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Danske Daily

Risk assets struggle amidst growth scare

Market movers today

- Key market themes continue to be **Brexit** and **US-China trade talks**. Markets will also be looking ahead to the **Fed meeting** on Wednesday. While a rate hike is widely expected, focus will be on signals on monetary policy in 2019. In the Scandies, an expected rate hike from the **Riksbank** on Thursday is likely to take centre stage.
- In terms of data today, we will get **final euro area inflation** for November and the **US Empire index**, which is the first regional US business survey for December. We expect euro inflation to be unchanged from the initial release, which showed headline inflation at 2.0% y/y and core inflation at 1.0% y/y. The US empire index is still at very high levels but is estimated to show a small decline in November.
- The **US NAHB housing index** for December is also due today. It dropped sharply in November and added to signs of a slowdown in the housing market.

Selected market news

Risk markets struggled on Friday as poor economic data arrived first from China and then Europe, sparking renewed anxiety over global economic growth. US and European equity markets fell and government bonds rallied. The dollar rose against developed and emerging market currencies. Consequently, the US dollar index flirted with year-high levels. This morning, S&P 500 futures are slightly up along with most Asian equity indices.

Friday's **Chinese industrial production** data confirmed that growth is weakening further into year-end and adds to expectations that we will see more easing from China soon. Industrial production growth dropped from 5.9% y/y to 5.4% y/y, whereas consensus expected the growth rate to remain unchanged. Retail sales growth slipped further from 8.6% y/y to 8.1% y/y, with consensus expecting 8.8% y/y. Fixed asset investments increased slightly, however, from 5.7% y/y to 5.9% y/y.

The data is broadly in line with our expectation that it will get worse before it gets better from around Q2. It also underlines why China would like to make a trade deal with Trump soon, to ease some of the downside pressure on the economy.

Euro area December flash PMIs were weak overall and do not point to a reversal of the growth slowdown this quarter, which began in Q3. The usual culprits remain in place, i.e. Brexit, politics, the global trade/China slowdown and have been accompanied by other downside risks such as the Yellow Vest protests in France.

Manufacturing PMI edged down slightly to 51.4. There were some signs of stabilisation in the subcomponents such as in new export orders and output indices. However, new orders at 48.6 are at the lowest level still since 2013. Service PMIs registered a marked fall from 53.4 to 51.4, likely to be driven mainly by France. New incoming business was at the weakest level in four years, but still in expansion territory at 51.4.

The disruption to French activity is particularly disappointing, as France was one of the key euro area growth drivers in Q3. In addition, judging from survey and car registrations data, it seems likely that the car sector will continue to act as a drag on growth in Q4.

Selected reading from Danske Bank

- *FOMC Preview - Fed set to hike again but removing more forward guidance*
- *China Weekly letter*
- *FX Strategy*

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Scandi markets

Sweden. An expected rate hike from the **Riksbank** on Thursday is likely to take centre stage this week.

Fixed income markets

The main event this week is the FOMC meeting. A rate hike is a done deal. Hence, focus will be on signals for 2019 and how close we are to the neutral rate and comments on the inversion of the yield. The Riksbank is due to meet on Thursday and we expect it to hike the policy rate, even though it might wait until February on the back of the global uncertainty and lower-than-expected November inflation data. Key focus will be the Riksbank's outlook for 2019 and whether it will hike again in summer 2019. Swedish rates have declined due to the global uncertainty, but we still like paying SEK FRA JUN19.

Negotiations between Italy and the EU continue this week. The Italian government has come to an agreement that will bring the 2019 deficit to 2.04% of GDP. The gap between the EU commission and Italy is closing fast. Hence, the risk of Italy being placed under an EDP seem unlikely and thus the rally in Italian government bonds is expected to continue this week, but at a more modest pace than seen over the past few weeks.

The Dutch Debt Agency released its funding outlook for 2019. There were no big surprises, but the funding requirement was some EUR4bn lower than the estimate from September and stands at EUR43bn. The reduction is due to lower redemptions from T-bills. The funding is spilt between T-bills (EUR19-23bn) and DSL (Dutch government bonds for EUR19-23bn). There will be a new 10Y (EUR12bn) and a new green bond with a maturity of >15Y (EUR4-6bn). The rest will be funded through off-the-run DSLs. A new green bond in the long end of the curve could ease some of the richness of the Dutch government curve. The Dutch government curve has also become expensive, though not as much as the German curve. See more in *Government Bonds Weekly*, 14 December 2018.

FX markets

On Friday, EUR/DKK reached a new high this year, rising to around the 7.4660 level. It is rare that the EUR/DKK trades this high. Historically, a move like this has often triggered FX intervention buying of DKK. We stick to our view that the current DKK weakness is temporary and that EUR/DKK should fall back below 7.4600 in 2019.

We expect the Riksbank to raise the repo rate on Thursday. If it does and is not overly dovish, EURSEK should go lower and could test the 5 December 10.1623 low, given that the money market (RIBA) is merely pricing in 55% for 25bp and given that it is not the consensus call among analysts (most think the Riksbank will wait until February).

Besides news on Brexit, majors will be awaiting the key Fed decision this Wednesday. The market has priced the Fed notably more dovishly recently, which suggests that risks are tilted towards a hawkish surprise. See *FOMC Preview - Fed set to hike again but removing more forward guidance,* 14 December. That said, there is a key risk that the FOMC could lower rate expectations (aka the dots) further out. For USD, it will thus be key whether Fed Chair Jerome Powell and co come across as (a) adamant to get to neutral or (b) cautious in not making policy contractionary. The former is our base case, which should be USD supportive near term.

Key figures and events

Monday, December 17, 2018				Period	Danske Bank	*Consensus*	Previous
7:00	DKK	House prices (Finance Denmark)	q/q|y/y	3rd quarter			
8:00	NOK	Trade balance	NOK bn	Nov			34.9
11:00	EUR	HICP inflation	m/m|y/y	Nov	**...|2.0%**	*-0.2%|2.0%*	0.2%|2.2%
11:00	EUR	HICP - core inflation, final	y/y	Nov	**1.0%**	*1.0%*	1.0%
11:00	EUR	Trade balance	EUR bn	Oct			13.4
14:30	USD	Empire Manufacturing PMI	Index	Dec		*20.2*	23.3
16:00	USD	NAHB Housing Market Index	Index	Dec		*61.0*	60.0
22:00	USD	TICS international capital flow, Net inflow	USD bn	Oct			-29.1

Source: Bloomberg, Danske Bank

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