# Financial Market Weekly

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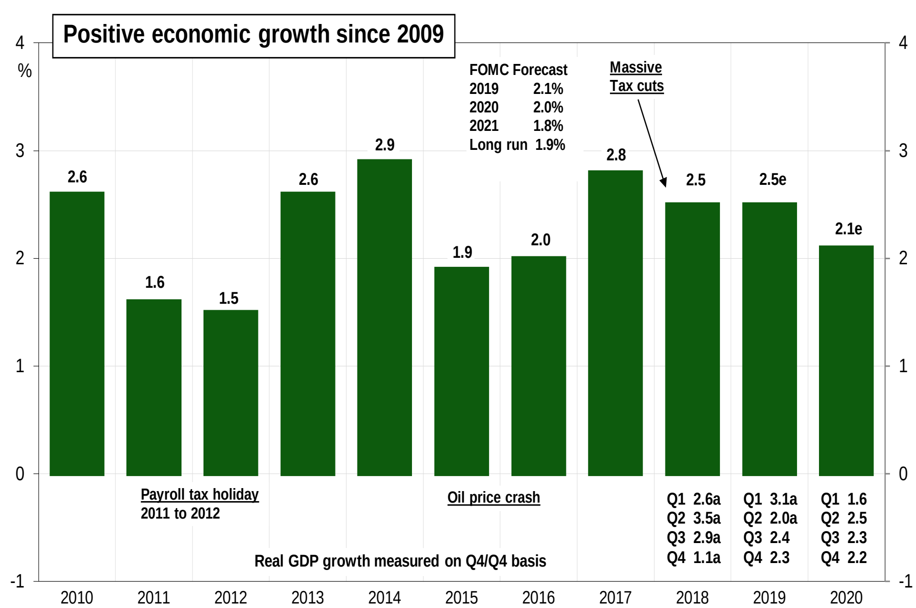
30 AUGUST 2019

## GDP GROWS 2.0% WITH BUSINESS INVESTMENT CONTRIBUTING ZERO




Glass half-empty thinking for Fed officials with real GDP growth still positive at 2.0% in the second look at the second quarter data on Thursday. Business investment has stopped adding to real GDP in the second quarter and this is one of the reasons for the Fed rate cut. At Chair Powell's press conference on July 31, "our business contacts tell us that the ongoing uncertainty is making some companies more cautious about their capital spending." Business investment in structures fell 9.4% at a seasonally adjusted annual rate (SAAR) subtracting 0.3 percentage points from 2.0% GDP growth. Equipment rose 0.7% SAAR adding less than one-tenth percentage point and Intellectual property products (software, R&D) rose 3.7% adding 0.17 percentage points to GDP growth in the second quarter.

| | Q1 18 | Q2 18 | Q3 18 | Q4 18 | Q1 19 | Q2 19p | Q2 19r |
|---|---|---|---|---|---|---|---|
| REAL GDP | 2.5 | 3.5 | 2.9 | 1.1 | 3.1 | 2.1 | 2.0 |
| REAL CONSUMPTION | 1.7 | 4.0 | 3.5 | 1.4 | 1.1 | 4.3 | 4.7 |
| CONSUMPTION | 1.2 | 2.7 | 2.3 | 1.0 | 0.8 | 2.9 | 3.1 |
| Durables | 0.2 | 0.6 | 0.3 | 0.1 | 0.0 | 0.9 | 0.9 |
| Nondurables | 0.1 | 0.6 | 0.5 | 0.2 | 0.3 | 0.8 | 0.9 |
| Services | 0.9 | 1.6 | 1.6 | 0.7 | 0.5 | 1.2 | 1.3 |
| INVESTMENT | 1.1 | -0.3 | 2.3 | 0.5 | 1.1 | -1.0 | -1.1 |
| Business Plant | 0.4 | 0.3 | -0.1 | -0.3 | 0.1 | -0.3 | -0.3 |
| & Equipment and | 0.4 | 0.2 | 0.2 | 0.4 | 0.0 | 0.0 | 0.0 |
| Intellectual Property | 0.4 | 0.5 | 0.2 | 0.5 | 0.5 | 0.2 | 0.2 |
| Homes | -0.2 | -0.2 | -0.2 | -0.2 | 0.0 | -0.1 | -0.1 |
| Inventories | 0.1 | -1.2 | 2.1 | 0.1 | 0.5 | -0.9 | -0.9 |
| EXPORTS | 0.1 | 0.7 | -0.8 | 0.2 | 0.5 | -0.6 | -0.7 |
| IMPORTS | -0.1 | 0.0 | -1.3 | -0.5 | 0.2 | 0.0 | 0.0 |
| GOVERNMENT | 0.3 | 0.4 | 0.4 | -0.1 | 0.5 | 0.9 | 0.8 |
| Federal defense | 0.0 | 0.3 | 0.1 | 0.2 | 0.3 | 0.1 | 0.1 |
| Fed nondefense | 0.2 | 0.0 | 0.1 | -0.1 | -0.2 | 0.4 | 0.4 |
| State and local | 0.2 | 0.2 | 0.2 | -0.1 | 0.4 | 0.4 | 0.3 |

Below line: Percentage point contributions to Q2 2019 2.0% real GDP
Second estimate for Q2 is Thursday, September 26

Business investment was zero in the second quarter due to the drag from structures (how many new offices, warehouses, factories does the economy need after a ten-year expansion?), offset by more software and R&D spending, and business equipment spending is approaching record levels and probably won't be growing further this cycle (see durable goods writeup on Monday this week). If the Fed is worried, then we must all be worried, so we will continue to monitor business investment spending for signs of a precipitous decline, and we will also monitor manufacturing sentiment, which is down in the dumps, with the release of the August ISM purchasing managers' report on Tuesday, September 3 at 10am.

Real business investment on equipment was solid in 2018, increasing 6.7%, where annual data gives a better breakdown of the spending. Investment on computers and for communications equipment and medical equipment was nearly half of the increase. Swing factors in down years which can depend on economies as far away as Brazil are construction equipment and farm equipment. There may be uncertainty, but long-lived durable goods equipment purchases are near record levels.

**How much business investment in equipment?**

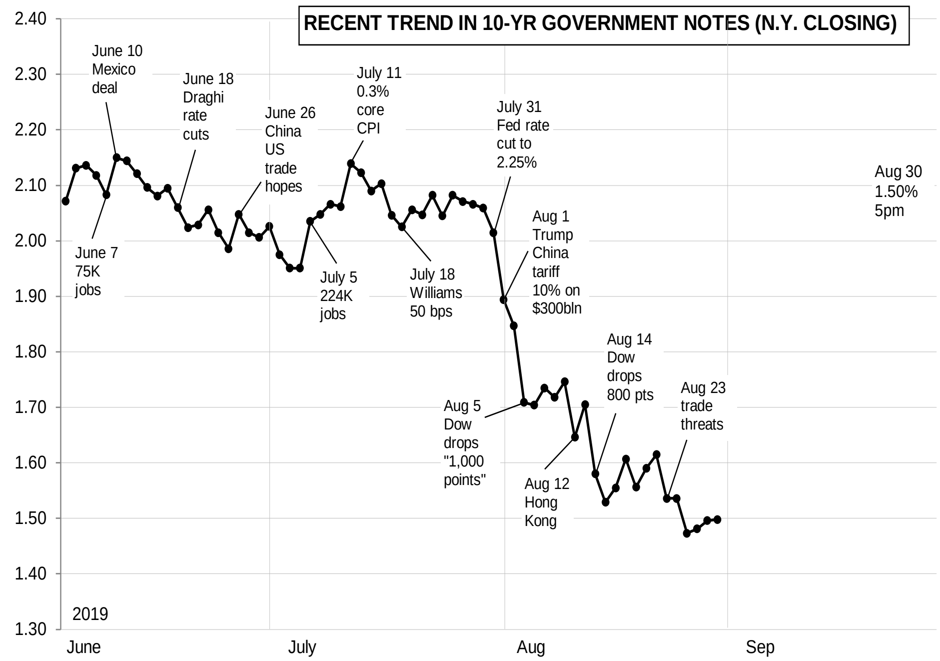
| | Percent | | |
|---|---|---|---|
| | 2018 | 2017 | 2016 |
| **Real Fixed Investment in Equipment** | 6.7 | 4.8 | -1.2 |
| Percentage Point Contributions | | | |
| Information processing equipment | 3.01 | 3.13 | 1.63 |
| Computers, peripheral equipment | 0.93 | 0.79 | -0.04 |
| Communications equipment | 0.92 | 1.49 | 1.27 |
| Medical equipment, instruments | 0.81 | 0.68 | 0.33 |
| Nonmedical instruments | 0.33 | 0.12 | 0.00 |
| Photocopy, related equipment | 0.02 | 0.03 | 0.09 |
| Office and accounting equipment | 0.02 | 0.02 | -0.02 |
| Industrial equipment | 0.92 | 1.24 | -0.22 |
| Fabricated metal products | 0.11 | 0.07 | -0.13 |
| Engines and turbines | -0.03 | 0.15 | -0.08 |
| Metalworking machinery | 0.13 | 0.20 | -0.16 |
| Special industry machinery | 0.05 | 0.25 | 0.04 |
| General equip. (materials handling) | 0.36 | 0.40 | -0.03 |
| Electrical transmission/distribution | 0.29 | 0.15 | 0.13 |
| Transportation equipment | 1.56 | -1.32 | -1.51 |
| Trucks, buses, truck trailers | 2.57 | -0.26 | 0.46 |
| Autos | -1.04 | -1.40 | -0.91 |
| Aircraft | 0.16 | 0.40 | -0.42 |
| Ships and boats | -0.08 | 0.03 | -0.17 |
| Railroad equipment | -0.04 | -0.09 | -0.47 |
| Other equipment | 1.34 | 1.63 | -1.23 |
| Furniture and fixtures | 0.08 | 0.24 | 0.14 |
| Agricultural machinery | 0.47 | 0.20 | -0.68 |
| Construction machinery | 0.45 | 0.39 | -0.07 |
| Mining, oilfield machinery | -0.10 | 0.47 | -0.62 |
| Service industry machinery | 0.11 | 0.28 | 0.11 |
| Electrical equipment | 0.05 | 0.05 | -0.01 |
| Other | 0.28 | 0.00 | -0.09 |

Uncertainty sparked by the trade war with China darkens the economic outlook Fed officials believe. It is quite a slow-moving storm as the tariffs keep getting escalated step-by-step. It would brake the economy hardest, potentially slowing GDP growth from 2% down to 1% when and if the tariffs get set to full force of 30% on the $540 billion of China imports in 2018. The second-wave of about $300 billion of imported goods from China (some exclusions) goes from zero to 15% in two steps with some goods tariffs raised on September 1 and the rest on December 15. The first-wave of $250 billion goes from 25% to 30% on October 1. The Trump administration hasn't said if that $300 billion is going from 15 to 30 percent yet. Smart. Keep that threat in reserve as a negotiating ploy. Keep in mind that imports from China are already slowing about 12% from the existing tariffs in the first six months of 2019 which, if the trend continues, would bring the 2018 $540 billion down to $475 billion in 2019.

| $BLN Nominal GDP expenditures | Q4 15 | YOY% | Q4 16 | YOY% | Q4 17 | YOY% | Q1 18 | Q2 18 | Q3 18 | Q4 18 | YOY% | Q1 19 | Q2 19 | SAAR |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Equipment & Intellectual Property | 1893.6 | 1.9 | 1917.5 | 1.3 | 2054.5 | 7.1 | 2101.4 | 2142.0 | 2166.0 | 2205.5 | 7.3 | 2236.9 | 2256.3 | 4.7 |
| EQUIPMENT | 1116.3 | 0.8 | 1088.9 | -2.5 | 1183.6 | 8.7 | 1201.8 | 1214.3 | 1227.9 | 1246.4 | 5.3 | 1249.0 | 1252.4 | 1.0 |
| Information processing equipment | 356.3 | 2.0 | 358.1 | 0.5 | 396.7 | 10.8 | 404.4 | 405.8 | 414.8 | 409.5 | 3.2 | 416.0 | 419.3 | 4.8 |
| Computers | 99.4 | -4.1 | 99.7 | 0.3 | 109.7 | 10.0 | 117.2 | 120.1 | 120.2 | 117.7 | 7.3 | 119.4 | 126.4 | 15.3 |
| Other processing equipment 1 | 256.9 | 4.6 | 258.4 | 0.6 | 287.1 | 11.1 | 287.2 | 285.7 | 294.6 | 291.8 | 1.6 | 296.6 | 292.9 | 0.8 |
| Industrial equipment | 218.4 | 0.3 | 217.6 | -0.4 | 238.2 | 9.5 | 243.1 | 242.1 | 246.9 | 251.6 | 5.6 | 250.8 | 252.5 | 0.7 |
| Transportation equipment | 306.3 | 8.5 | 283.6 | -7.4 | 288.7 | 1.8 | 294.9 | 301.5 | 299.7 | 311.0 | 7.7 | 309.4 | 305.1 | -3.8 |
| Other equipment 2 | 235.3 | -8.8 | 229.6 | -2.4 | 260.0 | 13.2 | 259.3 | 265.0 | 266.5 | 274.2 | 5.5 | 272.9 | 275.5 | 1.0 |
| INTELLECTUAL PROPERTY | 777.3 | 3.4 | 828.6 | 6.6 | 870.9 | 5.1 | 899.6 | 927.7 | 938.1 | 959.1 | 10.1 | 987.9 | 1003.9 | 9.6 |
| Software | 312.3 | 3.2 | 334.2 | 7.0 | 354.3 | 6.0 | 367.9 | 377.3 | 383.8 | 391.0 | 10.4 | 404.1 | 410.8 | 10.4 |
| Research & Development (R&D) | 386.3 | 3.3 | 411.9 | 6.6 | 430.9 | 4.6 | 444.4 | 461.6 | 464.1 | 476.8 | 10.7 | 492.0 | 500.5 | 10.2 |
| Entertainment, literary, artistic | 78.7 | 4.9 | 82.5 | 4.8 | 85.8 | 4.0 | 87.2 | 88.9 | 90.2 | 91.3 | 6.4 | 91.8 | 92.6 | 2.9 |
| 1 Communication, medical, photocopy, office and accounting equipment; nonmedical instruments | | | | | | | | | | | | | | |
| 2 Furniture; agriculture, construction, mining/oilfield, and service industry machinery; electrical equipment | | | | | | | | | | | | | | |

## MARKETS OUTLOOK

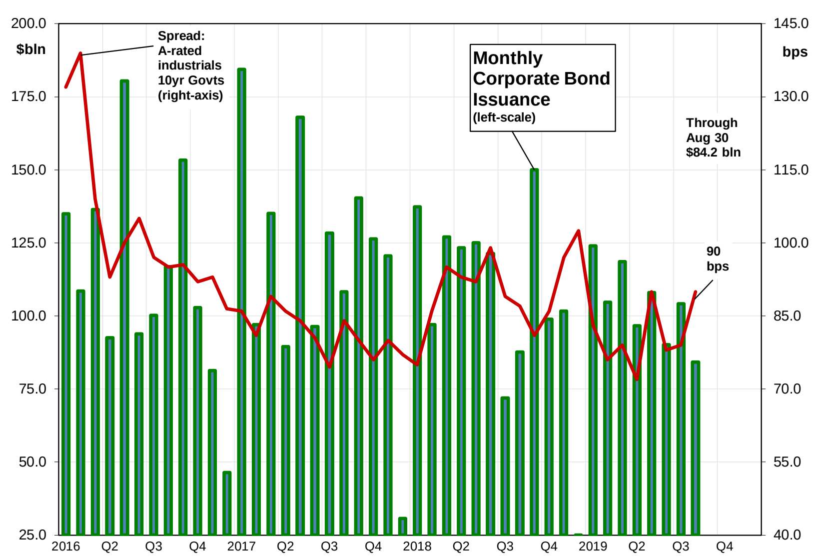
| | 29-Mar 2019 | 28-Jun 2019 | Q3 2019 | Q4 2019 | Q1 2020 | Q2 2020 | Q3 2020 | Q4 2020 |
|---|---|---|---|---|---|---|---|---|
| 30-Yr Treasury | 2.81 | 2.53 | 2.25 | 2.30 | 2.40 | 2.50 | 2.50 | 2.70 |
| 10-Yr Note | 2.41 | 2.01 | 1.75 | 1.80 | 2.00 | 2.10 | 2.20 | 2.40 |
| 5-Yr Note | 2.23 | 1.77 | 1.50 | 1.55 | 1.80 | 1.90 | 2.00 | 2.20 |
| 2-Yr Note | 2.26 | 1.76 | 1.50 | 1.60 | 1.70 | 1.80 | 2.00 | 2.20 |
| 3-month Libor | 2.60 | 2.32 | 2.00 | 2.00 | 2.00 | 2.00 | 2.00 | 2.00 |
| Fed Funds Rate | 2.50 | 2.50 | 2.00 | 2.00 | 2.00 | 2.00 | 2.00 | 2.00 |
| 2s/10s spread | 15 | 25 | 25 | 20 | 30 | 30 | 20 | 20 |




Trade news is still the focus. Trump added another 5% on top of all the China tariffs after the market close Friday, August 23. Dow futures fell almost 500 points early on Monday before Trump said at G7 that China wants a deal. Market seemed to believe it and 10-yr yields rose to the 1.55% high of the week on Monday. Interesting that the 2-yr 10-yr yield curve inverted starting Monday for the entire week. A brief curve inversion on Wednesday, August 14 sent the Dow closing 800 points lower on this 2s10s "recession call." This week, no one mentioned it. The market remains rational as ever with 10-year yields anticipating a 1.5% Fed funds rate someday.

## CORPORATE BONDS: SHUT FOR THE SUMMER THIS WEEK EXCEPT FOR ONE

Corporate offerings were $2.0 billion in the August 30 week versus $10.0 billion in the August 23 week. On Monday, Texas Instruments priced a $750 million 2.25% 10-yr (m-w +12.5bp) at 75 bps (A1/A+). The semiconductors company will use the proceeds for general corporate purposes, initially investing the proceeds (CDs, US government securities). Corporate bond yields (10-yr Industrials rated A2) were 90 bps above 10-yr Treasuries Friday versus 88 bps last Friday.



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## FEDERAL RESERVE POLICY

| Selected Fed assets and liabilities | | | | | Sep 10 |
|---|---|---|---|---|---|
| Fed H.4.1 statistical release | | | | | 2008** |
| billions, Wednesday data | 28-Aug | 21-Aug | 14-Aug | 7-Aug | pre-LEH |
| **Factors adding reserves** | | | | | |
| U.S. Treasury securities | 2095.130 | 2088.920 | 2080.710 | 2080.704 | 479.782 |
| Federal agency debt securities | 2.347 | 2.347 | 2.347 | 2.347 | 0.000 |
| Mortgage-backed securities (MBS) | 1489.605 | 1500.670 | 1514.174 | 1511.777 | 0.000 |
| Primary credit (Discount Window) | 0.005 | 0.075 | 0.000 | 0.003 | 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 | 0.069 | 0.043 | 0.045 | 0.030 | 62.000 |
| Federal Reserve Assets | 3807.9 | 3813.0 | 3834.1 | 3829.6 | 961.7 |
| 3-month Libor % | 2.12 | 2.15 | 2.17 | 2.18 | 2.82 |
| **Factors draining reserves** | | | | | |
| Currency in circulation | 1754.962 | 1751.265 | 1749.491 | 1749.273 | 834.477 |
| Term Deposit Facility | 1.668 | 0.000 | 0.000 | 0.000 | 0.000 |
| Reverse repurchases w/others | 4.255 | 15.153 | 2.744 | 3.622 | 0.000 |
| **Reserve Balances (Net Liquidity)** | 1504.243 | 1517.820 | 1511.264 | 1551.621 | 24.964 |
| Treasuries within 15 days | 14.674 | 14.674 | 54.814 | 54.814 | 14.955 |
| Treasuries 16 to 90 days | 70.603 | 70.603 | 43.341 | 43.341 | 31.549 |
| Treasuries 91 days to 1 year | 268.484 | 268.484 | 251.235 | 251.235 | 69.272 |
| Treasuries over 1-yr to 5 years | 830.985 | 826.882 | 853.064 | 853.063 | 170.807 |
| Treasuries over 5-yrs to 10 years | 291.712 | 289.608 | 265.734 | 265.731 | 91.863 |
| Treasuries over 10-years | 618.672 | 618.670 | 612.521 | 612.519 | 101.337 |
| **September 10, 2008 is pre-Lehman bankruptcy of 9-15-08 | | | | | |

The Fed meets September 17-18 to consider its monetary policy. The Fed will debate whether to cut interest rates. One rate cut is widely assumed to take place, a 25 bps drop to 2.0% for the Fed funds rate. August is finished, and so too is the Fed's wind down of its balance sheet. The president will be happy. Crazy quantitative tightening denounced in tweets. At the July 30-31 meeting, what got lost in the news of the first rate cut in peace time in the Fed's history is that the Federal Reserve speeded up the conclusion of the balance sheet wind down. It was scheduled to end in September and they moved that forward a month to August. One month. Why you would undertake such a minor tweak is beyond us, unless you are trying to get the president off your back.

The September meeting will provide an interest rate forecast update. They will also forecast rates out to the end of 2022. Ever since Powell's July 31 press conference, the market has gotten into its head that the policy changes ahead will be a "midcycle correction." A midcycle correction is three 25 basis point rate cuts in a row, just like the Fed under Greenspan did in the 1990s. Twice in the 90s. It will be interesting to see what happens with the rates forecasts because at the moment only one rate cut is in the forecast that they last did at the June 18-19 meeting. Market expectations using Fed funds futures did not change much this week. One rate cut (28.5 bps) is discounted at the September meeting. Two and almost a half rate cuts in total (59 bps) are discounted by the December meeting. That will make three rate cuts this year. Midcycle correction here we come.

**Odds of Rate Cuts**
**Fed funds futures**
**F8-30-2019**

| | Fed meeting |
|---|---|
| 28.5 | September |
| 59.0 | December |

BPS of cuts discounted at future Fed meetings

**Eurodollar futures say many more Fed rate cuts**

**Year-ends for Interest Rates**

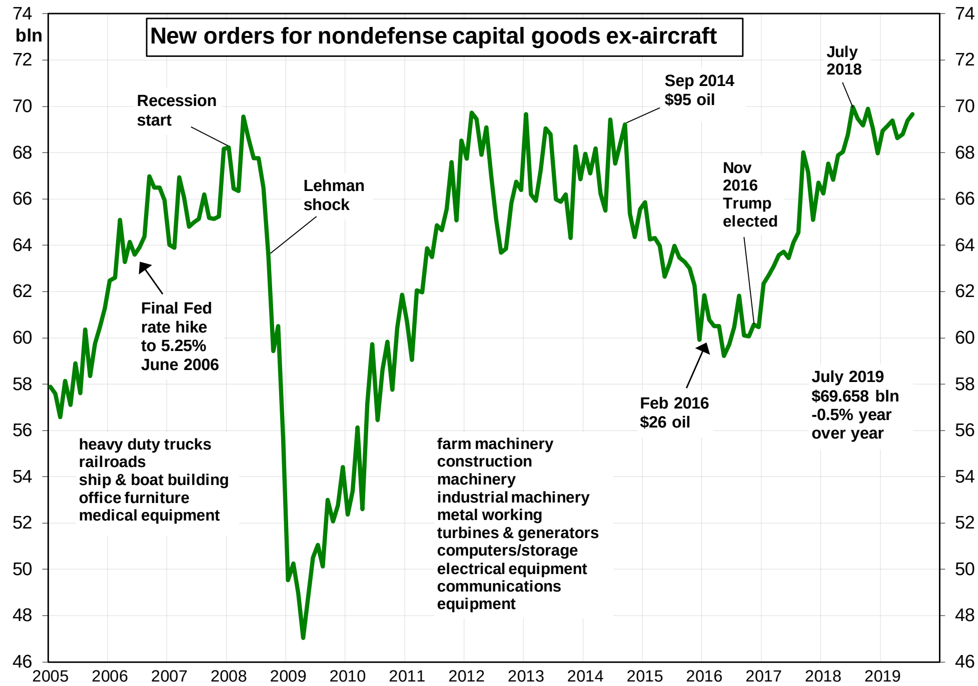
| Percent % | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|
| Eurodollar futures | 1.86 | 1.26 | 1.165 | 1.225 |
| Fed's June forecast | 2.5 | 2.25 | 2.5 | -- |

Eurodollar futures price where 3-month Libor will be in the future.
Friday, August 30, 2019 3-month Libor 2.14%

# OTHER ECONOMIC NEWS THIS WEEK

## Durable goods orders holding up in the calm before the trade storm (Monday)

Breaking economy news. Durable goods orders for July. We guess you are probably watching something else like Dow stock futures this morning. Trump giveth and taketh away. Dow futures tumbled 1.9% overnight, nearly 500 points, after Trump raised tariffs by tweet on China imports 5% across the board at 5pm Friday night. Trump then said early Monday morning at G7 in France that the trade talks with China were back on, great news for stock investors, and stock futures climbed back before the 930am New York opening. Someday soon stock market investors are going to wake up and realize they shouldn't sell stocks on these new trade sanctions announced by both sides. Wait for the trade tariffs to bring down business investment and for the economy to crater is our advice. No recession yet.

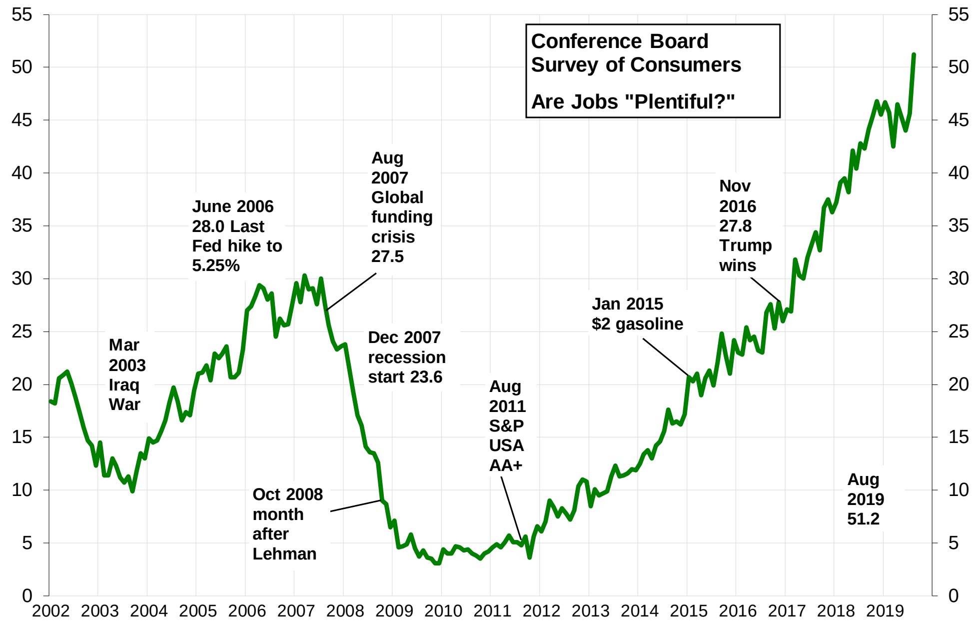



Durable goods orders rose 2.1% in July, up two months in a row, go economy go. Our proxy for business investment within the report is nondefense capital goods orders ex-aircraft which rose for a third straight month, +0.4% in July and are holding near record... high... levels. Fed officials are concerned about weak business investment, but they mistake the level of business investment with the growth in investment. Of course, growth is going to slow in business equipment purchases when the level of new orders returns to record high levels. Companies have bought most of the capital goods they need for now to produce their goods and sell their services. If equipment lasts 5 or 6 years, companies are not going to order the same record amount year after year after year.

Net, net, businesses continue to order new equipment at the highest levels in history and are ignoring the trade headwinds from the US and China economic war of words. Uncertainty is not stopping companies from buying long-lived capital equipment to meet the demand for their goods and services from other companies and consumers alike. For the moment, business leaders are not getting cold feet and retreating to the sidelines to see what happens to the economy. Sales are holding up so far and new equipment is still needed to make their businesses grow, but for how long remains the question as today's data for July comes before Trump's August 1 announcement of 10% tariffs on the rest of the some $300 billion of goods America imports from China each year. Stay tuned. Story developing. Events don't stop developing. It's starting to make our head spin. Thanks for reading. Have a nice day!

## Trade threats fail to shake consumer confidence (Tuesday)

Breaking economy news. Consumers remain upbeat with their confident outlook stoked by one of the strongest labor markets in history with over 50 percent saying jobs are plentiful. If politicians are thinking of running for president by promising voters jobs, they better think again, because consumers are saying jobs are widely available and very few are saying employment is hard to find. You have to go back nearly two decades and three presidents ago in the year 2000 to find the consumer this confident about the labor market and their ability to find work. Promise voters a chicken in every pot, but don't promise them jobs, as consumers know that the opportunities for work are the best in decades.




Net, net, the consumer remains confident despite the ongoing trade war between the US and China and this bodes well for the economic outlook in the second half of the year. The consumer had been worried at the turn of the year given the turbulent financial markets and Federal government shutdown, but this latest escalation in trade tariffs has not shaken their resolve. The consumer is two-thirds of the economy so their bubbly confidence more than compensates for the concerns registered by manufacturing executives and should be enough to keep the economy humming along at 2% economic growth. This expansion certainly looks sustainable and consumers may have even seen the Fed's rate cut on July 31 as good medicine for the economy which will help keep the economy on the sustainable growth path.

One thing is certain and that is that Fed officials have rarely seen the need to cut interest rates before with consumer confidence this high. A second rate cut in September is still widely expected, but if the economy holds its own and the trade war doesn't worsen, additional monetary stimulus in the fourth quarter may be unwarranted. Risk management rate cuts need to have some attendant risks to make sense and right now consumer confidence is steady as a rock and consumers just don't see the risks out there to their daily lives that concern Fed officials.

## Economy still running 2%, profits jump, trade picture darkens outlook (Thursday)

Breaking economy news. GDP is 2.0% in the second quarter now versus the first estimate a month ago that was 2.1%. Consumers bought more nondurable goods and spent more on services, but exports were a touch weaker and spending by state & local governments added less than the first GDP estimate a month ago.

First estimate for second quarter corporate profits showed a rebound after two negative quarters. Corporate profits jumped 5.3% in Q2 2019 and are 2.7% higher than a year earlier. After-tax corporate profits are up 5.1% in Q2 2019 and 2.7% higher than last year. Don't sell the stock market short yet please.

**ADVANCE TRADE STATISTICS FOR JULY**

| | Monthly | | | | Percent changes | | |
|---|---|---|---|---|---|---|---|
| | July | June | May | July | July 19 | June 19 | July 19 |
| Trade | 2019 | 2019 | 2019 | 2018 | June 19 | May 19 | July 18 |
| Balance | -72,340 | -74,161 | -74,802 | -73,057 | | | |
| Exports | 137,341 | 136,452 | 140,234 | 139,238 | 0.7 | -2.7 | -1.4 |
| Foods, Feeds, & Beverages | 11,752 | 12,046 | 11,971 | 12,019 | -2.4 | 0.6 | -2.2 |
| Industrial Supplies (1) | 42,686 | 44,574 | 44,371 | 46,858 | -4.2 | 0.5 | -8.9 |
| Capital Goods | 45,655 | 44,858 | 46,048 | 46,323 | 1.8 | -2.6 | -1.4 |
| Automotive Vehicles, etc. | 13,825 | 13,284 | 13,796 | 13,025 | 4.1 | -3.7 | 6.1 |
| Consumer Goods | 17,742 | 16,171 | 18,106 | 16,149 | 9.7 | -10.7 | 9.9 |
| Other Goods | 5,681 | 5,519 | 5,941 | 4,864 | 2.9 | -7.1 | 16.8 |
| Imports | 209,681 | 210,613 | 215,036 | 212,295 | -0.4 | -2.1 | -1.2 |
| Foods, Feeds, & Beverages | 12,763 | 12,699 | 12,786 | 12,420 | 0.5 | -0.7 | 2.8 |
| Industrial Supplies (1) | 43,850 | 43,139 | 46,348 | 49,082 | 1.6 | -6.9 | -10.7 |
| Capital Goods | 55,437 | 56,913 | 57,248 | 58,020 | -2.6 | -0.6 | -4.5 |
| Automotive Vehicles, etc. | 32,727 | 32,633 | 33,233 | 30,854 | 0.3 | -1.8 | 6.1 |
| Consumer Goods | 55,269 | 54,733 | 55,648 | 52,935 | 1.0 | -1.6 | 4.4 |
| Other Goods | 9,634 | 10,495 | 9,773 | 8,984 | -8.2 | 7.4 | 7.2 |

(1) Includes petroleum and petroleum products.

The advance look at the trade balance for July shows a narrowing in the deficit to $72.3 billion from $74.3 billion in June and $73.1 billion a year ago. Exports and imports are slightly off from year ago levels. Americans still continue to enjoy their imported goods but for how long? Automotive imports are 6.1% greater than a year ago, and consumer goods are running 4.4% more than last year. That will change if the Trump economics and trade teams have their way and the tariffs on all China imports make it up to 30% eventually later on this year in December when the final installment is due.

Net, net, the economy is still on cruise control and growing a steady 2.0% in the second quarter as the trade wind skies continue to darken. The 10% tariffs on $300 billion of China imports were not announced by the president until August 1.

The economy finished the final quarter of a ten year expansion at a slow but steady pace that looks sustainable if less than spectacular. Economic growth was strong enough to put the millions to work that had lost their jobs in the recession over a decade ago. There were 6.1 million unemployed in July 2019 versus 15.4 million at the peak in October 2009. For now, the economic outlook is a positive one with the economy still running ahead with 2 percent growth, corporate profits are rising, even if the trade picture is worsening and darkening the outlook with its risks. Stay tuned. Story developing.

## Not a lot of personal income, but a ton of spending for so-happy consumers (Friday)

Breaking economy news. That is if you glance away from the hurricane path projections. We are staying put at Mar-a-Lago and expecting the best Labor Day weekend ever! Bond yields ticking up a few basis points (three) at 1.53% before the 830am economic data. Bond yields still expecting a 1.5% Fed funds rate somewhere down the line. Bond yields are still below the 2-yr note yield, inverting the curve, and forecasting recession ahead. Dow stocks crashed 800 points when the curve first inverted (briefly) on Wednesday, August 14 with the president calling the heads of Wall Street firms wanting to know what was going on. It inverted starting on Monday this week and no one said a peep proving again how thoughtful the market is when it comes to analyzing the economy and Fed policy and what it means for where rates are heading.

The July personal income report. Personal income +0.1%. Personal spending 0.6% (didn't buy cars but everything else that wasn't nailed down). Real consumer spending up big at +0.4% in July starting the third quarter out with a bang. Oh, and inflation still "stubbornly low" at 1.6% year-to-year in July for core PCE inflation. The only thing stubborn about 1.6% core inflation is how stubborn some Fed officials are on thinking wrongly that low inflation is something that harms the economy.

Net, net, the economy is riding high on the backs of the consumer who is hitting the shops and malls with credit cards out and clearing the store shelves of all that retailers have got this summer. The consumer isn't worried, sitting at home watching the political debates concerned about the country's direction, they are out shopping and dipping into their savings to do it. Personal saving as a percentage of disposable personal income fell from 8.0% in June to 7.7% in July as consumers are determined to have a good summer no matter what the cost.

The Fed backed away from rate hikes and said they could be patient when the consumer and retail sales were wobbly at the turn of the year, but now consumers are spending like there is literally no tomorrow. Fed officials look like they completely misread the tea leaves on current economic conditions. This isn't an economy that requires the help of the central bank.

The consumer is spending like a rocket already and we are holding our GDP third quarter forecast at 2.4% as a result. Incredibly, consumer spending is running hot at 2.9% in the third quarter, with August and September data still to come, after that huge 4.7% jump in expenditures in the second quarter. There are no headwinds from the US-China trade war. Don't put the cart before the horse, Fed officials. Quit trying to cushion the blow before a downturn happens with a series of risk-management style rate cuts. The consumer is not uncertain. 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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