GLOBAL ECONOMIC DATA CONTINUE TO WEAKEN: CHINESE TRADE DATA; US BUSINESS SURVEYS; UK GDP

CHINA: Chinese exports and imports weakened sharply at year-end 2018. Exports fell 4.6 percent from a year earlier in December, and imports fell an even sharper 7.3 percent. Exports to the United States fell 3.5 percent on the year after rising 9.8 percent in November, while imports plunged 35.8 percent, a fourth consecutive year-over-year decline. Falling Chinese exports reflect lower commodity prices (trade data are not adjusted for inflation); a drop-off in purchases by businesses that front-loaded activity earlier in 2018 to avoid broadening tariffs; and weakening global growth momentum. Falling Chinese imports reflect lower commodity prices, weakening Chinese domestic demand, and Chinese tariffs on US soybeans and other US commodity exports. China’s trade surplus in goods with the United States rose to a record $324 billion US dollars in 2018 from $278 billion in 2017, both measured by the Chinese statistics. US data typically give slightly different totals because of definitional differences; they are unavailable for comparison this year because of the government shutdown. China’s government is loosening economic policies in reaction to weaker growth momentum. The People’s Bank of China announced January 4 that it will reduce the reserve requirement ratio for commercial banks by 1.0 percentage point, with half of the cut effective January 15 and the remainder effective January 25. The reserve requirement ratio cut will provide liquidity to offset the redemption of commercial banks’ borrowings from the central bank’s medium-term lending facility, which will not be renewed. PNC forecasts for the advance report of real GDP growth for the fourth quarter of 2018 to show growth slowing to 6.4 percent in year-over-year terms, with the fourth quarter’s sharp drop in imports and consequent increase in net exports offsetting weak consumption and investment spending in the GDP components. PNC forecasts for Chinese real GDP growth to slow further to 6.2 percent in 2019 as auto sales remain weak, exports to the US slow following American buyers’ front-loading of purchases in late 2018, and slow credit growth limits investment and sales of real estate. At the same time that Chinese and global growth momentum are faltering, lower US interest rates are cushioning financial pressures on China and other emerging markets: Foreign reserves rose $11.0 billion to $3.07 trillion US dollars in December as the US yield curve flattened and medium- and long-term interest rates fell.

UNITED STATES: December’s business sentiment surveys and CPI report confirm cooler growth and inflation at the turn of the year, consistent with PNC’s forecast for a pause in interest rate hikes from the Federal Reserve. The Institute for Supply Management’s Non-Manufacturing Index fell to 57.6 in December from 60.7 in November and was the coolest since July. The National Federation of Independent Business’s Small Business Optimism Index retreated for a fourth consecutive month to 104.4 in December from 104.8 in November; the index had reached a multi-decade high in August. The consumer price index fell 0.1 percent in December on a 7.5 percent plunge in gasoline prices and an 11.4 percent drop in fuel oil prices; food prices rose 0.4 percent, and all items excluding food and energy 0.2 percent. From a year earlier, the CPI rose 1.9 percent, the slowest since August 2017, while the growth of the core index excluding food and energy was unchanged at 2.2 percent.

UNITED KINGDOM: Prime Minister Theresa May is allowing debate to begin ahead of a vote on her Brexit deal during the week of January 14, but could delay the vote again if, as expected, a majority of members of parliament continue to oppose the deal. Further delays in a resolution to Brexit add to the risk of a precautionary recession in which businesses delay hiring and investment amid increasing uncertainty. We
still see a Hard Brexit as very unlikely. The Office for National Statistics’ monthly estimate of real GDP confirmed growth slowed in the fourth quarter: Real GDP grew 0.3 percent in the September to November quarter, not annualized, down from 0.8 percent in the preceding three months. Real GDP grew 0.2 percent in November from October, with manufacturing output contracting for a third consecutive month.

EUROZONE: The Accounts (minutes) of the ECB’s December 12 and 13 Governing Council Meeting, released January 10, explicitly raise the possibility of additional unconventional monetary stimulus in 2019, even after the Bank’s quantitative easing program ended at the end of December 2018. The Accounts read, “Looking ahead, the suggestion was made to revisit the contribution of targeted longer-term refinancing operations to the monetary policy stance.” Targeted Longer-Term Refinancing Operations a.k.a. TLTROs are multi-year fixed rate loans made by the ECB to Eurozone commercial banks at the ECB’s deposit rate, currently -0.4 percent. The comments emphasize that the ECB’s monetary stance will remain highly accommodative in 2019.

CANADA: Matching PNC’s forecast, the Bank of Canada held the overnight rate target unchanged at 1.75 percent at its January 9 monetary policy decision. The Bank’s quarterly Monetary Policy Report downgraded the outlook for real GDP growth in 2019 to 1.7 percent from 2.1 percent in the October 2018 Report, reflecting the blow to the energy industry from late 2018’s drop in oil prices. The Bank forecasts for growth headwinds from the housing sector to persist into 2019. The BoC also forecasts for inflation to temporarily slow in 2019 due to lower oil prices, and to average 1.7 percent in 2019, then rise to the Bank’s 2.0 percent target in 2020. PNC forecasts for the Bank of Canada to raise the overnight rate target 0.25 percentage point to 2.00 percent at its April 2019 decision, but further deterioration of the global growth outlook could push back the BoC’s rate hike to October. The Teranet-National Bank House Price Index™ fell 0.3 percent in December from November, a third consecutive monthly decline, and rose 2.5 percent from a year earlier, down from 3.1 percent in November.

JAPAN: Income growth remains solid ahead of the October hike in the value added tax from eight to 10 percent. Average cash earnings rose 2.0 percent from a year earlier in November, up from 1.5 percent in October, while average incomes of workers’ households grew 1.1 percent.

MEXICO: The Mexican economy is slowing sharply in January after President Lopez Obrador shut down gas pipelines in an effort to stop organized theft of gasoline. Mexican media report long lines at gas stations and disruptions to businesses, including manufacturers, that are unable to carry out normal business activities. The economy will bounce back quickly if the shutdown is short-lived.

BRAZIL: Inflation by the benchmark IPCA index slowed to 3.8 percent in December from 4.1 percent in November on falling transportation costs, reflecting pass-through of lower global oil prices. Lower commodity prices will be a headwind to industrial activity in Brazil in the first half of 2019.

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