

Level Shift or Leveling Off?

In the World

Economic data were better than expected across several major economies, helping alleviate some concern about the global growth trajectory in 2019. In China, first-quarter growth expanded 6.4%, slightly above expectations and steady versus the previous quarter. An acceleration in industrial output and strengthening consumer demand were key drivers, in addition to stimulus measures introduced last summer by the Chinese government. In light of the better-than-expected result, Beijing officials signaled a need to balance economic support with continued deleveraging, sparking investor concern that policymakers may slow stimulus efforts. Like China, the U.S. also grew more than expected, advancing 3.2% in Q1, handily outperforming consensus expectations for 2.2% growth, despite a five-week partial government shutdown. However, the underlying drivers of growth appeared more brittle: Less sustainable factors including a build-up in inventories and slower imports were responsible for most of the increase, while slower consumption growth raised some concern (see chart). Even so, stronger retail sales, a rebound in nonfarm payrolls, and a fall in jobless claims late in the first quarter, all helped paint a better picture of the U.S. consumer. In the eurozone, GDP growth ticked up 1.2% in the first quarter, also surpassing expectations as unemployment fell to a 10-year low and Italy exited recession territory.

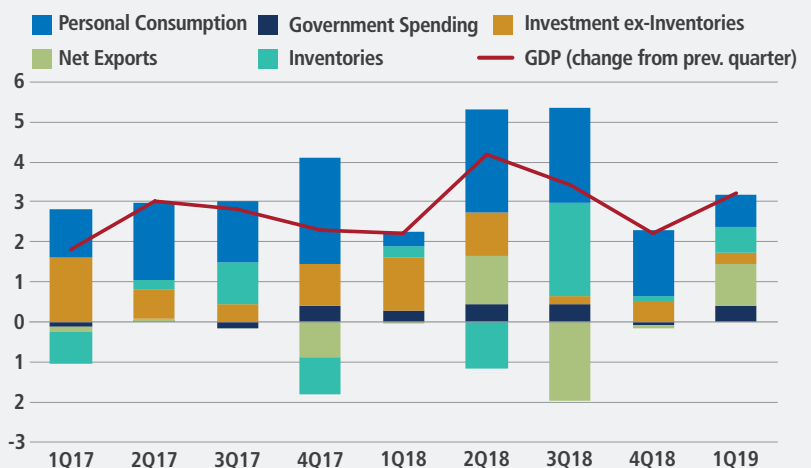
Robust risk sentiment helped several equity markets reach fresh all-time highs. Global equities surged over the month – resulting in double-digit returns for many indexes thus far in 2019 – on better-than-expected corporate earnings and economic data, continued accommodation from central banks, and progress on U.S.–China trade talks. The S&P 500 rose 4.0%, with the index constituents on pace to report a smaller-than-expected decrease in profit growth for the first quarter. Of the companies that have reported so far, 78% beat EPS (earnings per share) projections, and 57% announced sales forecasts

that exceeded expectations. The S&P 500 index, which is up over 18% so far this year, has now fully retraced the fourth quarter’s drawdown, and set a new all-time high. Credit markets also benefited from solid earnings and robust risk appetites: Spreads broadly tightened, with high yield spreads a remarkable 168 basis points (bps) tighter on the year. As risk assets rallied, bond yields across major developed economies broadly rose, and the U.S. dollar strengthened against most of these counterparts. Lastly, Brent crude oil ended the month above \$70 per barrel amid OPEC production cuts, U.S. sanctions on Venezuela’s oil industry, and concern about the upcoming expiration of Iran sanctions waivers.

Meanwhile, April featured idiosyncratic geopolitical developments with generally localized impact. Elections were in focus in April: Polls opened in India, Spain, and Ukraine, among others. Spain’s ruling Spanish Socialist Workers’ Party (PSOE) retained control and increased its seats, while the far-right Vox party entered Congress for the first time. In Ukraine, professional comic Volodymyr Zelensky handily defeated incumbent Petro Poroshenko in the second round of the presidential election, running on a strong anti-establishment and anti-corruption platform. In Turkey, tensions with the U.S. intensified as President Recep Tayyip Erdoğan remained committed to buying a missile defense system from Russia despite Turkey’s membership in NATO, which provoked the threat of sanctions from the U.S. and pressured the lira nearly 7% lower. In Argentina, continued weak economic data, increasing uncertainty ahead of the October presidential election, and weak liquidity weighed on Argentine assets; the peso continued its fall in April to mark a 15% decline so far in 2019. Finally, in the U.K., the Brexit deadline was postponed once again, this time until 31 October, making it likely the U.K. will partake in European Parliamentary elections in late May.

LOOKING UNDER THE HEADLINE

U.S. economic growth surprised to the upside in the first quarter despite a federal government shutdown and ongoing trade tensions. The initial gross domestic product (GDP) estimate registered 3.2%, far surpassing market estimates of 2.3% and the fourth quarter’s 2.2%. However, the composition of growth in the first quarter suggested the headline number may be masking some underlying weakness. A buildup of inventories and fewer imports accounted for much of the increase – both of which are volatile factors that may not be sustainable going forward. At the same time, consumer spending (the biggest part of the U.S. economy) slowed meaningfully versus the past few quarters, though was slightly above estimates. So while the headline growth rate spurred some optimism following growth concerns in the fourth quarter, its durability appeared less clear.



As of 30 April 2019. Source: Bureau of Economic Analysis (BEA).

Market snapshot

To view detailed on each asset class, visit pimco.com/monthly-market-update.

BONDS	U.S.				U.K.				EUROZONE				JAPAN				BRAZIL			
	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018
	Level	Change (bps)			Level	Change (bps)			Level	Change (bps)			Level	Change (bps)			Level	Change (bps)		
Target Rate*	2.50				0.75				-0.40				-0.10				6.50			
2 YR	2.27	+1	-22	+60	0.76	+12	+1	+31	-0.58	+2	+3	+2	-0.15	+2	-1	-1	7.37	+11	+1	-69
5 YR	2.28	+5	-23	+30	0.91	+15	+0	+18	-0.41	+4	-10	-11	-0.16	+3	-2	-4	8.58	-1	-27	-120
10 YR	2.50	+10	-18	+28	1.19	+19	-9	+9	0.01	+8	-23	-19	-0.04	+4	-4	-5				
30 YR	2.93	+11	-9	+27	1.69	+14	-13	+6	0.66	+8	-22	-39	0.57	+6	-15	-9				
5 YR ILBs	0.42	-2	-58	+71	-2.27	+19	-3	-9	1.32	+12	-15	-24					2.79	+3	-25	-85
10 YR Muni ^a	1.89	+1	-43	+31																
CURRENCIES	USD**				GBP/USD				EUR/USD				USD/JPY				USD/BRL			
	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018
	Level	Change			Level	Change			Level	Change			Level	Change			Level	Change		
	97.48	0.2%	1.4%	4.4%	1.30	0.0%	2.2%	-5.6%	1.12	0.0%	-2.2%	-4.5%	111.43	-0.5%	-1.6%	2.8%	3.92	0.0%	-1.2%	-14.6%
EQUITIES	S&P 500				FTSE 100				EURO STOXX 50				NIKKEI				BOVESPA			
	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018	Apr '19	MTD	YTD	2018
	Level	Change			Level	Change			Level	Change			Level	Change			Level	Change		
	2,946	4.0%	18.2%	-4.4%	7,418	2.3%	12.0%	-8.7%	3,515	5.3%	18.1%	-12.0%	22,259	5.0%	12.0%	-10.7%	96,353	1.0%	9.6%	15.0%

SECTOR SPREADS***				
	Apr '19	MTD	YTD	2018
	Level	Change (bps)		
MBS ^b	41	+6	+6	+11
IG ^c	105	-10	-36	+54
HIGH YIELD ^d	417	-18	-128	+206
EM EXTERNAL ^e	365	-8	-70	+124

COMMODITIES				
	Apr '19	MTD	YTD	2018
	Level	Change		
Oil	\$64	6.3%	40.7%	-24.8%
Gold	\$1,286	-0.6%	0.3%	-2.1%
Copper	\$290	-1.2%	10.3%	-20.3%
Grains ^f	\$27	-4.1%	-10.2%	-7.4%

*Central Bank Policy Rate

**U.S. Dollar Index (DXY)

***Sector spreads to like-duration government bonds

Source: Bloomberg

^aThomson Municipal Market Data (MMD) AAA Curve, ^bBarclays Global Agg MBS Index, ^cBloomberg Barclays Global Agg Credit Average OAS, ^dBarclays Global Agg High Yield Index, ^eJPMorgan Emerging Markets Bond Index, ^fDow Jones – UBS Grains Subindex

Outlook

Based on PIMCO's cyclical outlook from March 2019.

PIMCO expects world GDP growth to slow to 2.5%–3% this year from 3.3% in 2018. However, with China increasing stimulus and a trade deal between the U.S. and China in the making, we think there is a good chance that global growth will stabilize or even pick up moderately later this year. We expect **inflation globally to fall to 1.5%–2% from 2.2% in 2018** due to continued below-target inflation in the U.S., Europe and Japan.

In the U.S., we continue to expect growth to slow to 2%–2.5% in 2019 from nearly 3% last year. Factors contributing to the deceleration include fading fiscal stimulus, the lagged effect of tighter monetary policy over the past few years, and headwinds from the China/global slowdown. We estimate that China's easing will not filter through to U.S. growth until late 2019 or early 2020. **Headline inflation looks set to drop to 1.5%–2% this year, while core CPI moves sideways.** With growth slowing and inflation remaining below target, the Fed is likely to keep rates unchanged in 2019.

For the eurozone, we expect growth to slow to a trend-like pace of 0.75%–1.25% in 2019 from close to 2% in 2018, as weak global trade exerts significant downward pressure on the economy and Italy slipped into recession. An improvement in global trade conditions through this year should contribute to a gradual reacceleration. Reflecting firmer wage growth, **we expect a moderate pickup in core inflation, which has been stuck at 1% for some time.** In line with the European Central Bank's (ECB) forward guidance, we expect policy rates to remain unchanged this year.

In the U.K., we expect real growth in the range of 1%–1.5% in 2019, modestly below trend, and we continue to think that a chaotic no-deal Brexit is a low-probability event. **We see core CPI inflation stable at or close to the 2% target** as import price pressures have faded and domestic price pressures remain subdued. In the event of a soft Brexit by midyear, a rate hike by the Bank of England in the second half of the year would appear likely.

Japan's GDP growth is expected to be modest at 0.5%–1% in 2019, broadly unchanged from 0.7% in 2018. **With core CPI inflation expected to dip into negative territory** (due to temporary factors) around the middle of the year, we expect the Bank of Japan to keep its targets for short rates and the 10-year yield unchanged this year.

In China, we see growth slowing in 2019 to the middle of a 5.5%–6.5% range from 6.6% in 2018, but stabilizing in the second half of the year as fiscal and monetary stimulus find some traction and a likely trade deal between the U.S. and China supports confidence. We expect fiscal stimulus of 1.5% to 2% of GDP. **Inflation remains benign at 1.5%–2.5% in our forecast,** and we look for another rate cut by the People's Bank of China in addition to more reductions in banks' reserve requirement ratios. Yuan stability is well-anchored with a patient Fed and the understanding that this needs to be a component of the China–U.S. trade deal.

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