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

MONDAY MACRO UPDATE: EU-TURKEY SUMMIT, ECB, US AND EUROPEAN DATA

Berenberg Macro Flash

EU-TURKEY SUMMIT: DEAL POSSIBLE TODAY

Europe has started to tackle the migrant crisis in earnest. With luck, the EU and Turkey may strike a deal at their summit in Brussels today. The EU wants Turkey to (i) reduce illegal border crossings into Greece from the current daily rate of some 2000 to far less than 1000 a day and (ii) to take back migrants with no claim for asylum in the EU (that is, broadly speaking, to take back almost all non-Syrians who manage to cross the sea from Turkey to Greece). In return, the EU offers €3bn+ in cash for Turkey to take care of Syrian refugees in Turkey and visa-free travel for Turks to the EU from late 2016 onwards.

Our best guess remains that the EU and Turkey will clinch such a deal soon but that Turkey will comply with it only half-heartedly, keeping the flow of migrants into the EU somewhat elevated to maintain pressure on the EU. That would require the EU to tightly control some of its internal borders in order to restrict the flow of migrants there. According to draft conclusions prepared for today's summit, EU leaders will endorse the de facto closure of the Balkan route for migrants which Macedonia and other countries en route from Greece to Germany have enacted unilaterally already in the last two weeks. To deal with the resulting backlog of migrants in Greece, Athens will be offered generous help. That help will not include a major softening of credit conditions for Greece, though.

As usual, it could be noisy. Some issues may remain unresolved until the next EU summit on 17 March. In the meantime, we have to brace ourselves for ugly scenes as desperate migrants stranded in Greece may try to climb the fences. But in its usual bumbling way, the EU may be slowly getting a better grip on its most serious crisis in decades. A half-deal with Turkey may not come in time to spare Merkel's CDU a major setback at the regional elections in three of Germany's 16 federal states on 13 March. A local election in the state of Hesse on Sunday showed a strong rise in support for the radical right AfD to some 12% amid a low voter turnout. However, signs of progress at the EU-Turkey summit would help Merkel to keep criticism of her approach within her party at bay.

ECB: MODEST ACTION ON THURSDAY

The return of markets to calmer conditions has reduced the need for the ECB to come up with something drastic at its meeting this Thursday to stem a panic. The chances that the ECB would breach new ground by extending its asset purchases to corporate bonds including senior bank debt always looked slim. These chances have probably receded further. We look for the ECB to (i) scale up its monthly asset purchases modestly from €60 to €70 or 75bn, (ii) cut the deposit rate by at least 10bp from its current -0.3% and (iii) to offset the hit to bank balance sheets from a more negative deposit rate through either a generous long-term refinancing operation or a tiered deposit rate.

GERMAN ORDERS: STABILISING

After a significant drop in August and September in a first wave of concerns about China, German factory orders have largely stabilised thereafter. In January, orders declined by 0.1% mom following a 0.2% drop in the month before (revised up from an initial estimate of -0.7% mom) and 1.5% gain in October. Whereas domestic orders fell back in January by 1.6% mom after a strong surge in Q4, export orders rose 1.1% as orders from other Eurozone countries rebounded 7.5% mom in January after a very weak -6.6% in December.

Looking through such short-term volatility, the orders data suggest that industrial output should soon stabilise after a decline in the autumn 2015. However, the turmoil in financial markets in late January and February and the resulting decline in survey data such as the PMIs and Ifo business expectations for February indicate that firms will probably postpone some investment projects. We thus expect a modest drop in German factory orders for the next few months. Unless markets were to sell off sharply again or unless political risks were to materialise badly, the uptrend that had prevailed until July 2015 could then resume again in late spring, paving the way for a return to trend growth in German – and Eurozone GDP – by mid-2016.

US EMPLOYMENT: SOLID GAINS

Six weeks ago, markets were worrying that the US may be heading for a new recession. Like the concerns about an alleged crash in China or supposed negative effects of cheap oil, the data have not confirmed these anxieties so far. Instead, last Friday's solid US employment report shows that the US economy remains on track for GDP growth of just above 2%. While private consumption and the housing market support domestic demand nicely, weak exports reflected in industrial stagnation keep the overall pace of growth moderate. The data are good enough for the US Fed to hike rates again in June.

UK PMI: DOWN AGAIN

Following on from a very bad month in markets, UK PMI data disappointed across all sectors in February. Nevertheless, all indices remained above the '50' growth mark and the change for the last three months over the previous three months remained consistent with our call for a modest slowdown in Q1. Now that market tensions have eased, survey data may start to improve somewhat within the next two months. However, the UK data it will likely remain subdued relative the trends that prevailed until late 2015 until the risk and uncertainty associated with the EU referendum on June 23 has passed.

Joh. Berenberg, Gossler & Co. KG
60 Threadneedle Street
London EC2R 8HP
Phone +44 20 3207 7889
www.berenberg.com
holger.schmieding@berenberg.com