



R&R Weekly Column
By Brunello Rosa



With A Slowing Global Economy, Monetary Policy's Tide Is Turning

The global economy is now in the middle of an asynchronous slowdown, which is occurring mostly as a result of prolonged, [intensifying trade tensions](#), [rising geopolitical risks](#), and tightness in the labour market in a number of countries. Let us briefly examine the three major economic regions of the global economy.

In the US, Q1 GDP growth was surprisingly positive, but domestic demand weakened substantially, providing little comfort for the economy's future performance. The non-farm payrolls figures for May 2019, released last week, were weaker than expected; only 75,000 jobs were added, as opposed to the consensus expectation of 185,000 jobs or the previous reading of 224,000 jobs. This weaker figure was accompanied by slower growth in average hourly earnings: 3.1% y/y, versus a consensus expectation and previous reading of 3.2%. [In a recent interview](#), Fed's Vice-Chair Richard Clarida said that tariffs are expected to have a one-off effect on price levels, but a more lasting impact on economic activity. Therefore, if trade tensions do not subside, the negative demand shock to the economy from those tensions will eventually be larger than the negative shock to supply.


In the Eurozone, Q1 GDP also surprised mildly to the upside, but the latest ECB projections suggest that economic activity will decelerate in Q2 and Q3, so the [much-hoped for rebound in Q2](#) is unlikely to materialise. This is mostly because the largest European economy, [Germany](#), is fighting to exit a prolonged period of stagnation (it has been flirting with recession), while the third largest Eurozone economy, [Italy](#), has temporarily exited its technical recession in Q1 but risks entering a new one in Q2 2019. For the time being, [France](#) and [Spain](#) are the main drivers of economic growth in the Eurozone.


In China, [the policy stimulus of 2018](#) allowed the economy to also surprise to the upside in Q1, but the reignition of trade tensions this year have meant a new slowdown, which the authorities are fighting with fiscal, monetary and regulatory stimulus. Going forward, US tariffs are expected to continue weighing on exports and push inflation higher. All other regions in the world closely depend on developments from these three economic and geo-strategic giants, so economic activity is likely to decelerate globally.

Facing this situation, and waiting for fiscal policy to provide a larger counter-cyclical contribution (even as most government are busy "fixing their fiscal roof" now that "the sun is still shining"), central banks have already begun to act. In a number of jurisdictions, monetary policy, which had at least had a tightening bias, has now become neutral if not overtly more accommodative. In developed markets, last week the [Reserve Bank of Australia cut](#) (after [a long debate](#)) its main policy rate to a record low of 1.25%, following the [neighbouring RBNZ](#) by a month. During its latest press conference, President Draghi said that the [ECB's Governing Council has discussed possible easing measures](#). While the [BoJ has never abandoned its accommodative stance](#), the elephant in the room is clearly the Fed. The markets now price in the likelihood, indeed almost the certainty, that the Fed will cut rates in coming months.

In Emerging Markets, central banks have been even more proactive. In China, the PBoC Governor announced "there is tremendous room to adjust monetary policy if the trade war deepens." In India, a marked slowdown in the economy led the Reserve Bank of India to cut interest rates by 25bps (to 5.75%) for a third time this year, and suggest further cuts are in the pipeline. The central banks of the Philippines and Malaysia also recently cut their policy rates by 25bps, to 4.5% and 3% respectively.

Our Recent Publications

 [Review: ECB Is Not As Dovish As The Market Expected, But Is Ready To Ease](#), By Brunello Rosa, 6 June 2019

 [MACRO PICTURE - Argentina: Elections To Test The Austerity Measures](#), by Alessandro Magnoli Bocchi, Farah Aladsani, Fawaz Sulaiman Al Mughrabi and Lapo Fioretti, 5 June 2019

 [Review: RBA Cuts Its Cash Rate Due to Uncertainty On The Global Outlook](#), By Alex Waters, 4 June 2019

 [ECB Preview: Don't Expect Too Much Substance, But Still a Dovish Tone](#), by Brunello Rosa and Nouriel Roubini, 3 June 2019

Looking Ahead

The Week Ahead: US Retail Sales To Pick Up, China's Exports To Drop Sharply

In the US, inflation is expected to remain subdued (CPI May, c: 1.9% y-o-y; p: 2.0%) while retail sales are expected to pick-up (Retail sales May, c: 0.6% m-o-m; p: -0.2%).

In China, exports are expected to drop sharply due to higher US tariffs (c: -3.8% y-o-y; p: -2.7); inflation is likely to rise (CPI May, c: 2.7% y-o-y; p: 2.5%), while remaining below the PBoC's 3% target.

The Quarter Ahead: Trade Tensions To Weigh On Global Growth

US-China, trade talks are unlikely to resume until the June 28 G-20 summit.

In the EZ, a stronger EUR—by reducing import costs—may dampen inflation expectations below the ECB 2% target. The ECB announced that “funds under TLTRO3” will: *i)* start in September 2019 and end in March 2021, with a 2y maturity; *ii)* be offered quarterly, to preserve bank lending conditions and support the ECB's accommodative stance; and *iii)* “be offered at 10 bps above the main refinancing rate (0%) and can fall as low as the average deposit rate plus 10 bps.

In the US, Fed Chair Powell signaled openness to cutting rates as the Fed is “closely monitoring the impact of trade developments” and would “act as appropriate to sustain economic expansion”. Market expectations of a rate cut in 2019 rose to 99% (p: 94%). Barring shocks, the Fed is likely to cut between June and September (possibly in July) and – if needed – in December 2019.

In the UK, Boris Johnson—the front-runner to succeed Theresa May as PM—vowed to leave the EU “with or without a deal, on October 31” and promised to hold onto USD50bn owed to the bloc “until divorce conditions become more favorable”.

In China, the PBoC governor announced “there is tremendous room to adjust monetary policy if the trade war deepens”, joining US and EZ counterparts in displaying readiness to support a slowing economy.

The US warned **Turkey**: if by July 31 it does not abandon its S-400 acquisition plans: 1) Turkish pilots currently training in the US on F-35s will be expelled; and 2) all agreements with Turkish firms sub-contracted for jet manufacturing will be cancelled.

Last Week's Review

Real Economy: Loss Of Economic Momentum Has Spread To The US Labor Market

In the US, non-farm payrolls were weaker-than-expected (a: 75k; c: 185k; p: 224k) and average hourly earnings slowed (a: 3.1% y-o-y; c: 3.2; p: 3.2).

The US and Mexico reached a deal to curb migration, defusing President Trump's threat to impose a 5% tariff on all Mexican imports.

In the EZ, the ECB left interest rates unchanged, as expected (a: 0%; p: 0%), and inflation slowed to 1.2% y-o-y (c: 1.3%; p: 1.7%).

In Germany, industrial production fell (IP Apr., a: -1.9% y-o-y; c: -1.7; p: -0.9) as trade tensions and lower demand weigh on exports.

In Turkey, inflation slowed, as a weak domestic demand caps prices (a: 18.7% y-o-y; c: 19.1; p: 19.5).

In India, a marked slowdown in the economy led the RBI to: *i)* cut interest rates by 25bps for a third time this year (a: 5.75%; p: 6.00); and *ii)* suggest further cuts.

In Australia, the RBA cut interest rates by 25 bps to 1.25% (c: 1.25%; p: 1.5%) due to lower housing prices and a slowdown in China, the country's largest trading partner.

Financial Markets: Prospects Of Monetary Easing Boosted Equities And Weakened The USD

Market drivers: After a weaker-than-expected US labor data, investors expect the Fed to cut interest rates in response to a weakening growth outlook and escalating trade tensions.

Stocks: w-o-w, global stocks rose (MSCI ACWI, +3.6%), led by the US (S&P 500, +4.4%). Volatility fell (VIX S&P 500, -2.4 points to 16.3, 52w avg.: 16.3; 10y avg.: 17.4).

Bonds: globally, indices rose w-o-w (BAML Global bond index, +0.5%). The yield on a 10Y UST sank to 2.05% and the yield curve steepened.

FX: the USD weakened against a basket of currencies (DXY, -1.2%) and the EUR rose (EUR/USD, +1.5% at 1.133). EM currencies rose (MSCI EMs, +0.4% at 1,623).

Commodities: Oil prices fell (Brent, -1.9% to 63.3 USD/b), driven by doubts over the outlook for global demand.

Farah Aladsani contributed to this Viewletter.

The picture in the front page comes from [this website](#)



@RosaRoubini



Rosa & Roubini



Rosa&Roubini Associates

For more information, please call us on +44 (0)207 1010 718 or send us an email to info@rosa-roubini-associates.com

www.rosa-roubini-associates.com

118 Pall Mall, London SW1Y 5ED



Abbreviations, Acronyms and Definitions

a	Actual	LN	Northern League, Italy
AKP	Justice and Development Party, Turkey	MSS	Five Star Movement, Italy
ann.	annualized	m-o-m	Month-on-month
ARS	Argentinian Peso	mb	Million barrels
avg.	Average	mb/d	Million barrels per day
bn	Billion	MENA	Middle East and North Africa
BoC	Bank of Canada	MHP	Nationalist Movement Party, Turkey
BoE	Bank of England	mn	Million
BoJ	Bank of Japan	NAFTA	North-American Free Trade Agr.
bpd	Barrels per day	NATO	North Atlantic Treaty Organizat.
bps	Basis points	OECD	Organization for Economic Cooperation and Development
BS	Balance sheet	Opec	Organization of Petroleum Exporting Countries
c	Consensus	p	Previous
C/A	Current account	P2P	Peer-to-peer
CB	Central bank	PBoC	People's Bank of China
CBB	Central Bank of Bahrain	PCE	Personal Consumption Expenditures
CBK	Central Bank of Kuwait	PE	Price to earnings ratio
CBT	Central Bank of Turkey	PM	Prime minister
CDU	Christian Democratic Union, Germany	PMI	Purchasing managers' index
CNY	Chinese Yuan	pps	Percentage points
CPI	Consumer Price Index	pw	Previous week
DJIA	Dow Jones Industrial Average Index	QCB	Qatar Central Bank
DJEM	Dow Jones Emerging Markets Index	QAR	Qatari Riyal
d-o-d	Day-on-day	QE	Quantitative easing
DXY	US Dollar Index	q-o-q	Quarter-on-quarter
EC	European Commission	RE	Real estate
ECB	European Central Bank	RBA	Reserve Bank of Australia
ECJ	European Court of Justice	RRR	Reserve Requirement Ratio
EIA	US Energy Information Agency	RUB	Russian Rouble
EM	Emerging Markets	SWF	Sovereign Wealth Fund
EP	European Parliament	tn	Trillion
EPS	Earnings per share	TRY	Turkish Lira
EU	European Union	UAE	United Arab Emirates
EUR	Euro	UK	United Kingdom
EZ	Eurozone	US	United States
Fed	US Federal Reserve	USD	United States Dollar
FOMC	US Federal Open Market Committee	USD/b	USD per barrel
FRB	US Federal Reserve Board	UST	US Treasury bills/bonds
FX	Foreign exchange	VAT	Value added tax
FY	Fiscal Year	VIX	Chicago Board Options Exchange Volatility Index
GCC	Gulf Cooperation Council	WTI	West Texas Intermediate
GBP	British pound	WTO	World Trade Organisation
GDP	Gross domestic product	w	Week
IMF	International Monetary Fund	w-o-w	Week-on-week
INR	Indian Rupee	y	Year
IPO	Initial public offering	y-o-y	Year-on-year
IRR	Iranian Rial	y-t-d	Year-to-date
JPY	Japanese yen	ZAR	South African Rand
k	thousand	2y; 10y	2-year; 10-year
KSA	Kingdom of Saudi Arabia		



Rosa & Roubini Associates Ltd is a private limited company registered in England and Wales (Registration number: 10975116) with registered office at 118 Pall Mall, St. James's, London SW1Y 5ED, United Kingdom. VAT registration number GB 278 7297 39. **Analyst Certification:** We, Brunello Rosa and Nouriel Roubini, hereby certify that all the views expressed in this report reflect our personal opinion, which has not been influenced by considerations of Rosa & Roubini Associates's business, nor by personal or client relationships. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the views expressed in this report. **Disclaimer:** All material presented in this report is provided by Rosa & Roubini Associates-Limited for informational purposes only and is not to be used or considered as an offer or a solicitation to sell or to buy, or subscribe for securities, investment products or other financial instruments. Rosa & Roubini Associates Limited does not conduct "investment research" as defined in the FCA Conduct of Business Sourcebook (COBS) section 12 nor does it provide "advice about securities" as defined in the Regulation of Investment Advisors by the U.S. SEC. Rosa & Roubini Associates Limited is not regulated by the FCA, SEC or by any other regulatory body. Nothing in this report shall be deemed to constitute financial or other professional advice in any way, and under no circumstances shall we be liable for any direct or indirect losses, costs or expenses nor for any loss of profit that results from the content of this report or any material in it or website links or references embedded within it. The price and value of financial instruments, securities and investment products referred to in this research and the income from them may fluctuate. Past performance and forecasts should not be treated as a reliable guide of future performance or results; future returns are not guaranteed; and a loss of original capital may occur. This research is based on current public information that Rosa & Roubini Associates considers reliable, but we do not represent it is accurate or complete, and it should not be relied on as such. Rosa & Roubini Associates, its contributors, partners and employees make no representation about the completeness or accuracy of the data, calculations, information or opinions contained in this report. Rosa & Roubini Associates has an internal policy designed to minimize the risk of receiving or misusing confidential or potentially material non-public information. We seek to update our research as appropriate, but the large majority of reports are published at irregular intervals as appropriate in the author's judgment. The information, opinions, estimates and forecasts contained herein are as of the date hereof and may be changed without prior notification. This research is for our clients only and is disseminated and available to all clients simultaneously through electronic publication. Rosa & Roubini Associates is not responsible for the redistribution of our research by third party aggregators. This report is not directed to you if Rosa & Roubini Associates is barred from doing so in your jurisdiction. This report and its content cannot be copied, redistributed or reproduced in part or whole without Rosa & Roubini Associates' written permission.

