

Economic Update

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This weekly update provides a snapshot of changes in the economy and markets and their implications for investors.



Growth

The final estimate of 4Q18 U.S. real GDP growth was revised down from 2.6% to 2.2% q/q saar. Consumption, government spending and business fixed investment were all revised down slightly, but partially offset by lower imports. This week, 1Q19 GDP will be released, and there were some positive signs for U.S. and global growth last week. In the U.S., retail sales grew 1.6% m/m, and the flash manufacturing PMI held steady at 52.4. Globally, manufacturing PMIs in Japan, France, Germany and the eurozone were mostly subdued, but could experience a lift in the coming months given optimistic industrial production, retail sales and fixed asset investment data from China last week.



Jobs

Job openings fell by a substantial 538,000 in February, but this weakness is inconsistent with an otherwise strong labor market, so we will watch next month's JOLTS report to see if it could have been an anomaly. Nonfarm payroll gains rebounded to 196,000 in March, and the unemployment rate held steady at 3.8%. Wages grew by 3.3% for production and non-supervisory workers, their weakest year-over-year gain since last October, signaling slower growth in wages. Although the pace of job gains and improving employment is decelerating, jobless claims fell below 200,000 last week, indicating that the labor market is still tightening.



Profits

1Q19 earnings season continues, with 60 companies having reported (16.3% of market cap). Our current estimate for 1Q19 earnings is \$36.64, rising 0.3% y/y. So far, 83% of companies have beaten on earnings, while 33% have beaten on revenue. Financial and health care sectors are expected to experience positive earnings growth, while globally exposed sectors may struggle due to slower global growth and a stronger dollar. Meanwhile, lower y/y oil prices should weigh on energy sector profits. We anticipate low to mid single digit earnings growth for 2019 as a whole.



Inflation

Headline CPI increased by a more-than-expected 0.4% m/m in March, primarily due to rising energy prices, and rose 1.9% y/y. Core CPI remained steady, rising a modest 0.1% m/m and 2.0% y/y. Headline PCE fell to 1.4% y/y, as did core PCE to 1.8% y/y, in January, both below the Fed's 2% target. Despite a recent rebound in energy prices, we believe core inflation is unlikely to accelerate meaningfully in the months ahead.



Rates

The Federal Reserve maintained its target range for the federal funds rate at 2.25%-2.50% at its March meeting. It provided clarity on balance sheet normalization, first slowing the pace of asset reduction, and then concluding reduction by end of September, aiming to hold mostly Treasuries. Its economic projections showed real GDP growth slowing and inflation at or below its 2% target, yet Chairman Powell was positive about the health of the U.S. economy. Still, the FOMC indicated zero rate hikes in 2019, and one in 2020, striking a decidedly dovish tone.



Risks

- Unresolved trade tensions may exacerbate a slowdown in global growth.
- Corporate debt is rising, and declining in quality.
- Federal debt poses a long-term risk.



Investment Themes

- Risk assets have reasonable valuations and may have room to run heading toward the end of this cycle.
- Credit and short duration tend to perform well late cycle, while core bonds protect heading into a downturn.
- Long-term growth prospects and cheap absolute and relative valuations support international equities.

■ Denotes updated information

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MARKET INSIGHTS

Data are as of April 22, 2019

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