Global Watch

June 2019

Central Banks set to rubber stamp easing expectations

After a respite in the opening months of 2019, **trade tensions** resurfaced with a vengeance in May. Just as some tentative signs had started to emerge that global activity might be stabilising, the US and China engaged in another round of tit-for-tat tariffs and Trump turned his attention to Mexico. Unsurprisingly this led to a fall in equity markets, with bond yields also heading south. Moreover, market expectations that the **major central banks** would act in response to the growing risks to the economic outlook now look set to be validated. In the past month, both the Fed and the ECB have signalled a preparedness to **ease monetary policy** and are unlikely to be dissuaded from doing so by the latest US-China truce. Politics has also been a focus in Europe, with the recent elections resulting in a more fragmented Parliament and the joint-ruling far-right League party performing strongly in Italy, which has been at odds again with the Commission over budgetary policy. In the UK, Article 50 has been extended to the end of October but talks between the Conservatives and Labour to break the **Brexit impasse** failed. This culminated in Theresa May's resignation as Prime Minister and kick-started a Tory leadership race, the result of which will be known in late July. Amid all of this, the question of how and when the UK will exit the EU remains unclear, though the **risk of a 'no deal'** departure - and a related sharp fall in sterling - has increased.

Economic Research Unit

Bank of Ireland

Central Bank Outlook

Economic Conditions

	US	Euro Area	UK
Growth	3.2%	1.2%	1.8%
Unemployment	3.6%	7.6%	3.8%
Headline Inflation	1.5%	1.2%	2.0%
Core Inflation	1.6%	1.1%	1.7%

Policy Stance

US	Euro Area	UK
To sustain the economic expansion, lower interest rates on the cards	Prepared to deploy full toolkit to address persistently weak inflation	Outlook for interest rates continues to be Brexit dependent

Current Policy Rate

US	Euro Area	UK
2.25%-2.5%	0.0%	0.75%

Next Meeting

Source: Bank of Ireland, BEA, Eurostat, ONS, Fed, ECB, Bank of England
Growth: Annual % change in GDP (constant prices), US and Euro Area Q1 2019, UK February-April 2019
Unemployment: Rate (%), US May 2019, Euro Area April 2019, UK February-April 2019
Headline and Core Inflation: Annual % change, US PCE May 2019, Euro Area CPI June 2019, UK CPI May 2019, core inflation excludes food and energy (as well as alcohol and tobacco in the case of the Euro Area and UK)
Policy Rates: Federal Funds Rate, ECB Main Refinancing Rate, Bank of England Bank Rate

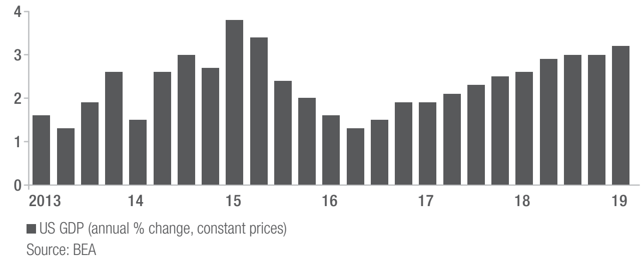
Economy

Subdued global growth

The IMF expects global GDP growth to dip to 3.3% this year (a downward revision of 0.2 percentage points) before ticking up to 3.6% in 2020, but cites increasing protectionism as a key risk.

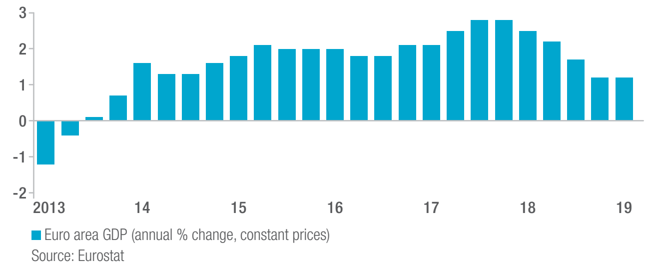
US holding up

US GDP increased by 3.2% year-on-year in Q1 2019 – the strongest rate of growth in almost 4 years – though trade tensions abound. The unemployment rate stood at 3.6% in May, while inflation was below target at 1.5%.



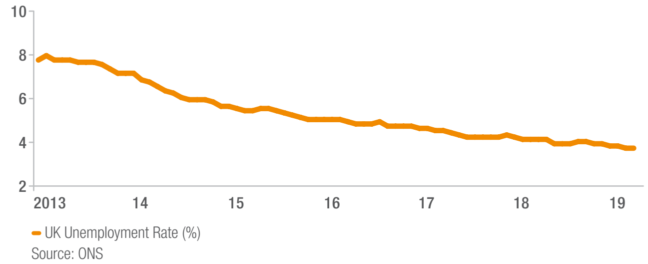
Euro area activity stabilises

Having slowed during the course of 2018, GDP growth in the Euro area was steady at 1.2% year-on-year in the first quarter of this year. The unemployment rate was 7.6% in April, with inflation coming in at 1.2% in June.



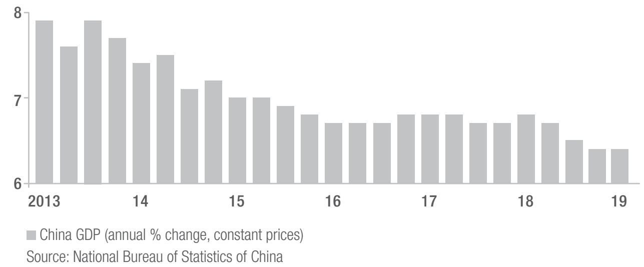
Moderate UK growth

Boosted by stockpiling ahead of the original Brexit date, annual GDP growth in the UK picked up to 1.8% in Q1 2019 but eased in April. Unemployment was stable at 3.8% in February-April, while inflation dipped to 2.0% in May.



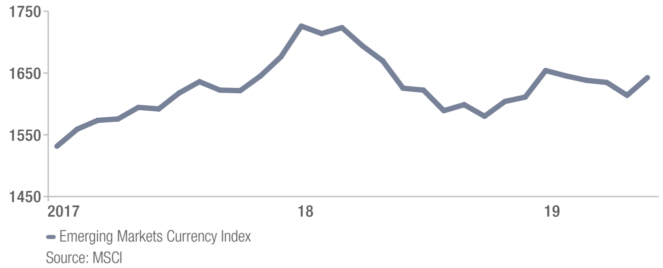
China facing headwinds

GDP in China rose by 6.4% year-on-year in Q1, within the authorities' 2019 growth target of 6-6.5%. The June tariff increase on $200bn worth of goods exports to the US will be a drag on activity in the period ahead though.



EM currencies volatile

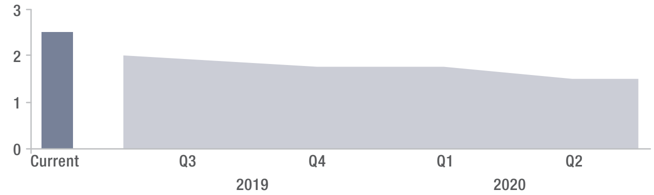
Emerging market currencies have come under pressure again in 2019 amid trade concerns and unsettled financial markets, though there has been some relief lately as the US dollar has been on the back foot.



Monetary

Fed turns dovish

The Fed left interest rates unchanged in June but in light of concerns about the broad economic outlook, indicated it may lower them to sustain the expansion in the US.



FED Federal Funds Rate (%) Market Expectations
Source: Fed & Bloomberg

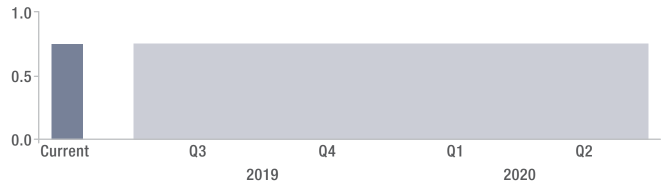
ECB prepared to ease

At its last meeting the ECB said interest rates would remain unchanged through end June 2020, but it has since signalled it is prepared to cut (most likely the deposit rate) and/or reactivate quantitative easing.

ECB Main Refinancing Rate (%) Market Expectations
Source: ECB & Bloomberg

BOE still Brexit dependent

Amid prolonged and increasing uncertainty, the Bank of England has kept interest rates on hold since last August with the future path remaining dependent on Brexit developments.

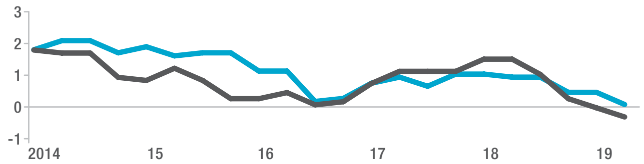


BOE Bank Rate (%) Market Expectations
Source: Bank of England & Bloomberg

Policy & Politics

Political drama in the UK

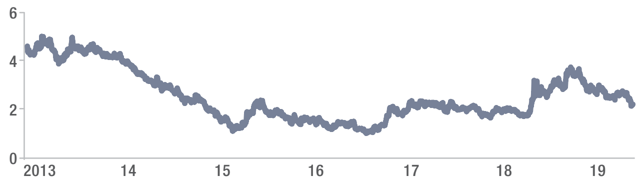
While Article 50 was extended until end-October, talks between the Conservatives and Labour ended without agreement and following Theresa May's resignation, a Tory leadership contest is underway.



UK Businesses' Investment Intentions Next 12 Months
Manufacturing Services (Score)
Source: Bank of England

Italy and Commission at odds

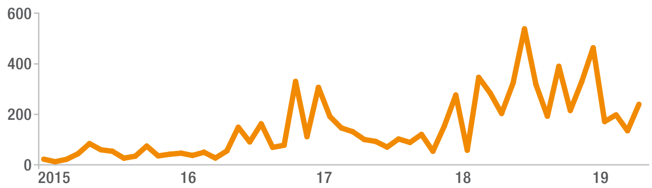
The Italian government has been on a collision course with the European Commission over budgetary policy. Bond yields have fallen recently but remain elevated relative to those in other Euro area countries like Portugal and Spain.



Italian 10 Year Government Bond Yield (%)
Source: Bloomberg

US-China tensions

After a brief détente, the US and China engaged in further tit-for-tat tariffs, though Trump did backtrack on proposed tariffs on Mexico and has deferred a decision on auto tariffs to the autumn. He's also back talking with China.

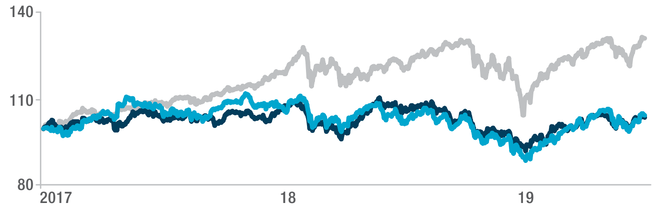


US Trade Policy Uncertainty Index
Source: Davs, Baker and Bloom

Markets

Stocks recover ground

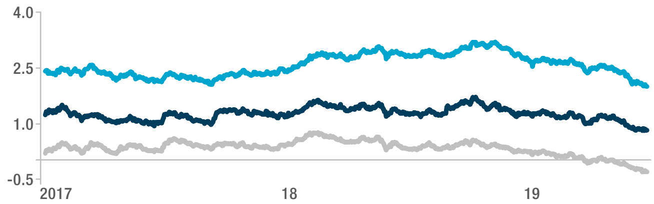
Global growth concerns saw equities lose ground at the start of Q2 2019, though the prospect of more accommodative monetary policy has provided a boost recently with the S&P 500 setting an all-time high.



Equity Indices (2017=100) S&P 500 Euro Stoxx 50 FTSE 100
Source: Thomson Reuters

Bond yields head south

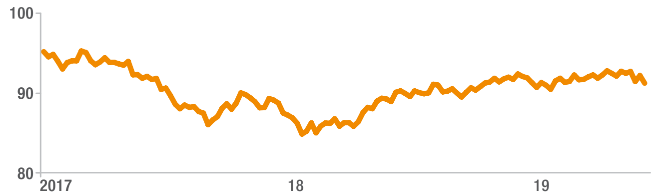
Bond yields have fallen sharply as the market prices in interest rate cuts, with US 10-year yields at an almost 3-year low of circa 2% and equivalent German yields in record negative territory of around -0.35%.



10-Year Government Bond Yields (%) US Germany UK
Source: Thomson Reuters

Dollar a little softer

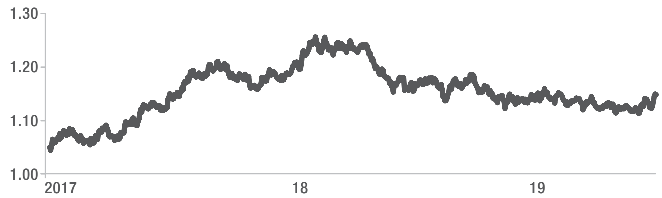
After strengthening through much of the second quarter of this year, the dollar has generally come off the boil lately as the Fed has signalled a readiness to lower interest rates.



Dollar Trade Weighted Index Major Currencies (March 1973=100)
Source: Fed

Respite for the euro

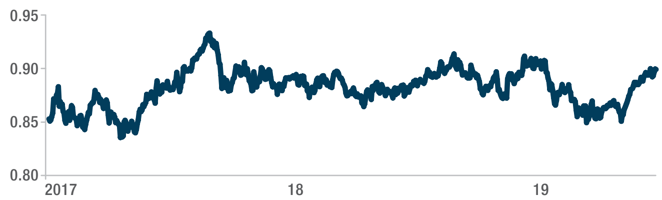
Having been on the defensive for most of H1, the single currency has gained some ground against the dollar in the past few weeks and is now trading at around the $1.13 mark.



€/$
Source: Thomson Reuters

Sterling slides

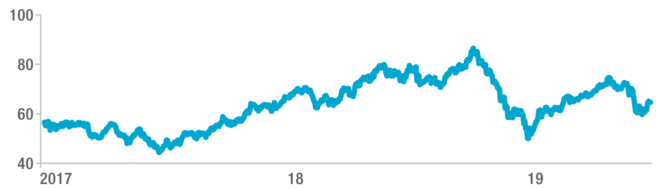
The pound has reversed a good portion of the gains it made in the first quarter of 2019, with the heightened risk of a 'no deal' Brexit sending it to almost 90p against the euro.



€/£
Source: Thomson Reuters

Oil prices fluctuate

Oil prices are being buffered on the one hand by concerns about global demand and on the other by US-Iranian tensions, with the latter resulting in a spike in Brent crude to over $66 in mid-to late-June.



Brent Crude Oil ($ per barrel)
Source: Thomson Reuters

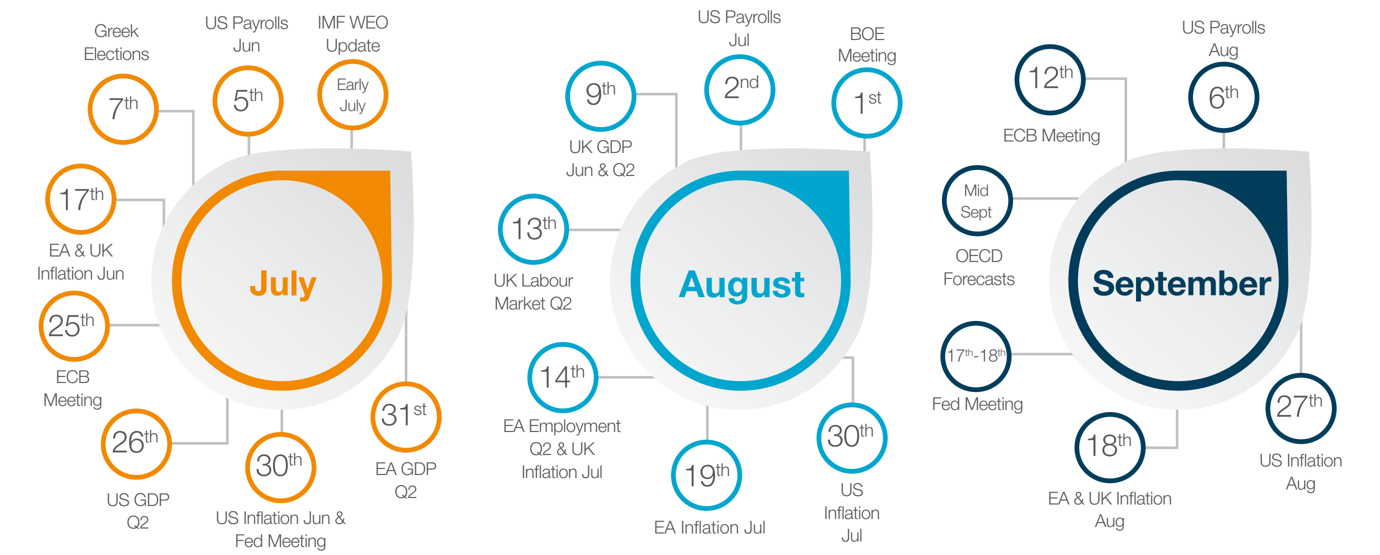
Forecasts

GDP Growth*	2018	2019 (f)	2020 (f)
Global Economy	3.6%	3.3%	3.6%
Advanced	2.2%	1.8%	1.7%
Emerging	4.5%	4.4%	4.8%

FX**	Current	End Sep 2019	End Dec 2019
€/$	1.13	1.14	1.15
€/£	0.89	0.90	0.87
£/$	1.27	1.27	1.32

*Annual % change, constant prices (Source: IMF)
**Current Rate is as of 28th June 2019 (Source: Bloomberg); Rate forecasts, assumes current EU-UK trading arrangements continue to apply (Source: Bank of Ireland)

Upcoming Events



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