Talking Points

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The latest view on the economy November 30, 2018

# G20-Questions

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Quite often for G20 meetings, the reality simply doesn't come close to living up to the pre-session hype—this one may be different. The confab in Argentina comes at a crucial point for the global economy, with a variety of geopolitical hotspots, trade issues coming to a head, oil prices hanging in the balance, and all against the backdrop of a global economy that is quite clearly losing momentum. Here is a list of arguably the top 20 issues and questions surrounding the global economy at this critical juncture, many of which will be addressed (and even possibly answered) at this weekend's meeting:

1. **Will the U.S./China trade battle simmer down, or heat up?** Of all the many moving parts in the global economy and issues heading into the G20, this is the biggest. President Trump has sent—likely purposefully—mixed signals heading into his dinner meeting with President Xi, suggesting that a "*deal*" is near, but also questioning whether he wants to reach said deal. Best guess is that the rhetoric gets dialled down a notch or two, but this issue returns as a thorn for the market in 2019, as the differences are simply too extreme to be readily resolved. We anticipate additional U.S. tariffs on China, and an even weaker yuan next year.

2. **Will USMCA be safely ratified in a timely manner?** Today's early-morning signing session of the USMCA quickly answered one of the top questions for the G20 sessions. But it now turns to the issue of whether a more sceptical U.S. House will pass it in 2019. We suspect it will be passed, but likely with some high drama in the interim.

3. **Will the steel and aluminum tariffs be removed any time soon?** Prime Minister Trudeau pointedly raised the issue in his speech at today's signing session, highlighting what an (unnecessary) drag they are on the North American economy.

4. **Will OPEC cut production to support oil prices?** The official OPEC meeting isn't until next Thursday, but some have suggested that the real meeting will be on the sidelines of the G20, between Saudi Arabia and Russia. We are assuming that output will be quietly trimmed, and WTI will gradually push back above $60 next year (from around $50 today).

5. **Will Turkey isolate Saudi Arabia?** Note that after a brutal sell-off in the summer, Turkish markets and the lira have mounted a steady recovery. True, the lira is still down 28% this year, but it's up more than 30% from the August lows.

6. **Whither Brexit?** Crunch time has arrived for the long-running Brexit saga. It even drew Mark Carney into the fray this week. (One Conservative Brexiteer calling him a *"failed, second-tier, Canadian politician",* who *"isn't doing a very good job".* Which raises the question: "Yes, but how do you *really* feel about him?"). The parliamentary vote is scheduled for Dec. 11, and let's just say

that the deal faces long odds. While there are a multitude of scenarios that could play out in coming weeks, the pound is leaning heavily to a hard landing of some sort; it's down more than 11% against the U.S. dollar since its spring high, and looks headed for more pressure ahead.

7. **Whither Italy's budget?** Moving past the rhetoric, there were glimpses of optimism on this front, as Italy sounded a slightly less fractious note. One can only hope, given that Italy's jobless rate rose to 10.6% last month amid sub-1% GDP growth over the past year.
8. **Will the EU slowdown morph into something bigger?** Beyond the dual distractions of Brexit and Italy, the underlying EU economy has cooled considerably. With Germany itself plagued with trade concerns, and Trump persistently threatening auto tariffs, Euro Area GDP growth braked to just a 0.7% annual rate in Q3. And this week it was reported that both Switzerland and Sweden also saw GDP dip last quarter. The softness is spreading beyond the core Euro Area.
9. **Is Japan stuck again?** GDP also dipped in Japan in Q3 and is now up just 0.3% y/y. The persistent threat of U.S. auto tariffs remains a key risk. Meantime, inflation remains among the lowest in the industrialized world.
10. **Was India's Q3 slowing a fluke?** In a sign that the cooling of growth truly is a global phenomenon, even the fastest growing major economy saw GDP slow notably last quarter (albeit to a still-hot 7.1% from 8.2%).
11. **Will China cool even further?** With Q3 GDP already coming in below expectations at 6.5%, and mounting concerns on the trade front, any downside surprises will raise eyebrows. And the dip in November's manufacturing PMI, smack on the key 50.0 level, won't soothe concerns.
12. **Amid this increasingly stormy backdrop, will the Fed soon pause?** We still expect the Fed to hike again at its Dec. 19 meeting, but the outlook for 2019 has been dialled back for a variety of reasons. While the market pounced on Powell's comment this week that rates are now *"just below"* neutral, this just pushed on the open door of much lower oil prices, a fading housing sector, and weaker financial markets. Bottom line, we now see just two rate hikes next year from the Fed. And, no, this does not reflect any impact from the President's most recent complaints about the Fed: as one wag put it, Trump seems to be suffering from *"irritable Powell syndrome"*.
13. **What does this mean for the Bank of Canada?** The BoC also has a decision in December (next Wednesday), but few expect a move at that point. The debate is on the early January decision, and we would assert that the Bank needs to see some recovery in oil prices to give it comfort in hiking. Today's soft details behind the 2.0% Q3 GDP advance were not comforting, nor the extremely unfortunate GM news earlier this week.
14. **Could the China slowdown weigh on the entire region?** Key G20 members that are likely to be swept into a cooldown include Australia, Korea and Indonesia, just to highlight a few. Note that, with the RBA pretty firmly locked

on the sidelines, Canadian short-term interest rates look to remain above those of Australia for some time yet, a very rare occurrence.

15. **Will South Korea keep hiking in that environment?** For the first time in a year, the BoK hiked this week, taking its key rate up 25 bps to 1.75% (curiously right in line with Canada).
16. **How will the new regime in Brazil fare?** Brazilian financial markets have been a rare source of strength this year, on hopes that the new leader, Bolsonaro, will help spur the budding economic recovery, and possibly even improve U.S. relations. He takes power at the start of 2019.
17. **And in Mexico?** AMLO takes power on Dec. 1, and Mexican markets have been a bit on edge, looking beyond the short-lived USMCA bump. The Bank of Mexico has been one of the most aggressive rate-hikers in the world this cycle, hiking rates 500 bps since the Fed got going. A slide in the peso has lifted inflation to nearly 5% y/y, while growth is likely to cool to a Canada-like 2%.
18. **Will Russia be chilled again?** The latest border “incident” with Ukraine has renewed the big chill with the West yet again. This comes just as Russian equities were one of the other rare bright spots this year (along with Brazil), although the rouble has been persistently weak.
19. **Can Argentina stop the slide?** The host nation of the G20 meeting happens to be the member that has struggled the most recently, with the peso chopped in half this year, the economy in a deep recession (GDP was down 4.2% y/y in Q2), and inflation flaring above 45% y/y.

**Bottom Line:** A number of key themes that dominated 2018 are reaching a crucial stage, either at the G20 meeting itself, or within a matter of weeks. How they shake out will shape our views on 2019, but it’s increasingly clear that growth is slowing broadly and the risk is for a deeper chill next year.

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And, finally, another trans-national issue (albeit a painfully parochial one for those who don’t reside in Toronto) is coming to a head this weekend…

20. Will William Nylander sign with the Leafs by 5 pm Saturday?

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