March 11, 2019

GLOBAL ECONOMIC HIGHLIGHTS

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CHINESE EXPORTS PLUNGE; UK DATA BAD PRE-BREXIT; US JOB GROWTH SLOWS, DETAILS BETTER; ECB LEANS DOVISH

CHINA: Exports plunged 21.2 percent from a year earlier in February, the largest drop since February 2016, when fears of a Chinese financial crisis and hard landing swept global financial markets. Several temporary factors contributed to the decline. Prices of oil, steel, and soy were lower on the year, and the Lunar New Year fell earlier in the month than in 2018, keeping factories closed longer while migrant workers returned to their hometowns to celebrate the holiday. In addition, some US importers front-loaded purchases of Chinese products in late 2018 to hedge against tariffs rising even more, and are now slowing purchases. But these factors only partially explain February's weakness. Falling Chinese exports confirm the slowdown of global manufacturing and goods trade signaled by weak global business surveys in early 2019. Trade policy uncertainty, the lagged effect of higher interest rates in 2018, and turn-of-year financial volatility slowed growth in early 2019, in China and much of the rest of the world. The effect is particularly evident in the IHS survey of global metal using industries, which was the weakest since the '08-'09 crisis in February. Chinese exports will stabilize in the rest of 2019, but will likely lag growth of the domestic economy, which will be boosted by fiscal stimulus and slightly faster credit growth. China's Premier Li Keqiang reinforced expectations for measured stimulus at his March 5 announcement of economic targets to the National People's Congress. Premier Li announced a slightly larger fiscal deficit target for 2019 of 2.8 percent of GDP, up from a 2.6 percent target in 2018, and facilitating a 3 percentage point reduction in the value added tax rate for manufacturers, who are hard hit by US tariffs and trade policy uncertainty. Fiscal stimulus will also finance lower payroll taxes (social insurance contributions) for small businesses. China is targeting credit and money supply growth in line with nominal GDP this year, aiming to keep macro leverage (debt to GDP) basically stable; policymakers pledge to "refrain from using a deluge of stimulus policies." China might cut benchmark interest rates after the Fed signals the end of its rate hike cycle, but a credit boom is unlikely near-term. PNC forecasts for Chinese real GDP growth to slow to 6.2 percent in 2019 from 6.6 percent in 2018, in line with Premier Li's announced target of growth in a range of 6.0 to 6.5 percent.

UNITED KINGDOM: The Markit/CIPS services PMI compounded the recessionary signal from the manufacturing PMI in February. The survey reported service sector employment falling the fastest since November 2011, paralleling the decline in manufacturing employment, which fell the fastest since February 2013. The UK is likely in a precautionary recession: Businesses are delaying hiring and investment while they make contingency plans for a worst-case outcome of the end-March deadline for the Brexit negotiation. Prime Minister Theresa May is planning to hold three Parliamentary votes March 12, 13 and 14: On the 12th she will hold another vote on the Withdrawal Agreement her government negotiated with the EU – Parliament rejected it on January 15 by a 432-202 margin, the most decisive vote against a government policy ever, and will very likely reject it again. On the 13th Parliament will vote on whether the UK should leave the EU in a no-deal Brexit. A majority of parliament signaled opposition to this choice on January 9, when they voted to restrict Prime Minister May's ability to manage the government's finances in the event of no deal. If both the March 12 and 13 votes fail, the Prime Minister will allow a March 14 vote to extend the Brexit negotiation with the EU. If it passes as seems likely, the EU will extend the negotiation to prevent a Hard Brexit and allow time for British public opinion to come to terms with Brexit's costs, like those demonstrated by the terrible February PMI data.

UNITED STATES: A weak jobs headline for February, with mixed but mostly positive details in the rest of the report. The US economy added just 20,000 nonfarm payroll jobs, the worst since September 2017, when Hurricanes Harvey and Irma sharply reduced hiring. February's weak job growth is giveback after very strong gains in December and January: Including the 12,000 in upward revisions to the prior two months, job growth has averaged a solid 186,000 since December, fast enough to keep the unemployment rate falling. Also positive, the unemployment rate dropped back to 3.8 percent in February from 4.0 percent in January and was close to its 49-year low of 3.7 percent reached in September and November, as government workers and contractors furloughed by the shutdown returned to work. Similarly, Americans who worked part-time for economic reasons fell to 2.6 percent of the labor force in February, a recovery to date low and the best since April 2006, from 3.1 percent in January, the highest since Hurricanes Harvey and Irma in September 2017. Wage growth was strong in February too: Average hourly earnings rose 0.4 percent on the month and 3.4 percent on the year, the fastest since March 2009. PNC forecasts for the unemployment rate to fall to 3.4 percent by the end of this year as job growth moderates but persists, lowering the unemployment rate to the lowest since the 1950s. But two details of the February jobs report suggest downside risk to this outlook. First, the average workweek edged down to 34.4 hours from 34.5 hours, despite a large shift of workers from part-time to full-time (which should have lifted average hours worked), on a drop in the construction workweek. Construction employment also fell on the month, by a large 31,000. February's Polar Vortex surely contributed to the month's weak construction data, but problems could persist: even after February's job losses, construction employment rose 3.1 percent from a year earlier; by contrast, housing starts fell 7.8 percent from a year earlier in the most recent data for January. Second, the unemployment rate for African Americans rose to 7.0 percent from 6.8 percent in January, was the highest since January 2018, and was up markedly from the cyclical low of 5.9 percent in May. This may just be noise; statistics tracking sub-samples of the household jobs survey, like the unemployment rate for African Americans, are more volatile than statistics based on the whole sample. But it could be a warning sign for the overall outlook. African American workers are often the last to be hired and first to be fired in business cycles; the black unemployment rate has averaged 1.4 percentage points higher than that of Americans with less than a high school diploma, of all races, since the end of the Great Recession, even though more than 90 percent of black labor force participants completed high school and 40 percent hold a college degree. The recent uptick in African American unemployment should be monitored as a potential leading indicator of broader labor market weakness. The black unemployment rate rose at least 1.1 percentage points in the six months preceding each of the last four recessions, with an average increase of 1.6 percentage points. With risks noted, it stands emphasizing that the economic expansion still seems set to persist in 2019 due to the service sector, which look much stronger than manufacturing in recent surveys: The ISM nonmanufacturing index rose to 59.7 in February from 56.7 in January and the IHS Markit services PMI rose to a seven-month high of 56.0 from 54.2.

EUROZONE: A dovish monetary policy decision from the European Central Bank. The ECB announced March 7 a plan to roll over maturing targeted longer term refinancing operation (TLTRO) loans, ruled out a 2019 rate hike, sharply downgraded the 2019 growth outlook, and modestly downgraded their short-term and longer-term inflation outlook. The bank announced a new round of TLTRO loans to Eurozone commercial banks, permitting them to roll over prior TLTROs that mature in 2020 and 2021. The new TLTROs, like the prior round issued June 2016 to March 2017, will be made in quarterly tenders starting in September 2019 and concluding in March 2021. The interest rate on the loans will be at highest the ECB's main refinancing operation rate – currently zero – and could be as low as the -0.4 percent deposit rate if commercial banks qualify for interest rate discounts by hitting targets for lending growth. TLTRO interest is paid when loans mature. The new round of TLTROs will be two-year fixed-rate loans, a shorter maturity than the four-year loans issued in 2016 and 2017. The TLTROs will ensure that funding does not limit Eurozone banks' capacity to grow loans, but is less aggressive than the prior round because the loans' maturity is shorter. The ECB also changed their forward guidance to say the Governing Council "expects" policy rates to hold unchanged at least through the end of 2019, longer than their prior guidance to hold rates unchanged at least through the end of summer. They kept unchanged their guidance that interest rates will stay unchanged "for as long as necessary" to raise inflation to their target of below but near two percent. The ECB is holding off on a rate hike in reaction to a weakened outlook for growth and inflation: Their March economic projections sharply downgraded the real GDP growth forecast to 1.1 percent in 2019 from 1.7 percent in the prior quarterly forecast, and also lowered the 2020 growth outlook by 0.1 percentage point to 1.6 percent. The projections also downgraded the inflation forecasts across the ECB's entire forecast horizon: HICP inflation is now forecasted at 1.2 percent in 2019, 1.5 percent in 2020, and 1.6 percent in 2021, down from the December forecasts of 1.6 percent in 2019, 1.7 percent in 2020, and 1.8 percent in 2021. The weaker near-term inflation outlook reflects lower oil prices and weaker business sentiment. The weaker longer-term inflation outlook reflects the ECB's recognition that structural factors are restraining inflation: an aging workforce, weak productivity growth, and labor market deregulations enacted in the sovereign debt crisis that weakened unions' power to secure wage increases. All these factors slow wage growth, in turn slowing inflation. Very notably, the March ECB decision was unanimous. Even the Governing Council's most vocal monetary policy hawk – German Bundesbank President Jens Weidmann – voted for more stimulus. Weidmann is one of three frontrunners to lead the ECB after President Draghi's term ends in October, along with Executive Board member Benoit Coeure and former Finnish central bank head Erki Liikanen. Weidmann's vote with the majority keeps him in the running for the post. The Eurozone countries' heads of state choose the ECB President, and will probably announce their decision in May. Countries with weaker economies and high debt like Italy want the ECB to keep monetary policy loose to support growth and higher inflation, even at the cost of lower income for savers in countries like Germany. Following the ECB decision, financial markets price in only about a 30 percent chance of a 0.1 percentage point policy rate hike over the next 12 months, down from a 70 percent probability in December. After the ECB's latest downgrades to their forecasts, their outlook is pessimistic enough that upside surprises to growth, inflation, and by extension to interest rate expectations are possible over the next 12 months. Assuming the unemployment rate continues to fall (it was at the lowest since October 2008 in December and January) and global growth stabilizes at a more moderate rate in the second half of 2019, PNC forecasts for the ECB to raise its deposit rate 0.1 percentage point to -0.3 percent at its March 2020 policy decision. If growth surprises to the upside, a rate hike could come as soon as January. In addition, if Bundesbank President Jens Weidmann wins the horse race to lead the ECB, Eurozone yield curves could steepen substantially as markets price in a less dovish trajectory for monetary policy in 2020 and beyond.

CANADA: An awesome February jobs report with robust job growth and faster wage growth keeps a rate hike on the table at the Bank of Canada's April 15 monetary policy decision. Employment rose a robust 56,000 in February, much better than the 1,200 consensus or PNC's 20,400 forecast, and more than twice the 25,000 forecast of the most optimistic forecaster in the Bloomberg consensus survey. As expected, the unemployment rate held steady at 5.8 percent, close to the November-December multi-decade low of 5.6 percent. Also matching PNC's forecast, average hourly earnings growth accelerated to 2.3 percent in year over year terms from 2.0 percent in January, narrowing the gap between the closely followed household survey and the payroll survey, which showed average hourly earnings growing 2.7 percent from a year earlier in the most recent December release.

JAPAN: The Nikkei services PMI rose to 52.3 in February from 51.6 in January and new orders were the strongest in 18 months; Japan's strong service sector PMI data stand in contrast to weak manufacturing surveys, paralleling the situation in the US and assuaging fears of a global recession in early 2019.

MEXICO: Mexicans like the economic policies of new president Andres Manuel Lopez Obrador much more than international investors, who have been worried by Fitch's recent downgrade to Pemex's credit rating, strikes demanding higher wages, and gasoline supply bottlenecks caused by the government's campaign to root out fuel theft. Consumer confidence jumped to its highest since comparable data began in 2001 in February, fueled by extremely upbeat forward-looking economic expectations.

BRAZIL: The IHS services PMI rose to 52.2 from 52.0 and was the strongest in a year, with new business improving at the fastest rate since 2013. The Vale mine disaster has not dented Brazil's domestic growth momentum.