



MORNING BRIEFING

February 3, 2020

Made in China

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

(1) On the road again. (2) Unmasked man. (3) Coronavirus going viral. (4) Not as bad as the flu? (5) Great Quarantine of China. (6) Wet markets full of weird and tainted meats. (7) Zoonosis. (8) Coronavirus makes it into the Panic Attacks record book as #66. (9) Before the virus hit the tape, S&P 500 forward revenues and forward earnings rose to new record highs. (10) LargeCaps dropping less than SMidCaps. (11) Why is Growth beating Value again? (12) Stay Home beating Go Global during health crisis. (13) Movie review: "Little Women" (+).

Virology 101: Flu Season? I went on a road trip last week to speak at the forecasting dinner events of the CFA Societies in Seattle, Kelowna (British Columbia), and Victoria (British Columbia). I didn't bring a face mask. In the airports, only a few people wore them. During my presentations, I started by acknowledging that I am not a virologist. However, I feel as though I've been taking an online night course on the subject since the coronavirus (a.k.a. nCoV2019) outbreak first got the stock market's attention on Friday, 1/24. My initial conclusion at the start of last week was that this viral episode's impact on the global economy shouldn't be any worse than the previous ones of SARS (2003), MERS (2012), Zika (2015-2016), and Ebola (2018).

Here it is a week later, and many countries have banned flights in and out of China. Russia has closed its border with China, which has quarantined Wuhan, where the outbreak began, and other major cities in Hubei province. Meanwhile, an estimated 5 million people have left Wuhan, either in anticipation of the quarantine or to be with family during the Lunar New Year holiday, which has been extended beyond the traditional one- to two-week celebration period. Foreign governments have been airlifting their citizens out of Wuhan and placing them in isolation for 14 days, which is believed to be how long it takes for the virus' symptoms to show up. Apple shut its 40-plus stores on the Chinese mainland. So did Ikea.

Our friend Jeffrey Kleintop, the Chief Global Investment Strategist at Charles Schwab, provided a useful chart on this subject in his 1/31 [commentary](#). It showed that the previous 13

world epidemics since June 1981 had almost no impact on the All-Country World MSCI stock price index, with its one-month post-outbreak performance averaging 0.4%, followed by three-month and six-month average gains of 3.1% and 8.5%, respectively.

Jeff concluded: “If the spread of the nCoV2019 virus tracks a pattern similar to those tracked in the past by the World Health Organization, the number of confirmed cases will rise sharply for eight to ten weeks, then the infection rate will likely start to taper off into the spring months. Travel may return, along with consumer spending, setting up for an economic rebound in the second quarter similar to the timeline for SARS in 2003...”

In other words, the coronavirus may play out in much the same manner as a typical flu season. Consider the following:

(1) *Deadly flu virus.* In the [Morning Briefing](#) a week ago, Melissa and I observed: “On a worldwide basis, 2,102 cases with 56 deaths attributable to 2019-nCoV have been confirmed through Sunday. By comparison, the Centers for Disease Control and Prevention (CDC) [estimates](#) that influenza has resulted in 9 million–45 million illnesses, 140,000–810,000 hospitalizations, and 12,000–61,000 deaths annually from 2010 through 2017 in the US alone. Preliminarily, the CDC [estimates](#) that 80,000 Americans died of the flu and its complications last winter—the disease’s highest death toll in at least four decades. The flu is also caused by a coronavirus.”

(2) *Grim scoreboard.* The Johns Hopkins Center for Systems Science and Engineering regularly updates its [online dashboard](#) for tracking the worldwide spread of the Wuhan coronavirus outbreak. The data visualization reflects statistics collected from multiple sources, including the World Health Organization (WHO), the CDC, the National Health Commission of the People’s Republic of China, and Ding Xiang Yuan, a social-networking site for health-care professionals that provides real-time information on cases.

On Sunday, 2/2, the dashboard showed 14,637 coronavirus cases worldwide, with 305 deaths to date.

(3) *Current flu season.* The CDC estimates that more than 19 million Americans have fallen ill with the flu so far this season, including 180,000 who have ended up in the hospital. About 10,000 Americans have died, including more than 60 children, so far. The current flu season

started with an unprecedented early surge in a B strain of the virus, which generally hits younger people harder. But now increasingly, cases of a flu A strain (H1N1) are being [reported](#) in the US.

(4) *Different this time?* A 1/31 Bloomberg [article](#) on the flu and the coronavirus observed: “Both viruses start off similarly: cough, fever, and in some cases difficulty breathing. The key difference is that people most at risk for the coronavirus will have either traveled to China or been in close contact with someone who is already infected.” It also reported that the coronavirus isn’t a risk for the average American or for anyone who hasn’t traveled to China recently or been exposed to someone who has. Influenza remains a greater risk so far.

(5) *Great Quarantine of China.* In his relatively optimistic commentary cited above, Jeff Kleintop provides a balanced warning: “Of course, we need to be careful about making simple comparisons to the past because these viruses are all unique, China is much more integrated into the global economy today, and the ability to quickly diagnose the virus and the widespread public awareness and adoption of effective safety measures is different from the past. If this virus deviates from the historical pattern, new cases may continue to accelerate past March and spread widely in and outside of China. The economic cost of lost production due to widespread shutdowns and the resources devoted to the crisis would have the potential to trigger a recession in the global economy already vulnerable to a shock due to last year’s trade-driven slowdown.”

The 1/31 *WSJ* included an [article](#) titled “Coronavirus Quarantine Will Ripple Through Global Manufacturing.” It observed that China now accounts for more than twice the share of global merchandise exports that it did in 2003, when the SARS virus hit. Furthermore, China has become increasingly important to global supply chains since the country entered the World Trade Organization in 2001.

The article mentioned previous supply shocks that shook up manufacturers around the world: “Evidence from previous unexpected supply shocks is discouraging. General Motors shuttered U.S. and European plants after earthquakes in Japan in 2011 and again in 2016 because vital parts that couldn’t be easily found outside Japan suddenly became unavailable. Floods in Thailand in 2011 forced long-lasting changes to supply chains, even after immediate effects had dissipated. Research published in 2015 suggests that as much as 60% of the total economic impact of Japan’s 2011 earthquake in terms of value added was borne by other

countries, with 25% carried by the U.S.”

(6) *Bad meat*. In a conversation with my taxi driver between the airport and downtown Victoria last Thursday, we discussed the coronavirus outbreak. He said that he visited a wet market when he was in China not too long ago. He said it was totally disgusting. Besides meat and fish, these markets sell live animals, including wild ones like snakes, Himalayan palm civets, raccoon dogs, wild boars, and cobras. They are wet with water, blood, fish scales, and chicken guts. They can be breeding grounds for zoonosis, i.e., zoonotic diseases that jump from animals to humans. Patients who came down with the coronavirus at the end of December all had connections to the Hunan Seafood Market in Wuhan.

According to a 1/31 NPR [article](#), “these markets often have many different kinds of animals—some wild, some domesticated but not necessarily native to that part of Asia. The stress of captivity in these chaotic markets weakens the animals’ immune systems and creates an environment where viruses from different species can mingle, swap bits of their genetic code and spread from one species to another, according to biologist Kevin Olival, vice president for research at the EcoHealth Alliance. When that happens, occasionally a new strain of an animal virus gets a foothold in humans and an outbreak like this current coronavirus erupts.”

According to a 1/25 NYT [article](#), the SARS outbreak 17 years ago “was ultimately traced to a coronavirus that jumped from bats to Asian palm civets, a catlike creature prized as a delicacy in southern China, and then to humans involved in the wildlife trade there. According to officials and scientists, the new virus also appears to have originated in bats and made the jump to another mammal, though which one is not yet clear.”

It’s conceivable that the shortage of pork attributable to last year’s severe outbreak of swine flu increased the demand for other meats, which was met by the wet markets. Meanwhile, on Saturday, Chinese authorities announced the recurrence of avian influenza (H5N1) in chickens in central China. Don’t worry: While H5N1 can be fatal in humans—with a mortality rate of 60%, according to the World Health Organization—it doesn’t spread easily to humans.

According to the Chinese Zodiac, 2019 was The Year of the Pig. It was a very bad year for pigs in China. This year is starting off very badly for the rest of us, particularly in China, where 2020 is The Year of the Rat. Bamboo rats [reportedly](#) are sold in the wet markets, by the way.

Strategy I: Panic Attack #66. After Friday's 1.8% drop in the S&P 500, Joe and I decided that the latest selloff belongs in our list of panic attacks since the start of the current bull market, making it #66 ([Fig. 1](#)). (See [S&P 500 Panic Attacks Since 2009](#).) By adding it to our list, we are signaling that we don't expect the coronavirus outbreak to cause a recession in the US and that the panic attack should be followed by a relief rally to new record highs yet again. We don't think it will lead to a bear market. So it should be another buying opportunity rather than a reason to sell. Nevertheless, the outbreak is a known unknown. Consider the following:

(1) *Correction or bear?* At the beginning of January, we warned that the stock market was vulnerable to a correction because the forward valuation multiple of the S&P 500 was back up to the previous cyclical high around 18.5 ([Fig. 2](#)). It had hit that level in early January 2018 and proceeded to plunge to that year's low of 13.5 on Christmas Eve day.

We're feeling a bit guilty because we've been hoping that the stock market wouldn't continue to melt up so fast, thus achieving our year-end target of 3500 for the S&P 500 well ahead of schedule. We've been rooting for a stall in the P/E-led rally to give earnings a chance to catch up. We certainly didn't expect that a pandemic might do the trick. If it turns out to be much worse than expected, then it could cause a global recession such that earnings would tumble along with the market's P/E multiple, which is how bear markets happen. That's not our forecast, but it is a risk, which is why we view the current selloff as a panic attack.

(2) *Earnings & revenues.* S&P 500 earnings rose sharply during 2018 thanks to Trump's tax cuts and to surprisingly strong growth in S&P 500 revenues ([Fig. 3](#) and [Fig. 4](#)). Both growth rates slowed significantly last year: from 23.8% to 1.2% for earnings and from 8.9% to 4.1% for revenues ([Fig. 5](#) and [Fig. 6](#)). They are expected to rebound to 8.6% and 4.8%, respectively, this year. Those were the latest analysts' consensus expectations just before the virus hit the tape.

By the way, our weekly proxies for both have been edging up to new record highs so far this year through the 1/23 week ([Fig. 7](#)). Now we will be watching both weekly forward revenues and forward earnings to see whether the latest global health crisis infects them too. Given our observations about the likely course of the virus, we expect that both might stall for a few weeks but not dive.

Strategy II: Virus Hits the Tape. The latest global health crisis first made market-moving

headlines on Friday, 1/24. The day before, the S&P 500 closed at 3325.54, almost matching the 1/17 record high of 3329.62. This stock index closed at 3225.52 on Friday, 1/31, down 3.1% from the record high. Let's have a closer look at the initial impact of the virus crisis on financial markets over the past eight days (1/23-1/31):

(1) *LargeCaps vs SMidCaps*. Here is the performance derby for the S&P 500/400/600: -3.1%, -3.8%, and -5.0%. That's not surprising since SmidCaps tend to get whacked more than LargeCaps when fears of a recession are rising.

(2) *S&P 500 sectors*. Here is the performance derby of the S&P 500 sectors: Energy (-6.8%), Health Care (-4.9), Materials (-4.2), Communication Services (-4.0), Industrials (-3.4), S&P 500 (-3.1), Financials (-2.7), Information Technology (-2.6), Real Estate (-2.1), Consumer Staples (-1.4), Consumer Discretionary (-1.2), and Utilities (1.1). The hardest hit sectors are the most exposed to any weakness in the global economy caused by the health crisis.

(3) *S&P 500 Growth vs Value*. The ratio of the stock price indexes of S&P 500 Growth to S&P 500 Value jumped back to its previous cyclical high of last August ([Fig. 8](#)). Over the past eight days, the former is down 2.5%, while the latter is down 3.6%. That seems a bit odd since the virus increases the risk of slower global economic growth. It makes sense, though, when we consider that Value includes lots of Energy companies. It also includes lots of Financials, which tend to underperform when the yield curve flattens—as it has over the past week, falling 23bps from 19bps on 1/23 to -4bps on 1/31.

(4) *Commodities & currencies*. Since 1/23, the Goldman Sachs Commodity Index (which is heavily weighted with energy), fell 6.0%, while the trade-weighted dollar was basically flat ([Fig. 9](#)). Over this same period, the price of a barrel of Brent crude oil is down 8.9%, while the price of copper is down 7.6% ([Fig. 10](#)).

(5) *Credit*. The credit markets are anticipating more cuts from the Fed over the next 12 months, as the 12-month forward federal funds futures yield fell to 1.14%, and the 2-year Treasury yield dropped to 1.33%, on Friday ([Fig. 11](#)). The Fed's range for the federal funds rate is currently at 1.50%-1.75%. The 10-year Treasury bond yield fell to 1.51% and the comparable TIPS yield fell below zero again, to -0.14%, on Friday.

(6) *US versus them*. Since 1/23, the US MSCI stock price index slightly underperformed other

major MSCI stock market indexes (in local currencies) around the world, as follows: EMU (-2.3%), Japan (-2.4), US (-2.9), and EM (-4.4). However, until the health crisis started, Stay Home (i.e., in the US) continued to outperform Go Global, as it has during most of the current bull market ([Fig. 12](#)). Last October, Joe and I got cabin fever and started to look for better values abroad. It hasn't been working out, as shown by the following performance derby (in local currencies) since 9/30/19 through the end of January: US (8.7%), Japan (6.3), EM (5.4), and EMU (3.0).

(7) *Chinese policy response*. Stocks in China are likely to fall sharply this week when the stock exchanges in Shanghai and Shenzhen reopen after a week-long closure. The People's Bank of China said it plans to add liquidity to the financial system this week to help support the markets.

Movie. "Little Women" (+) ([link](#)) is the seventh film adaption of the 1868 novel by Louisa May Alcott. It is a semi-autobiographical story of four sisters starring Saoirse Ronan as Jo, Emma Watson as Meg, Florence Pugh as Amy, and Eliza Scanlen as Beth. It follows their passage from childhood to womanhood. Like Alcott, Jo is a writer and writes a novel (titled "Little Women," of course) about how she and her sisters developed their own individual personalities and pursued their goals persistently despite challenges posed by social conventions. The story is about the strength that a close-knit family can provide children to help them flourish and succeed in life as happy young adults. In other words, it's a classic American tale about the importance of the family as a base for healthy individualism, i.e., the freedom to pursue one's own path in life.

CALENDARS

US: Mon: ISM & IHS Markit M-PMIs 48.5/51.7, ISM Price Index 51.5, Construction Spending 0.5%, Bostic. **Tues:** Factory Orders 1.1%. (DailyFX estimates)

Global: Mon: Eurozone, Germany, France, and Italy M-PMIs 47.8/45.2/51./47.3, UK M-PMI 49.8, China Caixin M-PMI 51.0, RBA Cash Target Rate 0.75%, Lagarde, Guindos. **Tues:** China Caixin NM-PMI 52.0, Lowe. (DailyFX estimates)

STRATEGY INDICATORS

Global Stock Markets Performance ([link](#)): Last week saw the US MSCI index fall 2.1%, for

its biggest drop since early August. The US MSCI ranked 12th of the 49 global stock markets we follow in a week, but only 2/49 countries rose in US dollar terms in the lowest count in 24 months. That compares to a 3.2% decline for the AC World ex-US index, its worst since October 2019 as all regions declined. EAFE was the best performer, albeit with a drop of 2.5%, followed by EMU (-2.8%). EM Eastern Europe (-5.4) was the worst performer, followed by EM Asia (-5.2), EM Latin America (-4.9), BRIC (-4.7), and EMEA (-4.0). Portugal was the best-performing country, rising 1.7%, followed by Egypt (0.4), Jordan (0.0), and Israel (0.0). Of the 23 countries that underperformed the AC World ex-US MSCI last week, Korea fared the worst, falling 7.7%, followed by Indonesia (-6.4), South Africa (-5.9), Thailand (-5.9), Russia (-5.8), and Brazil (-5.8). In January, the US MSCI rose 0.1%, ranking 13/49 as the AC World ex-US index fell 2.7% and all of regions fell. That compares to December's 2.8% gain for the US MSCI (which ranked 33/49) and 4.2% gain for the AC World ex-US in a month when all regions moved higher. EAFE was the only region to outperform the AC World ex-US in January, albeit with a decline of 2.1%. EM Latin America was January's worst-performing region with a drop of 5.7%, followed by EM Asia (-4.5), BRIC (-4.4), EM Eastern Europe (-4.1), EMEA (-3.1), and EMU (-3.0). The US MSCI's ytd ranking rose one place last week and currently stands at 13/49. The best country performers in January (and also ytd): Israel (4.7), Portugal (4.7), Egypt (3.2), Jordan (3.0), and Morocco (2.0). The worst-performing countries so far in 2019: Hungary (-10.7), South Africa (-8.9), Thailand (-8.6), the Philippines (-8.0), and Chile (-7.9).

S&P 1500/500/400/600 Performance ([link](#)): All three of these market-cap indexes fell last week for a second straight week. SmallCap was down its most in 47 weeks while LargeCap and MidCap had their biggest declines in 26 weeks. LargeCap's 2.1% decline was smaller than the drops recorded by MidCap (-2.8%) and SmallCap (-3.6). LargeCap ended the week 3.1% below its 1/17 record high, and MidCap was down 4.4% from its record high on 1/16. SmallCap fell back into a correction on Friday, at 10.8% below its 8/29/18 record. Just two of the 33 sectors moved higher, down from 6/33 sectors rising a week earlier. LargeCap Utilities' 0.8% gain was the biggest in the latest week, followed by LargeCap Consumer Discretionary (0.1). MidCap Energy (-7.4) was the biggest decliner last week, followed by LargeCap Energy (-5.6), SmallCap Tech (-5.5), MidCap Communication Services (-5.3), and MidCap Tech (-5.0). All three market cap indexes fell during January for the first time in five months. LargeCap's 0.2% drop was much better than the declines recorded by MidCap (-2.7) and SmallCap (-4.0). Ten of the 33 sectors advanced in January, compared to 30 rising in December. January's best performers: LargeCap Utilities (6.6), LargeCap Tech (3.9), MidCap Utilities (1.8), SmallCap Communication Services (1.4), and LargeCap Real Estate (1.4). January's biggest

laggards: SmallCap Energy (-23.1), MidCap Energy (-22.5), LargeCap Energy (-11.2), SmallCap Consumer Staples (-8.5), and MidCap Consumer Staples (-7.7).

S&P 500 Sectors and Industries Performance ([link](#)): Two of the 11 sectors rose last week, and five outperformed the S&P 500's 2.1% decline. That compares to three rising and five outperforming the S&P 500's 1.1% drop a week earlier. Utilities was the best-performing sector with a gain of 0.8%, ahead of Consumer Discretionary (0.1%), Consumer Staples (-0.8), Financials (-1.4), and Real Estate (-1.8). Energy was the biggest decliner with a drop of 5.6%, followed by the also-underperforming Materials (-3.5), Health Care (-3.3), Communication Services (-3.0), Industrials (-2.9), and Information Technology (-2.2). The S&P 500 fell 0.2% in January as 6/11 sectors moved higher and six beat the index. That compares to 10 rising and four beating the S&P 500's 2.9% rise in December. The leading sectors in January: Utilities (6.6), Tech (3.9), Real Estate (1.4), Communication Services (0.7), Consumer Discretionary (0.6), and Consumer Staples (0.2). January's laggards: Energy (-11.2), Materials (-6.2), Health Care (-2.9), Financials (-2.8), and Industrials (-0.5).

Commodities Performance ([link](#)): Last week, the S&P GSCI index fell 4.3%, bringing its two-week decline to 8.9%. Three weeks ago, the index was close to exiting a correction from its cyclical high on 10/3/18. It ended the latest week 22.6% below that high and back in a bear market again. Cocoa was the best performer last week with a gain of 1.6%, followed by Sugar (1.5%) and Gold (0.6). Lean Hogs was the biggest decliner with a drop of 16.1%, followed by Coffee (-6.8), GasOil (-6.6), Heating Oil (-6.3), and Copper (-6.1). January saw 13 of the 24 commodities climb even as the S&P GSCI Commodities index tumbled 10.9% for its worst decline since November 2018. That compares to 18 rising in December when the S&P GSCI Commodities index rose 6.6%. January's best performers were Cocoa (9.3%), Sugar (8.9), Gold (4.3), and Silver (0.5). January's laggards: Coffee (-20.9), Heating Oil (-19.5), GasOil (-18.1), Natural Gas (-15.9), and Crude Oil (-15.6).

S&P 500 Technical Indicators ([link](#)): The S&P 500 price index fell 2.1% last week for its biggest decline since early August, and weakened relative to 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 a 15th week following nine straight declines. Its 50-dma is now at a 23-month high of 6.7% above its 200-dma and has formed a Golden Cross for 45 weeks after 17 weeks in a Death Cross formation. The S&P 500's 50-dma rose for a 17th week following three down weeks, but at a slower pace as the price index fell to a 22-week low of 0.1% above its rising 50-dma from 2.8% a week earlier and a 10-month high of 4.6% above its

rising 50-dma in mid-January. It had bottomed in late August at 3.5% below its 50-dma, which was down from 6.6% above during February 2019—its highest level since October 2011. The 200-dma rose for a 34th week. It had been rising for 16 weeks through mid-May after falling from October 2018 to February 2019 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 35th week, but also at a slower pace as it weakened to a 10-week low of 6.9% above its rising 200-dma from 9.5% a week earlier. That's also down from a 24-month high of 11.0% above its rising 200-dma in mid-January. It had peaked at a seven-year high of 13.5% above its rising 200-dma during January 2018. That compares to 14.5% below on 12/24/18, which was the lowest since April 2009.

S&P 500 Sectors Technical Indicators ([link](#)): Just five of the 11 S&P 500 sectors traded above their 50-dmas last week: Consumer Discretionary, Consumer Staples, Real Estate, Tech, and Utilities. That's down from eight a week earlier and at the lowest count since early October. For a third week, the longer-term picture—i.e., relative to 200-dmas—had all sectors except Energy trading above. That's down from all 11 above in the prior three weeks when Energy was above for the first time since October 2018. That's still up from six at the end of August, which was the lowest count since early June. Ten sectors are in the Golden Cross club (with 50-dmas higher than 200-dmas), unchanged from a week earlier. That compares to just two sectors in the club during February and all 11 in January 2018. Energy has not been in a Golden Cross for 64 straight weeks. Eight sectors have rising 50-dmas now, down from nine a week earlier and all 11 rising in mid-January. Industrials' 50-dma turned down w/w and joined Energy and Materials. Still, that's up from just three in early October. Ten sectors have rising 200-dmas, unchanged from a week ago. The sole laggard, Energy, has been mostly falling since October 2018. Materials and Financials moved higher for a 23rd week in their successful attempts at new uptrends for the first time since September 2018. That compares to just two sectors with rising 200-dmas in January 2019, 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 maintained Q3's 2.1% (saar) pace during the final quarter of 2019, according to the preliminary estimate, a full percentage point below the 3.1% posted during Q1-2019. Trade gave the biggest boost to Q4 growth as real exports expanded 1.4% (saar) while real imports contracted 8.7%—its steepest decline since Q2-2009. Real residential investment grew 5.8% (saar), faster than Q3's 4.6%—which was the first positive reading in

seven quarters. Meanwhile, real personal consumption expenditure slowed for the second quarter, to 1.8% (saar), from 3.2% and 4.6% the prior two quarters. It was the weakest quarterly growth since the 1.1% increase at the start of 2019. Real goods consumption expanded only 1.2% (saar) last quarter—the weakest since Q2-2013—slowing steadily from 8.6% during Q2-2019, which was the best performance since Q3-2003. Growth in both durable (to 2.1% from 13.0%, saar) and nondurable (0.8 from 6.5) goods consumption slowed considerably over the two-quarter span, while the easing in services (2.0 from 2.8) spending was much less dramatic. Real government expenditures accelerated to 2.7% (saar) from 1.7% during Q3—with both federal (3.6 from 3.3) and state & local (2.2 from 0.7) government spending stronger. Inventory investment was the biggest drag on growth, slowing considerably to a six-quarter low of \$6.5 billion (saar) from \$69.4 billion during each of the prior two quarters. Real nonresidential fixed investment declined 1.5% (saar) during Q4, following losses of 2.3% and 1.0% the prior two quarters—the longest string of declines in a decade. Real investment on structures contracted sharply for the third straight quarter, by 10.1%, following losses of 9.9% and 11.1% during Q3 and Q2, respectively. Real spending on equipment dropped 2.9% (saar) during Q4, following Q3's 3.8% decrease, while investment in intellectual property products accelerated 5.9% (saar)—its 12th straight quarterly advance. For all of 2019, real GDP grew 2.3%, slowing from 2.8% during 2018 and the weakest since 2016's 1.6%.

Contributions to GDP Growth ([link](#)): Trade and consumer spending were the biggest positive contributors to Q4 real GDP growth, while inventory investment was the biggest drag. The details: 1) Real net exports contributed 1.48ppts to Q4 real GDP as real imports (1.32ppts) contracted at a fast pace and real exports (0.17) expanded. 2) Real consumer spending added 1.20ppts to GDP growth last quarter, with services (0.94ppt) the biggest contributor; real goods consumption added 0.26ppt, with durable (0.15) and nondurable (0.11) goods contributions on equal footing. 3) Real government spending (0.47ppt) contributed to GDP growth every quarter of 2019, with both federal and state & local government spending contributing 0.23ppt during Q4. 4) Real residential investment (0.21ppt) contributed to GDP growth for the second quarter after subtracting from growth the prior six quarters. 5) The biggest negative contribution came from inventory investment (-1.09ppt)—all nonfarm—which hasn't contributed positively to growth since Q1-2019. 6) Real nonresidential fixed investment (-0.20ppt) subtracted from GDP growth for the third consecutive quarter, led by continued declines in both structures (-0.30) and equipment (-0.17); spending on intellectual property products (0.27) continued to add to GDP growth.

Personal Income & Consumption ([link](#)): Both nominal and real consumer spending posted

just one decline during all of 2019, climbing to new record highs. Spending is likely to continue to climb this year as both income and savings are at high levels and inflation is subdued. Nominal spending increased 0.3% in December, matching its average monthly gain for the final quarter of the year, while real spending edged up 0.1% in December, slowing from November's 0.3%. Real wages & salaries was flat at its record high in December after climbing 1.2% during the four months through November; it was up 3.5% y/y. In the meantime, personal savings, based on the 12-month sum, attained a record-high \$1.3 trillion. As for inflation, December data show both headline and core inflation increased only 1.6% y/y, with the core rate—the Fed's preferred measure—holding below its target rate of 2.0% for the 15th consecutive month.

Consumer Sentiment Index ([link](#)): Consumer sentiment remained close to its cyclical high in January, leading Richard Curtin (the surveys chief economist) to note: "The maintenance of consumer sentiment near cyclical peak levels is surprising given the overall slow pace of economic growth, which was accompanied in January by renewed military engagements in the Mideast, an impeachment trial in the Senate, and a fast spreading coronavirus." The Consumer Sentiment Index (CSI) increased for the fifth month, from 89.8 in August to 99.8 in January—not far from March 2018's cyclical peak of 101.4—due to "record low unemployment, record gains in income and wealth, as well as near record lows in inflation and interest rates," according to the survey. The expectations component climbed steadily from 79.9 in August to a six-month high of 90.5 in January, while the present situation component dipped to 114.4 after reaching a 12-month high of 115.5 in December.

Employment Cost Index ([link](#)): Labor costs in the private sector slowed slightly last quarter, remaining tame on a y/y basis. Total compensation costs climbed 0.7% during Q4, down slightly from 0.8% during Q3. The yearly rate remained at 2.7% y/y, down from 3.0% at the end of 2018. The rate for wages & salaries advanced 0.7% last quarter, slower than Q3's seven-quarter high of 0.9%, with the yearly rate posting a steady 3.0% y/y increase every quarter of 2019. As for benefits inflation, it rose 0.5% for Q2, posting quarterly gains from 0.4% to 0.5% for six quarters; the yearly rate slowed to a four-quarter low of 3.3% y/y, down from 3.6% during the first half of 2019.

GLOBAL ECONOMIC INDICATORS

Eurozone Economic Sentiment Indicators ([link](#)): The Economic Sentiment Indexes (ESI) for both the Eurozone (+1.5 point to 102.8) and the EU (+1.9 to 101.3) posted sizable gains at the

start of 2020—with the Eurozone posting its third straight gain. Both bottomed during October, at their lowest readings since January 2015 for the former and October 2013 for the latter. Among the Eurozone's largest economies, ESIs in Germany (+2.0 points to 101.8) and France (+1.5 to 104.1) increased notably during the month, while Spain's (-1.0 to 102.0) dropped sharply after a posting a 1.3-point gain in December. Meanwhile, ESIs in Italy (-0.1 to 101.5) and the Netherlands (-0.3 to 99.9) were broadly stable. At the sector level, industry (+2.0 to -7.3) and construction (+1.2 points to 6.9) confidence moved higher in January, while retail trade (-0.8 to -0.1) and services (-0.3 to 11.0) moved lower, with consumer confidence holding at -8.1.

Eurozone CPI Flash Estimate ([link](#)): January's CPI headline rate is expected to accelerate for the third month, to 1.4% y/y, after falling to 0.7% in October (which was the lowest since November 2016). It would be the 15th consecutive month the headline rate was below 2.0%. Meanwhile, the core rate is expected to slow to 1.1%—from recent highs of 1.3% the prior two months—back near August's recent low of 0.9%. Looking at the main components, food, alcohol & tobacco (to 2.2% from 2.0% y/y) is expected to record the highest rate, followed by energy (1.8 from 0.2), which turned positive in December for the first time in five months. Meanwhile, the services rate is expected to slow for the second month, to 1.5% y/y in January from 1.9% in November. The rate for non-energy industrial goods is forecast to remain at 0.5%.

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