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GLOBAL ECONOMIC HIGHLIGHTS

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US OPTS AGAINST ESCALATING TARIFFS ON CHINA; UK LIKELY IN RECESSION AHEAD OF BREXIT VOTES

CHINA: President Trump decided against higher tariffs on Chinese imports or broadening their scope on March 1, going back on threats he made earlier in 2019, in another sign that his administration and the Chinese government will announce a trade truce later in March. US Trade Representative Robert Lighthizer testified to Congress on February 27 that there are still large gaps between US demands and China's offer on trade, but it appears that other voices in the Trump administration that advocate an earlier resolution to the trade conflict instead of a more ambitious, but harder to achieve agreement, won the policy debate. Chinese manufacturing sentiment surveys point to a further contraction of activity in February, paralleling drops in output reported in many other foreign economies – knock-on effects of trade policy uncertainty, stock market volatility in late 2018, and the approach of the Brexit deadline. The Caixin general manufacturing PMI bounced back to 49.9 in February from 48.3 in January, but the CFLP manufacturing PMI weakened to 49.2 from 49.5 and was the weakest since February 2016. The CFLP non-manufacturing PMI edged down to 54.3 from 54.7 and was close to its 2014-2018 average of 54.1.

UNITED KINGDOM: The manufacturing sector is contracting and the UK is probably in recession ahead of the end-March Brexit deadline: The Markit/CIPS manufacturing PMI dipped to 52.0 in February from 52.6 in January and was the second-lowest since July 2016, and the details were HORRENDOUS. Pre-production inventory accumulation was the highest in the series history (going back to the year 2000) for a second consecutive month, a sign that businesses are doomsday prepping ahead of the Brexit deadline. Meanwhile, output expectations were the lowest in series history – even worse than during the global recession of 2008-2009. The largest share of manufacturers cut payrolls since February 2013, in a second month of net job losses for the sector. Prime Minister Theresa May plans to hold a series of three votes in Parliament on Brexit policy March 12, 13 and 14: On the 12th, she will hold another vote on the Withdrawal Agreement her government negotiated with the EU – Parliament already rejected it on January 15 by a huge 432-202 margin (the largest margin voting against a government policy in Parliament's history), and will very likely reject it again in March. On March 13, Parliament will vote on whether the UK should leave the EU without a Withdrawal Agreement – the no-deal Brexit that would cause disastrous supply chain disruptions for manufacturing and many other sectors. On January 9, a Parliamentary majority voted to restrict Prime Minister May's ability to manage the government's finances in the event of No Deal, a sign that a solid majority opposes the option. If both the March 12 and 13 votes are rejected, Prime Minister May will allow a vote on March 14 to extend the UK's negotiation with the EU – if passed, as seems likely, the EU will agree to continue the status quo to prevent a Hard Brexit and allow time for British public opinion to acknowledge that the costs of Brexit (like those demonstrated in the terrible February factory sentiment data) are much larger than its advocates argued prior to the June 2016 referendum, and that policy should shift as a result.

UNITED STATES: Current housing data still point to contractions, but leading indicators like building permits and pending home sales are stabilizing in early 2019 on lower long-term interest rates. Building permits rose 0.3 percent in December from November, while starts and completions fell 11.2 percent and 2.7 percent, respectively, on the month. Permits rose 0.3 percent from a year earlier, while starts and completions fell 10.9 percent and 8.4 percent, respectively. The National Association of Realtors® index of pending home sales rose 4.6 percent in January as lower interest rates boosted buyers' spending power. The

Conference Board's Consumer Confidence Index® recovered to 131.1 in February after dropping to 121.7 in January due to the government shutdown and stock market volatility. The present situation sub-index was the strongest since December 2000, but expectations were below levels averaged in 2018 and 2017, consistent with our forecast for US growth to slow in 2019 as stimulus wears off and a higher federal funds rate restrains growth in sectors depending on variable-rate credit like auto sales. The US trade deficit reached a new record high in December as exports fell 2.8 percent and imports rose 2.4 percent. The IHS Markit manufacturing PMI fell to an 18-month low of 53.0 in February from 53.9 in January and the ISM manufacturing PMI fell to a 27-month low of 54.2 from 56.6.

CANADA: Average weekly earnings rose 1.8 percent on the year in December despite a drop in the average work week to 32.5 hours from 32.8 hours a year earlier; these data from Canada's payroll employment survey imply average hourly earnings rose about 2.7 percent on the year, better than the tepid 2.0 percent growth of average hourly earnings in the January household jobs report. Nonfarm payroll employment rose 2.0 percent on the year, also better than the 1.8 percent growth of household employment in January. The IHS Markit manufacturing PMI fell to a 26-month low in February, paralleling the Chinese and US PMIs' drops. Real GDP slowed to a weak 0.4 percent annualized in the fourth quarter of 2018 as consumer purchases of durable goods and construction spending on residential and nonresidential structures fell from a quarter earlier; both exports and imports fell slightly on the quarter. For all of 2018, real GDP growth slowed to 1.8 percent from 3.0 percent in 2017. The monthly GDP accounts for December showed manufacturing down from November and construction output falling for a seventh consecutive month. The fourth quarter's weak GDP report is not pretty, but neither is it surprising – the weakness in energy, manufacturing, and construction have been apparent in higher frequency indicators for several months. A rate hike from the Bank of Canada is still possible at the April 15 decision if, as we expect, job growth stays solid in the next two monthly releases. PNC forecasts for the February jobs report, to be released Friday March 8, to show a solid 20,400 jobs added from January and the unemployment rate holding at 5.8 percent, close to its lowest since comparable data began in the 1970s. PNC forecasts for average hourly earnings to pick up from 2.0 percent in January to 2.3 percent as the gap between the soft household survey and stronger payroll survey narrows.

EUROZONE: The IHS Markit manufacturing PMI fell to 49.3 in February (close to the 49.2 flash estimate) from 50.5 in January; the index's fall below fifty, indicating contraction of manufacturing output, was the Eurozone's first since June 2013. The unemployment rate was 7.8 percent in January, tying the previous month for the lowest since October 2008 – December's unemployment rate was revised down to 7.8 percent from the 7.9 percent reported in the prior release. HICP inflation was little changed at 1.5 percent in year over year terms in the February flash estimate after 1.4 percent in January; Eurostat's three indexes of core inflation (excluding various combinations of food, energy, and alcohol and tobacco) were also little changed on the month, ranging between 1.0 and 1.2 percent in the same terms, and undershooting the ECB's medium-term target of inflation below but close to 2 percent. The ECB's upcoming March 7 Governing Council decision will keep the bank's monetary stance unchanged, but could answer four key questions about the policy outlook. First, the release of their March economic projections will inform whether the central bank will make its first post-crisis rate hike this year, as PNC forecasts. The projections will probably lower the outlook for growth in 2019 from the December 2018 projections, which forecasted real GDP growth of 1.7 percent in 2019 and 2020 and 1.5 percent in 2021. If the ECB maintains the 2020-2021 growth forecasts unchanged, it would support PNC's forecast for a deposit rate hike in September. But if the March projections instead downgrade both the 2019 and 2020 growth projections, it would signal the Governing Council plans to delay an initial rate hike until 2020. Second, the ECB will probably give some guidance about how it would respond to a no-deal Brexit in the unlikely case that the UK does not extend its negotiation with the EU by the end of March. Third, the ECB will probably provide detail about if and when it will extend a new round of Targeted Longer Term Refinancing Operation loans, multi-year loans to ECB commercial banks fixed at the current deposit rate; TLTROs made in the aftermath of the sovereign debt crisis will mature in the next 18 months, and another round would roll over the existing loan stock. Fourth, the Governing Council could provide a more granular description of the range of views among its members, and not just the consensus, to prepare markets for new leadership after President Draghi's term ends October 31. The three leading candidates to succeed him are the German central bank head Jens Weidmann, French member of the ECB Executive Board Benoit Coeure, and former head of the Finnish central bank Erkki Liikanen. Liikanen and

Coeure are moderates on interest rates, while Weidmann advocates faster rate hikes than currently priced in by financial futures markets. President Draghi's successor will become apparent to financial markets soon: Draghi was officially nominated for the presidency in May 2011, ahead of assuming office on November 1.

JAPAN: The Nikkei manufacturing PMI for Japan fell to 48.9 in February (revised up from the 48.5 flash estimate) from 50.3 in January and was the weakest since August 2016; Markit's press release cited lower sales to China as a drag on new export orders and by extension the overall index. Several current and former Bank of Japan policymakers stated in interviews in late February that the Bank could intensify its quantitative easing program if the Japanese expansion falters or the yen appreciates and reduces the outlook for inflation, including BoJ Governor Haruhiko Kuroda in testimony to parliament at mid-month. Against the context of more dovish policy guidance from the Fed, ECB, Bank of England, and Bank of Canada, the Bank of Japan's more dovish guidance is a further sign that the global rate hike cycle is nearly over.

INDIA: Real GDP grew 6.6 percent in year over year terms in the fourth quarter of 2018, with a broad-based slowdown in agriculture, manufacturing, and utilities offsetting faster growth in construction and a stabilization of the mining sector. India's trade deficit widened slightly to 3.9 percent of GDP in the latest quarter from 3.75 percent a year earlier, a sign that, even before the Reserve Bank of India's February policy rate cut, and the government's announcement of fiscal stimulus programs ahead of the April-May elections, India's policy stance was already expansionary. Stimulus policies have lifted growth since the turn of the year: The Nikkei manufacturing PMI rose to a 14-month high of 54.3 in February from 53.9 in January, with improvements in new orders, output, inventories, and employment. Indian growth should be solid in the next few months, but will probably face headwinds after the election.

MEXICO:.The Bank of Mexico's Quarterly Report marked down the real GDP forecast for 2019 to a range of 1.1 to 2.1 percent from 1.7 to 2.7 percent in the prior quarter's report, and marked down the forecast for growth in 2020 to a range of 1.7 to 2.7 percent from 2.0 to 3.0 percent previously. The IHS Markit manufacturing PMI jumped to a 13-month high of 52.6 in February from 50.9 in January, paralleling the pickup in manufacturing in India and Brazil and bucking the softer trend in the US, Canada, China and Europe. Mexico's minimum wage rose 16.2 percent to $8.80 a day in regions bordering the United States on January 1, triggering strikes in many locations across the country as workers in manufacturing and service jobs demand commensurate wage increases.

BRAZIL: The Brazilian Senate passed a law tightening mine safety regulations and increasing the costs of allowing mining disasters on February 27 in reaction to the collapse of a mining dam owned by Vale on January 25, which killed an estimated 300 people. Brazilian mining companies will focus on improving safety in 2019, slowing production and investment to ensure that no further disasters occur. The IHS Markit manufacturing PMI rose to 53.4 in February, the highest in 11 months, after 52.7 in January.

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