



MORNING BRIEFING

July 1, 2019

Glittering Gold, Soaring Bitcoin

See the [collection](#) of the individual charts linked below.

(1) Trump & Xi agree to keep talking. (2) Putting more tariffs on hold. (3) Trump has a need to win. (4) Fed back on pause? (5) A golden year so far for gold. (6) Ultra is making a comeback in easy monetary policy. (7) Gold price inversely correlated with TIPS yield. (8) The copper/gold ratio coincides with US bond yield. (9) With inflation in a coma, gold may be a hedge against global political turmoil. (10) Bad batch of Eurozone and US economic indicators. (11) Bitcoin more like digital tulips than stable money. (12) The key to unlock ransomware is priced in bitcoins. (13) Movie review: "Yesterday" (+ +).

Geopolitics: He Said, Xi Said. So what did we learn from the G20 meeting over the weekend? President Donald Trump wants to be reelected next year for a second term. Chinese President Xi Jinping may be president for life, but he realizes he might have to deal with Trump through 2024. Xi said: "Forty years on, enormous change has taken place in the international situation and China-U.S. relations, but one basic fact remains unchanged: China and the United States both benefit from cooperation and lose in confrontation."

To get reelected, Trump needs the US economy to continue growing and creating more jobs. Escalating the US-China trade war now risks hurting the US economy as next year's presidential election approaches. What's the point of doing that and losing the election? Better to win another term first, then get tougher on China.

So the two leaders agreed to resume trade negotiations and declared a ceasefire on any additional tariffs. Trump suggested that he will allow US companies to sell some components to Huawei, but not those that involve national security issues. He claimed that the Chinese will soon be purchasing more US agricultural products.

All this should be positive for the stock market. Indeed, despite trade tensions, the S&P 500 gained 6.9% last month, its best June since 1955, on its way to a 17.3% rise during the first six months of 2019, its best first half since 1997. On the other hand, the G20 news suggests that the Fed might hold off on lowering the federal funds rate at the 7/30-31 meeting of the FOMC.

Gold I: Mixed Message. June was a good month for gold, which made this year's first half a good one for gold. The price of the precious metal rose 10% from \$1,280.30 per ounce at the end of last year to \$1,409.00 at the end of last week. It jumped 9% during June ([Fig. 1](#)). It's now at its second-highest level since 5/14/13, but is still 26% below its record high of \$1,895.00 on 9/6/11. It has also rallied strongly so far this year relative to the euro (10%), pound (9), and yen (8). So not surprisingly, gold is up 9% ytd relative to the trade-weighted dollar ([Fig. 2](#)). On the other hand, it hasn't outperformed the S&P 500, which is up 17.3% ytd and 6.9% during June ([Fig. 3](#)).

Why this year? And why particularly in June? The solid performances of both gold and the S&P 500 during June and so far this year probably reflect the pivots by both Fed Chairman Jerome Powell and

European Central Bank (ECB) President Mario Draghi away from monetary normalization, with recent hints that they are considering going back to ultra-easy monetary policies.

The Fed chairman moved in that direction in a 6/4 speech, while the ECB president did the same on 6/18. Their comments drove interest rates down, with 10-year government bond yields falling around the world. In the US, the 10-year Treasury bond yield fell to 2.00% at the end of last week, the lowest since 11/8/16, while the comparable German and Japanese yields fell deeper into record-low negative territory at -0.33% and -0.13%, respectively ([Fig. 4](#)). (See our 6/25 [Morning Briefing](#) titled “Lots of Central Bank Liquidity.”)

The lower bond yield in the US is bullish for gold, particularly since it has been led lower by a significant drop in the 10-year US Treasury TIPS yield. Lower bond yields are also bullish for the stock market as they boost valuation multiples, provided that they don't foreshadow a recession. Consider the following:

(1) *There's no inflation to hedge against with gold.* The 10-year US Treasury bond yield has dropped 124bps from 3.24% on 11/8/18 to 2.00% on Friday ([Fig. 5](#)). Over this same period, the comparable TIPS yield is down 86bps to only 0.31%, one of the lowest rates since 9/11/17.

The spread between these two yields over that period is down 38bps to 1.69% ([Fig. 6](#)). This spread is widely considered to be a proxy for the fixed-income market's outlook for the annual inflation rate over the next 10 years, so its narrowness suggests inflationary expectations remain low. If that's the case, then why would the gold price be as strong as it is? After all, gold is widely viewed as a hedge against inflation.

But there is no inflation to worry about. Indeed, on Friday, we learned that the headline and core PCED inflation rates were just 1.5% and 1.6% y/y through May ([Fig. 7](#)). The core rate hit the Fed's 2.0% target only six times since it was publicly set by the Fed at the start of 2012!

(2) *Gold is getting TIPsy.* The answer to why gold is rallying can be found in the fact that the gold price tends to be highly correlated with the inverse of the 10-year TIPS yield ([Fig. 8](#)). In other words, gold does best when the TIPS yield is falling. That makes sense, since both speculators and investors in gold have to pay for storing the metal somewhere. If the inflation-adjusted financing cost is going down, gold is cheaper to store.

(3) *Gold diverging from other commodities.* In the past, I have often observed that the price of gold seems to confirm the underlying trend in the CRB raw industrials spot price index as well as its basic metals component ([Fig. 9](#) and [Fig. 10](#)). However, the price of gold has been diverging from both of these indexes so far this year.

That's an odd divergence. Is gold signaling that other commodity prices will soon be heading higher? That seems unlikely given the persistent weakness of the global economy. On the other hand, if the US and China strike a trade deal, there could be a “peace dividend” for the global economy, which would boost global growth. However, in this scenario, the price of gold is likely to move lower again.

(4) *Copper-to-gold ratio coincides with bond yield.* While the TIPS yield seems to drive the price of gold, it is interesting to see that the ratio of the price of copper to the price of gold has been highly correlated with the nominal 10-year US Treasury bond yield ([Fig. 11](#)). The same can be said about the ratio of the CRB raw industrials spot price index to the price of gold versus the bond yield ([Fig. 12](#)).

This makes lots of sense, though causality runs both ways: A weaker (stronger) copper price signals a bullish (bearish) environment for the bond price leading to lower yields. A lower (higher) bond yield, led

by the TIPS yield, tends to be bullish (bearish) for the gold price.

Gold II: Reversal of Fortune. Gold is no longer an inflation hedge because inflation is no longer a problem thanks to the four secular forces of deflation (i.e., the 4Ds: Détente, Demography, Disruption, and Debt), which we discussed most recently in the *Morning Briefing* cited above. Instead, gold might be a hedge against weak economic growth. Why would weak growth be bullish for gold? Economic weakness tends to inflame destabilizing anti-globalization nationalistic political forces around the world; gold is a refuge from economic and political instability.

The latest batch of global economic indicators shows widespread economic deterioration:

(1) *Eurozone sentiment eroding.* Especially troubling is the drop in the Eurozone Economic Sentiment Indicator from a recent high of 114.5 during December 2017 to only 103.3 during June, the lowest since August 2016 ([Fig. 13](#)). This series is highly correlated with the y/y growth rate of the region's real GDP growth rate, which was just 1.2% y/y during Q1.

(2) *US Q2 real GDP growth estimate lowered.* The FRB Atlanta [GDPNow](#) model estimate for real GDP growth during Q2 was lowered to only 1.5% (saar) on Friday, as real consumer spending was lowered slightly from 3.9% to 3.7%. That's still a solid number for consumer spending.

On the other hand, the Citigroup Economic Surprise Index plunged from a recent high of 27.3 on 2/1 to -68.3 during 6/28, virtually matching the year's low of -68.8 on 4/25 ([Fig. 14](#)).

(3) *US regional surveys depressed by escalating trade war.* Also of concern is the plunge during June of the average business conditions index of the five regional surveys conducted by the FRBs of Dallas, Kansas City, New York, Philly, and Richmond ([Fig. 15](#)). This does not augur well for this morning's national M-PMI release, or for manufacturing in general during June. Debbie and I believe that the weakness was exacerbated by the escalation of the US-China trade war in early May. The ceasefire announced at the G20 meeting could provide at least a temporary boost to the US and global economies, as discussed in the first section.

Bitcoin: Embezzelcoin. In late 2017, when bitcoin was soaring toward a record-high price of \$18,961 on 12/18/17, a distant relative asked me what I thought about the cryptocurrency ([Fig. 16](#)). He had bought one bitcoin when it was around \$4,000 in mid-2017. I said it reminds me of digital tulips. "What do you mean?," he responded. He is a Millennial who had never heard of the Dutch Tulip Bubble from 1634-38. I explained what happened back then and noted that the bubble was mostly confined to Amsterdam, whereas the bitcoin bubble is global.

Of course, some bitcoin fans believe that bitcoin has a legitimate role in a portfolio as a hedge against the madness of central banks. I concede that point. However, as we saw last year, it can crash, which is what it did on its way back down by a gut-wrenching 83% from the high of \$18,962 on 12/18/17 to a low of \$3,224 on 12/14/18. But now, it's back up to \$12,356. It certainly is volatile and hardly a stable store of value, which makes it a very poor candidate to replace more stable forms of money.

Some of this volatility may be attributable to the illegitimate uses of bitcoin. I've noticed more news stories this year about hackers planting ransomware on the computer systems of small city governments in the US. They successfully extort tens of thousands of dollars in exchange for the software key to unlock the frozen computer systems. Payment has to be made in bitcoin.

In June, Riviera Beach, a city in Florida, paid hackers \$600,000 in bitcoin with the hope of having its systems restored. Also during the month, Lake City, Florida facing a ransomware demand, authorized

the payment of \$490,000 in bitcoin to a hacker in order to regain access to its phone and email systems. At the end of the month, the village of Key Biscayne confirmed it had been hit by a cyberattack, though it wasn't clear if it was related to ransomware.

Cities and small businesses are becoming more popular targets for hackers, who recognize frequently unsophisticated systems. According to FBI estimates, there were 1,493 ransomware attacks in 2018, with victims paying a total of \$3.6 million.

In my book [Predicting the Markets](#) (2018), I wrote:

"I'm particularly intrigued by the impact of bitcoin and other cryptocurrencies on our monetary system. Blockchain, the software that runs these digital currencies, is allowing banks to eliminate clearinghouse intermediaries in their transactions and to clear them much more rapidly. Smartphone apps allow consumers to use these digital devices to deposit checks and make payments. These innovations could reduce employment and bank branches in the financial sector, much as Amazon is doing in the retail space. Central bankers are scrambling to understand the implications of bitcoin and blockchain. In time, central banks likely will incorporate these technologies into their operations, perhaps spawning bitdollars, biteuros, bityen, etc."

I concluded:

"Libertarians might long for a day when central banks are replaced by a monetary system based on a digitized currency that is unregulated by governments. I doubt that the central monetary planners will allow that to happen. But who knows? Technology has disrupted major industries. Maybe it will disrupt central banking!"

The International Monetary Fund (IMF) is studying cryptocurrencies. The 6/27 IMFBlog is titled "[Five Facts on Fintech](#)." It reviews the findings of a report titled "[Fintech: The Experience So Far](#)." Based on the IMF's research, countries generally foresee the emergence of crypto assets backed by central banks. The study surveyed central banks, finance ministries, and other government agencies in 189 countries. More specifically:

"The survey reveals wide-ranging views of countries on central bank digital currencies. About 20 percent of respondents said they are exploring the possibility of issuing such currencies. But even then, work is in early stages; only four pilots were reported. The main reasons cited in favor of issuing digital currencies are lowering costs, increasing efficiency of monetary policy implementation, countering competition from cryptocurrencies, ensuring contestability of the payment market, and offering a risk-free payment instrument to the public."

Increasingly, at the top of the list for the central bankers is the need to improve cybersecurity in the payments system. Banning cryptocurrencies that are not officially backed by central banks undoubtedly will be considered. Whether this is even feasible is a matter for future discussion.

Movie. "Yesterday" (+ +) ([link](#)) is a feel-good movie about The Beatles. The rock group doesn't exist in the movie. After a brief global power outage, only one person ever heard of The Beatles, and he happens to be a wannabe rock singer. He starts singing their catchy tunes (like "Hey Dude") to bigger and bigger audiences on his way to becoming a global phenom with the help of Ed Sheeran. It's nice to recall a time when we all enjoyed singing the same Beatles songs together and feeling good about one another. Actually, even their happy lyrics didn't do much to bring us quarrelsome lot together during the 1960s and 1970s, which were just as divisive as current times in many ways. By the way, Coke doesn't

exist in the movie either, so no one heard of "[I'd Like To Teach The World To Sing \(In Perfect Harmony\)](#)."

CALENDARS

US. Mon: Construction Spending 0.1%, ISM & IHS Markit M-PMIs 51.0/50.1, Clarida. **Tues:** Motor Vehicle Sales 17.0mu, Williams, Mester. (DailyFX estimates)

Global. Mon: Eurozone, Germany, France, and Italy M-PMIs 47.8/45.4/52.0/48.7, Eurozone Unemployment Rate 7.6%, Germany Unemployment Rate 5.0%, UK M-PMI 49.5, Japan M-PMI 49.5, Japan Consumer Confidence 39.2, China Caixin M-PMI 50.1. **Tues:** Germany Retail Sales 0.5%_{m/m}/2.7%_{y/y}, RBA Cash Rate 1.00%, Lowe, Carney. (DailyFX estimates)

STRATEGY INDICATORS

Global Stock Markets Performance ([link](#)): Last week saw the US MSCI index fall 0.3% and end the week 0.5% below its record high on 6/20. The AC World ex-US rose 0.4% for the week to 12.9% below its record high in January 2018. The US MSCI's weekly performance ranked 39th among the 49 global stock markets we follow in a week when 31/49 countries rose in US dollar terms. That compares to the prior week's 27/49 ranking, when the US MSCI rose 2.2% as 45 markets rose. EM Eastern Europe was the best performer last week with a gain of 0.8%, followed by EMU (0.7%), EAFE (0.6), and EM Asia (0.5). The regions underperforming last week: EM Latin America (-1.2), EMEA (0.1), and BRIC (0.2). Greece was the best-performing country with a gain of 4.8%, followed by New Zealand (4.3), Turkey (3.4), Israel (2.2), and Argentina (2.0). Of the 23 countries that underperformed the AC World ex-US MSCI last week, Pakistan fared the worst, falling 5.9%, followed by Colombia (-2.3), Morocco (-1.9), Mexico (-1.9), and Brazil (-1.5). In June, the US MSCI rose 6.9% in its best performance since January, ranking 15/49 as the AC World ex-US index rose 5.8% and all regions moved higher. That compares to the US MSCI's 6.5% tumble in May, which was its worst performance since December and ranked 28/49 as it trailed the 5.9% decline for the AC World ex-US, in a month when nearly all regions fell. The best-performing regions in June: EMU (7.2), EM Eastern Europe (6.3), EM Latin America (6.0), EAFE (5.8), and EM Asia (5.8). June's worst-performing regions, albeit with gains: EMEA (4.7) and BRIC (5.6). The US MSCI's ytd ranking dropped two places last week to 10/49, with its 17.6% ytd gain still well ahead the AC World ex-US (11.6). All regions and 41/49 countries are in positive territory ytd. Among the regions, five are outperforming the AC World ex-US ytd: EM Eastern Europe (19.9), EMU (13.6), BRIC (12.3), EMEA (12.1), and EAFE (11.8). Regions underperforming the AC World ex-US: EM Asia (8.6) and EM Latin America (10.8). The best country performers ytd: Greece (29.3), Russia (28.4), Argentina (27.2), Egypt (23.1), and Switzerland (20.0). The worst-performing countries so far in 2019: Pakistan (-16.8), Sri Lanka (-9.5), Chile (-3.5), Turkey (-3.3), and Jordan (-1.4).

S&P 1500/500/400/600 Performance ([link](#)): Two of these three indexes rose for a fourth week following four straight declines. SmallCap's 1.7% gain outpaced the 0.9% increase for MidCap and the 0.3% decline for LargeCap. LargeCap ended the week 0.4% below its record high on 6/20, which was its first in seven weeks. MidCap improved to 5.1% below its 8/29 record high. SmallCap remained in a correction at 13.2% below its 8/29 record after narrowly averting a bear market at the end of May. Nineteen of the 33 sectors moved higher last week compared to 30 rising a week earlier. Last week's best performers: SmallCap Materials (3.5%), SmallCap Energy (3.2), SmallCap Industrials (3.1), MidCap Industrials (2.6), and MidCap Materials (2.6). LargeCap Real Estate (-2.7) and MidCap Real Estate (-2.7) were the biggest decliners, followed by LargeCap Utilities (-2.1), MidCap Utilities (-2.1), and SmallCap Real Estate (-1.4). All three market-cap indexes rose in June and registered their best gains since January. LargeCap's 6.9% gain was smaller than the increases recorded by MidCap (7.5) and SmallCap (7.3). All 33 sectors advanced in June, compared to just one sector rising during May.

June's best performers: SmallCap Materials (13.2), MidCap Materials (12.1), LargeCap Materials (11.5), MidCap Industrials (10.8), and MidCap Tech (10.2). June's laggards, albeit with gains: SmallCap Communication Services (0.3), MidCap Real Estate (0.8), LargeCap Real Estate (1.3), SmallCap Real Estate (1.6), and SmallCap Consumer Staples (2.8). In terms of 2019's ytd performance, all three indexes are still off to a healthy start for the year. LargeCap leads with a gain of 17.3% ytd, slightly ahead of MidCap (17.0) and well ahead of SmallCap (12.8). Thirty-two of the 33 sectors are positive ytd, with the cyclicals leading the top performers: MidCap Tech (26.7), LargeCap Tech (26.1), MidCap Industrials (23.3), LargeCap Consumer Discretionary (21.0), and SmallCap Tech (20.7). MidCap Energy (-0.4) is the sole decliner so far in 2019, followed by these underperformers: SmallCap Energy (2.7), SmallCap Communication Services (2.9), SmallCap Consumer Staples (4.6), and MidCap Consumer Staples (5.1).

S&P 500 Sectors and Industries Performance ([link](#)): Four of the 11 S&P 500 sectors rose last week as five outperformed the S&P 500's 0.3% decline. That compares to all 11 rising a week earlier, when five outperformed the S&P 500's 2.2% rise. Materials and Financials were the best-performing sectors with gains of 1.5%, ahead of Industrials (0.3%), Energy (0.2), and Information Technology (-0.2). Last week's biggest underperformers: Real Estate (-2.7), Utilities (-2.1), Health Care (-1.2), Consumer Staples (-1.0), Communication Services (-0.8), and Consumer Discretionary (-0.3). The S&P 500 soared 6.9% in June as all 11 sectors moved higher and five beat the index. That compares to one rising and five beating the S&P 500's 6.6% decline in May. The leading sectors in June: Materials (11.5), Energy (9.1), Information Technology (9.1), Industrials (7.8), and Consumer Discretionary (7.6). June's laggards: Real Estate (1.3), Utilities (3.1), Communication Services (4.3), Consumer Staples (4.8), Health Care (6.5), and Financials (6.6). All 11 sectors are higher so far in 2019, compared to just two sectors rising during 2018, when the S&P 500 fell 6.3%. These five sectors have outperformed the S&P 500's 17.3% rise ytd: Information Technology (26.1), Consumer Discretionary (21.0), Industrials (20.2), Real Estate (18.5), and Communication Services (18.3). The ytd laggards: Health Care (7.1), Energy (11.1), Utilities (12.8), Consumer Staples (14.5), Financials (15.9), and Materials (16.0).

Commodities Performance ([link](#)): Last week, the S&P GSCI index rose 1.0% as 17 of the 24 commodities moved higher. That compares to 14 rising a week earlier when the index rose 3.5% for its best gain in 18 weeks. The index had nearly climbed out of a correction during mid-April, with a drop of just 10.0% from its high in early October after being down as much as 26.9% from that high on 12/24. It's now 15.4% below its October high. Coffee was the strongest performer for the week, as it rose 8.7%, ahead of Natural Gas (6.4%), Nickel (5.1), Unleaded Gasoline (4.4), and Feeder Cattle (2.4). Corn was the biggest decliner, with a drop of 5.1%, followed by Cocoa (-3.1), Lean Hogs (-2.4), and Wheat (-0.7). June saw 18 of the 24 commodities climb as the S&P GSCI Commodities index rose 4.3%. That compares to seven rising in May when the S&P GSCI Commodities index tumbled 8.7% for its worst decline since November. June's best performers were Crude Oil (9.3), Gold (7.8), Unleaded Gasoline (7.1), Lead (6.9), and Nickel (5.8). June's laggards: Lean Hogs (-11.6), Natural Gas (-5.9), Cotton (-2.9), Zinc (-2.6), and Kansas Wheat (-2.4). The S&P GSCI commodities index is up 13.6% ytd following a decline of 15.4% in 2018. The top-performing commodities so far in 2019: Unleaded Gasoline (45.7), Crude Oil (28.8), Lean Hogs (24.6), Brent Crude (20.3), and Nickel (19.0). The biggest laggards in 2019: Natural Gas (-21.5), Live Cattle (-15.8), Cotton (-8.5), Feeder Cattle (-6.7), and Kansas Wheat (-5.6).

S&P 500 Technical Indicators ([link](#)): The S&P 500 price index fell 0.3% last week, but continued its successful test of its short-term 50-day moving average (50-dma) and its long-term 200-day moving average (200-dma). The index's 50-dma relative to its 200-dma rose for 19th time in 20 weeks to a 38-week high, forming a Golden Cross for a 14th week after 16 weeks in a Death Cross formation. The index had been in a Golden Cross for 137 weeks through late November, and its previous Death Cross lasted for 17 weeks through April 2016 (when its 50-dma bottomed at a then-four-year low of 4.5%

below its 200-dma in March 2016). The current Golden Cross reading of 4.0% is up from -5.2% in early February, which had matched the lowest reading since November 2011. It's still down from a 55-month high of 7.2% in February 2018. The S&P 500's 50-dma rose at a slower rate, with the price index dropping to 2.2% above its 50-dma from 2.6% above a week earlier. That's up from a 22-week low of 4.2% below its falling 50-dma at the end of May, but down from 6.6% during mid-February, which was its highest since October 2011. The 200-dma rose for a third week following three straight declines. It had been rising for 16 weeks through mid-May after falling from October to February in the first downtrend since May 2016 (when it had been slowly declining for nine months). The index traded above its 200-dma for a fourth week, but dropped to 6.3% above its rising 200-dma from a 10-month high of 6.6% above its rising 200-dma a week earlier. That compares to 14.5% below its falling 200-dma on 12/24, which was the lowest since April 2009 and remains well below the seven-year high of 13.5% above its rising 200-dma during January 2018.

S&P 500 Sectors Technical Indicators ([link](#)): All 11 S&P 500 sectors traded above their 50-dmas for a second week and for the first time since early April, unchanged from a week earlier. All 11 were last below in early January. The longer-term picture—i.e., relative to 200-dmas—shows 10 sectors trading above currently, unchanged from a week earlier, as Energy was below its 200-dma for a 38th week. Nine sectors are in the Golden Cross club (with 50-dmas higher than 200-dmas), unchanged from a week earlier and the highest count since early November. Financials has been back in a Golden Cross for just 10 weeks, while Health Care was out for a ninth week and Energy for a 33rd week. All 11 sectors had been in a Golden Cross in January 2018 (for the first time since a 26-week streak ended in October 2016). Just three sectors still have falling 50-dmas now, unchanged from a week earlier, as Materials turned up and Communication Services turned down. Energy's 50-dma fell for a ninth week while Industrials and Materials have been mostly falling for the past six weeks. Six sectors have rising 200-dmas, down from seven a week earlier as Health Care turned down again for the sixth time in seven weeks. Among the remaining laggards: Energy, Financials, and Materials have had mostly falling 200-dmas for more than eight months now and Industrials for seven weeks, which compares to just two sectors with rising 200-dmas in early January, in what was then the lowest count since all 11 sectors had falling 200-dmas two years before.

US ECONOMIC INDICATORS

GDP ([link](#)): Real GDP growth accelerated by an unrevised 3.1% (saar) during Q1, according to the third estimate, after slowing steadily from 4.2% during Q2-2018 to 2.2% during the final quarter of last year. While there was no revision to headline growth, there were notable revisions within the components. Trade gave the biggest boost to Q1 GDP growth, as the real trade deficit (to -\$905.0 billion from -\$955.7 billion) narrowed dramatically from Q4's record gap. Revisions show Q1's gain in real exports (to 5.4% from 4.8%, saar) was revised higher for the second time, while the decline in real imports (-1.9 from -2.5) narrowed for the second time. Real capital spending (4.4 from 2.3) expanded at double the rate previously reported, reflecting big upward revisions to growth in investment in intellectual property products (12.0 from 7.2) and structures (4.3 from 1.7); spending on equipment was unchanged at -1.0% (saar). Government spending (2.8 from 2.5) was revised slightly higher, reflecting stronger state & local (4.6 from 4.0) government expenditures. Revisions show real residential (-2.0 from -3.5) continued to contract, though at a slower pace, posting its fifth consecutive quarterly decline. Meanwhile, real consumer spending (0.9 from 1.3) was revised still lower to show spending grew at its slowest pace in a year: Consumer spending on services (1.0 from 2.1) was revised lower, while durable goods consumption (-2.4 from -4.6) contracted at a slower pace, and the gain in nondurable goods (2.3 from 2.0) spending was slightly faster than previously reported. Revisions still show Q1's real private inventory investment (\$122.8 billion from \$125.5 billion) accumulated inventories at their best rate since Q2-2015, though below prior estimates.

Contributions to GDP Growth ([link](#)): Trade was the number-one contributor to GDP growth during Q1, pushing consumer spending down to the number-two spot; real residential investment remained the biggest drag on GDP. Some details: (1) Real net exports of goods & services accounted for 0.94ppt of Q1 GDP, as both exports (0.65) and imports (0.30) contributed positively. (2) Real consumer spending added 0.62ppt to growth, as positive contributions from services (0.48) and nondurable goods (0.32) consumption more than offset the drag from durable goods (-0.17) spending. (3) Nonresidential fixed investment (0.61) continued to elevate economic growth during Q1, driven by investment in intellectual property products (0.53), with structures (0.13) also contributing; equipment (-0.06) investment had little impact. (4) The positive contribution from inventory investment (0.55) continued to be driven solely by nonfarm (0.56) inventories. (5) Real government spending (0.48) contributed to Q1 growth after subtracting at the end of last year; state & local spending (0.48) accounted for the entire gain. (6) Residential investment (-0.08) subtracted from GDP growth for fifth consecutive quarter.

Personal Income & Consumption ([link](#)): Both nominal and real consumer spending in May climbed to new record highs, while inflation remained subdued. Nominal spending climbed for the fourth time this year, up 0.4% in May and 2.2% ytd, while real consumer spending rose 0.2% and 1.5%, respectively, over the same periods. We calculate real consumer spending accelerated 4.1% (saar) during the three months through May, based on the three-month average, posting its best three-month spending spree since last July; the measure was flat in February. Real consumer outlays on durable and nondurable goods shot up 15.4% and 6.3% over the comparable three-month period, while consumer services consumption increased 1.8% (saar). Real wages & salaries held at its record high in May, after climbing the first three months of the year, expanding 1.6% (saar) during the three months through May, based on the three-month average, half March's pace. Meanwhile, May data show headline inflation was only 1.5% y/y, while the core rate—the Fed's preferred measure—was unchanged at 1.6% y/y, remaining below its target rate of 2.0%.

Consumer Sentiment ([link](#)): Consumers were not as confident in June as they were in May, as tariff concerns and slowing employment gains lowered expectations. The Consumer Sentiment Index (CSI) sank to 98.2 in June after jumping from 97.2 in April to 100.0 in May, as the expectations component dropped 4.2 points last month to 89.3, after soaring to 93.5 in May—which was the best reading since January 2004. (Both the headline and expectations indexes were slightly above their mid-June readings of 97.9 and 88.6, respectively.) Meanwhile, the present situation component rose to 111.9 (vs 112.5 preliminary) in June after falling from 113.3 to 110.0 the prior two months. June's decline was entirely due to households in the top third of the distribution, who frequently mentioned the negative impact of tariffs, cited by 45% versus 30% in May. "Most of the June slippage was concentrated in prospects for the national economy, with the unemployment rate expected to inch upward instead of drifting downward in the year ahead," Richard Curtin, director of the University of Michigan consumer survey, said in a statement. Meanwhile, the report notes that interest rates were expected to increase by the fewest respondents in six years, and falling mortgage rates have started to have a positive impact on home buying.

Pending Home Sales ([link](#)): The Pending Home Sales Index (PHSI)—measuring sales contracts for existing-home purchases—rebounded 1.1% in May to 105.4 after dipping in April. Sales fell 0.7% y/y, the 17th straight month of annual declines, though appear ready to swing positive again. Regionally, three of the four major regions saw sales rise during the month, though only the South is showing a y/y gain: Midwest (3.6% m/m & -1.2% y/y), Northeast (3.5 & -0.5), South (0.1 & 0.7), and West (-1.8 & -3.1). Lawrence Yun, NAR chief economist, said that lower-than-usual mortgage rates have led to the increase in pending sales for May. "Rates of 4% and, in some cases even lower, create extremely attractive conditions for consumers. Buyers, for good reason, are anxious to purchase and lock in at these rates." He noted that while "contract signings and mortgage applications have increased, there is still a great need for more inventory."

GLOBAL ECONOMIC INDICATORS

Eurozone Economic Sentiment Indicators ([link](#)): The Economic Sentiment Index (ESI) for both the Eurozone (-1.9 points to 103.3) and the EU (-1.5 points to 102.3) fell markedly in June—to their lowest readings since August 2016 and December 2014, respectively. These measures peaked at 18-year highs of 114.5 and 114.3 at the end of 2017. ESIs fell in all of the Eurozone's largest economies, with Germany (-2.9 points to 102.6) posting the biggest decline, followed by Italy (-1.5 to 100.2), the Netherlands (-1.5 to 102.8), France (-1.0 to 103.9), and Spain (-0.6 to 104.8). At the sector level, sentiment was mixed, with the ESI for construction (+3.6 points to 7.7) up sharply, climbing back near January's record high of 8.4, and retail trade (+1.0 to 0.1) sentiment also improving. Meanwhile, industry (-2.7 to -5.6) recorded the sharpest drop in sentiment, followed by services (-1.1 to 11.0) and consumer (-0.7 to -7.2) confidence—with industry sentiment sliding to its lowest level since September 2013.

Eurozone CPI Flash Estimate ([link](#)): June's CPI rate remained below 2.0% for the seventh consecutive month, according to the flash estimate, while the core rate moved back above 1.0%. The headline rate remained at May's 13-month low of 1.2% y/y last month, after easing from April's 1.7%; it was at a recent peak of 2.2% in October. Looking at the main components, all but non-energy industrial goods are estimated to have inflation rates of 1.6% y/y for June. Rates for both services (to 1.6% from 1.0%) and food alcohol & tobacco (1.6 from 1.5) are expected to move higher, while energy's (1.6 to 3.8) is forecast to move lower. The core rate—which excludes energy, food, alcohol, and tobacco—is expected to accelerate to 1.1% y/y after decelerating from 1.3% to 0.8% in May.

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