Actually, Winter is Leaving

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Global growth is stabilizing after a rocky ride around the turn of the year. Financial markets and a wave of recent economic indicators are singing from the same song sheet on that point—albeit long-term bonds are still chirping a tad off-key. But with North American yield curves almost normalizing, equities flirting with record highs, and even commodity prices showing some spark, **fears of a serious economic downturn have faded, at least for now**.

Recession worries were not unreasonable earlier this this year. After all, the global economy was beset by the shock waves from the U.S./China trade war, the delayed impact of Fed tightening and a flat yield curve, a five-week U.S. government shutdown, a particularly harsh winter in North America; and, of course the confidence-shredding slide in equity markets in 2018Q4. Yet, on each one of those fronts, the clouds have either parted or are parting. Equities have flared back with purpose, with the MSCI World Index up in 14 of the past 17 weeks and within 1% of recouping its Q4 declines. Fed rate hikes have come to a full stop, with QT soon to follow, the shutdown ended, and the weather is now nearly normal. And, hope springs eternal on the trade front, with rumours running rampant of a late-May/early-June summit for Presidents Trump and Xi.

With that milder backdrop, **the economic data also are turning a corner**. The first hints came from financial markets and sentiment surveys that conditions were improving, and now the hard economic data are beginning to flag that reality. This week saw a better-than-expected 6.4% y/y print for **China's Q1 GDP**; unchanged from Q4, but near the top end of this year's growth aspiration of 6.0%-to-6.5%. Industrial output and retail sales were also solid in March, each up more than 8% y/y. **Rebounding retail sales was a global theme**, as consumers emerged from deep hibernation almost everywhere. Clearly needing a serious break from Brexit, U.K. sales popped 1.1% in March and 6.7% y/y. U.S. consumers also rushed the malls last month, with a 1.6% jump in sales crushing expectations and finally reversing the nasty December plunge. While tax refunds are skimpy this year, we still expect retail activity to hold up well in coming months, as spending has been well behind labour income growth recently (nudging the savings rate above 7%). Even Canadian sales got into the act with a 0.8% gain in February (i.e., still knee-deep in winter).

No doubt, the upswing in the economic data is **far from uniform**—there have still been quite a few clunkers, including a March dip in U.S. industrial production and a February sag in Canadian manufacturing. But the economic surprise index looks to have bottomed out, with now almost an even split between upside and downside surprises in recent weeks. And, for all the recession chatter earlier this year, it now looks like U.S. Q1 GDP growth will come in close to a 2% pace (we are officially now at 1.8%), not so different from the 2.2% in Q4 and a long way from an outright downturn. Some serious support from trade has led the way, with net exports likely to account for more than half of that growth. The same can't quite be said for Canada, where we believe growth will stay locked below 1% in Q1 (officially at 0.7%) after the tiny 0.4% Q4 rise, with the oil production cuts biting hard. However, in both economies, we fully expect marked improvement in Q2 growth to 2.3%-to-2.5%, and the recent uptick in retail spending provides plenty of comfort on that call.

Speaking of clunkers, it's **not springtime for every economy**. Much of **Europe** continues to struggle, especially on the manufacturing front. Sideswiped by trade wars, hit by the first serious sag in Chinese auto sales in years, and weighed by homegrown political uncertainty, the EU economy has nearly stalled. The German government chopped their GDP growth call for this year in half to just 0.5% (even below where we were), and it looks like the EU will struggle to grow by 1% (after 1.8% in 2018). The flash April PMIs starkly showed where the issue lies, as manufacturing was a weak 47.8 (and just 44.5 in Germany), while services were just okay at 52.5. In a nutshell, while EU consumers are holding up, exporters are struggling. Taking the good—China and the U.S.—with the not-so-good—Europe—leaves the overall global growth outlook steady at 3.2% this year (versus 3.6% last year). Still, that is a far cry from the most dire predictions as 2019 began.

Financial markets led the way out of that early-year gloom initially, but they are now finding a second wind from the firming economic backdrop. Beyond the steady comeback in stocks, **long-term yields** have bounced from the lows hit just over three weeks ago. The most extreme move has been at the long end of the GoC curve, where 10s and 30s are up more than 20 bps even with a pullback late this week. This has pulled 10-year yields just back above the overnight target rate, as well as back above 3-month bills, as is the case in the Treasury market. But perhaps most tellingly, **commodity prices** have been steadily grinding higher, partly on a less-strong US$, but mostly due to the better tone for global growth. Bellwether copper hit a 10-month high this week, while oil just keeps on keeping on, with WTI now back close to last year's average level at just under $64. True, both are still down slightly from a year ago, but both have also mounted Phoenix-like recoveries from the start of the year.

On balance, growth took a mighty blow from the many challenges late last year, but managed to stay standing, with a lot of help from the Fed's abrupt policy pivot. What remains is a global economy that has transitioned from two years of above-average growth to a spell of below-average growth—but still growth. The issue now for financial markets is how long this **more subdued growth backdrop** will last; we suspect it **can grind along for a prolonged stretch**, but the slower backdrop is more **vulnerable to shocks**, either trade or geopolitical.

Full disclosure, despite the Game of Thrones reference in the title, I have never seen even a minute of the series. Value of precious/limited time and all that, you understand. Of course, besides absorbing all things economic/financial, there's still plenty of time for the Leafs (*"Still alive!... just keep Drake out of the building"*), and the odd show. On the latter, while there was an amazing mix of massive stories this past week—from the tragic (Notre Dame), to the remarkable (the Masters), to the redacted (Mueller), to the political (Alberta)—note that perhaps the best Jeopardy player ever is currently at work, including winning a record $131,000 in a single game in the latest session; that's akin to firing a 51 in 18 holes of golf. Besides being, literally, a know-it-all, James Holzhauer is also a serious gambler, who likes to bet big. Maybe he's the same guy who took Tiger at 14-1, or the Dow 5000 points ago in late December.