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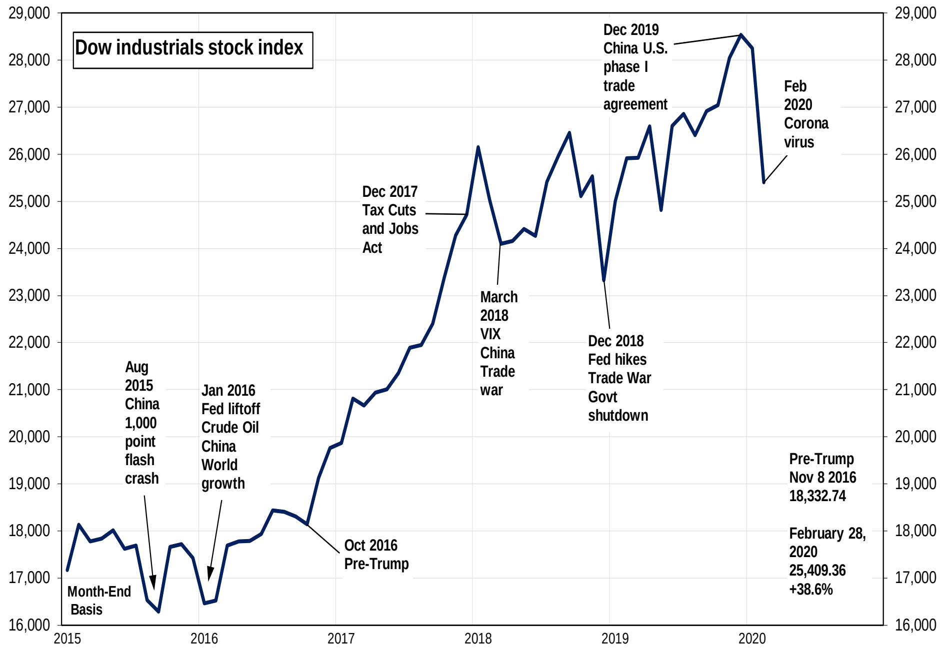
28 FEBRUARY 2020

AMERICA'S TRADE DEFICIT RED INK ISN'T JUST CHINA



This wasn't meant to be a commentary about the stock market, but how can it not be? The S&P 500 has fallen 15.2% from record levels earlier this year. While the world waits to see how quickly China's factories can get up and going again, we will take a look at the annual figures for U.S.-China trade as seen from the U.S. side. We haven't heard much about the phase II U.S.-China trade talks lately and this seems to be off the radar of market concerns for now. There's still something left in the tank of the 38.6% Trump stock market rally since election night November 8, 2016, but stocks have not gone anywhere the last two years since the Tax Cuts and Jobs Act increased profits with the biggest corporate tax cut in history.

Trade War 2019			
Trade deficit in goods			
$ billions		Exports	Imports
China	345.6	106.6	452.2
EU	177.8	337.0	514.8
Germany	67.1	60.2	127.4
Mexico	101.7	256.3	358.1
Japan	68.9	74.6	143.6
Vietnam	55.7	10.8	66.6
South Korea	20.6	56.8	77.5
Canada	27.0	292.6	319.7
World	852.9	1,645.5	2,498.4

The U.S. wasn't winning the trade war with China yet last year. Imports may have been lower, but U.S. exports to China fell to $106.6 billion from $120.1 billion in 2018 after China put tariffs on many U.S. goods in the middle of 2018. Soybeans recovered to $8.0 billion in 2019 from $3.1 billion in 2018. The peak was $14.2 billion in 2016. Aircraft and parts was $10.5 billion in 2019 down from $18.2 billion in 2018. The phase I

U.S.-China trade agreement fact sheet put out in January has "enhanced trade" as just one of the various aspects of the agreement and it's well down the list. It says goods and services purchases from China will exceed the 2017 level by no less than $200 billion. U.S. goods exports to China were $129.8 billion in 2017, so the goal seems quite ambitious.

Imports dropped to $452.2 billion in 2019 from $539.7 billion in 2018 due to the tariffs. This isn't helping consumers or businesses that need supply-chain imputs to manufacturing, and it isn't clear how many factories will come back to the USA. TV and video equipment fell to $9.5 billion from $11.7 billion, but the U.S. is unlikely to build TVs here ever again. A similar story for household appliances and furniture.

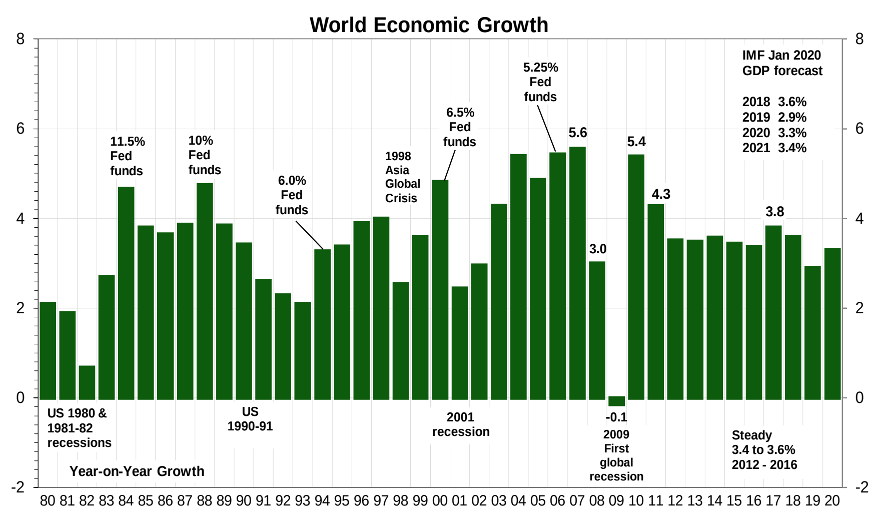
U.S. Exports of goods to China

Billions of dollars	2019	2018	2017	2016	2015
Civilian aircraft, engines, equip, parts	10.459	18.221	16.264	14.577	15.440
Semiconductors	9.114	7.117	6.077	5.956	5.976
Soybeans	7.992	3.129	12.231	14.212	10.494
Passenger cars, new and used	7.232	6.638	10.208	8.843	9.056
Industrial machines, other	6.286	6.822	5.448	4.875	4.483
Pharmaceutical preparations	4.357	3.024	2.681	2.166	2.005
Medicinal equipment	4.144	3.727	3.453	3.231	2.887
Plastic materials	3.343	3.981	4.004	3.525	3.559
Chemicals-other	3.045	3.197	2.982	2.468	2.415
Crude oil	2.901	5.431	4.379	0.361	0.015
Measuring, testing, control instruments	2.798	3.128	2.765	2.649	2.639
Pulpwood and woodpulp	2.315	2.920	3.359	3.368	3.425
Electric apparatus	2.224	2.422	2.317	2.108	2.117
Other industrial supplies	2.054	2.171	2.111	1.839	1.855
Chemicals-organic	1.989	2.470	2.294	2.144	2.239
Other parts and accessories of vehicles	1.941	2.864	2.720	2.332	1.868
sub-total	72.194	77.262	83.293	74.654	70.473
Total	106.626	120.148	129.797	115.594	115.873

U.S. Imports of goods from China

Billions of dollars	2019	2018	2017	2016	2015
Cell phones and other household goods	64.552	71.872	70.340	61.465	64.538
Computers	42.380	47.179	45.401	40.408	43.805
Toys, games, and sporting goods	26.513	28.223	26.727	25.044	26.355
Apparel, textiles, nonwool or cotton	24.453	25.140	24.114	24.143	25.645
Telecommunications equipment	24.443	33.883	33.441	29.037	27.085
Computer accessories	18.709	32.501	31.650	28.252	30.456
Furniture, household goods, etc.	16.920	22.694	20.669	18.645	17.894
Household appliances	14.069	16.047	14.147	13.716	14.218
Other parts and accessories of vehicles	13.013	16.383	14.387	14.232	14.868
Electric apparatus	12.949	16.089	14.171	13.132	13.627
Footwear	10.958	11.429	11.536	12.005	14.182
Apparel, household goods - cotton	10.251	12.405	12.272	12.705	14.410
Industrial machines, other	10.194	11.819	10.590	8.881	9.075
Photo, service industry machinery	9.512	10.697	9.546	8.587	8.356
Televisions and video equipment	9.495	11.702	10.619	9.259	10.654
sub-total	308.411	368.063	349.610	319.511	335.168
Total	452.243	539.675	505.220	462.419	483.201

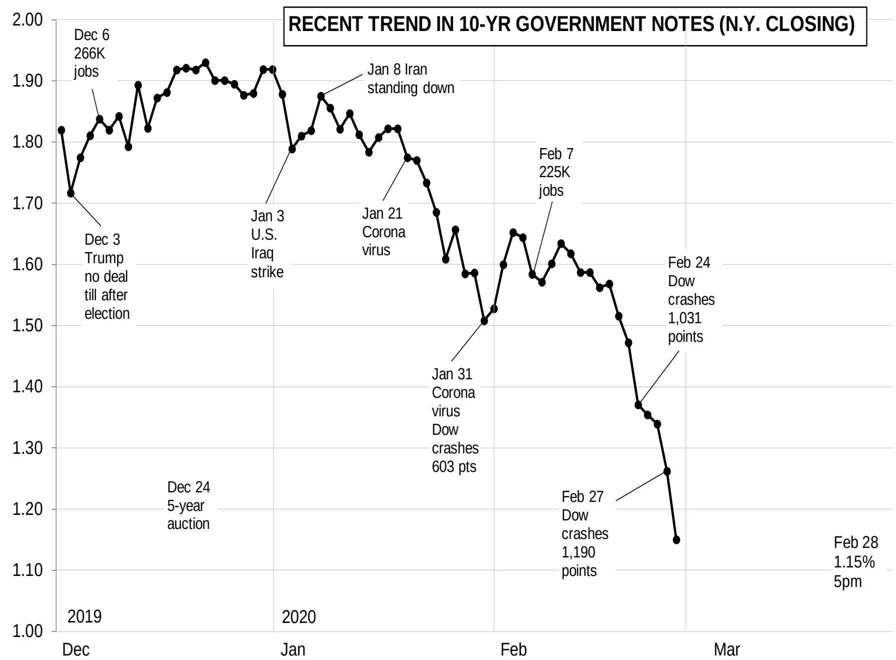
To conclude, China is not just an important trading partner of the U.S., worries over the outlook for its economy have figured importantly in many of the stock market sell-offs looking back to 2015. Even Federal Reserve officials point to the risks from China from time to time. Disruptions to China's economy have the potential to slow world growth dramatically this year. The IMF said in their January update that world economic growth would rebound to 3.3% in 2020 from 2.9% in 2019. The only global recession recorded was in 2009 when the U.S. let Lehman go bankrupt. A back-of-the-envelope analysis would find China had roughly a 15% share of world GDP in 2019. If growth in China slows from 6% to 3% for the full year 2020, then world economic growth would slow to 2.8% from the 3.3% forecast.



MARKETS OUTLOOK

	29-Mar 2019	28-Jun 2019	30-Sep 2019	31-Dec 2019	Q1 2020	Q2 2020	[illegible]	Q4 2020	Q1 2021	Q2 2021
30-Yr Treasury	2.81	2.53	2.11	2.39	[illegible]	[illegible]	[illegible]	2.50	2.60	2.70
10-Yr Note	2.41	2.01	1.67	[illegible]	[illegible]	[illegible]	2.10	2.20	2.30	2.40
5-Yr Note	2.23	1.77	[illegible]	[illegible]	[illegible]	1.75	1.90	2.05	2.15	2.25
2-Yr Note	2.26	[illegible]	[illegible]	[illegible]	1.60	1.70	1.80	2.00	2.10	2.20
3-month Libor	2.60	[illegible]	[illegible]	1.90	1.90	1.90	1.90	1.90	1.90	1.90
Fed Funds Rate	2.50	[illegible]	2.00	1.75	1.75	1.75	1.75	1.75	1.75	1.75
2s/10s spread	15	25	5	35	25	20	30	20	20	20

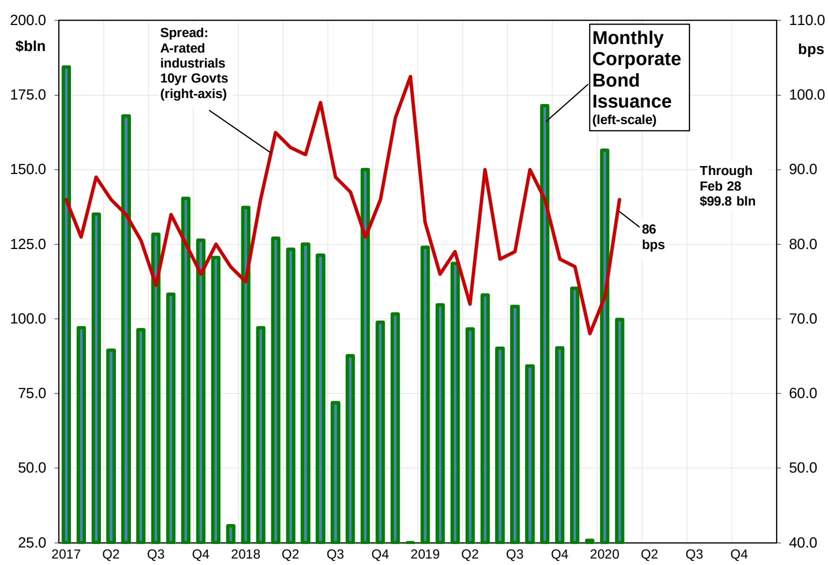
Under development



~~A quiet week with daily closes ranging from~~ 10-year Treasury yields broke the record low of 1.32% made in 2016 months before Trump won the election. Yields fell as low as 1.11% on Friday, and were already down as low as 1.14% before Powell's "We're Watching-It" press statement at 230pm EST. Rate forecasts are suspended. Fed rate cuts from an already-low 1.75% level won't boost corporate borrowing or engender new investment in the future. The housing market could see a boost or homeowners might refinance. Mortgage rates were 3.45% this week for a wider 210 bps spread above 10-yr Treasury yields. If mortgage yields sink closer to Treasuries, a 0.75% Fed funds and 10-yr Treasury rate next year means a 2.6% mortgage.

CORPORATE BONDS: NO ISSUANCE THIS WEEK

Corporate offerings were $1.0 billion in the February 28 week versus $37.8 billion in the February 21 week. Corporate bond yields (10-yr Industrials rated A2) were 86 bps above 10-yr Treasuries Friday versus 72 bps last Friday.



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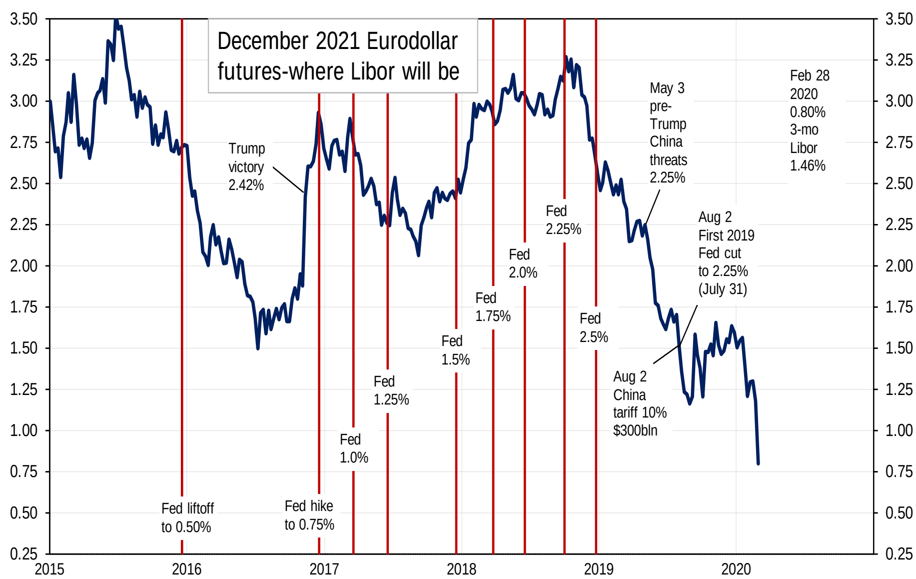
FEDERAL RESERVE POLICY

The Fed meets March 17-18, 2020 to consider its monetary policy. We expect a 25 bps rate cut to 1.5%. We hope not. But Powell's "closely monitoring" press statement says action is imminent. Coronavirus fears have led to a stampede out of the stock market. Monetary policy stimulus famously seeks to improve financial conditions, and the statement from Fed Chair Powell (what about the other FOMC members) at 230pm EST on Friday stopped the slaughter temporarily. The President surely is asking for a rate cut. Immediately.

Selected Fed assets and liabilities					Sep 10
Fed H.4.1 statistical release					2008**
billions, Wednesday data	26-Feb	19-Feb	12-Feb	5-Feb	pre-LEH
Factors adding reserves					
U.S. Treasury securities	2474.060	2451.688	2442.621	2427.880	479.782
Federal agency debt securities	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	1371.843	1385.784	1391.526	1387.289	0.000
Repurchase agreements	143.440	163.900	164.400	170.250	126.750
Primary credit (Discount Window)	0.013	0.005	0.000	0.000	23.455
Term auction credit (TAF auctions)	0.000	0.000	0.000	0.000	150.000
Asset-backed TALF	0.000	0.000	0.000	0.000	
Maiden Lane (Bear)	0.000	0.000	0.000	0.000	29.287
Maiden Lane II (AIG)	0.000	0.000	0.000	0.000	0.000
Maiden Lane III (AIG)	0.000	0.000	0.000	0.000	
Central bank liquidity swaps	0.044	0.067	0.055	0.048	62.000
Federal Reserve Assets	4206.4	4219.8	4230.9	4214.9	961.7
3-month Libor %	1.61	1.70	1.70	1.74	2.82
Factors draining reserves					
Currency in circulation	1800.040	1799.719	1796.425	1794.675	834.477
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000
Reverse repurchases w/others	2.300	5.149	0.309	4.112	0.000
Reserve Balances (Net Liquidity)	1680.070	1659.021	1695.082	1652.873	24.964
Treasuries within 15 days	34.812	31.238	52.182	53.364	14.955
Treasuries 16 to 90 days	188.784	170.808	129.306	115.176	31.549
Treasuries 91 days to 1 year	355.980	361.944	376.189	378.638	69.272
Treasuries over 1-yr to 5 years	913.398	906.588	918.350	917.955	170.807
Treasuries over 5-yrs to 10 years	325.382	325.396	319.315	319.329	91.863
Treasuries over 10-years	655.702	655.715	647.278	643.419	101.337

**September 10, 2008 is pre-Lehman bankruptcy of 9-15-08

What's the market saying? It's nothing less than a death leap for yields off the cliff. Fed funds futures look for 37 bps, or more than one rate cut, at the March 17-18 meeting. The daily effective Fed funds rate is 1.58% today and by July the market says it will be 0.87%, and by January 2020 it will be 0.63%. Wow. 100 bps of rate cuts by the December 2020 Fed meeting. We don't know what to say, so we won't.



Press Release

February 28, 2020

Statement from Federal Reserve Chair Jerome H. Powell

For release at 2:30 p.m. EST

The fundamentals of the U.S. economy remain strong. However, the coronavirus poses evolving risks to economic activity. The Federal Reserve is closely monitoring developments and their implications for the economic outlook. We will use our tools and act as appropriate to support the economy.

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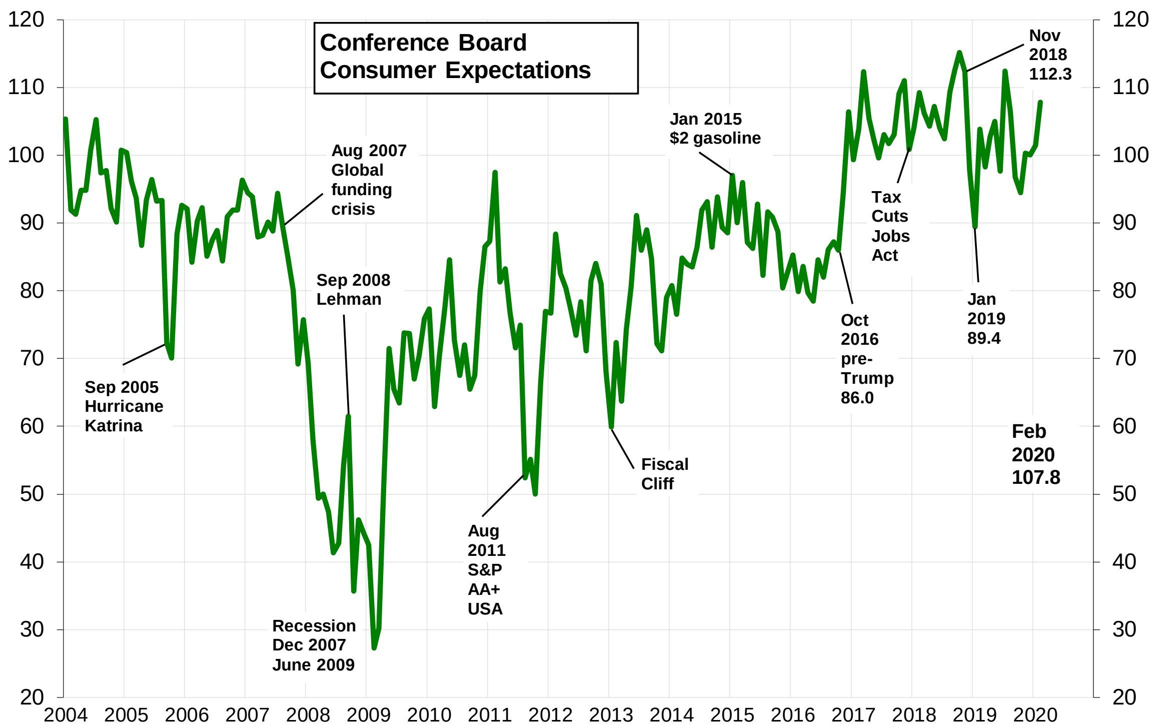
OTHER ECONOMIC NEWS THIS WEEK

Confidence down today, great expectations for the future (Tuesday)

Breaking economy news. The consumer confidence index is up, but from a lower level than a month ago which sounds like it is down to us. The confidence index was revised down to 130.4 in January from the initial report of 131.6, and it rose to 130.7 in February. Expectations jumped higher from a lower revised level to 107.8 in February from 101.4 they say for January now. Meanwhile, the labor market isn't quite as strong as it was a month ago with jobs not as plentiful and some signs that the right job is harder to get. We will see if this matches up with February nonfarm payroll employment due out in a report on Friday, March 6.

Net, net, consumer confidence is down a little from where we thought it was at the start of the year despite the best economy with the lowest unemployment in a generation. Expectations for the future are high however. Consumers are upbeat about their prospects later this year despite the election year rhetoric saying the economy isn't working for all Americans. Despite the increasing concern over the spread of the coronavirus, on average, America is upbeat about the future with their expectations moving up sharply in February. If it holds up, this confidence consumers have about their future may help keep consumer spending on an even keel and right now the consumer is the economy with business investment down in the dumps. Stay tuned. Story developing. 12 o'clock and all is well for now. We will see if consumers have a change of heart after yesterday's spectacular 1,000 point fall in the Dow industrials.

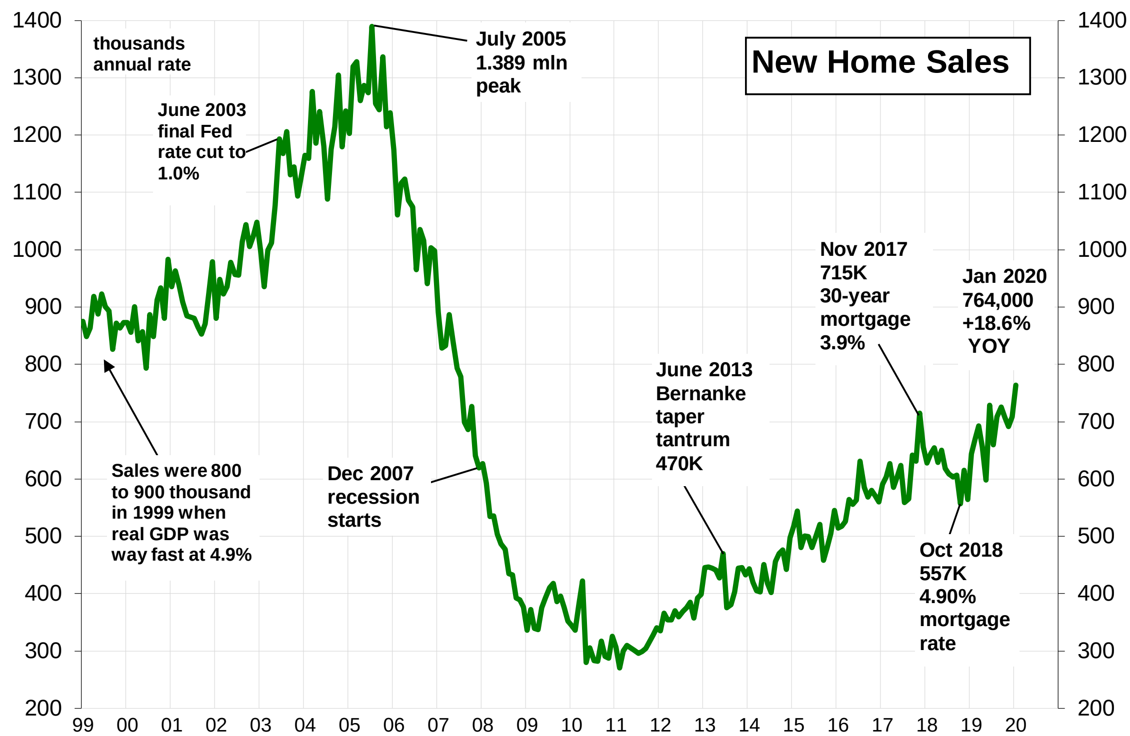


New home sales soar on warmer January temps (Wednesday)

Breaking economy news. New home sales rose 7.9% in January to 764 thousand at an annual rate which sets a new record level for homebuying activity since the mid-2000s housing bubble bust. There's still a long way to go on the road to full recovery as the peak in July 2005 for the housing bubble was 1.389 million. Blame the weather with new home sales up 30.3% this month in the Midwest although sales were also strong out West with a 23.5% jump after falling for some idiosyncratic reason in December.

There's a lesson somewhere here for Fed officials who may be contemplating some additional coronavirus rate cuts to bolster the economy. You can only go to the well so many times as they say before the water runs dry. The reversal of the gradual path of rate hikes originally foreseen by Fed policymakers for 2019 has already brought new home sales back from the depths. Mortgage rates were climbing with the Fed pushing interest rates to 2.5% in December 2018. Ahead of this new home sales reached an important low point at 557 thousand in October 2018 when mortgage rates were 4.90%. New home sales have since rebounded 37.2% to 764 thousand today so sales may have gotten most of the boost they are going to see from cheaper financing costs for new homes for now.

Net, net, new home sales soared in January to new record levels since the housing market crash over a decade ago. Blame the global warming trend for the surge in January as warmer than seasonal temperatures boosted many areas of the economy that are ordinarily pushed down because of the freezing temperatures outside. The strength of new home sales should generate a little extra consumer expenditures on household items like appliances and furniture and the spending is sorely needed because the coronavirus is likely to weigh on GDP growth in the first quarter. Stay tuned. Story developing.



GDP growth unchanged at 2.1% and durable goods orders are up (Thursday)

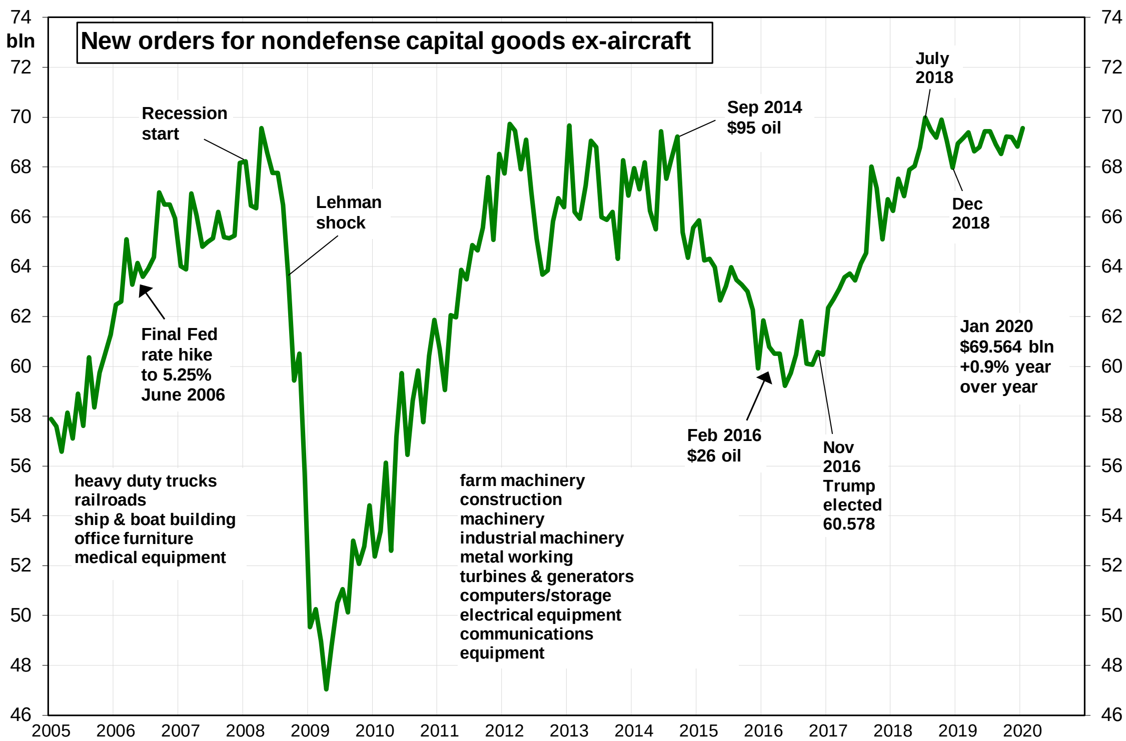
Breaking economy news. Second look at real GDP growth for the fourth quarter of 2019, and the January data on durable goods orders.

The GDP components data were little changed from the first look. Inventories were a 1.0 percentage point drag that should add to Q1 2020 growth. On the other hand, imports won't add 1.3 percentage points again in the first quarter of 2020. We look for 1.5% Q1 2020 economic growth.

Durable goods orders in January fell 0.2%. Our interest is in nondefense capital goods orders ex-aircraft which are a monthly proxy of business investment and these rose 1.1% to $69.564 billion in January. Business investment looks like it has peaked at the high levels seen previously.

	Q3 18	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19p	Q4 19r
REAL GDP	2.9	1.1	3.1	2.0	2.1	2.1	2.1
REAL CONSUMPTION	3.5	1.4	1.1	4.6	3.2	1.8	1.7
CONSUMPTION	2.3	1.0	0.8	3.0	2.1	1.2	1.2
Durables	0.3	0.1	0.0	0.9	0.6	0.2	0.2
Nondurables	0.5	0.2	0.3	0.9	0.5	0.1	0.0
Services	1.6	0.7	0.5	1.3	1.0	0.9	1.0
INVESTMENT	2.3	0.5	1.1	-1.2	-0.2	-1.1	-1.1
Business Plant	-0.1	-0.3	0.1	-0.4	-0.3	-0.3	-0.2
& Equipment and	0.2	0.4	0.0	0.1	-0.2	-0.2	-0.3
Intellectual Property	0.2	0.5	0.5	0.2	0.2	0.3	0.2
Homes	-0.2	-0.2	0.0	-0.1	0.2	0.2	0.2
Inventories	2.1	0.1	0.5	-0.9	0.0	-1.1	-1.0
EXPORTS	-0.8	0.2	0.5	-0.7	0.1	0.2	0.2
IMPORTS	-1.3	-0.5	0.2	0.0	-0.3	1.3	1.3
GOVERNMENT	0.4	-0.1	0.5	0.8	0.3	0.5	0.5
Federal defense	0.1	0.2	0.3	0.1	0.1	0.2	0.2
Fed nondefense	0.1	-0.1	-0.2	0.4	0.1	0.0	0.1
State and local	0.2	-0.1	0.4	0.3	0.1	0.2	0.2
Below line: Percentage point contributions to Q4 2019 2.1% real GDP							
Third estimate for Q4 is Thursday, March 26							

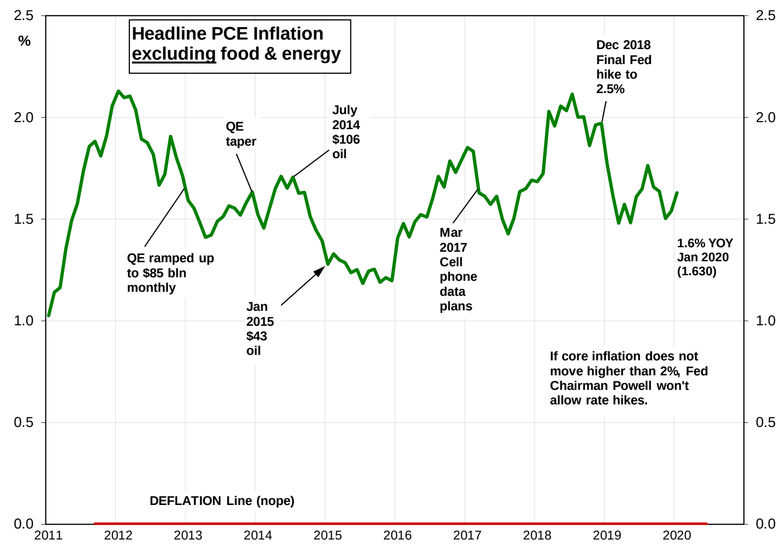
Net, net, today's economic news might as well be ancient history as far as the markets are concerned. GDP in the 4th quarter was unchanged at 2.1% and then there was news that businesses in January even went out and did a little more investment spending in equipment, but this is all ancient economic history as far as the stock markets and bond markets are concerned. Stay tuned. Story developing.



Consumer spending remains slower, PCE inflation up, but short of 2.0% Fed target (Friday)

Breaking economy news in breaking, braking markets. The monthly personal income report for January if you have any and believe us you elites out there won't have as much savings from your stock market holdings in next month's financial statements. The baby boom generation will have to keep on working longer than they thought. Personal income rose 0.6% in January from an off-month, downward revised 0.1% gain in December. We never figured out what to do with the personal income data frankly. Never did see much connection between income and spending. Personal spending in January rose 0.2% after a 0.4% rise in December, and spending would have been stronger except that consumers already started saving for a rainy day with a 7.9% savings rate in January up from 7.5% in December. They are going to need those savings in the months ahead if the financial markets don't settle back down. One thing is for certain, the swift sell-off in stocks is not going to make companies plow more money into new investments.

There was a little more inflation with PCE inflation rising 1.7% year-to-year in January up from 1.5% year-to-year in December. Fed officials are unlikely to be fooled however as most of the inflation rise is due to energy prices and that's not going to last with the coronavirus hit to crude oil prices in February likely to keep consumer inflation short of the Fed's 2% target. Core inflation is slightly lower at 1.6% year-to-year in January and wasn't going anywhere while the economy was stronger so it won't be heating up further as the coronavirus slows economies around the globe from which the U.S. will not be immune.



Net, net, the economy was already slowing in January before the stock market storm and panic selling hit America as consumers spent just 0.1% in real terms for the month. Right now, real consumer spending is rising just 1.0% in the first quarter with February and March data left to go. Real consumer spending was already slow in the fourth quarter at just 1.7% which backed up the quarter's 2.1% real GDP growth. At this point the Trump economics team would love to see 2% economic growth but they are unlikely to get it unless the stock market can stabilize before the shock hits the consumer hard and they decide to spend less as they become more cautious about the economic outlook. The problem with stock market corrections is that they start for one reason like the coronavirus and then find new reasons to keep the selling coming and driving share prices even lower.

Stay tuned. Story developing. The best economy in fifty years is looking like it has peaked and the financial market storm is exactly what we see before the economy enters a recession and frankly it will be a miracle if the U.S. can somehow miss going into a recession before the November presidential elections. All eyes are on Trump administration officials to see if they can somehow coordinate a response with the Federal Reserve and instill confidence in consumers and businesses and markets in the days and weeks ahead. The 2020 economic outlook hinges on whether Washington can find a fix for this financial markets turbulence that threatens the best economy in fifty years. Bet on it.

Analyst Certification

The views expressed in this report accurately reflect the personal views of **Christopher S. Rupkey**, the primary analyst responsible for this report, about the subject securities or issuers referred to herein, and no part of such analyst's compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed herein.

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