Macroeconomic Outlook

Signs of Life in Global Manufacturing


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The beleaguered manufacturing sector is showing signs of improvement.

U.S. real gross domestic product (GDP) growth held roughly steady at 2.1 percent annualized in the third quarter versus 2.0 percent in the second quarter. The data showed a moderation in government spending and personal consumption expenditure growth, which came in at 3.1 percent annualized after an unsustainably strong 4.6 percent reading in the prior quarter. However, this was largely offset by a smaller drag from inventories and net exports.

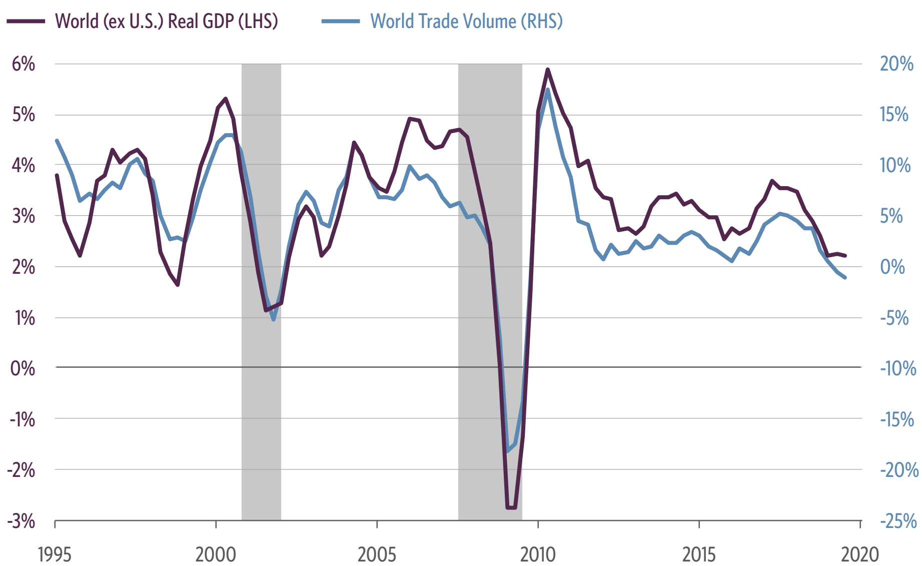
Despite the pullback in consumer spending growth, the U.S. household sector has remained a bright spot as clouds have gathered over the global economy. The manufacturing sector has borne the brunt of the escalation in U.S.-China tariffs, while also contending with headwinds in the form of U.S. dollar appreciation and weakness in foreign demand. Beyond the United States, the trade war and China's ongoing financial deleveraging have detracted from global trade volumes, which are contracting on a year-over-year basis for the first time since 2009 (see chart, top right). The global trade recession has weighed on GDP growth in economies that are particularly trade- and investment-oriented. Real GDP growth in China slowed to 6.0 percent year over year in the third quarter, the slowest pace in several decades, while German GDP grew by just 0.3 percent annualized in the third quarter after contracting by 1.0 percent in the prior quarter.

The good news is that the manufacturing sector represents only 11.0 percent of U.S. GDP and 8.4 percent of nonfarm payrolls. We see encouraging signs of an upturn in goods production, which a tentative U.S.-China trade truce should support. Meanwhile, growth in the much larger services sector has moderated, with real personal spending on services having softened over the past year. Also noteworthy to us was the decline in the employment diffusion index of the IHS Markit purchasing managers index (PMI) for services, which fell to 47.5 in October before rebounding in November and December. Global PMIs also showed a sequential improvement in labor market conditions in November (see chart, bottom right).

Fiscal policy is estimated to have boosted U.S. real GDP growth by about 0.6 percentage point in 2019. This substantial fiscal support should fade in 2020, resulting in no contribution to growth (a -0.6 percentage point shift in the growth impulse). We expect Fed policy to remain on hold in the near term, with monetary policymakers having indicated that the bar is high for further rate changes. This message has since been reinforced by the Fed's senior leadership, who have noted that "monetary policy is in a good place." The recent rally in stocks and bear steepening of the yield curve suggests that markets agree.

Global Growth Has Slowed, With Trade Volumes Now Contracting

Percent Change Y/Y

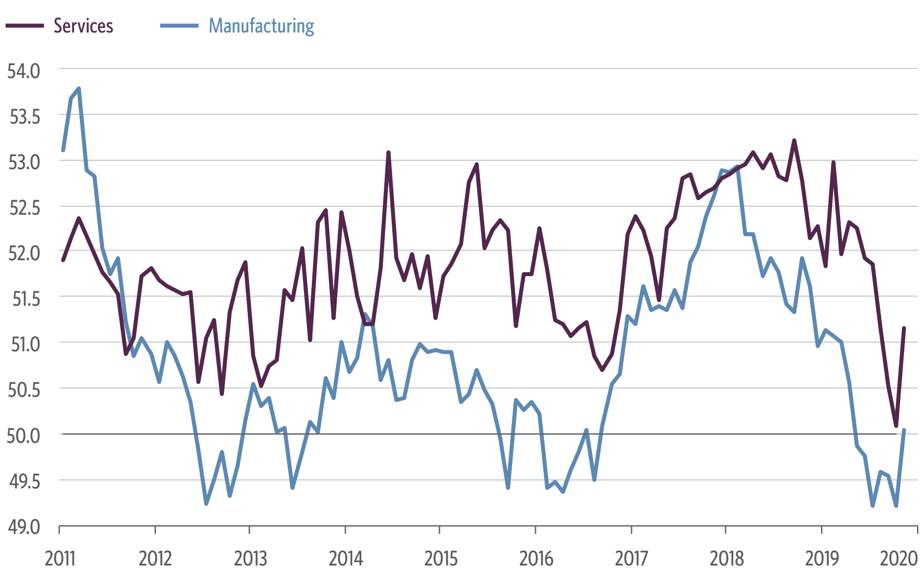


Source: Guggenheim Investments, Haver Analytics, Federal Reserve Bank of Dallas, Netherlands Bureau for Economic Policy Analysis. Trade data as of 6.30.2019; GDP data as of 9.30.2019. Shaded areas represent recession.

The U.S.-China trade war has harmed global trade volumes, which contracted on a year-over-year basis in the second quarter for the first time since 2009.

Global Labor Market Conditions Improved in November

JP Morgan Global PMIs: Employment Diffusion Indexes



Source: Guggenheim Investments, Haver Analytics, JP Morgan/IHS Markit. Data as of 11.30.2019. Note: Readings above 50 denote expansion.

Global PMIs show softening labor market conditions across services as well as manufacturing.