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GLOBAL ECONOMIC HIGHLIGHTS

Gus Faucher Chief Economist | **Stuart Hoffman** Senior Economic Advisor | **William Adams** Senior Economist | **Kurt Rankin** Economist | **Abbey Omodunbi** Economist

THE PNC FINANCIAL SERVICES GROUP | The Tower at PNC Plaza | 300 Fifth Avenue | Pittsburgh, PA 15222-2401

ONE-OFF TAILWINDS LIFT US' FIRST QUARTER GDP; MONETARY POLICY TILTS DOVISH IN JAPAN AND CANADA

UNITED STATES: Real GDP grew a better than expected 3.2 percent in the first quarter of 2019, exceeding the 1.9 percent consensus forecast and providing further evidence that fears of a recession in early 2019 were unfounded. Some of the drivers of the first quarter's growth look like one-off boosts: Inventories rose sharply in the quarter and added 0.65 percentage points to GDP; this was the third quarter in which inventories added to GDP growth. Imports fell as businesses ended front-loaded purchases of Chinese goods in late 2018 that were intended to avoid potential increases in tariffs; lower imports added 0.58 percentage points to GDP, since domestic demand was directed toward US-produced goods and services. Strong growth of state and local investment spending added another 0.41 percentage points to GDP. The Congressional Budget Office estimated that the government shutdown subtracted 0.4 percentage points from growth in the first quarter, but federal expenditures were actually flat on the quarter; the Bureau of Economic Analysis's preliminary GDP estimate did not break out the impact of the shutdown. Subtracting from growth, personal consumption expenditures on durable goods fell an annualized 5.3 percent in the quarter (lower auto sales in an unusually cold winter), nonresidential investment in structures fell 0.8 percent, and residential investment 2.8 percent. Nonresidential investment in structures grew 1.3 percent from a year earlier in the first quarter, the slowest since the third quarter of 2016. Total nonresidential fixed investment, including not only structures but also equipment and intellectual property products, slowed to 4.8 percent growth in year-over-year terms, the slowest since the first quarter of 2017. Residential investment fell 3.1 percent from a year earlier, a second consecutive year over year decline; residential investment is in the worst stretch since 2011. Real GDP growth will slow in the rest of 2019 as the one-off tailwinds supporting the first quarter fade, but residential investment will recover over the course of 2019 and keep growth positive. New home sales rose 4.5 percent in March to the highest since November 2017. While existing home sales fell 4.9 percent in March, this was after an 11.2 percent surge in February. Existing home sales rose 1.4 percent in the first quarter of 2019 from the fourth quarter of 2018, the first quarterly increase since the fourth quarter of 2017. Seasonally-adjusted mortgage applications for home purchase (Reported weekly by the Mortgage Bankers Association) have averaged 11.0 percent higher since the turn of the year than in the fourth quarter of 2018, a strong sign that housing sales will pick up in 2019 and support stronger residential investment. And federal spending will be a tailwind through mid-2019 as the government catches up on spending delayed by the shutdown. PNC forecasts for the Bureau of Labor Statistics' April jobs report to show nonfarm payroll employment up a moderate 175,000 from March, the unemployment rate unchanged at 3.8 percent, and average hourly earnings up 3.3 percent from a year earlier.

JAPAN: The Bank of Japan made dovish albeit mostly symbolic changes to its monetary stance at its April 25 monetary policy decision. They announced a new component of their forward guidance, stating that the short-term and long-term interest rate targets would hold unchanged "for an extended period of time, at least through around spring 2020," as the BoJ waits for the impact of the 2018-2019 global slowdown and October 2019 value added tax hike to fade. Since financial markets did not anticipate a rate hike before spring 2020 – and actually imply a rate cut is more likely – the new guidance has no market moving implications. The BoJ also broadened the types of collateral it would accept at its discount window, and said that they "will consider" the introduction of an ETF Lending Facility, which would seemingly make ETFs available to short-sellers betting that Japanese stock prices will fall – a step that would work against the BoJ's goal of supporting stock prices, and so one they are very unlikely to use. The statement is probably an attempt to mollify financial market participants who worry that liquidity in stock and bond markets is falling as the BoJ becomes an ever-larger holder of Japanese financial assets. The BoJ held unchanged the stance of its key monetary instruments: The short-term policy rate is -0.1 percent, the target for the 10-year government bond yield is "around zero percent," with some fluctuation permitted around that level, and the BoJ continues to buy ETFs and REITs at annual rates of ¥6 trillion yen and ¥90 billion yen, respectively. The labor market is softening modestly on manufacturing's weakness, but the overall economy is resilient. The unemployment rate ticked up to 2.5 percent in March; it has been in a range of 2.3 to 2.5 percent since January 2018. Employment rose 0.3 percent on the month and 1.0 percent on the year, with male employment flat on the month and growth slowing in year-ago terms; the weakness of the manufacturing sector pushed the unemployment rate for men up to 2.8 percent in March, the highest since April 2018. Inflation is little changed and trending between 0.5 and 1.0 percent, well below the BoJ's 2.0 percent target. The CPI index was unchanged in March, as was CPI less fresh food and CPI less fresh food and energy; from a year earlier, CPI rose 0.5 percent, CPI less fresh food 0.8 percent, and CPI less fresh food and energy 0.4 percent. The April preliminary report of CPI for the Tokyo metropolitan region showed total CPI up 0.3 percent on the month and both core measures up 0.2 percent; CPI rose 1.4 percent from a year earlier, CPI excluding fresh food 1.3 percent, and CPI excluding fresh food and energy 0.9 percent.

CANADA: The Bank of Canada downgraded its outlook for real GDP growth in 2019 to 1.2 percent in its April *Monetary Policy Report* from 1.7 percent in the January *Report*, reflecting the drag from trade policy uncertainty, the housing market's correction, logistics bottlenecks affecting oil shipped between Alberta oilsands and refiners, and a less stimulative budget for Ottawa. They revised the monetary policy statement to remove discussion of the neutral interest rate, a signal that the BoC no longer expects to raise interest rates before ending the current rate hike cycle. However, BoC Governor Stephen Poloz stated in the April 24 press conference following the *Monetary Policy Report's* release that the BoC's policymakers believe Canada's slowdown is temporary, and if they are correct, that the BoC's next move is much more likely an interest rate hike than a cut.

EUROZONE: Weak sentiment surveys reinforce the message from the weak IHS Markit flash manufacturing and services PMIs for the Eurozone, which showed the economy's slowdown persisting in April. The Ifo Business Climate Index for Germany dipped to 99.2 in April from 99.7 in March and was the second worst after February since May 2016. The European Commission's Consumer Confidence Index also dipped in April and matched January for the second-weakest after December since June 2017. The center-left Socialist Workers' Party won the largest share of parliamentary seats in Spain's April 28 general election, and will take over from the conservative party in leading the government. The far-right Vox party won seats in the election, the first time a Spanish far-right party has done so since the end of fascist rule in 1975. The election has little immediate market-moving implication since Euroskeptics and pro-Catalan independence parties will stay marginalized. But the stinging defeat of the center-right conservative party might foreshadow an equally stark defeat for the British Tories in the May 23 European Parliamentary elections, which could be a catalyst for a British general election or at least a change of leadership in the Tory party.

CHINA: The People's Bank of China extended 267.4 billion yuan of loans to commercial banks through its Targeted Medium-term Lending Facility on April 24, up from 257.5 billion in the January operation; the loans, at 3.15 percent and 15 bps below the 3.30 percent MTLF rate, are designed to encourage commercial banks to increase lending to small- and micro-size businesses. The next round of the US-China trade negotiations will begin April 30 when US Trade Representative Robert Lighthizer meets Chinese Vice Premier Liu He in Beijing to see if either side is willing to make concessions to finish their bilateral trade agreement. Profits of industrial firms jumped 13.9 percent from a year earlier in March, another sign that stimulus channeled toward real estate investment is benefitting upstream suppliers.

UNITED KINGDOM: A recession is likely in the second and third quarters of 2019: The Confederation of British Industry's Business Optimism Index held under zero in April after negative readings in March 2019 and December 2018. A similar persistently negative period in 2011-2012 coincided with a near recession, and in 2016 with the year's memorable plunge in the British pound sterling exchange rate.

MEXICO: The unemployment rate rose to 3.6 percent in March, matching December for the highest since December 2016. However, the labor force participation rate leaped to 60.3 percent from 59.5 percent, suggesting some of March's increase is either a big monthly jump in jobseekers or, more likely, seasonal noise around the Easter holiday.

BRAZIL: Inflation at mid-month April rose to 4.7 percent from 4.6 percent at month-end March and 4.2 percent in mid-March. Both food, energy, and core inflation have increased in recent reports. The Central Bank of Brazil's weekly survey of professional forecasters showed the median estimate for real GDP growth in 2019 fell to 1.7 percent in the April 18 survey from 2.0 percent a week prior. Brazil's pension reform cleared the first legislative hurdle in a congressional committee vote April 23, renewing hopes that a reform will help the country regain its investment grade credit rating. The pension reform proposal will now move on to the House's Special Committee, and will need to pass through the Chamber of Deputies, the Constitution and Justice Commission (CCJ), and the Senate to become law.