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Markets and Trends 2020: Melodrama – next act

Helaba's economic and capital market outlook takes us into the world of theatre and answers the ques-tion of what kind of play will be performed in 2020: a melodrama, a comedy or a tragedy?

- The stage is set for a recovery in the global industrial cycle
- Higher economic growth in Germany
- No return to positive yields on the German bond market
- DAX above 14,000 points over the course of the year

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Baseline scenario: Melodrama – next act (70 percent probability)

As we approach the end of 2019, the global economy is teetering on the brink of recession – the economic equivalent of a nervous breakdown. However, Helaba's economists forecast that the global econ-omy will regain its momentum as we move into 2020 and will continue to expand, albeit the pace of growth will be limited. For this genre of theatre – the melodrama – it is essential that the play has a happy ending, despite significant risks and uncertainties. In this sense, the expectation is that the pro-tagonists will see reason in order to do what is necessary, since neither the United States nor China have any incentive to escalate the trade conflict to such an extent that the global economy goes to pieces. With the easing of the trade war and an orderly, lasting Brexit solution, the prospects for the world economy will brighten again. Fiscal policy in 2020 as a whole will have a slightly expansionary impact and the monetary policy turnaround initiated during the course of this year by the major central banks will have increasingly positive implications for the economy.

"In a downturn, people always ask me: Where is a rebound supposed to come from? It may seem like a platitude, but it typically comes from the very place where economic woes were previously concentrated. The stage is set for a recovery in the global industrial cycle!", declares Dr. Gertrud R. Traud, Helaba's Chief Economist.

Thanks to the significance of its industrial sector, Germany is likely to be among the principal beneficiar-ies. Private consumption and construction activity will continue to provide momentum. However, struc-tural impediments and a lack of reforms will limit momentum. As a result, despite a

cyclical recovery, the average growth rate over the course of 2020 will be a modest one percent in Germany. The euro area is expected to perform slightly better, expanding by 1.3 percent.

In the United States, the recovery will be a little more sluggish in 2020. Despite an assumption of an easing in tensions, its relationship with China will not see a return to pre-2018 conditions. While the economy will benefit from steps taken in 2019 to loosen monetary policy, fiscal policy is not expected to provide any stimulus effects. This is because the election campaign will make it practically impossible for the Democrats to cooperate with the US president. At 2 percent, annual average growth is likely to be somewhat lower than in 2019.

Overall, the study includes 14 country analyses and summaries of the German federal states of Hesse, Thuringia, North Rhine-Westphalia and Brandenburg.

Familiar protagonists

Most of the male leads in the new season are well known: once again, the tall blond across the pond and his opposite number in London will be in the spotlight. Usually, a melodrama is accompanied by music. For the first time, a woman is holding the conductor's baton at the European Central Bank. In the short term, Christine Lagarde will not deviate significantly from her predecessor’s score. In order to underline its willingness to act, the Governing Council of the ECB is likely to reduce the deposit rate once again before taking a longer monetary policy breather. In view of a stabilisation in the economy and a modest inflation rate in 2020, the US Federal Reserve will maintain its "wait and see" stance.

Stage directions for the Investor

In 2020, the potential for gains from equities and bonds will be limited. Helaba's economists expect the yield on 10-year German government bonds to be -0.2 percent by the end of the year. Besides a contin-uation of the ECB's loose monetary policy, persistently low inflation expectations suggest that there is no prospect of a sustained return to positive yields. In the case of equities, there are likely to be tempo-rary exaggerations due to the ongoing lack of investment alternatives. However, a DAX excursion above the 14,000-point mark is unlikely to prove sustainable. Towards the end of the year, the index will be trading at around 13,500 points.

In view of extremely low interest rates, real estate will remain popular with investors. However, the re-cent economic weakness could cause rents and property prices to increase at a somewhat slower pace in 2020. The situation on the German housing market will not ease as long as restrictive political measures continue to weigh on new construction activity.

The US dollar is clearly overvalued and US trade and budget deficits suggest caution is the order of the day. Political headwinds for the euro are also likely to ease in 2020. If the euro area shows signs of eco-nomic recovery, the euro-dollar exchange rate will rise to 1.25 by the end of the year.

Gold will continue to shine in the limelight in 2020, too. In the course of the year, the precious metal is likely to rise to 1,700 US dollars per ounce. In euro terms, the exchange rate will only lead to a sideways movement around a level of 1,400 euros per ounce.

Negative alternative scenario “Tragedy” (10 percent probability)

In Helaba’s negative alternative scenario, the world economy is like a classic tragedy. In the process, the main protagonists experience vicissitudes of fate: With its cast of Brexit villains, the United Kingdom sinks completely into political chaos. The US president attempts to get reelected by escalating the trade conflict and thereby risking a currency war. The result is a global recession. The DAX falls below 9,000 points. In the global devaluation race, the US dollar becomes an involuntary winner while the euro struggles with increasing political conflicts within the single currency area. The euro-dollar exchange rate falls to 0.95. Prices for German government bonds and US Treasuries are likely to rise sharply, driv-en by monetary easing. Gold lives up to its reputation as a crisis asset and surpasses previous highs.

Positive alternative scenario “Comedy” (20 percent probability)

In Helaba’s positive alternative scenario, a fundamentally upbeat sentiment prevails around the world – just like in a comedy. The sometimes-bizarre personality traits of some of the actors are no longer perceived as a burden, but instead culminate in a successful collaboration between nations. Economic growth in Germany, the euro area and the United States accelerates significantly. This gives ECB Presi-dent Lagarde the backing she needs to execute a turnaround in monetary policy. Yields on 10-year Government bonds rise to 0.8 percent and the euro-dollar exchange rate climbs to 1.35. This is greeted with fervent applause from equity markets – the DAX is able to top the 15,000-point mark.

In addition to the print edition, we also provide our annual outlook online at https://www.helaba.com/int/research/ ↗.

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