

The Week Ahead: US-China trade talks take centre stage; US and Eurozone inflation

► **Global: G-20 summit key for trade talks and global growth**

All eyes will be on the G-20 summit this week (28-29 June) to see if US President Donald Trump and Chinese President Xi Jinping can make a breakthrough in trade negotiations. We do not expect a trade deal at the G20 meeting, but see prospects of both parties striking a conciliatory tone at the end of the meeting. We believe Trump is likely to tone down his earlier threat to impose 25% tariffs on the remaining USD325 billion worth of Chinese imports, potentially paving the way for the negotiations to re-start. However, if trade talks fail to make any headway, the risk-off market sentiment could result in the USD and other safe haven currencies strengthening, with risky assets likely seeing a sharp selloff. The outcome of the G-20 meeting will also be important for the major central banks, including the Fed and the ECB, which turned more dovish and signalled their willingness to ease monetary policy last week (page 2). We believe that the timing and magnitude of the monetary easing by the Fed will depend on the result of the US-China trade talks, along with incoming data in the coming months. Globally, geopolitical tensions remain elevated amidst the ongoing US-Iran developments, with oil prices strengthening markedly to USD65.2 p/b at the end of last week.

► **US: PCE inflation likely to remain at 0.2% m-o-m in May**

The main US data releases this week will be May PCE inflation, durable goods and the final estimate of 1Q GDP growth. Consensus expects core PCE inflation to have remained steady at 0.2% m-o-m in May, keeping the y-o-y print unchanged at 1.6% and suggesting limited upside inflationary pressures. Following the FOMC meeting last week, we now believe that the probability of an 'insurance' rate cut this year has increased significantly. Fed Chair Jerome Powell revealed at the FOMC's post-meeting press conference that consensus is building for a cut, although comments following the blackout period highlighted differences (which were also visible in the Fed's 'dot plot'). Fed Vice Chair Richard Clarida outlined the positive economic backdrop, with "sustained growth, a strong labour market and inflation near our objective". We expect the Fed to be in a data wait-and-watch mode, unless the G-20 meeting disappoints, which would raise the likelihood of a July cut.

► **Europe: Eurozone June inflation and Carney testimony**

The Eurozone's June inflation report will also be watched closely this week, after ECB President Mario Draghi stressed last week that the ECB would act decisively to boost inflation. We believe that Draghi's speech has opened the door for further QE or rate cuts into negative territory in 2019. Consensus forecasts core inflation to rise marginally to 0.9% y-o-y in June, from 0.8% in May, although this is unlikely to convince the ECB that price pressures are rising meaningfully. In the UK, BoE Governor Mark Carney will testify before Parliament's Treasury Committee on 26 June. We expect Carney to strike a cautious tone on the growth outlook amidst Brexit uncertainties and increased global growth slowdown concerns (page 3).

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I. Recent Events and Data Releases

A. G4 Economies

US: Fed opens door for rate cut in 2019

The Fed kept rates on hold at its 18-19 June policy meeting but sent a clear message that the next move would be a cut. The tone of the meeting was dovish in all respects, including the FOMC statement, dot-plot projections and Fed Chair Jerome Powell's post-meeting comments. We believe that the probability of an 'insurance' rate cut this year has increased significantly following the FOMC meeting, although the timing and magnitude of any policy easing remain uncertain and will depend somewhat on US-China trade developments. The markets are currently pricing in a total of c.69 bps of cuts by end-2019, which still seems aggressive given the state of the domestic economy and the stock market's performance. That said, we do not rule out the possibility of the Fed remaining on hold if there is a positive outcome to the US-China trade talks at the G-20 meeting (and beyond), alongside some improvement in business sentiment. The Fed has not, at this point, committed to a July cut. The incoming economic data over the next few weeks will be critical in determining the Fed's decision, in our view.

Probability of 'insurance' rate cut in 2019 increases considerably after June FOMC meeting

Fig. 1. US: Summary of FOMC's median economic projections, %

	2019	2020	2021	Longer run
Real GDP growth, 4Q y-o-y				
June	2.1	2.0	1.8	1.9
March	2.1	1.9	1.8	1.9
Unemployment rate, 4Q average				
June	3.6	3.7	3.8	4.2
March	3.7	3.8	3.9	4.3
PCE inflation, 4Q y-o-y				
June	1.5	1.9	2.0	2.0
March	1.8	2.0	2.0	2.0
Core PCE inflation, 4Q y-o-y				
June	1.8	1.9	2.0	-
March	2.0	2.0	2.0	-
Median FFTR, year end				
June	2.4	2.1	2.4	2.5
March	2.4	2.6	2.6	2.8

Source: Federal Reserve

The changes to the FOMC statement were largely in line with our expectations. In a move away from its previous patient stance, the FOMC highlighted its flexibility to act if needed, citing increased uncertainties regarding the global economic outlook. However, the Fed still sees strong domestic growth ahead and tight labour market conditions, although it expressed more concern about inflation and the investment outlook. Its growth projections were left unchanged for 2019, but the core PCE forecast was lowered markedly to 1.8% for 2019 from 2% previously. The dot-plot projections showed no change in the 2019 interest rate projections despite eight FOMC members now expecting at least 25 bps of rate cuts in 2019 (seven members expect 50 bps cuts). James Bullard (St. Louis Fed) dissented and voted to cut rates by 25 bps at last week's meeting. Notably, the median estimate for 2020 saw a marked downward revision indicating a 25-bps cut in the FFTR, from a hike of the same magnitude in its March projections. Fed Chair Jerome Powell added more colour to the June dot-plot projections during his post-meeting press

Eight FOMC members now expect at least 25 bps rate cut in 2019

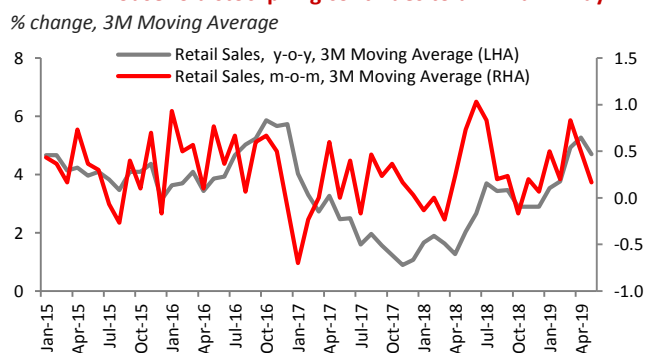
conference and stated that a number of those who predicted a flat rate path also agreed that the case for additional monetary accommodation had strengthened since the May meeting. The next two weeks will be critical to determining the timing and magnitude of the move, with Fed communication central in guiding the market, in our view.

UK: BoE on hold; global uncertainties highlighted

The BoE voted unanimously to keep monetary policy steady at its 20 June meeting, in line with our and the market's expectations. The MPC reiterated that its base case was for further tightening of monetary policy, albeit at a gradual pace and to a limited extent, assuming a smooth Brexit transition. However, the tone of the meeting turned relatively dovish, especially considering the fact that a number of MPC members had made hawkish comments ahead of the policy meeting. The minutes highlighted that downside risks to the growth outlook have increased since its last meeting in May. Trade tensions, the weakening global growth backdrop and the prospect of a 'no deal' Brexit were highlighted as the key downside risks. The committee re-emphasised that the monetary policy response to the Brexit outcome will not be automatic and could be in either direction. Our core scenario remains that the BoE will keep rates on hold in 2019, though Brexit developments in 2H will be critical. This will especially be the case if the new Conservative Party leader takes a hard-line stance on leaving the EU without a deal.

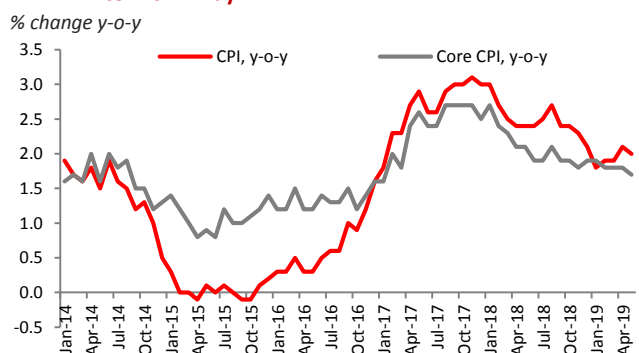
BoE highlights increasing downside risks to growth outlook

Fig. 2. UK: The support to retail sales volumes in 1Q from household stockpiling continues to unwind in May



Source: UK Office for National Statistics

Fig. 3. UK: Both headline and core inflation soften on annual terms in May



Source: UK Office for National Statistics

UK: Economic activity loses momentum in 2Q

Incoming data from the UK showed further weakening in the economy in 2Q2019. Headline retail sales volumes contracted by 0.5% m-o-m in May, following a 0.1% fall in April. Clothing (-4.5%) and fuel (-2.3%) were the key drivers of the drop in May. The weak April and May prints may also have reflected an unwinding of household stockpiling made in 1Q2019, ahead of the original Brexit date, making it hard to get a clear read on the true underlying state of the economy. Meanwhile, inflation data for May also showed that both headline and core inflation softened, reflecting the fading of the Easter effect on air fares. Importantly, core inflation weakened to 1.7% y-o-y in May (April: 1.8%) – the lowest point since January 2017 – suggesting that underlying price pressures were softening.

Retail sales volumes contract for second consecutive month in May, led by clothing and fuel segments

Japan: No changes to monetary policy in June, as widely expected

The BoJ kept its monetary policy steady at its 20 June meeting, including its forward guidance, in line with our and the market's expectations. The policy statement remained largely unchanged, indicating that the BoJ will continue its wait-and-see approach. During his post-meeting press conference, Governor Haruhiko Kuroda highlighted that the BoJ could take various measures to ease monetary policy further, but that he does not see any immediate need for such action. We do not see the BoJ announcing any significant easing measures in the near term, but expect some potential tweaks to its forward guidance at its July meeting. Given the dovish stance adopted by the Fed and the ECB in recent weeks, the BoJ could also turn dovish at its upcoming 30 July meeting if downside risks to global and domestic growth increase further. We believe that the BoJ has only limited scope for further monetary easing in the near term, especially considering the side-effects of negative interest rates on local banks' profitability.

No major surprises at BoJ policy meeting in June

II. Economic Calendar

Fig. 4. The week ahead

Time*	Country	Event	Period	Prior	Consensus
Expected this week					
	UAE	M2 Money Supply, m-o-m	May	0.5%	
	UAE	Central Bank Foreign Assets	May	365.5B	
	UAE	CPI, y-o-y	May	-2.1%	
	Saudi Arabia	GDP Constant Prices, y-o-y	1Q	3.6%	
	Saudi Arabia	M2 Money Supply, y-o-y	May	2.6%	
	Saudi Arabia	SAMA Net Foreign Assets SAR	May	1868.5B	
	Bahrain	M2 Money Supply, y-o-y	May	8.8%	
	Bahrain	CPI, y-o-y	May	1.0%	
	Kuwait	CPI, y-o-y	May	0.7%	
	Kuwait	M2 Money Supply, y-o-y	May	2.6%	
	Qatar	GDP Constant Prices, y-o-y	1Q	0.3%	
Monday, 24 June					
12:00	Germany	Ifo Business Climate	Jun	97.9	97.4
Tuesday, 25 June					
16:45	US	Fed's Williams Makes Opening Remarks at Finance Forum			
18:00	US	New Home Sales	May	673K	685K
18:00	US	Conf. Board Consumer Confidence	Jun	134.1	131
20:00	US	Fed's Bostic Speaks on Housing			
21:00	US	Powell to speak at Council on Foreign Relations in New York			
Wednesday, 26 June					
2:30	US	Fed's Bullard Gives Welcoming Remarks at Lecture in St. Louis			
10:00	Germany	GfK Consumer Confidence	Jul	10.1	10
13:15	UK	BOE's Carney, Cunliffe, Tenreyro and Saunders Speak			
16:30	US	Durable Goods Orders	May P	-2.1%	0.0%
16:30	US	Durables, ex-Transportation	May P	0.0%	0.1%
16:30	US	Cap Goods Orders, Non-def, ex-Air	May P	-1.0%	0.1%
16:30	US	Cap Goods Shipments, Non-def, ex-Air	May P	0.0%	0.1%
16:30	US	Wholesale Inventories, m-o-m	May P	0.8%	0.5%
17:30	US	Fed's Daly Speaks to the Forecasters Club of New York			
Thursday, 27 June					
3:50	Japan	Retail Sales, y-o-y	May	0.5%	1.2%
16:00	Germany	CPI EU Harmonized, y-o-y	Jun P	1.3%	1.3%
16:30	US	GDP Annualized, q-o-q	1Q T	3.1%	3.2%
16:30	US	Personal Consumption	1Q T	1.3%	1.3%
16:30	US	Core PCE, q-o-q	1Q T	1.0%	1.0%
18:00	US	Pending Home Sales, m-o-m	May	-1.5%	1.0%
20:00	Eurozone	ECB's Nowotny, ESM's Regling Speak at Event in Vienna			
	Egypt	GDP Constant, q-o-q	1Q	4.2%	
Friday, 28 June					
3:30	Japan	Tokyo CPI, y-o-y	Jun	1.1%	1.0%
3:30	Japan	Tokyo CPI, ex-Fresh Food, y-o-y	Jun	1.1%	1.0%
3:50	Japan	Industrial Production, m-o-m	May P	0.6%	0.7%
12:30	UK	GDP, q-o-q	1Q F	0.5%	0.5%
13:00	Eurozone	CPI Core, y-o-y	Jun A	0.8%	0.9%
13:00	Eurozone	CPI Estimate, y-o-y	Jun	1.2%	1.2%
16:30	US	Personal Income	May	0.5%	0.3%
16:30	US	Personal Spending	May	0.3%	0.5%
16:30	US	PCE Core Deflator, m-o-m	May	0.2%	0.2%
16:30	US	PCE Core Deflator, y-o-y	May	1.6%	1.6%
17:45	US	MNI Chicago PMI	Jun	54.2	53.8
18:00	US	U. of Mich. Sentiment	Jun F	97.9	98

* UAE time

Source: Bloomberg

Fig. 5. Last week's data

Time*	Country	Event	Period	Prior	Consensus	Actual
MENA Economies						
	Saudi Arabia	CPI, y-o-y	May	-1.9%		-1.5%
	Saudi Arabia	Non-Oil Exports, y-o-y	Apr	-1.4%		-15.5%
	Bahrain	GDP Constant Prices, y-o-y	1Q	5.3%		2.7%
	Egypt	Trade Balance	Mar	-3589M		-4149M
Monday, 17 June						
11:00	Turkey	Unemployment Rate	Mar	14.7%	14.1%	14.1%
16:30	US	Empire Manufacturing	Jun	17.8	11	-8.6
Tuesday, 18 June						
0:00	US	Net Long-term TIC Flows	Apr	-\$25.9B	\$31B	\$46.9B
11:00	Turkey	Industrial Production, m-o-m	Apr	2.2%	0.1%	-1.0%
11:00	Turkey	Industrial Production, y-o-y	Apr	-2.0%	-2.2%	-4.0%
13:00	Eurozone	CPI Core, y-o-y	May F	0.8%	0.8%	0.8%
13:00	Germany	ZEW Survey Expectations	Jun	-2.1	-5.6	-21.1
13:00	Eurozone	ZEW Survey Expectations	Jun	-1.6		-20.2
16:30	US	Housing Starts	May	1281K	1239K	1269K
Wednesday, 19 June						
3:50	Japan	Trade Balance	May	¥60.4B	¥1200B	¥967.1B
12:30	UK	CPI, m-o-m	May	0.6%	0.3%	0.3%
12:30	UK	CPI, y-o-y	May	2.1%	2.0%	2.0%
12:30	UK	CPI Core, y-o-y	May	1.8%	1.6%	1.7%
15:00	US	MBA Mortgage Applications	14-Jun	26.8%		-3.4%
22:00	US	FOMC Rate Decision (Upper Bound)	19-Jun	2.5%	2.5%	2.5%
22:00	US	FOMC Rate Decision (Lower Bound)	19-Jun	2.25%	2.25%	2.25%
22:00	US	Interest Rate on Excess Reserves	20-Jun	2.35%	2.35%	2.35%
Thursday, 20 June						
9:30	Japan	All Industry Activity Index, m-o-m	Apr	-0.4%	0.7%	0.9%
10:00	Japan	Machine Tool Orders, y-o-y	May F	-27.3%		-27.3%
12:30	UK	Retail Sales, inc-Auto Fuel, m-o-m	May	-0.1%	-0.5%	-0.5%
12:30	UK	Retail Sales, inc-Auto Fuel, y-o-y	May	5.1%	2.7%	2.3%
15:00	UK	Bank of England Bank Rate	20-Jun	0.75%	0.75%	0.75%
15:00	UK	BOE Asset Purchase Target	Jun	435B	435B	435B
16:30	US	Current Account Balance	1Q	-\$143.9B	-\$124.3B	-\$130.4B
16:30	US	Philadelphia Fed Business Outlook	Jun	16.6	10.4	0.3
18:00	US	Leading Index	May	0.1%	0.1%	0.0%
18:00	Eurozone	Consumer Confidence	Jun A	-6.5	-6.5	-7.2
	Japan	BOJ Policy Balance Rate	20-Jun	-0.1%	-0.1%	-0.1%
	Japan	BOJ 10-Yr Yield Target	20-Jun	0.0%	0.0%	0.0%
Friday, 21 June						
3:30	Japan	National CPI, y-o-y	May	0.9%	0.7%	0.7%
3:30	Japan	National CPI, ex-Fresh Food, y-o-y	May	0.9%	0.7%	0.8%
4:30	Japan	Markit Japan PMI Manufacturing	Jun P	49.8		49.5
11:30	Germany	Markit Germany Manufacturing PMI	Jun P	44.3	44.6	45.4
12:00	Eurozone	Markit Eurozone Manufacturing PMI	Jun P	47.7	48	47.8
12:30	UK	PSNB, ex-Banking Groups	May	6.8B	4.1B	5.1B
17:45	US	Markit US Manufacturing PMI	Jun P	50.5	50.5	50.1
18:00	US	Existing Home Sales	May	5.2M	5.3M	5.3M

* UAE time

Source: Bloomberg

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