M.M.WARBURG & CO
BANK

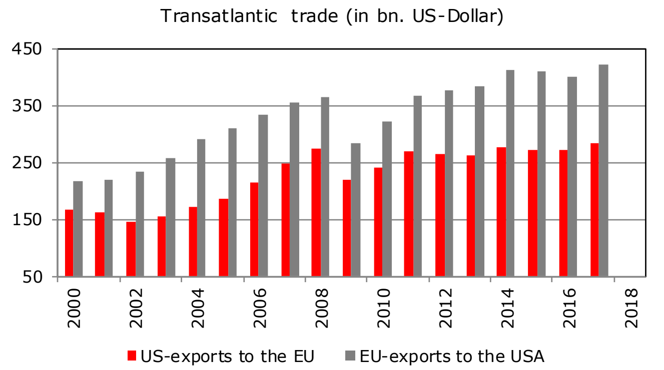
ECONOMIC SITUATION AND STRATEGY

27. July 2018

Hurray, we've got a deal!

Expectations were running rather low before the meeting of US President Trump and EU Commission President Juncker. Trump did not seem to have high hopes for EU cooperation with his idea of fair trade while Juncker mentioned no concrete offers to appease Trump and stop the trade hostilities from escalating into a trade war. In this light we are more than pleased about how the summit actually turned out.

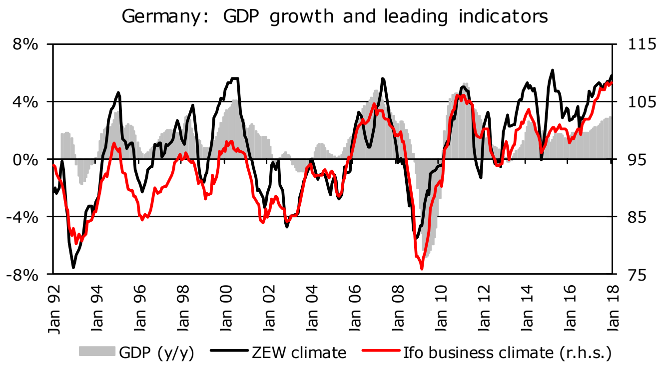
Although it would be premature to call this a final peace agreement in the transatlantic trade conflict, we have at least a truce. It is encouraging when the world's two largest economic powers start talking with each other again rather than about each other (via Twitter) and agree to renewed close friendship, commitment, and stronger trade relations. This should not only benefit the US but also Europe. While almost all politicians in the EU have emphasized especially in the past few weeks how committed they are to maintaining good and close trade relations with the US, President Trump was singing a different tune. However, he, too, was calling the summit a breakthrough in his post-meeting tweet: "Great meeting on Trade today with @JunckerEU and representatives of the European Union. We have come to a very strong understanding and are all believers in no tariffs, no barriers and no subsidies. Work on documents has already started and the process is moving along quickly. European Union Nations will be open to the United States and at the same time benefiting by everything we are doing for them. There was great warmth and feeling in the room – a breakthrough has been quickly made that nobody thought possible!"



That means new tariffs are off the table for now. And that are good news indeed for all EU countries but especially Germany with its high trade and current account surplus – it may even be the best news in quite a while. The EU and the US will soon assemble a joint commission to abolish all tariffs, trade barriers, and subsidies that stand in the way of free trade and fair competition. The language of the joint statement is not clear whether this includes only subsidies or also tariffs for non-automotive capital goods. If this exception applies to the latter, too, this would mean that the US retains the option of using tariffs on European cars as negotiation leverage in the future. In that case, Trump would have kept an ace up his sleeve. However, Jean-Claude Juncker noted in his press conference with President Trump that no new tariffs (including any on automobiles) will be introduced in the upcoming negotiations. Limiting the upcoming negotiations to subsidies on certain capital goods serves to facilitate agreement by the 28 EU countries on a comprehensive trade accord with the US. After all, produce that is a key export category for some countries has been explicitly exempt from the subsidy restriction. That is a major concession particularly to France where resistance to a new trade agreement with the US has been rather strong so far.

Trade in services and in chemical, pharmaceutical, and medical products as well as soy beans are to be promoted in particular going forward. The EU and the US furthermore want to reinforce their strategic collaboration in the energy sector. Soy bean trade should be especially important to Donald Trump as the trade conflict with China has caused a dramatic drop in demand and prices for US soy beans. This has forced the US government to subsidize US soy bean farmers to the tune of up to 12 billion dollars. Europe’s hot summer and resulting harvest shortfalls may get the EU to import US soy beans soon. That is good news for Trump and US farmers who are the main support for him and the Republican Party – and the November mid-term elections are not far off. Moreover, President Trump does not approve of the close fossil-fuel trade relations between the EU (especially Germany) and Russia. Jean-Claude Juncker’s offer to buy more liquid natural gas from the US is a clear concession. However, this has to be a longer-term deal considering that liquid natural gas has to be shipped from the US and there is currently hardly any terminal capacity for unloading and storing larger amounts of combustible materials from the US in European seaports. It is probably just a coincidence that Germany is planning to build its first liquid natural gas terminal in Brunsbüttel. Trump’s counter concession to Juncker’s offers is to examine existing tariffs on European steel and aluminum.

Even though the transatlantic trade conflict has not been finally resolved, the agreements reached indicate that a reasonable and amicable solution is more probable than not despite the residual risks. Finally, one should not forget that Trump also announced significant progress in the trade conflict with China late last May just to threaten penalty tariffs on all US imports of Chinese goods barely two months later. The now more likely agreement between the US and the EU will put further pressure on China to negotiate a trade accord with the US, too. As things stand right now, the transatlantic negotiations are leaving China at a disadvantage. The US-European agreements to protect their enterprises from unfair trade practices of other countries and pursue WTO reform with similar-minded countries are both calling out China. It would be a big boost for global trade and growth prospects if this should prompt China to forge its own trade accords with the US. Rather than sinking global trade in a quagmire of protectionism this could lead to more free trade than ever before. However, we are not there yet.



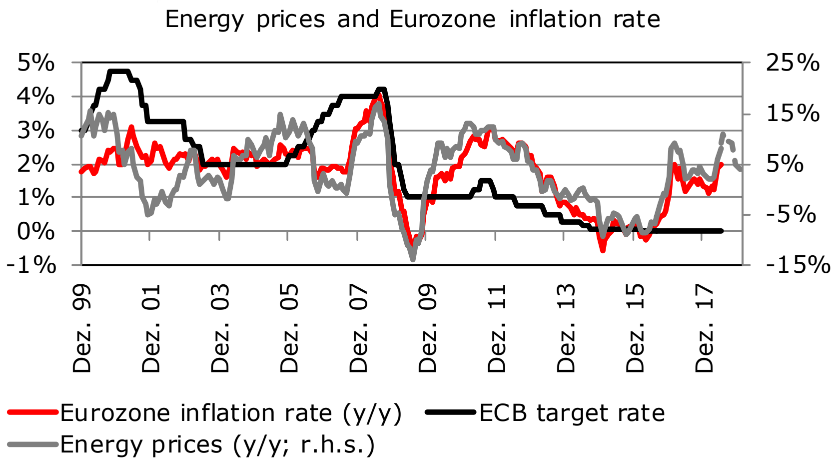
Overall, current developments should help alleviate the economic uncertainties that handicapped especially European economies and companies in the past few months. Notwithstanding the residual risks, the danger of a trade war escalation seems to have been largely averted. As a result, the main leading indicators for the euro area should stabilize and improve soon so that growth momentum can pick up again in the second half of the year. At least this would be the case if Donald Trump remains somewhat more committed to his relations with the EU than with his wives. Recently he tweeted: “Obviously the European Union, as represented by @JunckerEU and the United States, as represented by yours truly, love each other!” Let us hope this remains the case.

Weekly outlook for July 30-August 3, 2018

	Feb	Mar	Apr	May	June	July	Release
DE: Prelim. Inflation rate, m/m	0.5%	0.4%	0.0%	0.5%	0.1%	0.2%	July, 30
DE: Prelim. Inflation rate, y/y	1.4%	1.6%	1.6%	2.2%	2.1%	1.9%	July, 30
DE: Retail sales, m/m	-0.2%	0.3%	1.6%	-2.1%	1.5%		July, 31
DE: Change in unemployment in 1000s	-21	-18	-8	-12	-15	-17	July, 31
DE: Unemployment rate	5.4%	5.3%	5.3%	5.2%	5.2%	5.1%	July, 31
DE: PMI manufacturing, final	60.6	58.2	58.1	56.9	55.9	57.3	August, 1
DE: PMI services, final	55.3	53.9	53.0	52.1	53.9	54.4	August, 3
EUR-19: Business climate	1.48	1.44	1.39	1.44	1.39	1.42	July, 30
EUR-19: Business confidence	114.3	112.8	112.7	112.5	112.3	112.4	July, 30
EUR-19: Consumer confidence, final	0.1	0.1	0.3	0.2	-0.6	-0.6	July, 30
EUR-19: Industry confidence	8.8		7.3	6.9	6.9	7.0	July, 30
EUR-19: Prelim. Inflation rate, y/y	1.1%	1.3%	1.3%	1.9%	2.0%	1.9%	July, 30
EUR-19: Unemployment rate, s.a.	8.6%	8.5%	8.4%	8.4%	8.3%		July, 30
EUR-19: PMI manufacturing, final	58.6	56.6	56.2	55.5	55.0	55.1	August, 1
EUR-19: Producer prices, m/m	0.1%	0.0%	0.0%	0.8%	0.3%		August, 2
EUR-19: Producer prices, y/y	1.7%	2.0%	1.9%	3.0%	3.5%		August, 2
EUR-19: PMI services, final	56.2	54.9	54.7	53.8	55.0	54.4	August, 3
EUR-19: Retail sales, m/m	0.3%	0.6%	-0.1%	0.0%	0.4%		August, 3

MMWB estimates in red

Chart of the Week: ECB stays its course



The ECB confirmed its position on interest rates and bond purchases at today's meeting. There was no doubt that the ECB would leave key lending rates unchanged. The statement that key lending rates will remain unchanged beyond "the summer of 2019" also stayed. However, there was a minor update to the phase-out of the bond purchase program. While the ECB declared last month that it will reduce its net purchases from 30 to 15 billion euros starting in October and phase out the program to the end of the year, today's statement also addressed the reinvestment of maturing bonds. The proceeds of maturing bonds will be reinvested for an "extended period" and in any case for as long as necessary to provide continuing sufficient liquidity. The press release gave no further information on the reinvestment, though. The post-meeting press conference confirmed upon asking that the ECB's capital key will remain the anchor for the reinvestments but they were otherwise not discussed. Reinvestment details may, however, be on the agenda at the next meeting. There were overall very little news to report and the press conference only lasted a mere 40 minutes.

Market data overview

Stock marktes	As of 27.07.2018 13:46	Change versus 20.07.2018 -1 week	26.06.2018 -1 month	26.04.2018 -3 months	26.07.2017 -1 year	29.12.2017 YTD
Dow Jones	25527	1,9%	5,1%	5,0%	17,6%	3,3%
S&P 500	2837	1,3%	4,2%	6,4%	14,5%	6,1%
Nasdaq	7852	0,4%	3,8%	10,3%	22,3%	13,7%
DAX	12872	2,5%	5,2%	3,0%	4,6%	-0,4%
MDAX	27037	1,7%	4,8%	4,8%	8,5%	3,2%
TecDAX	2969	3,1%	8,1%	13,5%	30,3%	17,4%
EuroStoxx 50	3525	1,9%	4,6%	0,5%	1,0%	0,6%
Stoxx 50	3159	1,9%	4,9%	3,0%	0,8%	-0,6%
SMI (Swiss Market Index)	9174	2,0%	8,2%	3,8%	2,0%	-2,2%
Nikkei 225	22713	0,1%	1,7%	1,8%	13,3%	-0,2%
Brasilien BOVESPA	79405	1,1%	11,2%	-8,1%	22,1%	3,9%
Russland RTS	1146	2,8%	2,9%	-0,1%	12,3%	-0,7%
Indien BSE 30	37337	2,3%	5,2%	7,6%	15,3%	9,6%
China Shanghai Composite	2874	1,6%	1,0%	-6,6%	-11,5%	-13,1%
MSCI Welt (in €)	2162	1,4%	3,9%	8,1%	10,3%	6,0%
MSCI Emerging Markets (in €)	1089	2,1%	2,4%	-0,4%	2,7%	-3,0%
Bond markets						
Bund-Future	163,14	61	105	483	136	146
Bobl-Future	131,83	-18	-28	101	-9	22
Schatz-Future	111,95	-5	-14	8	-8	-2
3 Monats Euribor	-0,32	0	0	1	1	1
3M Euribor Future, Dec 2017	-0,30	0	-1	0	-16	0
3 Monats $ Libor	2,34	0	0	-2	102	64
Fed Funds Future, Dec 2017	2,22	1	5	3	75	0
10 year US Treasuries	2,98	9	10	-1	70	57
10 year Bunds	0,41	11	8	-18	-8	-1
10 year JGB	0,10	7	7	4	2	5
10 year Swiss Government	-0,03	3	-1	-15	-6	10
US Treas 10Y Performance	558,94	-0,8%	-0,7%	0,3%	-3,9%	-3,9%
Bund 10Y Performance	616,78	-0,3%	0,0%	2,5%	3,0%	1,6%
REX Performance Index	484,17	-0,3%	-0,2%	1,1%	0,8%	0,7%
US mortgage rate	0,00	0	0	0	0	0
IBOXX AA, €	0,76	0	-1	-8	-6	8
IBOXX BBB, €	1,57	-2	-3	12	22	34
ML US High Yield	6,55	-4	6	6	63	40
JPM EMBI+, Index	803	0,3%	2,2%	-0,6%	-2,6%	-4,0%
Convertible Bonds, Exane 25	7436	0,1%	1,4%	0,5%	3,3%	0,5%
Commodities						
CRB Spot Index	433,59	0,2%	-1,2%	-2,8%	-1,8%	0,3%
MG Base Metal Index	318,98	2,1%	-6,3%	-8,7%	2,1%	-11,1%
Crude oil Brent	74,50	2,1%	-0,8%	-0,2%	46,8%	11,8%
Gold	1219,99	-0,7%	-3,2%	-7,4%	-2,3%	-6,4%
Silver	15,48	-0,1%	-5,0%	-6,1%	-5,7%	-9,0%
Aluminium	2049,00	-1,4%	-5,3%	-10,0%	6,7%	-9,2%
Copper	6266,50	2,4%	-6,7%	-9,6%	-0,5%	-13,0%
Iron ore	63,93	0,5%	-1,5%	-2,1%	-2,5%	-10,3%
Freight rates Baltic Dry Index	1708	1,1%	29,1%	24,2%	76,4%	25,0%
Currencies						
EUR/ USD	1,1629	-0,4%	-0,4%	-4,4%	-0,1%	-3,0%
EUR/ GBP	0,8875	-0,7%	0,7%	2,1%	-0,4%	0,0%
EUR/ JPY	129,26	-1,3%	1,0%	-2,7%	-0,8%	-4,3%
EUR/ CHF	1,1595	-0,3%	0,5%	-3,2%	4,0%	-0,9%
USD/ CNY	6,8279	0,9%	3,8%	7,9%	1,1%	5,0%
USD/ JPY	111,23	-0,2%	1,1%	1,8%	0,0%	-1,3%
USD/ GBP	0,76	0,0%	1,0%	6,4%	-0,3%	3,3%

Carsten Klude
+49 40 3282-2572
cklude@mmwarburg.com

Dr. Rebekka Haller
+49 40 3282-2452
rhaller@mmwarburg.com

Martin Hasse
+49 40 3282-2411
mhasse@mmwarburg.com

Dr. Christian Jasperneite
+49 40 3282-2439
cjasperneite@mmwarburg.com

Bente Lorenzen
+49 40 3282-2409
blorenzen@mmwarburg.com

Julius Böttger
+49 40 3282-2229
jboettger@mmwarburg.com