political situation in the UK is very unstable, with a government, a majority and a parliament that are particularly divided. We identify 4 possible scenarios: (1) Soft Brexit (50% probability) with an extended transition period, followed by a specific customs union arrangement, free trade in goods but only partial access for services (intermediate regimes of mutual recognition and equivalences, some oversight by the ECJ...). (2) Very soft Brexit (20% probability), with an extended transition period, after which the UK remains in the EU customs union and in a close-to-EEA relationship relatively to the single market (incl. Few restrictions on movements of people). (3) A hard Brexit (20% probability), on WTO terms with very little access for services. (4) No Brexit (10% probability). It would probably require early elections and a major change in government, followed by another referendum. A “no Brexit” scenario may be confirmed only after a long period of uncertainty (withdrawal of the UK’s invocation of Art. 50).

**Market impact** | Scenarios (3) and (4) would be accompanied by financial turbulence but for very different reasons. It would probably be necessary to go through a serious political crisis to question Brexit (scenario 4). With regard to (3), we stick to the view that the likelihood of a hard Brexit is low but negotiations get bogged down which is not good news. We expect rising tensions in the coming months. This might even be the precondition to reach a compromise later. In the event that the outcome is ultimately unfavourable for the UK, we would see a weakening of the GBP and below-trend GDP growth.

Risk # 5

**20%**  
probability

**Continuation of the contagion in the “emerging world”**

**Analysis** | Emerging markets have been suffering since the start of the year, impacted by (1) the Fed’s rate hikes, (2) by the trade war rhetoric (3) by the tightening in domestic monetary conditions (many EM central banks have risen their key rates) and (4) by the deterioration of the outlook in several countries at the same time (Argentina, China, Turkey, South Africa and Brazil). In fact, even though the systemic risk is lower than in the past (given the lesser vulnerability of emerging countries), most markets have dropped since the beginning of the year. Fears of more intense trade war between the US and China would undoubtedly push to a larger contagion (because value chains are very integrated).

**Market impact** | Credit spreads and equity markets would be highly hurt; it all the more true that emerging currencies would remain under pressure with more capital outflows. Even though the emerging world is not a homogeneous block, it has a clear tendency to behave like a block when market conditions deteriorate sharply. That’s why caution about emerging markets is still required at present. The rise in oil prices is another factor of vulnerability for many EM countries (oil importers). Having said, that EM markets have already priced in most bad news, and at some point, they should become attractive again.

Risk # 6

**15%**  
probability

**Pro-cyclical fiscal policy pushes the Fed to raise its rates more quickly than expected**

**Analysis** | The expansionist budgetary policy (tax cuts and increase in public spending) has continued to boost GDP growth in 2018. With growth close to 3%, inflation that is likely to exceed 2% on average this year and an economy that is close to full employment (with a positive output gap), the real fed funds rate should be higher than it is now, in a normal cycle. So, technically, the Fed is “behind the curve”. The Fed must clearly avoid any communication errors. Markets could react poorly if rates surge. The most recent example of a bond crash dates back to February 1994 and was triggered by a 25bp increase in rates (not prepared). This type of policy mistake is highly improbable today: the Fed is now reporting that it would not over-react should inflation accelerate temporarily. However, we note that the short-term positive impact of the budgetary policy should allow the Fed to continue to raise interest rates without increasing the risk of recession and, as such, without damaging the financial markets.

**Market impact** | There is no systemic risk in our opinion. The rise in Italian bond yields has tightened local financial conditions and that will weigh on the ongoing recovery in Italy. And it may even endanger the public-debt sustainability in the medium term. But, at present levels of GDP growth and interest rates, debt is still sustainable. The risk remains domestic since Italian savings are abundant and government-debt securities are mainly held by residents (at 70%): in the short term, they have the ability to absorb the issuance of additional Treasury securities. Moreover, the ECB has anti-contagion tools that it could mobilise to avoid a contagion to other peripheral markets. All of this explains the absence of contagion on peripheral sovereign spreads and on corporate credit spreads. If the Fed accelerates its monetary normalisation (with more rate hikes than expected), credit spreads would probably jump and equity markets fall in the US and probably also in many EMs. This situation would be conducive to a widening of spreads between Europe and the US.

Risk # 7

**15%**  
probability

**A Chinese “hard landing”/ a bursting of the credit bubble**

**Analysis** | Chinese economic growth is slowing down but the authorities are working hard to stimulate the economy (through FX management, monetary and fiscal policies) so that the economy is expected to remain resilient. That being said, the country’s economic model is fragile: the excess of credit is visible, non-financial corporate debt has surged since the GFC.

The good news is that the NFC debt to GDP ratio had started to drop since late 2017. We will continue to monitor closely the trend in Chinese private debt, especially if the economy slows. In the case of hard landing or the bursting of the credit bubble, the Chinese authorities would be unable to avoid a stronger depreciation of the Yuan.

**Market impact** | A hard landing linked to a burst of the credit bubble would have a very negative impact and its cascading effects would be particularly disastrous: vulnerability of banking systems (in China and elsewhere), vulnerability of the global financial system, vulnerability linked to China's public and private debt, negative impact on regional and global trade, and thus on commodities and emerging countries, impacts on the currencies of commodity-exporting countries, advanced countries and emerging countries, etc.

Risk # 8

10%  
probability**A long-term and significant increase in long-term interest rates**

**Analysis** | The increase in long-term rates can come from at least six sources: (i) a significant upswing in (nominal, real or potential) growth prospects, (ii) more aggressive tightening of interest rate policies, (iii) the "true" end of QEs (the end of reinvesting maturing papers in the US, an even more drastic reduction in the ECB's asset purchasing programme), (iv) a resurgence of inflation or inflation expectations, (v) a massive reversal of fiscal and tax policies, or (vi) a resurgence of specific political risks. Nevertheless, these factors remain unlikely. In the case of the Eurozone: growth is slowing and the ECB intends to maintain very accommodative monetary conditions. This is indeed a necessary condition for inflation to recover gradually. However, the desire to lower the degree of monetary accommodation - including ending QE by year end - remains intact. A moderate rise in European bond yields seems inevitable. But a marked increase is unlikely (except in Italy).

**Market impact** | A sharp rise in long rates would be bad news in the US, where the sensitivity of the economy to long-term rates has increased with corporate re-leveraging: this would weaken growth and in itself would sow the seeds for a future decline in long rates. It should also be noted that a sharp rise in long-term rates would stop the rate hikes from the Fed. Another reason not to believe in a long-lasting and wide rise in US and European long-term bond yields. Having said that, regarding bond yields, risks remain tilted to the upside in the short-term in the US (overheating risks with the possibility of additional wage acceleration).

## MACROECONOMIC CONTEXT

### Our convictions and our scenarios

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This section provides a reminder of our central scenario and alternative scenarios.



#### Central scenario (70% probability): global growth slows gradually but surely

- **Growth is slowing worldwide: Since this summer economic trends have diverged.** Growth has weakened in the Eurozone but remains solid in the US. Surveys remain high, especially in the services sector, in spite of rising risks. However, the business climate in the manufacturing sector is suffering from weaker global trade and rising oil prices. Emerging economies have been hit by the financial spillover from Argentina and Turkey, due to the broad-based appreciation of the USD (as a substantial proportion of their debt is in dollars). This has led to capital outflows from emerging economies and a depreciation of their currencies, which has, in turn, stoked local inflation. All in all, central banks have simultaneously begun to move their monetary policies to a more hawkish stance in many EM countries. Lastly, the economic slowdown has been more pronounced than expected in China, which has led the authorities to shift course in economic policy.
- **World trade:** Global trade has weakened since the start of the year (+3.8% year-on-year in July compared to 4.8% in December). Protectionist rhetoric has pushed down business confidence, particularly in Europe. However, keep in mind that the products targeted so far account for a small share of world trade and that retaliatory measures have been moderate. That said, uncertainty is tending to drag down investment and disrupt value chains that have developed in lock-step with the expansion in global trade over the past 15 years. In light of the above, we continue to expect the global trade to global GDP ratio to decline, with growth in trade lagging slightly behind global GDP.
- **United States:** Unsurprisingly, 3%-plus growth is being forecast in Q3 2018, and the US economy continues to create jobs. The job market is becoming tighter and wages are beginning to accelerate. Surveys (the non-manufacturing ISM peaked in October) continue to point to above-potential growth in the coming quarters. Monetary and financial conditions remain accommodative despite Fed rate hikes and the dollar's appreciation. Fiscal stimulus, including tax cuts and higher spending, is what is driving the economy at this point in the cycle. A recession is highly unlikely in 2019, but the cycle-end story will probably return to the fore at some point by next summer, as the fiscal multiplier impact fades and as the effects of ongoing monetary policy tightening show up. We therefore forecast a slowdown in growth by 2020, with GDP growth closer to 2% by then.
- **Eurozone:** Last month, we revised our growth forecasts slightly downward, to 2.0% for 2018 and to 1.8% for 2019. It is likely that we will revise our forecasts once again in light of the rise in oil prices, which is particularly significant in euros. Protectionism has undermined confidence (in the manufacturing sector), but the latest surveys (especially in services) suggest that the Eurozone is holding up well. At this stage, we do not expect the fiscal policy announced in Italy to have a significant impact on the economy: the gains from a relaxation of fiscal policy will probably be erased by the tightening of local financial conditions (increase in interest rates). Barring an exogenous shock, peripheral economies will remain in catch-up mode, especially as the ECB plans to stick to its ultra-accommodative stance, despite ending its asset purchase programme (APP) by the end of 2018. On the political front, illegal migration remains the main issue and is likely to keep tensions high in the run-up to May 2019 European elections. In Germany, elections in Bavaria on 14 October will serve as a test.
- **United Kingdom:** Brexit negotiations are teetering on the brink and the dissension within the Conservative party is particularly acute (especially regarding whether or not to remain in the customs union), to the extent that the deadline for reaching an agreement with the EU this year probably won't be met. We should expect rising tensions over the coming months. The EU, meanwhile, wants to demonstrate that an exit is not in any country's interest. All in all, we do expect a "last minute" agreement, but no doubt not until 2019, which will give the UK a transition period until December 2020. We expect this to weigh on growth for as long as the uncertainty persists.
- **China:** The Chinese economy is slowing, due, in part, to the weakening in global growth. Trade tensions with the US continue to grab headlines. The Chinese government's retaliatory measures against the US

in the wake of Donald Trump's customs tariffs are extremely measured. China seems to be expecting things to calm down once the US mid-term elections are behind us. China has shifted its economic policy in favour of a pro-growth fiscal policy and an accommodating monetary policy. Even so, the risks to growth now look to be on the downside.

- **Inflation:** Core inflation remains low at this stage of the cycle in advanced economies, and should recover gradually. That said, the slowdown in inflation in recent years is primarily structural in nature, as it is tied to supply-side factors, while the cyclical component of inflation has weakened (with a flattening of the Phillips curve). Core inflation is likely to pick up only slightly in advanced economies. An "inflationary surprise" remains possible with rising oil prices and the pick-up in wages (United States, Eurozone) but would not last long (due to a lack of pricing power) and would drag down corporate margins more than final sale prices, all the more so if global growth slackens. Things are different in emerging economies, where inflationary pressures are greater in many countries, in reaction to which many central banks have raised their key rates.
- **Oil prices:** Oil prices have increased sharply (\$86/bbl. for Brent as of 4 October) to an almost four-year high. This is primarily due to expectations that supply will decline as US sanctions on Iran begin to take effect, which in practice will mean that many countries will halt (or reduce) their oil imports from Iran. Currently, OPEC and Russia seem reluctant to offset this supply shortage and US producers say they are unable to do so (at least not in the short term). Short-term risks are therefore on the upside. Rebalancing by boosting supply will take time, with US production already very high. Our equilibrium-price assumption (around \$75) could be revised up. Uncertainty over oil supply is very high - no-one can predict the extent of the supply shortage.
- **Central banks will continue to remove monetary accommodation at a gradual pace.** The Fed will continue to raise its key interest rates. We expect the Fed to follow through with one more 25bp hike in December 2018 and two additional hikes in H1 2019, followed by a pause, and for it to reduce its balance sheet at the announced pace (with a gradual non-replacement of maturing securities). Meanwhile, the ECB will halt its monthly asset purchases at the end of December, as announced. However, it will continue to replace maturing securities (between €160 and 200 billion in 2019) without clarifying its reinvestment policy in order to retain some flexibility. Its first rate hike is not expected until Q3 or Q4 2019.

**The protectionist measures announced by Trump have ratcheted up uncertainty worldwide, fed the appreciation in the dollar and capital outflows from emerging economies, which furthermore are quite vulnerable to international to global trade issues. Emerging economies overall are weaker. Advanced economies are sensitive to different kinds of risks (mid-term elections in the US, Brexit, Italy, rising oil prices). Donald Trump's political strategy after the mid-term elections is unclear. In the very short term, a more serious confrontation with China on trade remains likely, at a time when rising oil prices are putting pressure on the manufacturing sector and threatening corporate margins.**



**Downside risk scenario (25% probability):  
a marked trade-war-driven economic slowdown, a geopolitical crisis  
or a sudden repricing of risk premiums**

- The risk of further protectionist measures from the US followed by retaliations from the rest of the world remains high as the 6 November mid-term elections draw near (as Trump seeks to satisfy his electoral base). China and the EU are particularly exposed to this risk.
- Aggravation of geopolitical tensions in the Middle East. Oil prices could rise above \$100.
- The uncertainty over rising trade tensions (primarily between the United States and China) against a backdrop of geopolitical risks (with Iran), crises in several large emerging economies (Turkey, Argentina), political risk in Brazil, a slowdown in China and political tensions in Europe (a deteriorating budget in Italy, Brexit) is encouraging companies to remain cautious.

**Consequences:**

- All things being equal, a trade war would drag down global trade and trigger a synchronised slowdown in growth and, in the short term, inflation. That said, a global trade war would quickly become deflationary by creating a shock to global demand.
- An abrupt repricing of risk on fixed income markets, with an across-the-board rise in spreads on govies and credit, on both developed and emerging markets, and a decline in market liquidity.
- Amidst the resulting financial turbulence, the cycle-end story would resurface in the US.
- Central banks would cease recalibrating their monetary policies and, in the worst, albeit highly unlikely, case, would once again resort to unconventional tools, such as expanding their balance sheets.



**Upside risk scenario (5% probability):  
a pick-up in global growth in 2019**

**Donald Trump makes an about turn after the US mid-terms, reducing barriers to trade and engaging in bilateral negotiations with China. Domestically, the theme of increasing infrastructure spending could return to centre stage and extend the cycle in the United States.**

- Acceleration driven by business investment and a rebound in global growth.
- Pro-cyclical US fiscal policy generating a greater-than-expected acceleration in domestic growth. Growth is reaccelerating in the Eurozone after a dip. Growth picks up again in China on the back of a stimulative policy mix in H1.
- Central banks would react late, initially maintaining accommodative monetary conditions.

**Consequences:**

- An acceleration in global growth would boost inflation expectations, forcing central banks to consider normalising their monetary policies more rapidly.
- An increase in real key rates, particularly in the US.
- Risk of boom/bust

## Macroeconomic picture by area

### United States

#### GDP growth remains strong amid buoyant confidence

- Confidence remains strong among businesses while surveys are surprisingly positive; some signs of concern reported linked to the escalation in tariffs against China.
- Industrial activity stabilised on an upward trend, supported by domestic demand, with solid orders of capital goods and generally positive retail sales.
- Inflation data remained broadly aligned with the Fed's projections, with PCE measures now at target level.
- As widely expected, the Fed hiked rates in September (2.00% to 2.25%), increasingly confident in its economic and inflation outlook, and suggested a further hike in 2018 followed by progressive gradual tightening of monetary policy in 2019.
- After a first round of tariffs on imports of \$50bn, a second round on \$200bn of imports from China was implemented. NAFTA: after a preliminary Mexico-US agreement, Canada and US also reached an accord.

### Risk factors

- Tariffs and retaliation negatively impacting the economic performance, both directly (prices) and indirectly (confidence)
- Fed tightening impacting interest rate-sensitive segments (housing, consumer credit)
- Abrupt and severe tightening of financial conditions
- Geopolitical risks linked to a more hawkish shift by the US Administration

### Eurozone

#### Growth still positive but decelerating in a context of rising risks.

- After a very disappointing year's start (GDP grew by only 0.8% in H1), economic indicators stabilised during the summer, although without validating a strong rebound. Core inflation remains stuck at around 1% per year, but wage increases should allow it to rise slightly in the coming months.
- The announcement of a proposed Italian budget that does not comply with European rules threatens to increase internal tensions in the Eurozone. In addition, the Eurozone is more exposed to trade tensions than the United States.

- Rise in anti-establishment parties
- Rise in the euro
- External risks (in particular trade war risks)

### United Kingdom

#### The job market provides an important support despite the Brexit uncertainty

- Growth rebounded in Q2 (+0.4%), confirming that the weak Q1 figure (+0.2%) underestimated the real trend. The labour market remains in good shape and real wages returned to positive territory.
- However, the uncertainty surrounding Brexit is dragging down confidence and investment. There are still major differences between the negotiating parties standing in the way of an agreement over withdrawal from the EU, and time is running out. The likelihood of a hard Brexit seems to be increasing.

- A hard Brexit
- The current account deficit remains very high

### Japan

#### Expecting retrieval activities after rounds of typhoons and earthquakes

- Real GDP is likely to decline in Q3 18 as a result of earthquakes, heavy rains, floods and scorching heat waves. Inventory adjustment in producer goods continues to weigh on growth. The weaker yen has failed to boost exports as the global economic slowdown takes its toll on shipments. The good news is that PM Abe has managed to persuade US President Trump not to impose higher levies on vehicles for now.
- The economy should regain strength in Q4 as producers try to recoup the losses incurred in the previous quarter. Disaster relief and reconstruction projects will amplify the upward momentum. Corporate Japan plans to expand capex at the highest pace since 2006 despite the serious trade dispute. In the meantime, wage growth is strong enough to absorb higher consumer inflation.

- Tariffs and quotas imposed by the U.S. could raise costs and hamper supply chains

**China**

- China's economy is slowing, but the potential slowdown still looks manageable.
- US/China trade tensions have continued. The US announced a 2nd tranche of tariffs on \$200bn of Chinese goods, with 10% of the tariff effective from 24th September, and 25% from 1st January 2019. China retaliated on \$60bn of US goods with a 5-10% tariff.
- There are signs of the export momentum cooling in China and its neighbours.
- That said, policy supports are also becoming more visible. Credit growth is stabilising, local government bond issuance has been accelerating, while the PBOC has committed to keeping ample liquidity.
- In addition, China continued to push ahead with reforms and initial measures, including a 3rd cut in import tariffs this year, to offer more tax benefits to foreign investors on their FDI, and also cut personal income tax.
- Policymakers are looking to protect the RMB from a further significant depreciation for now.
- There is likely to be continued uncertainty regarding US trade measures, the effectiveness of policy supports, and whether China could push further serious structural reforms.

**Risk factors**

- US/China trade tensions, with upcoming US mid-term elections
- Policy mistakes in managing near-term risks and the structural transition
- Geopolitical noise regarding North Korea

**Asia (ex JP & CH)**

- Notwithstanding all the noise related to the escalation of the trade issue between China and the US, trade in the region is proving fairly resilient. Some measures have been implemented to weaken the import dynamics in India and Indonesia in order to correct the negative dynamics of the Trade Balance and Current Account.
- Inflation figures have remained fairly benign in the region, with the usual exception of the Philippines, where headline inflation is above 6% versus a Central Bank upper threshold of 4%.
- Monetary policies confirmed their hawkish stance. BSP and BI once again increased their monetary policy rates by 50bps and 25bps respectively. In both cases, we expect further tightening to come.
- Tariffs have been implemented on \$200bn of Chinese exports to the US, with China retaliating soon after with \$60bn of tariffs. Trade protectionism escalation is a risk factor for the countries in the region that are most integrated in the Chinese supply chain.

- Trade in the region still holding up
- Inflation still very benign with the exception of the Philippines
- BSP and BI continued with their hiking cycle
- Increasing risks for countries integrated in the supply chain with China

**Latam**

- Macroeconomic data in Q3 2018 are still signalling some weakness in the largest countries of the region such as Brazil, Mexico and Argentina while the smallest economies keep running at a more robust pace.
- On the inflation front, the overall environment remained benign. In Mexico, inflation in the first half of the month was lower than expected indicating a possible return to a converging path towards the target interrupted in June.
- The region's main Central Banks maintained monetary policy unchanged in their recent meetings. Following the revised IMF plan in support of Argentina, BCRA has changed its Monetary Policy framework, abandoning the inflation target in favour of Monetary aggregate targets.
- According to September polls, the elections in Brazil (on October 7<sup>th</sup>) will see J. Bolsonaro (PSL) and F. Haddad (PT) going through to the second round (on October 28<sup>th</sup>).

- Three largest countries producing a weaker performance than the smaller countries
- Inflation turning benign in Mexico
- Change of Monetary Policy framework in Argentina
- Busy political agenda continues, with upcoming elections in Brazil on 7<sup>th</sup> and 28<sup>th</sup> October

**EMEA (Europe Middle East & Africa)**

**Russia: we forecast 1.7% YoY growth for 2018-2019**

- Despite the threat of potential US sanctions down the road, the macroeconomic scenario remains supportive helped by high oil prices. Russia will among the few emerging market sovereigns with the "twin surpluses" in 2018, while accumulating assets at the National Wealth Fund.

**South Africa: we lower growth forecast to 0,7% YoY in 2018**

- With sizeable current account deficit financed by portfolio inflows (not FDI) and inadequate external liquidity, SA remains vulnerable to EM turmoil.
- These risk are supplemented by vulnerabilities from the fiscal side and contingent liabilities from SOEs.

**Turkey: we downgrade forecast a slowdown in growth in 2018 to 1.8%**

- The TRY has depreciated significantly given large external imbalances, poor external liquidity and non-orthodox policies of the government.
- Despite a sizeable hike in interest rates in September, Turkish assets will remain under pressure. Turkish corporates have begun to default. This will impact the health of the heavily indebted (in foreign currency) and very large banking sector very negatively.

- Lower oil prices and stepped-up US sanctions
- Fall in commodity prices, capital outflows, fiscal slippage, and delays in structural reforms
- Continued market turmoil, further drop GDP and in asset prices



## Macro and Market forecasts

Macroeconomic forecasts (8 October 2018)						
Annual averages (%)	Real GDP growth %			Inflation (CPI, yoy, %)		
	2018	2019	2020	2018	2019	2020
US	2.9	2.6	1.9	2.5	2.3	2.2
Japan	0.9	1.2	0.4	0.8	1.1	2.0
Eurozone	2.0	1.8	1.8	1.7	1.7	1.9
Germany	1.9	1.8	1.9	1.8	1.6	1.6
France	1.6	1.7	1.6	2.1	1.6	1.4
Italy	1.1	1.1	1.2	1.1	1.6	1.7
Spain	2.7	2.3	1.7	1.5	1.5	2.3
UK	1.3	1.5	1.6	2.4	2.3	2.4
Brazil	1.2	2.0	1.8	3.7	4.9	4.8
Russia	1.8	1.7	1.7	2.9	4.6	4.0
India	7.7	6.1	6.7	4.3	4.7	5.1
Indonesia	5.2	5.4	5.4	3.3	4.0	4.3
China	6.6	6.3	6.2	2.1	2.5	2.7
Turkey	2.3	-1.0	1.5	16.5	16.5	7.2
Developed countries	2.2	2.1	1.7	2.0	1.9	2.1
Emerging countries	4.9	4.6	4.7	4.1	4.2	3.8
World	3.8	3.6	3.5	3.2	3.3	3.1

Source: Amundi Research

Key interest rate outlook					
	04/10/2018	Amundi + 6m.	Consensus Q1 2019	Amundi + 12m.	Consensus Q3 2019
US	2.25	2.75	2.75	3.00	3.00
Eurozone	0.00	0.00	0.00	0.00	0.00
Japan	-0.10	-0.10	-0.10	-0.10	-0.10
UK	0.75	0.75	0.75	1.00	1.00

Long rate outlook					
2Y. Bond yield					
	04/10/2018	Amundi + 6m.	Forward + 6m.	Amundi + 12m.	Forward + 12m.
US	2.88	2.9/3.1	3.08	2.9/3.1	3.15
Germany	-0.53	-0.4/-0.3	-0.30	-0.3/-0.2	-0.29
Japan	-0.12	-0.2/-0.0	-0.09	-0.1/0.1	-0.08
UK	0.86	0.80/1.00	1.00	0.9/1.1	1.10

10Y. Bond yield					
	04/10/2018	Amundi + 6m.	Forward + 6m.	Amundi + 12m.	Forward + 12m.
US	3.20	3.10/3.25	3.26	3.10/3.20	3.29
Germany	0.53	0.65/0.75	0.64	0.55/0.75	0.74
Japan	0.15	0.15/0.25	0.22	0.10/0.20	0.28
UK	1.66	1.6/1.8	1.74	1.70/1.80	1.81

Currency outlook					
	02/10/2018	Amundi + 6m.	Consensus Q1 2019	Amundi + 12m.	Consensus Q3 2019
EUR/USD	1.15	1.18	1.18	1.21	1.22
USD/JPY	113.66	109	110	108	108
EUR/GBP	0.89	0.89	0.89	0.90	0.90
EUR/CHF	1.13	1.16	1.15	1.18	1.19
EUR/NOK	9.45	9.25	9.32	9.15	9.20
EUR/SEK	10.38	10.10	10.23	9.90	9.97
USD/CAD	1.28	1.26	1.28	1.24	1.26
AUD/USD	0.72	0.74	0.73	0.76	0.75
NZD/USD	0.66	0.67	0.66	0.68	0.69
USD/CNY	6.87	6.80	6.85	6.76	6.79

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