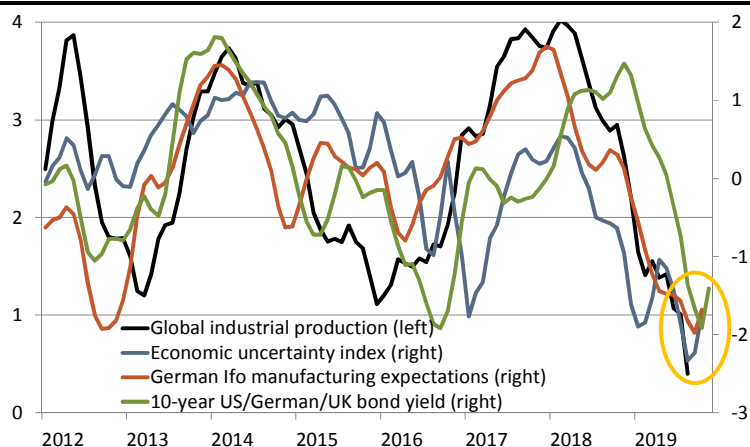


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15 November 2019

Global economy: more signs of hope

Policy uncertainty, business expectations and bond yields are turning



Global industrial output, yoy change in %, left-hand scale; global economic policy uncertainty index, German Ifo manufacturing expectations and GDP-weighted average 10-year-bond yield for US, Germany and UK, right-hand scale, normalised by average and standard deviations since 2012. Sources: NBEPA, PolicyUncertainty.com, Ifo, Reuters, Berenberg

- Flashing amber instead of red:** A growing number of indicators suggest that the downturn in global trade and manufacturing is approaching the bottom. None of these indicators is reliable. Financial indicators, which tend to turn around well ahead of economic data, are too fickle for that. Economic surveys, which are more reliable but have only a short lead time over actual output, have not yet shifted enough to confirm an imminent turnaround. Still, the fact that many indicators are pointing in the same direction strengthens hope that the worst could soon be over.
- Waiting for tensions to fade:** Since late 2018, we have maintained a simple call for the global economy: the downturn in global trade and manufacturing will end if and when the trade tensions stoked by US President Donald Trump start to fade. After these tensions escalated sharply in early May and then again in August 2019, the newsflow on [trade](#) and [Brexit](#) has turned neutral to mildly encouraging in the past three months.
- Growing evidence:** Three categories of data point to a potential turnaround in early 2020. First, in line with other **financial indicators**, both bond yields and equity markets have risen in the past few months. This shows that markets are driven by genuine hope of an improvement to come. If the looser monetary policies of the US Federal Reserve and European Central Bank had been the major factor, yields would have fallen instead. Second, judging by **economic surprise indices**, hard economic data are no longer coming in worse than professional pundits projected. Third, some **indicators of business sentiment and activity** have started to bottom out. Expectations among German manufacturers, who are heavily exposed to global trade, are an obvious example (see chart). In IHS Markit's Global Manufacturing PMI, export orders have stabilised and manufacturing output has edged up in the past two months.
- Expect a modest upturn in 2020:** We see no economic reason for a recession in the advanced world in the next two years. Unless political risks begin to mount again, trade and manufacturing should recover gradually over the course of 2020. Following a small upward revision to Eurozone GDP for Q3 2019 from 1.1% to 1.2% yoy, we raise our call for Eurozone growth in 2020 from 0.9% to 1.0% – the first upward revision after a series of downgrades.
- Fingers crossed:** Of course, it could all still go wrong. If the trade war between the US and China escalates again, if the US starts a new trade war by imposing costly import tariffs on cars from Europe and other regions, or if China's generic downturn worsens, global trade and manufacturing output could weaken further. That risk remains serious. Fortunately, the recent newsflow has been mostly encouraging. As Trump is approaching election season and China is battling an ongoing loss of underlying growth momentum, both sides should be inclined to avoid a renewed escalation that would damage their own economies, as well as global business investment.

Holger Schmieding
 Chief Economist
 +44 20 3207 7889
 holger.schmieding@berenberg.com

Kallum Pickering
 Senior Economist
 +44 20 3465 2672
 kallum.pickering@berenberg.com

Florian Hense
 European Economist
 +4420 3207 7859
 florian.hense@berenberg.com

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This document was compiled by the above mentioned authors of the economics department of Joh. Berenberg, Gossler & Co. KG (hereinafter referred to as “the Bank”). The Bank has made any effort to carefully research and process all information. The information has been obtained from sources which we believe to be reliable such as, for example, Thomson Reuters, Bloomberg and the relevant specialised press. However, we do not assume liability for the correctness and completeness of all information given. The provided information has not been checked by a third party, especially an independent auditing firm. We explicitly point to the stated date of preparation. The information given can become incorrect due to passage of time and/or as a result of legal, political, economic or other changes. We do not assume responsibility to indicate such changes and/or to publish an updated document. The forecasts contained in this document or other statements on rates of return, capital gains or other accession are the personal opinion of the author and we do not assume liability for the realisation of these.

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Contacts



BERENBERG

PARTNERSHIP SINCE 1590

BERENBERG CAPITAL MARKETS LLC

Member FINRA & SIPC

Internet www.berenberg-us.com

E-mail: firstname.lastname@berenberg-us.com

EQUITY RESEARCH

CONSTRUCTION

Robert Muir +1 646 949 9028
Daniel Wang +1 646 949 9025

GENERAL MID CAP - US

Samuel England +1 646 949 9035
Alex Maroccia +1 646 949 9033
Brett Knoblauch +1 646 949 9032

HEALTHCARE

BIOTECH/THERAPEUTICS

Shanshan Xu +1 646 949 9023

MED. TECH/SERVICES

Ravi Misra +1 646 949 9028

SPECIALTY PHARMA/BIOTECH

Patrick R. Trucchio +1 646 949 9027

CAPITAL GOODS

Andrew Buscaglia +1 646 949 9040

LEISURE

Brennan Matthews +1 646 949 9024

INDUSTRIAL MATERIALS

Paretosh Misra +1 646 949 9031

MULTI-CHANNEL RETAILING

Sumit Sharma +1 646 949 9034

REAL ESTATE

Nate Crosssett +1 646 949 9030
Connor Siversky +1 646 949 9037

SHIPPING & TRANSPORTATION

Donald McLee +1 646 949 9026

SOFTWARE & IT SERVICES

Gal Munda +1 646 949 9021
Joshua Tilton +1 646 949 9036

TECHNOLOGY HARDWARE

Andrew DeGasperi +1 646 949 9044

ECONOMICS

Mickey Levy +1 646 949 9099
Roiana Reid +1 646 949 9098

EQUITY SALES

SALES

Albert Aguiar +1 646 949 9218
Daniel Claeys +1 646 949 31 44
Nate Emerton +1 617 292 82 11
Kelleigh Faldi +1 617 292 8288
Ted Franchetti +1 646 949 9231
Rich Harb +1 617 292 8228
Zubin Hubner +1 646 949 9202
Jessica London +1 646 949 9203
Anthony Masucci +1 646 949 9217
Ryan McDonnell +1 646 949 9214
Emily Mouret +1 415 802 2525
Peter Nichols +1 646 949 9201
Kieran O'Sullivan +1 617 292 8292
Rodrigo Ortigao +1 646 949 9205

CRM

Alexandra Angove +1 646 949 9211
Sammy Chea +1 646 949 9241

CORPORATE ACCESS

Adriane Klein +1 617 292 8202
Olivia Lee +1 646 949 9207

EVENTS

Meridian Della Penna +1 646 949 9208
Laura Hawes +1 646 949 9209

SALES TRADING

Isaac Carp +1 646 949 9107
Ronald Cestra +1 646 949 9104
Mark Corcoran +1 646 949 9105
Michael Haughey +1 646 949 9106
Christopher Kanian +1 646 949 9103
Lars Schwartzau +1 646 949 9101