Source: International Monetary Fund, Bloomberg as of April 9, 2019

Chart of the Week: The International Monetary Fund (IMF) lowered its forecast for 2019 global GDP growth for the third time in six months to 3.3%, which would be the slowest growth since 2009 (see chart). The IMF projects that GDP growth will rebound to 3.6% in 2020. Interestingly, the data and markets were telling a different story about 2019 growth last week which could indicate that the IMF moved too quickly with their latest downgrade. Adding to the jump in Chinese PMI data received previously, there was further evidence last week that the Chinese stimulus is having a positive impact. Exports from China increased to 14.2% year-over-year (Y/Y) in March from -20.8%. In addition, loans more than quadrupled in March with aggregate financing at 2.86 trillion yuan. Back in the U.S., initial jobless claims fell to 196,000, which is a 49-year low. Though it is still early in the 1Q earnings season, the earnings and loan growth so far from the large U.S. banks were generally better than expected. Better expectations for economic growth were also reflected in the financial markets with the U.S.10-year Treasury yields rising 7 basis points to almost 2.57% and inflation expectations firmed. The futures markets priced in less of a probability of a rate cut from the Federal Reserve last week as well. Avalon expects no monetary policy rate changes from the Federal Reserve in 2019 and sees very little threat of recession in the U.S. over the next twelve months.

WEEK IN PREVIEW

- Geopolitical: Markets continue to monitor the progress of the trade negotiations between the U.S. and China closely. There is a shortened trading week in the U.S. and other parts of the world with markets closed on Good Friday.
- U.S.: March retail sales provide another reading on the consumer. The retail sales data has seemed very questionable since the government shutdown, but consensus expects significant improvement in March. April PMI data provides another look at the current state of the economy with the manufacturing component expected to improve slightly to 52.8 from 52.4, above the growth or contraction line of 50. 1Q GDP estimates from the Atlanta and NY Fed stand at 2.27% and 1.40%, respectively. Fedspeak on the calendar with the release of the Beige Book on Wednesday and six scheduled speeches continue the flow of monetary policy information.
- 1Q S&P 500 Earnings: Only 6% of companies have reported but 83% and 59% have beaten earnings and sales expectations, respectively. Earnings are expected to decline -4.3% Y/Y versus -4.5% last week, while sales expectations improved to 4.8% from 4.6%. The improvements were driven by the financials with JPM and WFC beating consensus earnings estimates. Forty-nine S&P 500 companies report with another heavy dose of financials including C, BAC, BLK, GS, MS, AXP, JNJ, NFLX, IBM and PEP.
- Europe: April Eurozone PMI readings are expected to improve but the manufacturing component is still likely to remain below 50. The German ZEW survey should show some improvement in expectations. The Brexit deadline was extended to October 31 but the path to an agreement remains unclear. The U.K. reports February unemployment along with March CPI and retail sales.
- Asia: Japan reports March CPI along with trade data. China has March industrial production and retail sales along with 1Q GDP forecast at 6.3% Y/Y.
- Central Banks: The central banks of Kazakhstan and South Korea meet with no expected changes to monetary policy rates.

WEEK IN REVIEW

- The S&P 500 posted its third straight week of improvement with a gain of over 0.5%. Continued signs of better global growth and a good start to 1Q earnings helped boost stocks. Financials, communications services and technology were leading sectors while healthcare was the big laggard. WTI and Brent oil prices were higher with energy stocks lower on the week with Chevron purchasing Anadarko Petroleum and MLPs rising fractionally. Small cap stocks underperformed with the Russell 2000 up 0.14%. The U.S. 10-year Treasury yield rose to almost 2.57% and high yield credit spreads reflecting increased risk tolerance by narrowing.
- Developed international stock indexes underperformed the S&P 500 in U.S. dollar terms. On a hedged-currency basis, developed market stocks were down -0.15%. The U.S. dollar was weaker against developed and emerging market currencies. The non-hedged stock returns were 0.22% for MSCI EAFE and 0.36% for MSCI Emerging Markets.
- The 10-2 yield curve widened and ended at almost 17 basis points. Another curve measure of three-month yield six quarters forward – three-month yield continues to be inverted at -5 basis points. The yield curve has historically provided an accurate forecast of future recessions when the difference in these measures turns negative, also known as inversion. Yield curves are one of the major indicators that we monitor to judge recession risk, but these inversions typically happen a year or more in advance of an economic recession. In addition, stocks have historically had significant advances post-inversion. The three-month yield six quarters forward yield is now reflecting that the market expects little net change in short-term rates over the next year and a half. Much of the decline in the forward-looking three-month yield came in response to the weak European economic data and it has been retracing much of the decline as better U.S. and Chinese data are reported. Our view remains that the odds of a recession in 2019 remain low and Avalon expects no rate hikes from the Federal Reserve in 2019. Avalon continues to monitor the data closely. Please see our **Avalon Perspectives** publication, *The Yield Curve and Equity Returns*, from April 26, 2018, for more details.

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DISCLOSURES