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GLOBAL ECONOMIC HIGHLIGHTS

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EUROPEAN CENTRAL BANK AND BANK OF JAPAN REINFORCE EXPECTATIONS FOR EASING IN SECOND HALF OF 2019

EUROZONE: European Central Bank sources leaked a story to Bloomberg on July 18 that their staff economists are conducting a review of the bank's monetary policy framework, which could change its inflation target from "below but near two percent" to an explicitly symmetric target. That would mean that in the future, the ECB would react as aggressively to raise inflation when it is below target as they do when inflation is over target. ECB President Mario Draghi stated in a speech to the ECB's summer policy conference that a key to the ECB's policy response to low inflation was "clarifying the symmetry of [their] aim." If the Bloomberg story is correct, the policy review would institutionalize Draghi's point of view and make the ECB's monetary policy strategy more like the Fed's and those of other advanced economy central banks. More immediately, the ECB is likely to hold its policy stance unchanged at its July 25 monetary policy decision and signal a rate cut in September, although a rate cut or restart of quantitative easing is not out of the question in July. Financial markets price in roughly 50-50 odds of a July 25 rate cut and 90 percent odds of a cut in September. The final estimate for inflation in June by the benchmark HICP index was 1.3 percent in year-over-year terms, a hair higher than the 1.2 percent flash estimate; most measures of core HICP were between 1.1 and 1.3 percent in the same terms, in line with recent trends. Service prices jumped 0.7 percent on the month and service price inflation accelerated to 1.6 percent in year-over-year terms from 1.0 percent in May; services inflation has been volatile in recent months due to fluctuations of fuel prices that flow through to prices of airfares and other transportation services.

JAPAN: Bank of Japan Governor Haruhiko Kuroda stated at a press conference on July 18 that the BoJ would consider available data "until the last minute" before making a decision about their policy stance at the Bank's July 29 and 30 Policy Board meeting. As Governor Kuroda states, the choice between additional stimulus or leaving policy unchanged in July is a coin toss, but the BoJ, like the ECB, is very likely to lower its short-term policy rate, currently -0.1 percent, and to expand its purchases of exchange-traded funds, before the end of 2019. In addition to headwinds from the global manufacturing slump and trade policy uncertainty, Japanese growth will weaken further after the government raises the value added tax in October; Japan experienced a moderate recession after its most recent value added tax hike in 2014.

UNITED STATES: The University of Michigan Consumer Sentiment Index was little changed at 98.4 in the July preliminary release after 98.2 in June, and the Bloomberg Consumer Comfort Index rose to a new expansion to date high of 64.7 from 62.6 and was the strongest since November 2000. Building permits fell 6.1 percent in June from May and housing starts 0.9 percent, disappointing given that effective mortgage interest rates have fallen dramatically since the fourth quarter of 2018. The regional divergence of housing data suggests that limits on mortgage interest deductions enacted as part of the 2018 tax law are a headwind for construction in markets with high home values: In the second quarter, building permits were 3.3 percent below their peak in the first quarter of 2018 in the South, and 6.6 percent below it in the Midwest, but a larger 13.7 percent below it in the West and 15.2 percent in the Northeast. The Federal Reserve's Beige Book, which compiles surveys of business contacts conducted by regional Fed branches, reported little overall change in the "modest" pace of US growth in data collected through early July, and continued tight labor market conditions. Respondents to several regional Fed branches reported headwinds to manufacturing from tariffs and other trade-related issues.

CHINA: In a teleconference meeting between US and Chinese negotiators on July 17, the Chinese representatives "urged the Trump administration to 'make up its mind'" about whether they want a deal, according to subsequent reporting by the South China Morning Post. A slightly more detailed sectoral breakdown of the second quarter GDP report, published the day after the headline numbers' release, shows that value added a.k.a. sectoral GDP in the construction industry grew 5.1 percent from a year earlier in the second quarter, better than during its recent trough in the second and third quarters of 2018, while growth of other industrial sectors (manufacturing is the majority) was the weakest since the first quarter of 2009. Service sector growth was the weakest since at least 1992.

CANADA: CPI inflation slowed to 2.0 percent in June from 2.4 percent in May as oil and gasoline prices fell; CPI inflation also was 2.0 percent in April. The Bank of Canada's three preferred measures of core inflation continue to hold in a tight range around the bank's 2.0 percent target: they ranged from 1.8 to 2.2 percent in June after a 1.8 to 2.3 percent range in May; unlike in the United States where the central bank is concerned that inflation is chronically below target, inflation is on target in Canada, another reason why the Bank of Canada is not expected to follow the Fed in cutting interest rates in the second half of 2019. New claims for employment insurance fell 2.5 percent from a year earlier in May, a sign of labor market strength. Retail sales fell 0.1 percent in value terms in May from April and 1.0 percent in real terms; sales at motor vehicle and parts dealers rose 0.5 percent on the month. Retail e-commerce sales rose 21.8 percent from a year earlier in May while sales at cannabis stores rose 14.8 percent from a month earlier; Canada legalized cannabis nationally for recreational use in October 2018.

UNITED KINGDOM: Hard Brexit risk receded marginally after Parliament voted July 18 to block the next government from "proroguing" the Parliament; proroguing is a procedural action that could have allowed the prime minister to make Brexit policy without Parliament's assent. The leading candidate for Prime Minister Boris Johnson has discussed proroguing Parliament as a way to force a Hard Brexit through Parliament, where a majority opposes it; Parliament voted March 13 to rule out Hard Brexit under any circumstances. A Hard Brexit, while now appearing very unlikely, is still not impossible: The prime minister could persuade Members of Parliament (MPs) to change their views on Hard Brexit; a political crisis could paralyze the government and Parliament and prevent action to stop Hard Brexit, which would occur by default without action before the October deadline; or a general election could increase the number of members of Parliament who support Hard Brexit. There is no parliamentary election scheduled until 2022, but a snap election could be called if the Prime Minister loses the support of his political coalition and no replacement can win the support of a majority of MPs. Retail sales rose 1.0 percent in June from May, better than the decline expected by consensus, and rose 3.8 percent from a year earlier, outpacing inflation; sales excluding auto fuel rose 0.9 percent on the month and 3.6 percent on the year. Home price growth decelerated to 1.2 percent from a year earlier in May from 1.4 percent in April, tying March for the weakest since January 2013.

BRAZIL: Service sector activity rose 4.8 percent from a year earlier in May, bouncing back after monthly declines in March and April; May's growth was the fastest since February 2014. Even so, Brazil's data flow continues to disappoint: The Central Bank of Brazil's weekly survey of professional forecasters showed the median estimate for real GDP growth in 2019 was 0.8 percent in the July 12th survey, down marginally from the prior week. The median estimate for real GDP growth has fallen for 20 consecutive weeks.

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