MARS CAPITAL PARTNERS

Weekly Macro Review

w/c 13 August 2018

Key Themes

Positive developments on trade this week. NAFTA talks between the US and Mexico continued possibly with some breakthroughs on new rules on auto trade and agricultural trade. Canada is yet to re-join talks. Talks are set to resume between the US and China later this month. The USTR process for the next tranche of tariffs continues with public hearings taking place this week.

Growth and spending data remained positive but CPI datapoints were weaker in the Eurozone and UK.

US data was somewhat positive. Retail sales were stronger in July, but growth was revised lower for June. Much slower growth in industrial production for the start of Q3. Regional data was mixed – a stronger Empire State Manufacturing Survey, but slower growth from the Philly Fed Business Outlook Survey.

Eurozone –flash GDP quarterly growth was unchanged from the previous quarter and the annual rate slowed slightly to +2.2%. Industrial production declined in June after a stronger result in May - declines were recorded across the larger Euro economies. CPI declined in July (with some larger declines across key Euro economies also) but accelerated higher on an annual basis. The annual rate is still influenced mostly by higher energy prices – annual CPI ex energy is growing at a more moderate +1.4%.

UK retail sales data was stronger with sales volume growth accelerating in July - June results revised higher also. CPI growth was zero for the month (goods components declined) and there was no change in the annual rate of 2.3%.

Brexit – no outcomes announced from the lower level talks of last week, little progress made on key points of the withdrawal agreement. An increasing focus on preparedness for Brexit with 'no deal' as the UK government will commence release of 'no deal' contingency plans starting this week.

The Zew Financial Market report (25 Jun – 9 Jul) highlights that economic expectation indices have fallen across most major economies, but the assessment of current conditions remains broadly positive.

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Europe – Germany Prelim Q2 GDP, German CPI (Final Jul), German Zew Conditions and Sentiment Survey, Eurozone Q2 Prelim GDP, Eurozone Industrial Production (Jun), Eurozone CPI (Final – Jul), Eurozone Zew Conditions and Sentiment Survey

Japan – Industrial production (Final – Jun), Japanese Zew Conditions and Sentiment Survey

Great Britain – CPI (Jul), Retail Sales (Jul), UK Labour Market (Jun), UK Zew Conditions and Sentiment Survey

Canada – CPI (Jul)

Australia – Wage Price Index Q2, Labour Market (Jul), RBA Governor Lowe speech

Other – Chinese New Loans (Jul)

Trade – US-China Trade Dispute, NAFTA, Brexit

US Data

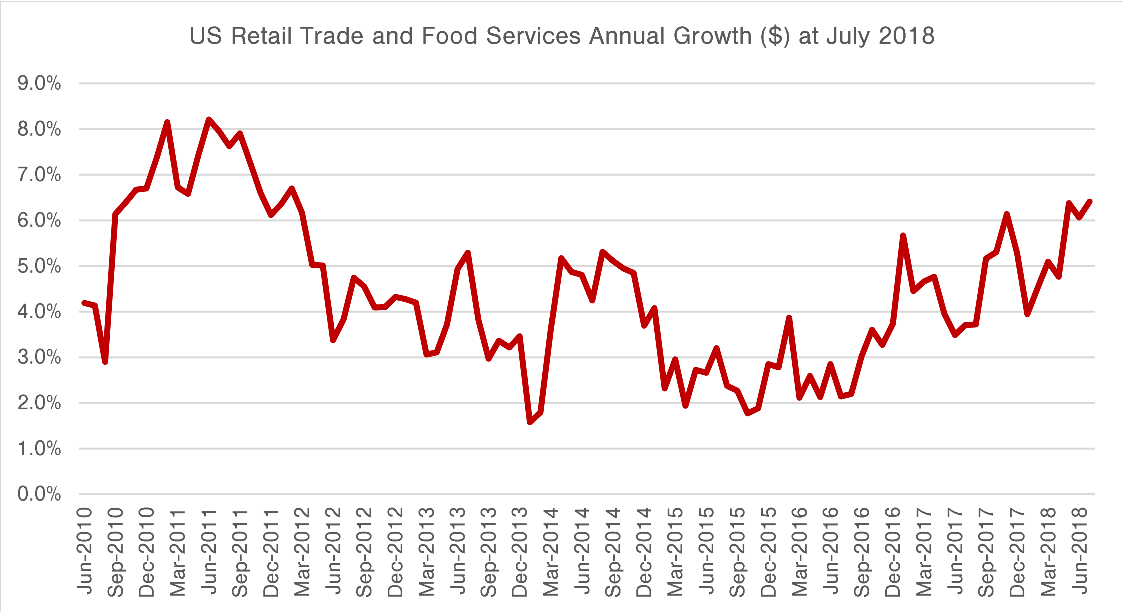
Advance Retail Sales (Jul)

Retail sales continued to grow in the latest month;

July +0.5% versus June +0.2% (June revised lower from +0.4% previously reported)

On an annual basis, the growth of retail trade accelerated to +6.4% ay July versus +6.1% at June.

The trend in annual growth has been accelerating for most of 2018;



The strongest performing categories this month were;

Food Services – growing at +1.3% in the month and +9.7% annual, accounted for 12% of total retail sales for 30% of retail sales growth in the month.

Non-store retailers – growing at 0.8% in the month and +8.7% for the year, accounted for 11% of total retail sales and 18% of retail sales growth in the month.

General Merchandise stores – growing at 0.7% in the month and +3.2% for the year, accounted for 12% of total retail sales and 16% of retail sales growth in the month.

Food and Beverage stores – growing at +0.6% in the month and 4.6% for the year, accounted for 12% of retail sales and 14% of the retail sales growth in the month.

Gasoline stations – growing at 0.8% in the month and +22.2% for the year, accounted for 9% of total retail sales in July and 14% of total retail sales growth in the month.

Clothing and clothing accessories stores – growing at +1.3% in July and +6.4% for the year, accounted for 5% of total retail sales in July and 12% of the growth in the month.

https://www.census.gov/retail/marts/www/marts_current.pdf

US Industrial Production (Jul)

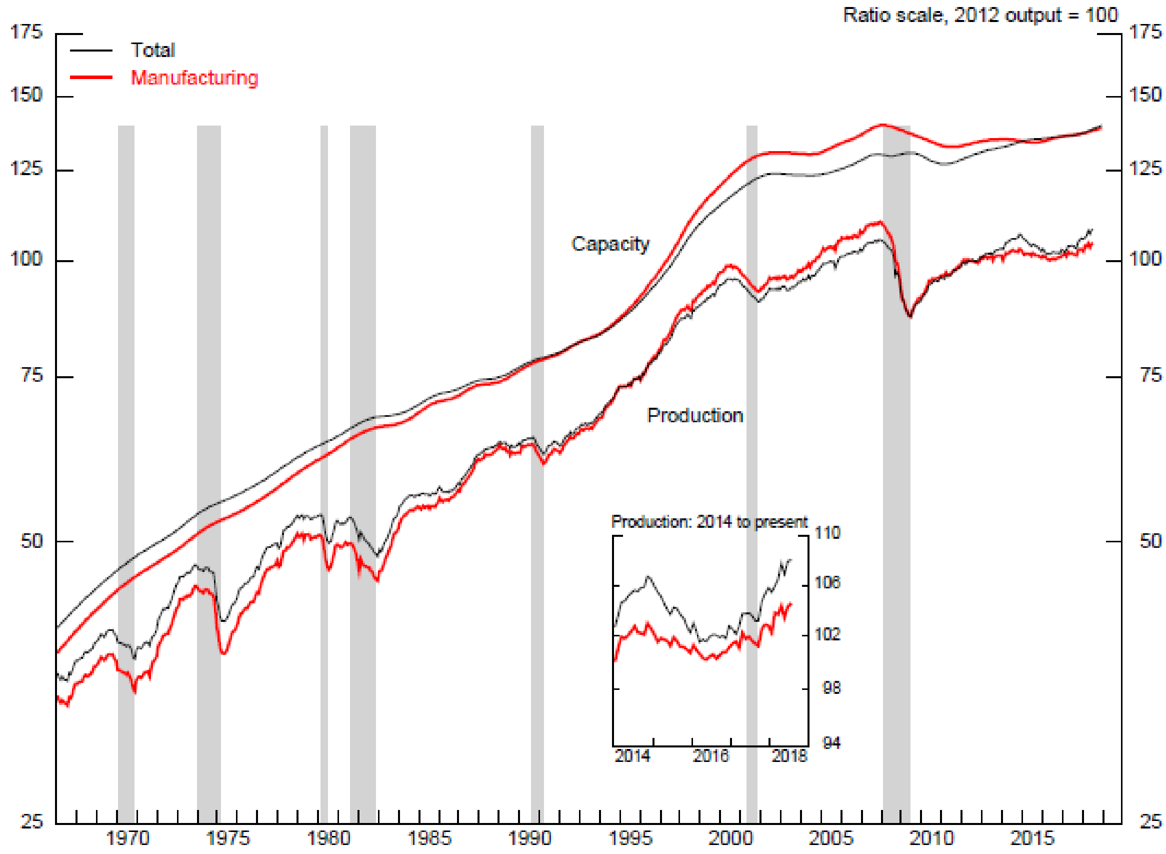
Industrial production in the US grew at slower pace in July after a larger upward revision in June;

July +0.1% versus June +1% (revised up from +0.6%)

Over the last 12 months, total industrial production grew by +4.2%.

In the latest year, growth in industrial production was the result of higher growth in mining +12.9% versus much lower growth for manufacturing +2.8% and utilities +2.3%.

1. Industrial production, capacity, and utilization



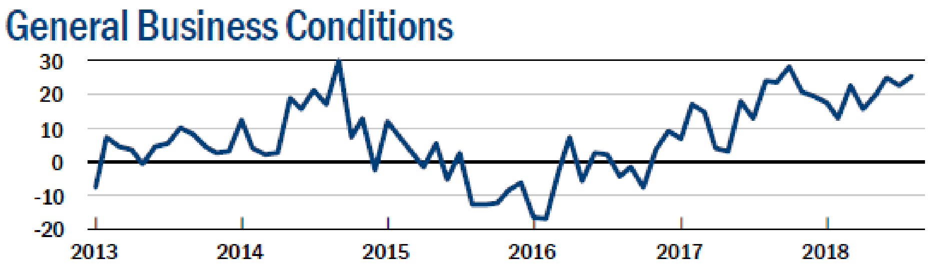
This is a weak start to Q3. The final growth rate for Q2 (annualised) was +6%, accelerating from +2.5% in Q1.

https://www.federalreserve.gov/releases/g17/current/

Empire State Manufacturing Index (Aug)

One of the earlier reads on regional manufacturing for August, the Empire State Manufacturing Survey continued to expand at a faster rate. This was a more positive report than the previous month but there are pockets of caution in the 6mth outlook, especially regarding employment and the employee work week.

General Business Conditions indicator; Aug 25.6 versus Jul 22.6



Shipments grew at a much faster pace – with a large decline in those respondents reporting 'lower' shipments.

As a measure of future demand/shipments, new orders still expanded, but at a slower pace, declining 1.1pts in the month. Less respondents reported higher new orders. In the 6mth outlook, new orders also expanded at a slower pace.

Unfilled orders, deliveries and inventories increased at a faster pace, with inventories now back up to a reading of zero.

Prices paid increased in the latest month but remain below recent highs. Prices received continues to flat-line, with less firms reporting higher prices received. The 6mth outlook is for much of the same.

Employment also continued to increase but at a slower rate, declining 4.1pts in the month. Again, less firms reported an increase in number of employees. The 6mth outlook sees an increase in the number of firms reporting a lower number of employees (but the index still in expansion). The average work week indicator fell to zero – with equal number of firms expecting higher and lower average employee work weeks.

The 6month general business expectations increased but remain below recent peaks. A positive point is the expected expansion in capital expenditure.

https://www.newyorkfed.org/medialibrary/media/survey/empire/empire2018/esms_2018_8_survey.pdf?la=en

Philly Fed Business Outlook Survey (Aug)

A weaker read for manufacturing activity in the region.

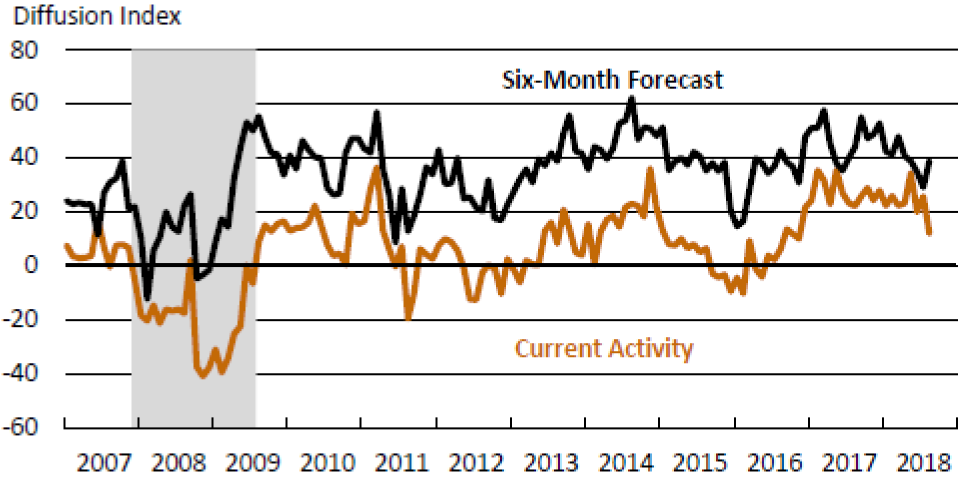
The current activity index continued to expand, but at a much slower pace;

Aug 11.9 versus July 25.7

The expectation for conditions 6months from now is more positive;

6mths from now v Aug 38.8 versus the result for July 29

Chart 1. Current and Future General Activity Indexes
January 2007 to August 2018



Note: The diffusion index is computed as the percentage of respondents indicating an increase minus the percentage indicating a decrease; the data are seasonally adjusted.

In the latest month, most concerning is the drop in new orders, as a measure of future demand; Aug 9.9 versus July 31.4. The expectations for 6mths from now is far more positive with the index increasing by 10pts.

Slower expansion was evident across shipments, unfilled orders and delivery times.

Prices paid continued to expand, but at a slower pace. Price received by firms also expanded at a slower pace.

Number of employees and average employee work week also grew at a slower pace.

Expectations for the next 6 months mostly expanded at a faster pace – the exceptions were inventories, average employee work week and capex.

https://www.philadelphiafed.org/research-and-data/regional-economy/business-outlook-survey/2018/bos0818

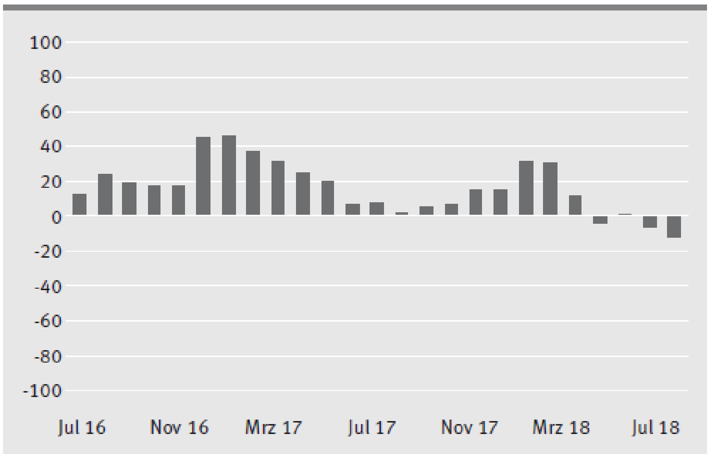
The Zew Financial Market Report - Covers the period 25 June to 9 July 2018

The report covers an assessment of the current conditions and economic expectations. There is quite a divergence between the current assessment (which is positive) and the future expectations (which is becoming more negative).

The assessment of the current economic situation was unchanged from the previous month and remains at 78.7 with most respondents assessing the economic situation as ‘good’.

Economic expectations; the headline; “Economic expectations are again declining significantly”

Konjunkturerwartungen USA



Saldo der positiven und negativen Einschätzungen bezüglich der Konjunktur in den Vereinigten Staaten in sechs Monaten. Quelle: ZEW

Economic expectations indicator fell again for the 6th month and is now at -12.2pts – the lowest since 2011.

http://ftp.zew.de/pub/zew-docs/frep/082018.pdf

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Europe

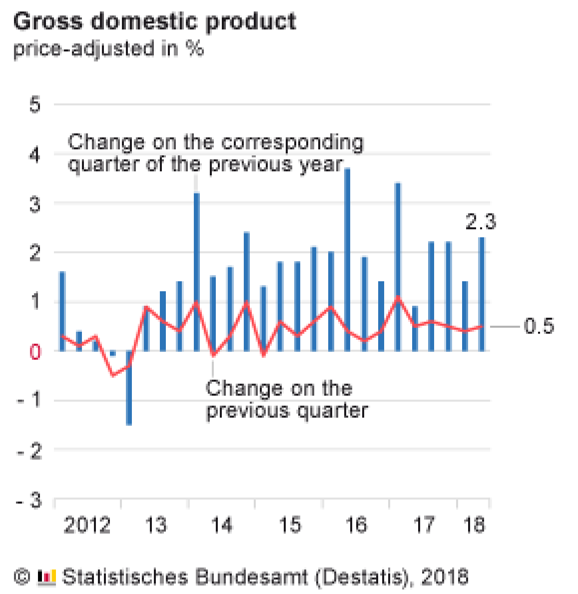
German Prelim Q2 GDP

Second quarter GDP growth was slightly higher than in Q1;

Q2 +0.5% versus Q1 +0.4%

Annual GDP growth accelerated to +2.3% in Q2 (price adjusted) versus +1.4% in Q1.

Positive contributions to growth came from; domestic demand including household and government consumption and capital formation. Prelim results show that while exports increased, there was an even stronger rise in imports.



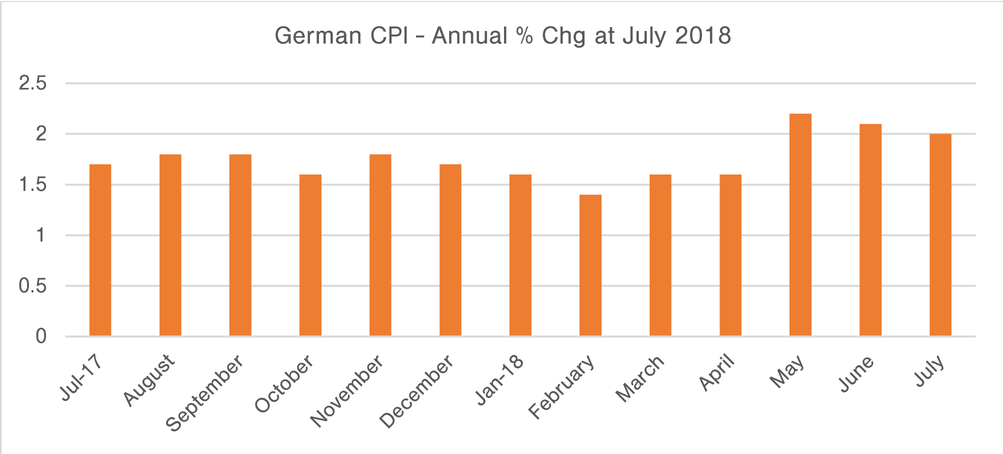
More detailed results will be released 24 Aug 2018.

https://www.destatis.de/EN/PressServices/Press/pr/2018/08/PE18_299_811.html

German CPI (final – Jul)

CPI in Germany grew by +0.3% in July versus +0.1% June

Despite the higher monthly rate, the annual rate slowed in July to +2% versus +2.1% in June.



Latest month; the higher CPI growth was the result of package holidays +19.3%. Most other categories recorded lower growth or declines including most energy-related prices.

Annual; Annual CPI continues to be heavily influenced by higher energy prices – CPI ex energy (HH energy and motor fuels) is much lower at +1.4%. In the latest month, CPI ex energy (HH energy and motor fuels) grew at the same rate as the headline CPI +0.3% - the effect of these energy prices is possibly starting to wane.

Annual growth in goods prices +2.4% (versus -0.6% in July versus June)

Annual growth in services prices +1.6% (versus +1.1% in July versus June) - A major factor contributing to the increase in service prices was the development of net rents exclusive of heating expenses (+1.6%), as households spend a large part of their consumption expenditure on this item.

https://www.destatis.de/EN/PressServices/Press/pr/2018/08/PE18_300_611.html

Germany - The Zew Financial Market Report - Covers the period 25 June to 9 July 2018

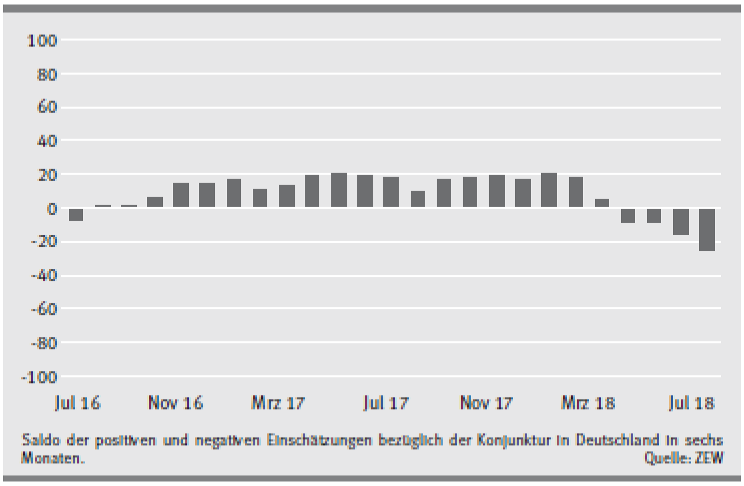
It's a very downbeat report and is consistent with the data at the time. The Aug German PMI data stabilised, and it wasn't until after this report, w/c 23 July, that President Trump met with EC President Juncker and agreed not to implement auto tariffs while trade negotiations take place. This might at least slow the deterioration in German and European sentiment.

There is quite a divergence between the assessment of the current situation and the economic expectations. The current assessment is broadly positive, while expectations are deteriorating.

Current conditions; the assessment of the economic situation in Germany fell by 8pts to 72.4. This was mostly due to the shift of respondent assessments from 'good' to 'normal'. The vast majority of respondents (72.9%) assess the current situation as 'good'.

Economic Expectations "International trade conflict worsens the economic outlook"

Konjunkturerwartungen Deutschland



The translation highlights that this is quite a downbeat report. Some highlights;

The expectations indicator fell again in August and is now -24.7, which is 8.6pts below the July read. This is the lowest reading since Aug 2012 and is significantly below the long term average of 23.3pts.

“For 96% of the survey participations, the international trade conflict is the single factor for the deterioration of the economic forecasts”.

“What is new, however, is that the expectations for the more domestic markets-oriented industries are sinking. The expectations for example, consumption and trade are down by 10.5pts to a value of 31.3 points”.

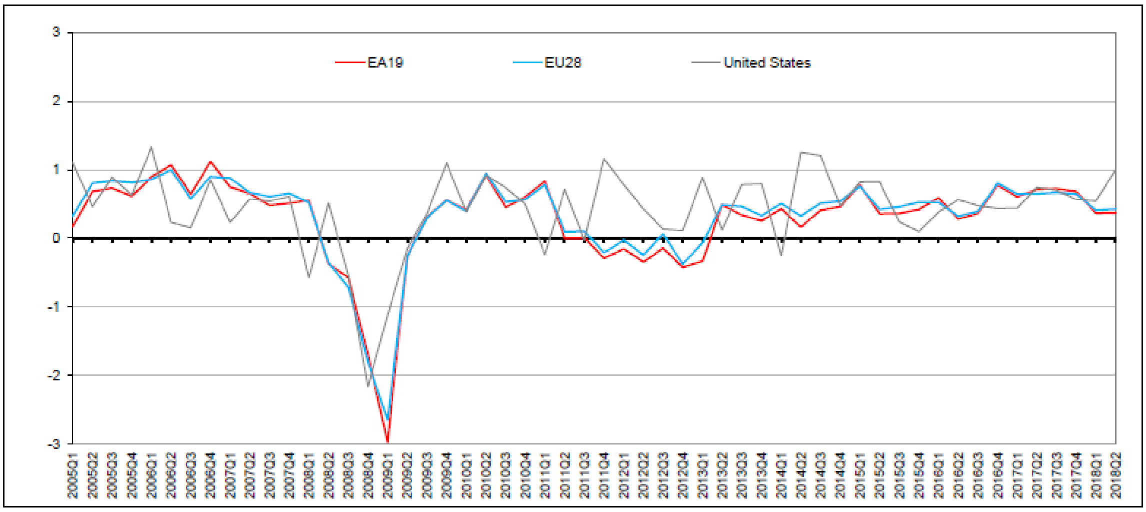
Eurozone Q2 prelim GDP

GDP grew at a consistent pace in latest quarter;

Eurozone Q2 +0.4% versus Q1 +0.4%

The annual rate of growth slowed; +2.2% in Q2 versus +2.4% (EU28)

EU28, euro area and United States GDP growth rates
% change over the previous quarter



Spain and Poland are growing well above the total EU rate at +2.7% and 5% respectively.

The other larger economies such as Germany, France, Italy and UK are all growing at below the current total EU rate of 2.2%

(Germany +1.9%, France +1.7%, Italy +1.1% and UK +1.3%).

The main aggregates are due 7 Sept 2018

http://ec.europa.eu/eurostat/documents/2995521/9105264/2-14082018-BP-EN.pdf/e28c60ea-1ad0-47fd-b7e1-668cdb9ba016

Eurozone Industrial Production (Jun)

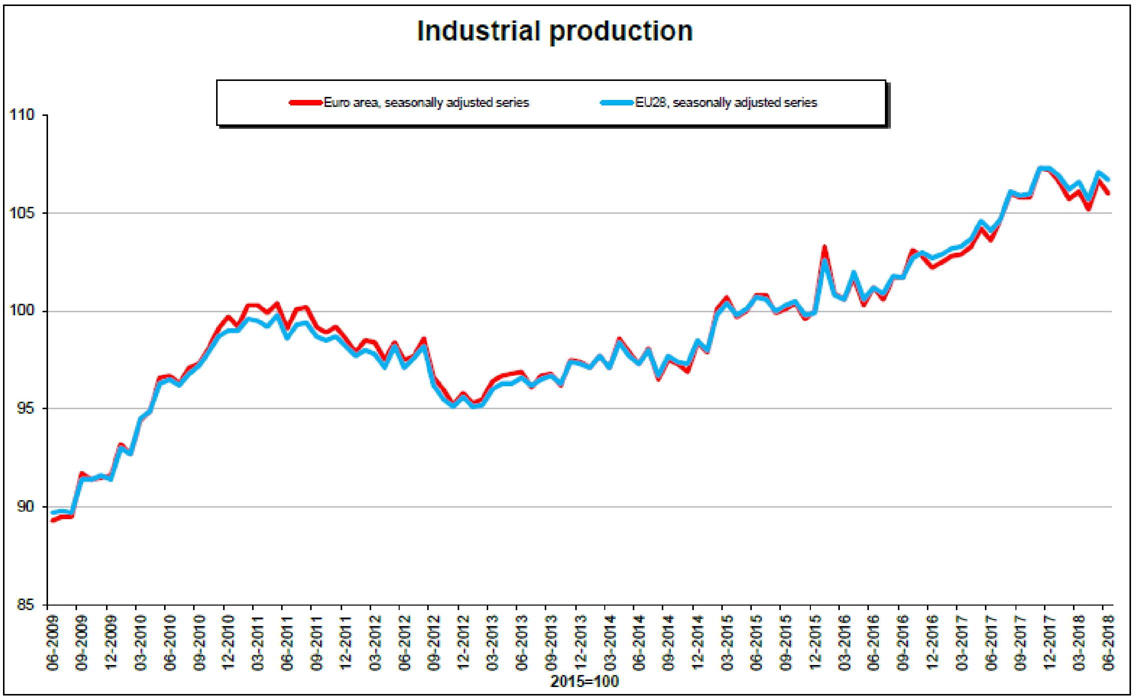
After a stronger May result, Eurozone industrial production fell in June across both the EU28 and EA19 groups;

<u>EA19</u>; June -0.7% versus May +1.4%

Declines were evident across all categories, except Energy (+0.5%). Industrial production in June 2018 versus June 2017 is growing at +2.5% for total industry.

<u>EU28</u>; June -0.4% versus May +1.3%

Similarly, declines were recorded across all categories except energy. Total industrial production for June 2018 versus June 2017 is growing at +2.6%.



Across key member states (June versus May); Germany -0.6%, Spain -0.7%, France +0.6%, Italy +0.5%, Poland +0.1% and UK +0.4%.

http://ec.europa.eu/eurostat/documents/2995521/9105355/4-14082018-AP-EN.pdf/7cc8a4b0-ae39-41f0-8fa2-ffd9aff86d4f

Eurozone CPI (Jul) - Final

CPI in the Euro Area and EU declined in the latest month. But the annual rates accelerated slightly higher.

Monthly data;

EuroArea (EA19); July -0.3% versus June (final) +0.1%

Euro Union (EU28); July -0.2% versus June (final) +0.1%

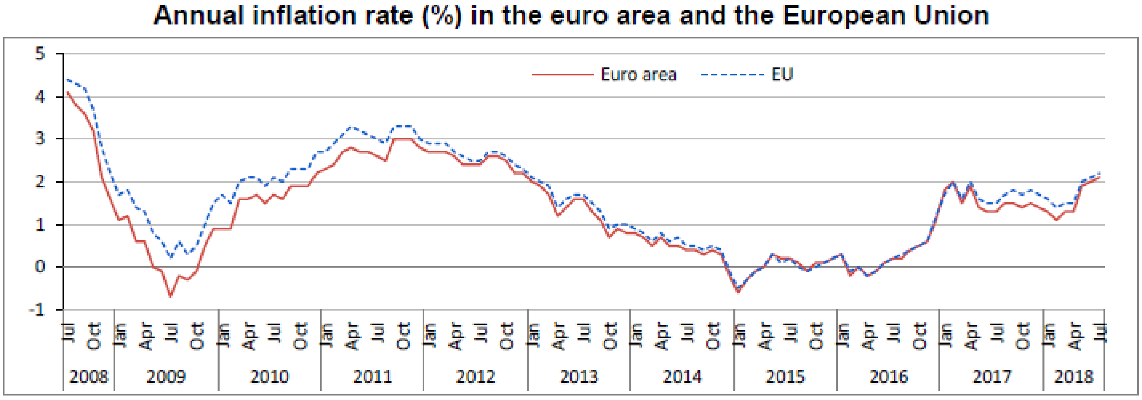
There were some large declines in the month among some of the bigger European economies; Italy -1.4% (mth), Spain -1.2%, France -0.1%,

Annual growth; despite the lower monthly growth, annual inflation continued to accelerate;

EA19; July +2.1% versus June 2%

EU28; July +2.2% versus June +2.1%

Headline CPI growth has accelerated since early 2018.



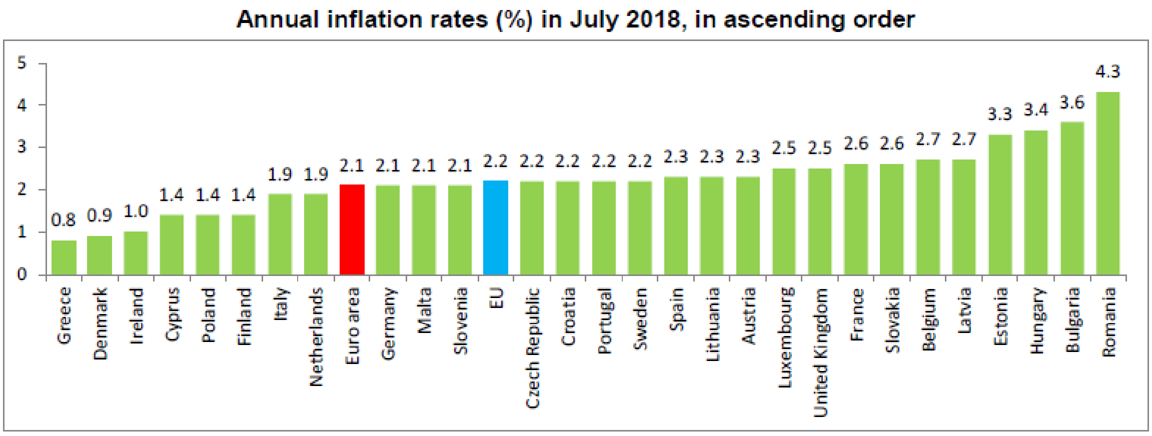
The headline rate of CPI growth is heavily influenced by high growth in energy prices; the annual rate accelerating to +9.5% in July versus +8% in June. Despite its much smaller weight, energy prices contributed +0.89%pts to the annual growth in headline CPI – the largest contribution of all components.

CPI ex Energy continues to grow at a more moderate pace; annual at July +1.4% and in the month -0.4%

Food, alcohol and tobacco prices are growing at a higher rate, with annual rates having accelerated from March 2018. Food, alcohol and tobacco prices are growing at +2.5% annual at July. Unprocessed food prices are growing at an annual rate of +2.6% - but declined by -0.7% in the month.

Services prices (approx. 44% of the CPI weight) continue to grow at a steady annual pace of +1.4% in July. Services made the second largest contribution to overall CPI growth.

<u>Headline CPI by Country;</u> Of the larger economies, headline CPI growth in Spain and France is above the EA19 average while German PI growing in line with the average and Italian CPI below the average.



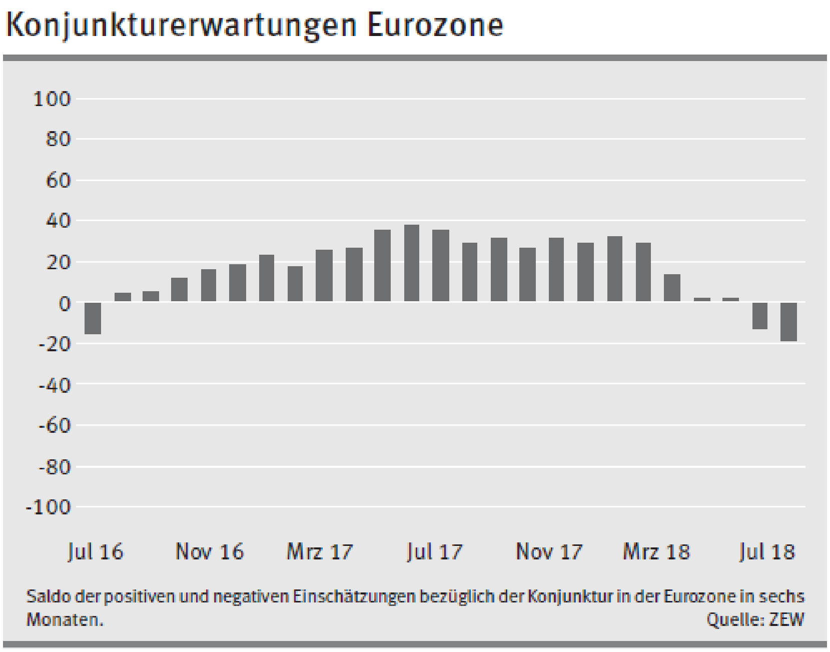
http://ec.europa.eu/eurostat/documents/2995521/9105279/2-17082018-AP-EN.pdf/f1680451-6124-493f-9ba8-c38f47b69776

Eurozone - The Zew Financial Market Report - covers the period of 25 Jun – 9 July 2018

There is still a divergence between current assessment and expectations, but the current assessment isn't quite as positive as in the US or Germany (a broader range of countries to consider).

The assessment of the current economic situation fell by -3.7pts to 36.2. This was due mostly to the shift in respondent assessments of the current situation from 'good' to 'normal'. A majority of respondents (59.8%) assess the current situation as 'normal'.

Economic expectations; the key headline "Economic expectations worsen again significantly"



Economic expectations indicator fell by a further 6.1pts to -18.7 pts. This was the level reached after the Brexit decision in July 2016.

http://ftp.zew.de/pub/zew-docs/frep/082018.pdf

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Japan

Industrial Production (Final - Jun)

The decline in industrial production was revised lower, declining at a slightly slower pace in June;

June – 1.8% (prelim -2.1%) versus May -0.2%

Industrial production was -0.9% below the same time a year ago

Shipments were revised higher from -0.2% to +0.3%

The decline in inventories was confirmed and the inventory ratio was slightly lower in the month, but well up on the prior year.

	Seasonally Adjusted Index		Original Index	
	index	Percent change from the previous month(%)	index	Percent change from the previous year (%)
Production	102.5	-1.8	104.8	-0.9
Shipments	101.8	0.3	103.3	-0.2
Inventories	111.4	-1.9	112.1	2.4
Inventory Ratio	116.5	2.3	115.2	5.2

http://www.meti.go.jp/english/statistics/tyo/iip/index.html

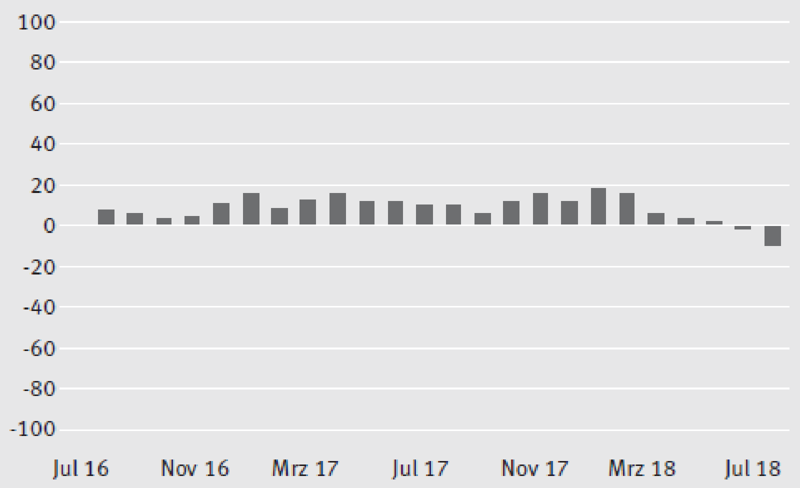
Japan - The Zew Financial Market Report - covers the period of 25 Jun – 9 July 2018

Similarly, in Japan, there is some divergence between the assessment of the current situation (normal) and the economic expectations (deteriorating).

The assessment of the current economic situation in Japan was little changed. Most respondents (75%) assess the current situation as 'normal'.

Economic expectations in Japan - the headline; "Decline in economic expectations continues"

Konjunkturerwartungen Japan



Saldo der positiven und negativen Einschätzungen bezüglich der Konjunktur in Japan in sechs Monaten.
Quelle: ZEW

The economic expectations index declined for the sixth month in a row and fell to -9.7pts the lowest since April 2011. International trade conflict is cited as the key reason for the deterioration. Of particular focus is on the further development of the trade conflict between the US and China, which is one of the most important trading partners of Japan.

http://ftp.zew.de/pub/zew-docs/frep/082018.pdf

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United Kingdom

UK – CPI (Jul)

The headline CPI for the month of July came in at 0% versus June 0%. (July 2017; 0%)

Month chg; The contributor to the low monthly change in CPI was mostly goods related; All goods declined by -0.6%;

Alcoholic Bevs & tobacco; -0.2%

Clothing footwear; -3.7%

Furniture/HH equip; -1.8%

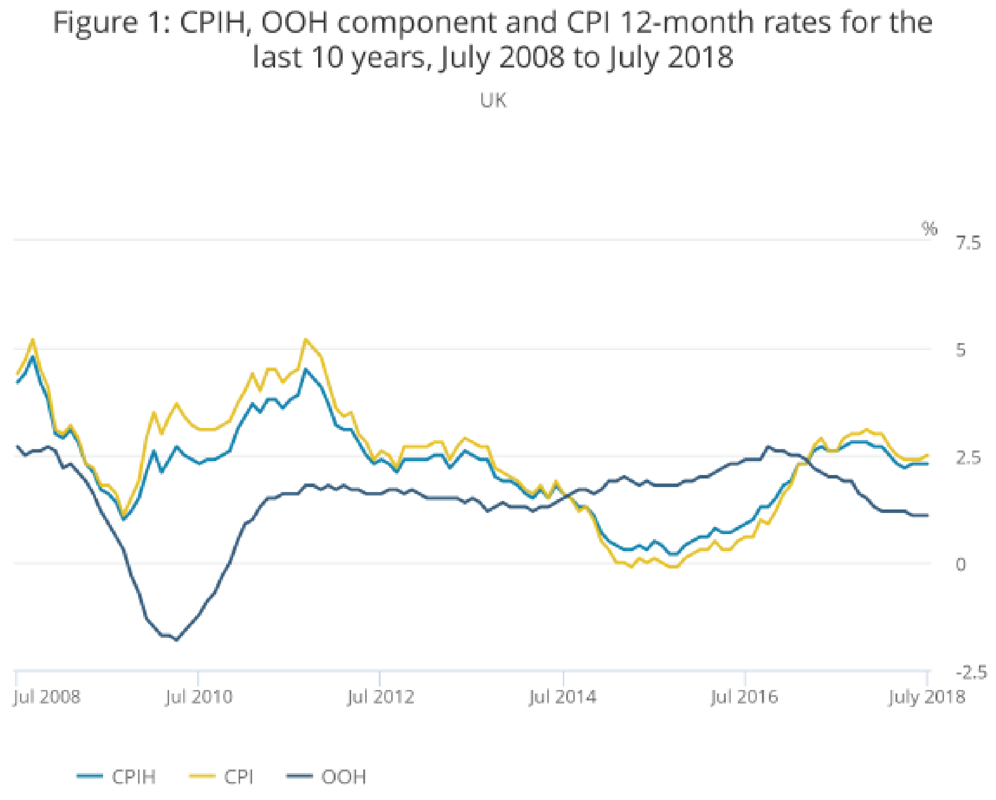
Misc goods and services; -0.8%

On an annual basis, CPI growth was unchanged versus the prior month;

Annual CPI (incl owner occ housing costs); July +2.3% versus June +2.3%

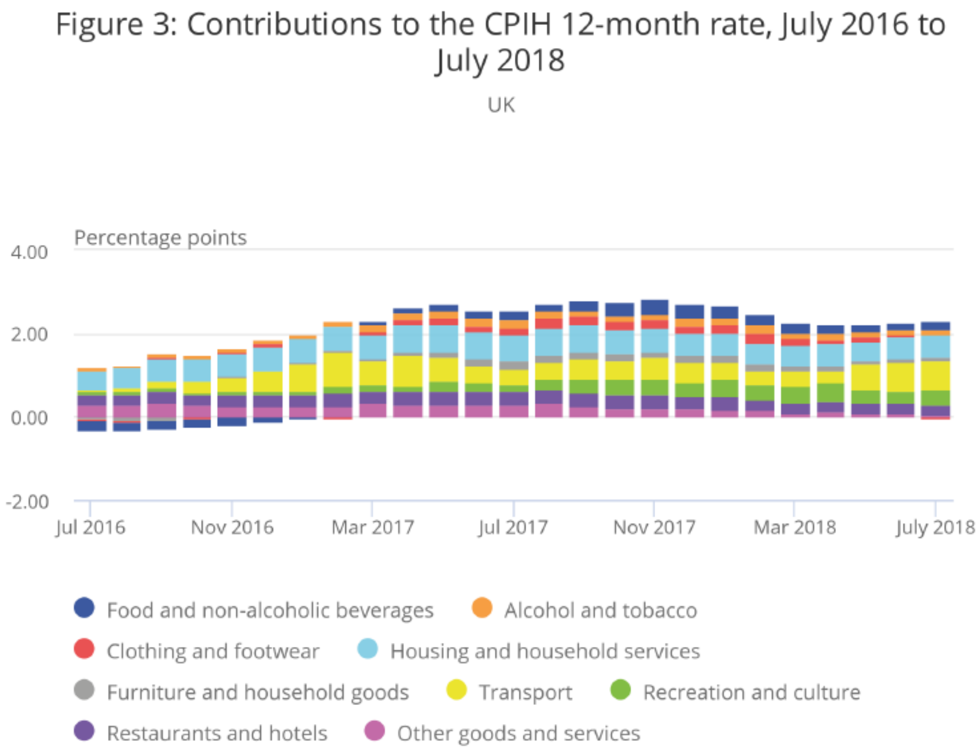
Figure 1: CPIH, OOH component and CPI 12-month rates for the last 10 years, July 2008 to July 2018

UK



The largest contributor to annual CPI growth over the last 3 months has been transport (fuels);

UK



Source: Office for National Statistics

The higher contribution of transport costs was offset by lower contribution from other categories such as clothing/footwear, alcohol and tobacco, other goods and services.

Transport prices, which includes Fuels, also grew at an annual pace of +5.6% in July – well above the total index of +2.3%. The electricity, gas and other fuels component of housing costs are growing at an annual rate of +6.7% (but with a small overall weight).

CPIH ex energy, food, tobacco and alcoholic beverages is growing at more moderate pace; July -0.1% and annual at July +1.8%

Another barometer of underlying inflation is the change in services prices;

All Services; July +0.4% and annual at July +2%

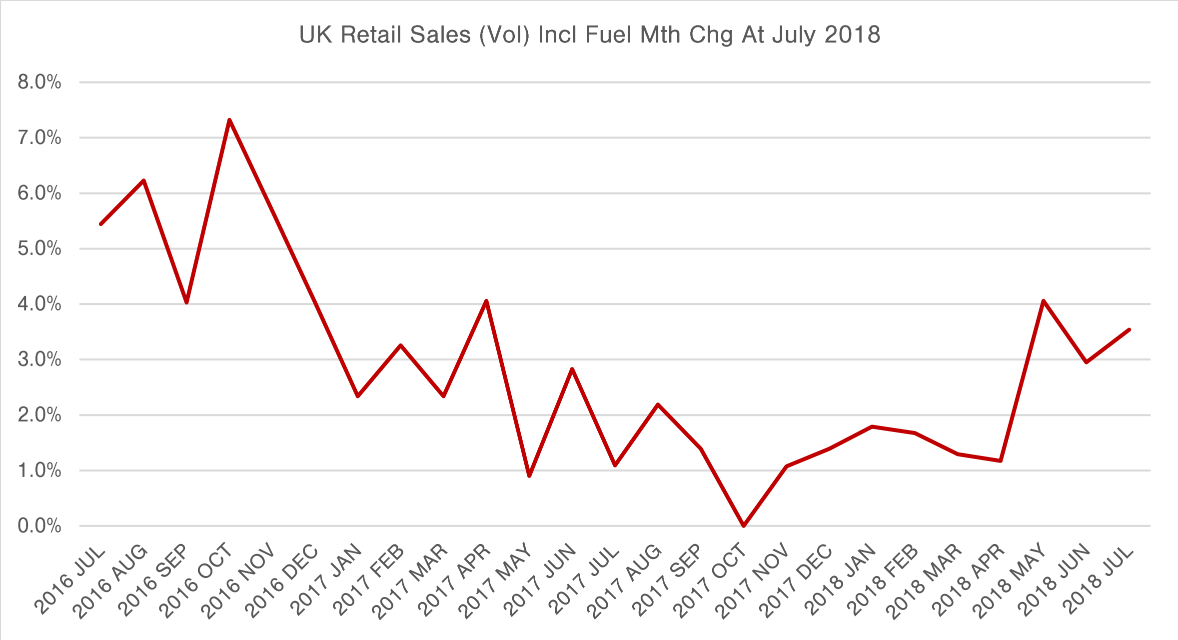
https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/july2018

UK Retail Sales (first estimate - Jul)

An overall stronger result for July retail sales (vol);

July +0.7% versus June +0.5% (first est for June had been reported at -0.5%)

The annual rate of growth accelerated from +2.9% in June to +3.5% in July. Annual growth in July 2017 was +1.1%.



The trend overall appears to be positive. These comments from the ONS regarding the shift to online are important;

> "Many consumers stayed away from some high street stores in July, but online sales were very strong, supported by several retailers launching promotions. Food sales remained robust as people continued to enjoy the World Cup and the sunshine."

All categories contributed to growth in the last year. But in the latest month, Petrol Stations detracted from vol growth (petrol prices increased +11.9% on the year) and Food Store retail made no contribution. From the ONS;

> "In contrast, many retailers in the non-food stores sector reported a reduction in footfall, despite its positive contribution to growth due to its large weight to total retail"

Great Britain (July 2018 compared with June 2018)

Figure 3: Contributions to month-on-month growth in the quantity bought and amount spent in the four main retail sectors

Great Britain (July 2018 compared with June 2018)

https://www.ons.gov.uk/businessindustryandtrade/retailindustry/bulletins/retailsales/july2018

UK Labour Market – Apr-June

In the latest quarterly estimate, UK employment growth has slowed. But unemployment growth has also slowed – because there has been a large decline in participation.

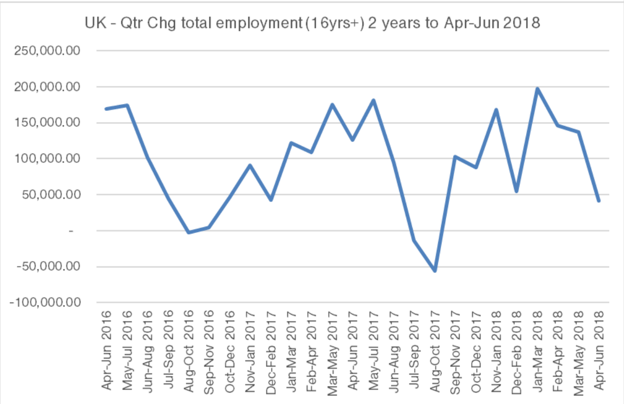
Below provides a quick snapshot; in the latest quarter Apr-Jun, employment growth was lower than the est change in the labour force due to population growth, which meant that unemployment probably 'should' have increased. But because so many people left the labour force, total unemployment continued to decline;

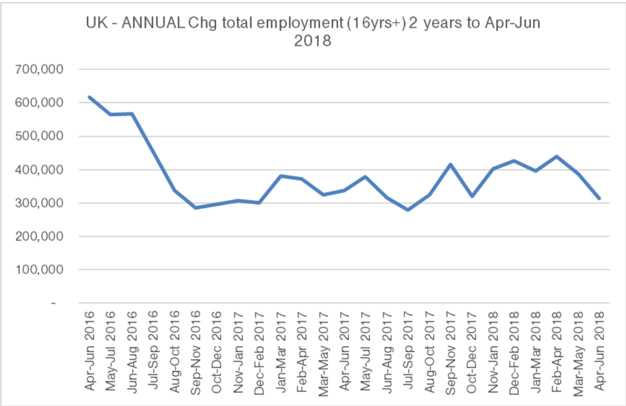
	16yrs+ (000's Persons)	
	Latest Qtr Chg Apr-Jun 2018	ANN Chg Apr-Jun 2018
Estimated change on the Labour Force due to pop growth	48	193
How many jobs available for them? (employment growth)	42	313
Difference (is employment growing faster than population?)	-7	119
How many people left the labour force (change in participation)?	-71	-5
The remainder is the reduction in total unemployed persons	-65	-124
Double check - change in total economically active	-23	189
Double check - change in total economically active	-23	189

The report in a bit more detail....

Total in employment; +42k of which most of the growth was in the 65yrs+ age group; +7k were 16-64yrs and +35k were +65yrs+.

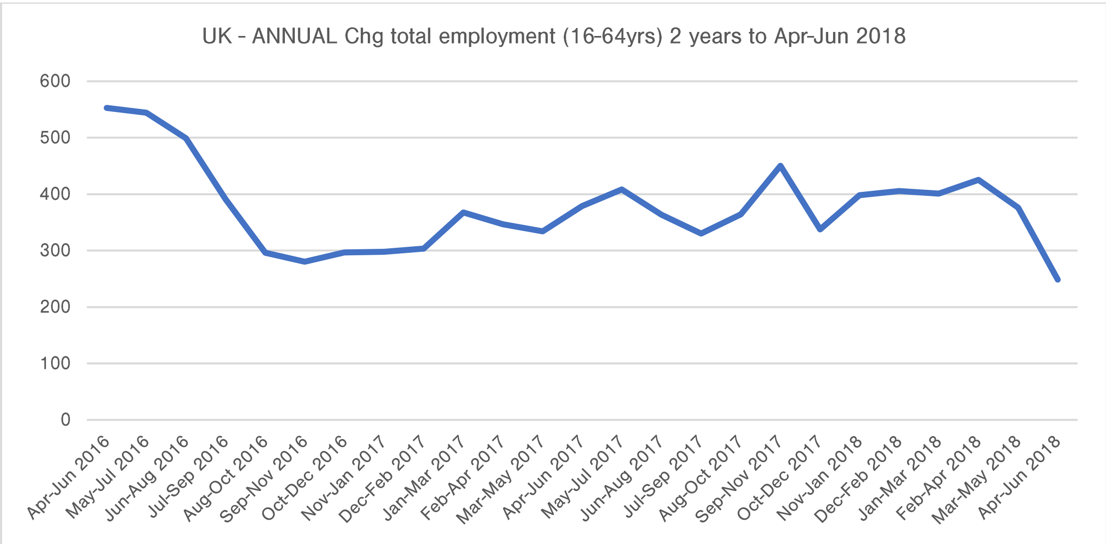
The quarterly growth in employment has been slowing, which is starting to feed into slower annual growth;





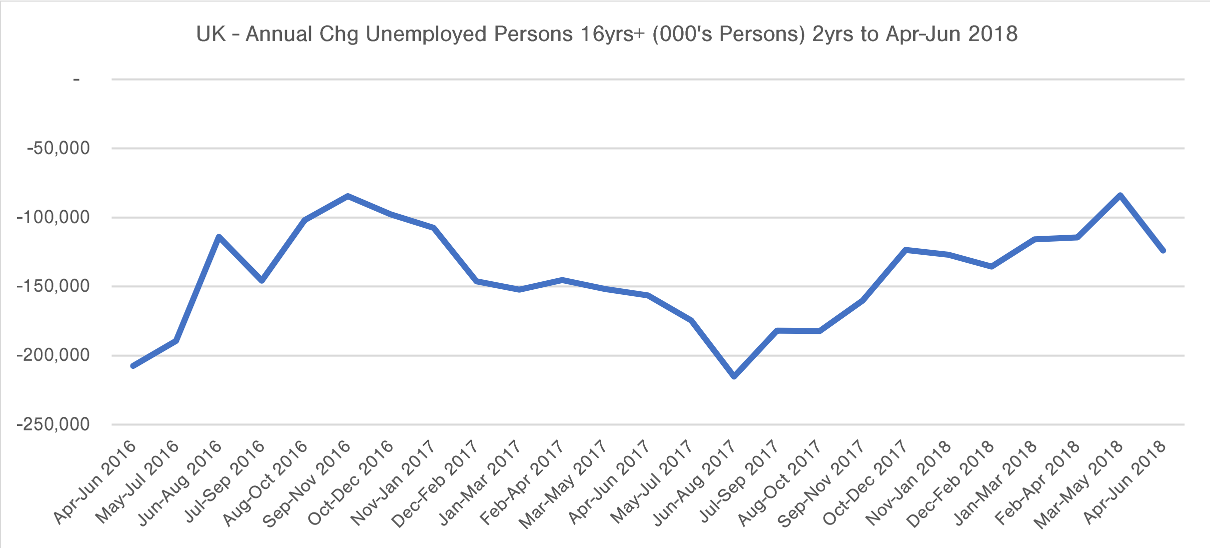
Annual employment growth has slowed to 312k persons in the latest quarter, below the 2-year average of 380k persons and well off the highs from two years ago.

The trend for employment growth looks worse if you restrict the data to 16-64yrs;



The annual level of employment growth 16-64yrs has slowed from +401k persons in Feb-Apr 2018 to +249k persons in Apr-Jun 2018.

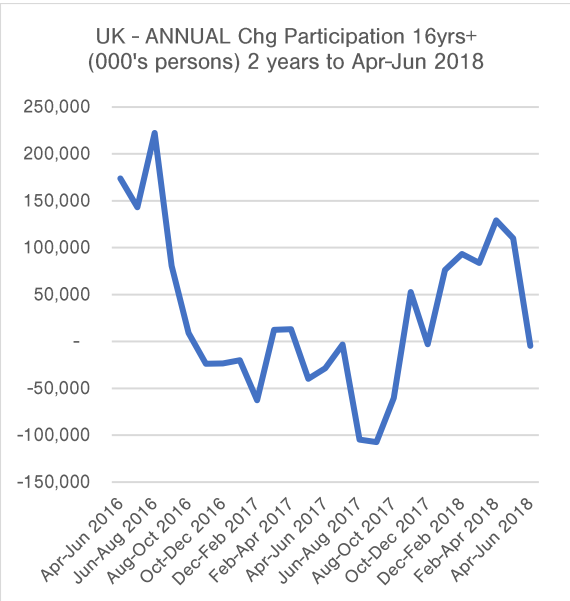
Total unemployed persons have continued to decline, now at a faster rate even on an annual basis. In the latest quarter, those unemployed 16yrs+ declined by 65k persons, most of which were 16-64yrs. In the year, total unemployed persons have declined by 124k persons of which 122k are aged 16-64yrs. These look like great numbers but it doesn't make much sense when you consider that employment growth has slowed.

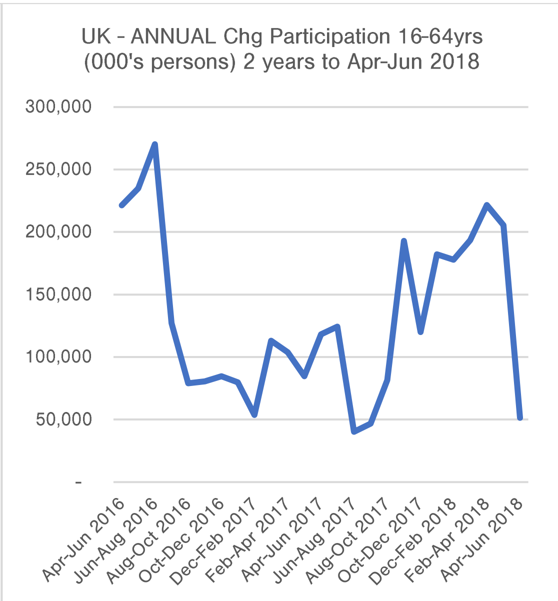


The only way this math works is if participation changes.

Participation; In the latest quarter, 71k persons aged 16yrs+ left the labour market. Again, if you restrict this to 16-64yrs, 72k persons left the labour force. Which means that 1k persons aged 65yrs+ came back into the labour force.

The latest quarterly changes in participation are showing up in the annual changes in participation;





For the moment, the slower increase in participation is keeping the unemployment growth level negative.

https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/uklabourmarket/august2018

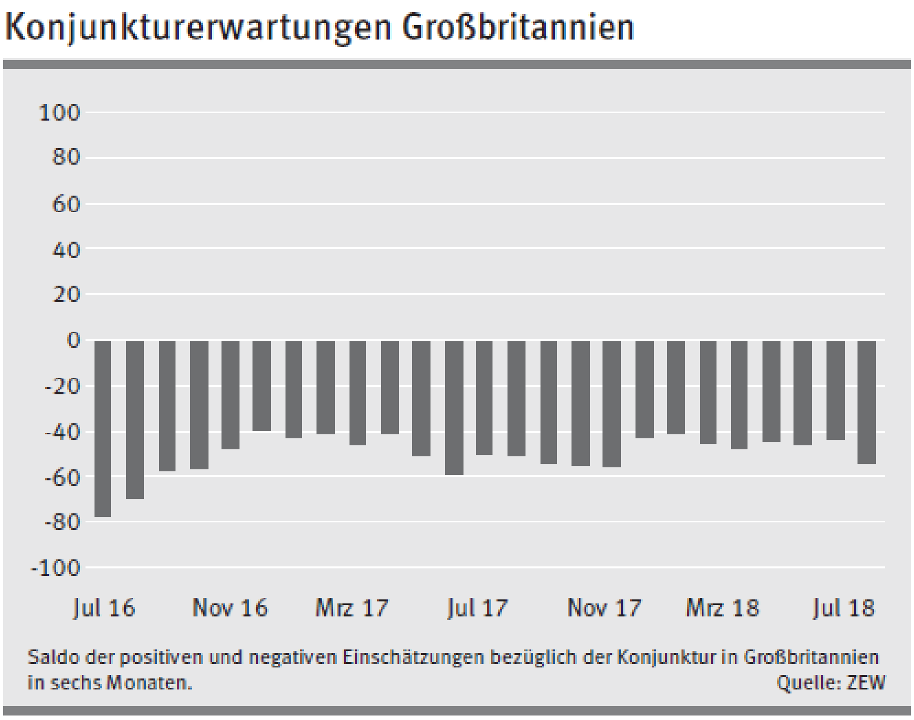
UK - The Zew Financial Market Report - Covers the period 25 June to 9 July 2018

The period of this sentiment reading was taken when the UK government released its Brexit Chequers plan and several high-profile government ministers resigned.

There is less divergence between the assessment of the current situation and economic expectations.

The assessment of the current economic situation worsened, falling 3.2pts to a reading of -9pts. This was different to other country results as there was a large change in respondent assessments shifting from 'normal' to 'less'. There is a much higher proportion of respondents that assess the current situation as 'less' 20.7% and only 11% assess the current situation as 'good'. The only country with a worse reading is Italy.

Economic expectations in the UK - the headline; "Economic expectations worsened significantly"



The economic expectations survey indicator fell to -53.6pts.

http://ftp.zew.de/pub/zew-docs/frep/082018.pdf

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Canada

CPI July

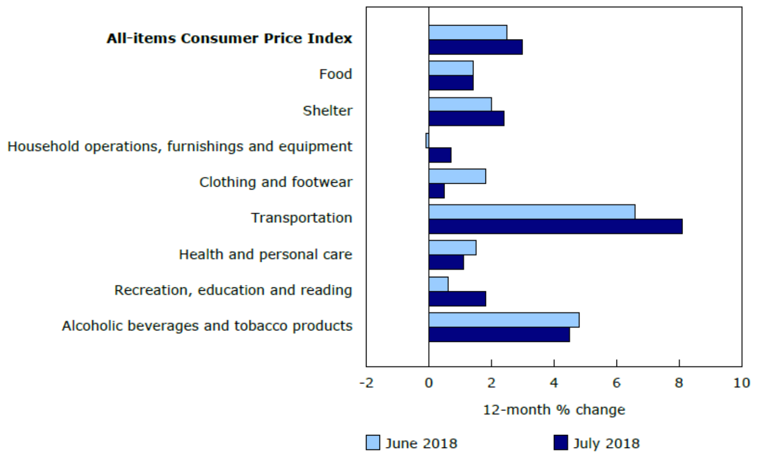
There was a large acceleration in headline CPI growth in July.

Latest month; July +0.5% versus June +0.2%

Annual rate; July +3% versus June +2.5%

There are several contributors to the acceleration in CPI growth;

Chart 2
Consumer prices increase in all major components



Source(s): Table 18-10-0004-01.

Annual; transportation +8.1%, gasoline +25.4% and alcoholic bevs & tobacco +4.5%, overall energy costs +14.2% and non-durable goods +4.4%

Latest month; transport +1.1%, of which gasoline +0.8%, recreation/education/reading +2%, overall services +1.1% and energy costs +1%.

The Bank of Canada has several measures of core inflation – all of which show very little change in underlying CPI growth;

Consumer Price Index (CPI) statistics, measures of core inflation and other related statistics - Bank of Canada definitions
Monthly
Table: 18-10-0256-01 (formerly CANSIM 326-0023)

	Canada				
Alternative measures - Core Inflation, Annual	**Mar-18**	**Apr-18**	**May-18**	**Jun-18**	**Jul-18**
factor model, CPI-common	1.90	1.90	1.90	1.90	1.90
weighted median approach, CPI-median	2.00	2.00	2.00	2.00	2.00
trimmed mean approach, CPI-trim	2.00	2.10	1.90	2.00	2.10

https://www150.statcan.gc.ca/n1/daily-quotidien/180817/dq180817a-eng.htm?HPA=1

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Australia

Australia – Wage Price Index (Q2)

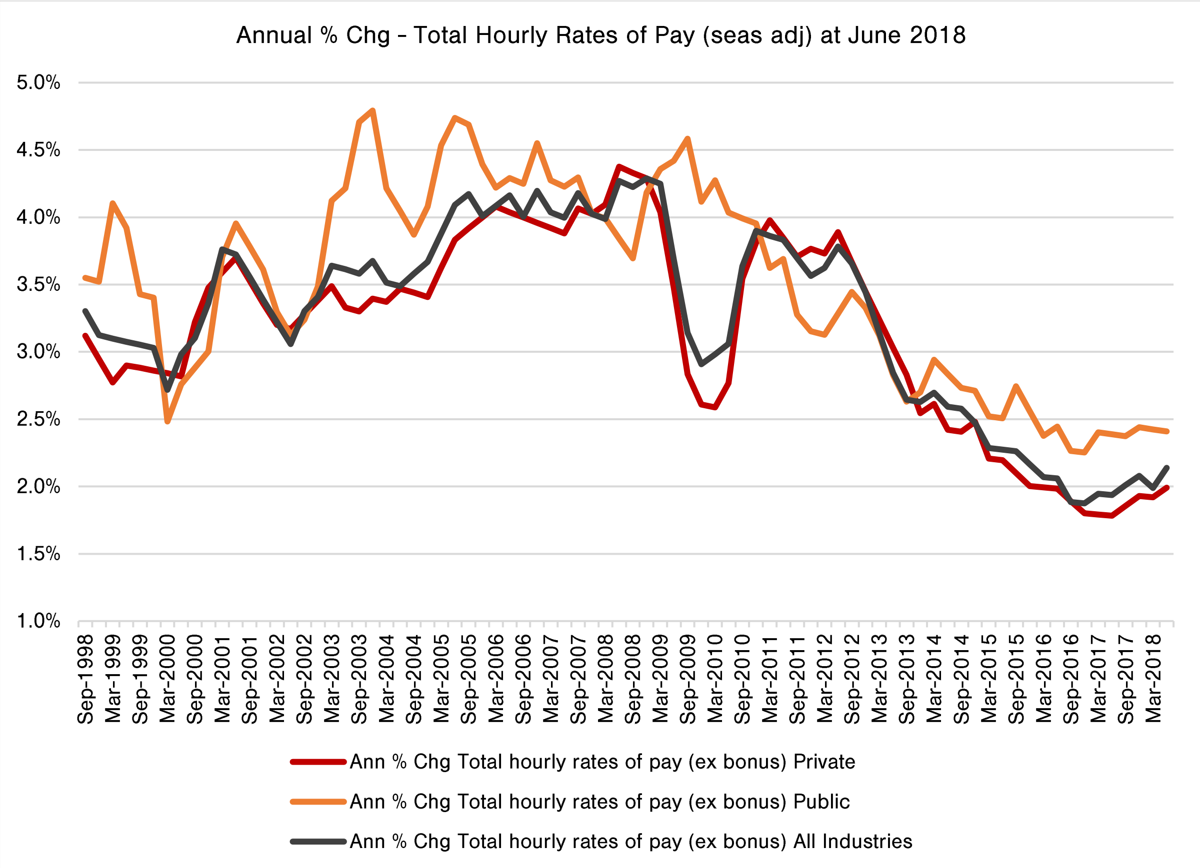
On a seasonally adjusted basis, growth of the wage price index accelerated in the latest quarter across the private sector. The changes are small (using a second decimal place), but the shift in the annual trend is positive.

<u>Quarterly all industries total hourly rates of pay</u>; Q2 +0.62% (the highest growth since March 2014) versus Q1 +0.47%.

Private sector hourly rates of pay; Q2 +0.55% versus Q1 +0.47%

Public sector hourly rates of pay; Q2 +0.61% versus Q1 +0.61%

<u>Annual all industries total hourly rates of pay</u>; at Q2 +2.14% accelerating from the annual rate at Q1 +1.99%.



If you look at the data on a 'trend' basis, then it isn't as positive in the latest quarter, but the general shape of the trend is similar.

RBA Governor Lowe – "we aren't likely to hit our inflation target if wages don't rise".

http://www.abs.gov.au/AUSSTATS/abs@.nsf/Latestproducts/6345.0Main%20Features2Jun%202018?opendocument&tabname=Summary&prodno=6345.0&issue=Jun%202018&num=&view=

Australia – Labour Market report (Jul)

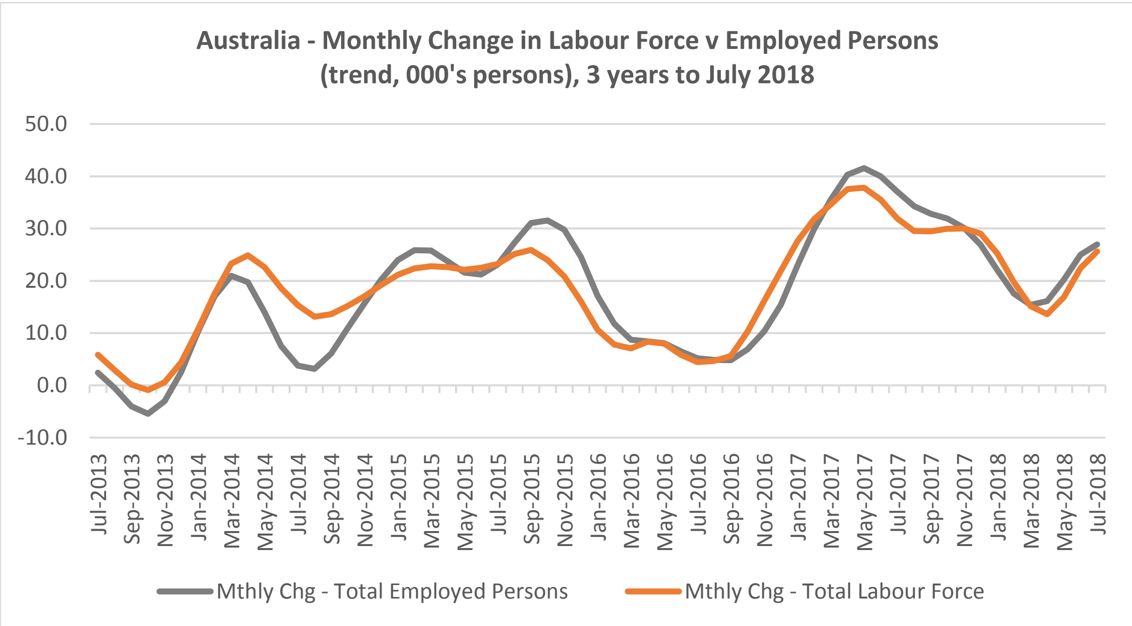
The July labour report was good.

Employment growth; a slight acceleration in July; +27k persons versus June +25k persons (the seasonally adjusted data has a decline of 3k employed persons for the month).

Most of the employment growth in the month was FT in nature; FT +18.2k persons and PT +8.8k persons.

The current annual rate of employment growth is +300k persons which is well above the 10-year average for July of +182k persons.

Employment grew only slightly faster than the labour force in July, which means there was only a small reduction in total unemployed persons;



Unemployed persons declined at a slightly slower pace; July -1.3k persons versus June -2.6k persons.

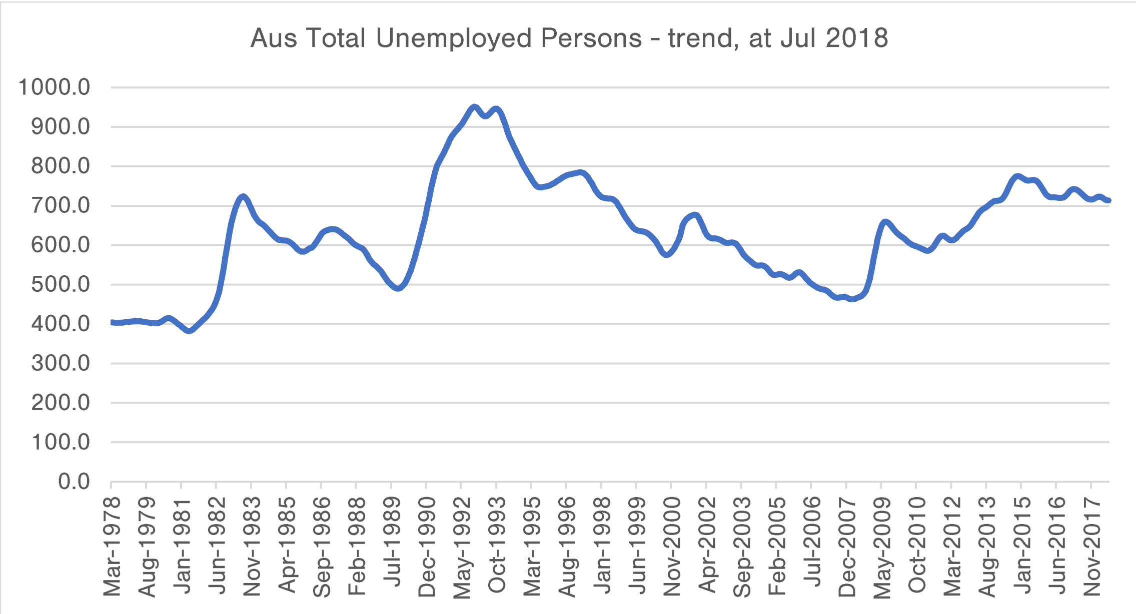
The current unemployment rate; seas adjusted 5.3%, trend 5.4% (unchanged)

The annual change in unemployed persons; July -12.6k persons. The 10-year average change in unemployed persons for July is +24.3k persons, so the current small decline is still good by historical standards. The real issue is that given strong employment growth, why hasn't unemployment fallen further?

The overall reason for the smaller change in unemployed persons is the increase in participation. Over the last year, participation has increased by +0.335%pts or +68k persons have come into the labour force (52k female). The table below summarizes (and simplifies) the interaction among the main labour market aggregates over the last year:

				Annual chg 000's people - July 2018
The estimated change in the Labour Force due to pop growth				218.497
How many jobs available for them? (employment growth)				299.192
	Difference (employment growing faster than pop est)			-80.696
How many people came back into the Labour Force? (chg in part rate)				68.056
The reminder is the reduction in total unemployed persons				-12.639

Despite recent record high employment growth, the total number of unemployed people remains stubbornly high;



Note: Reporting here uses the trend series, so is slightly different to seasonally adjusted data – the ABS recommend using the trend data, but seasonally adjusted is what ends up being reported in the media.

http://www.abs.gov.au/AUSSTATS/abs@.nsf/ProductsbyCatalogue/3AE3C968A8A9CC98CA2582CE00152220?OpenDocument

RBA Lowe Speech – Opening Statement to the House of Reps Standing Committee on Economics

Global outlook – remains positive, but risks have increased. Key uncertainties; escalation in trade tensions, a larger then expected increase in US inflation (sizeable fiscal stimulus while low spare capacity) – possibility that US Fed will need to withdraw accommodations faster, with disruptive consequences for fin markets (ie rising rates). Country specific issues – EM's as a source of potential stress in global financial markets.

Housing Market and HH debt – prices in Syd and Melb slowing, despite concerning some, the slowdown is a shift from an unsustainable trend. Credit is slowing as a result of tighter lending criteria.

Wages – while there has been an uptick in the latest data, changes are likely to be gradual. Wont see a return to higher inflation (to within the RBA band) until wages growth starts to pick up. Still spare capacity in the labour market, higher wage growth will be gradual.

Inflation – remains at the lower end of the band, while core measures are just outside of the 2-3% range. Inflation expected to move gradually into the range over the next few years. Likely to slow in the ST due to mandated changes – which the RBA see's as a good thing.

The three things the RBA has focused on in its communication this year;

Things are moving in the right direction.

Next move in rates likely to be an increase, not a decrease, but not for a while. Likely when we start to see faster growth in incomes/wages.

> "It is important to remember, though, that higher interest rates will be accompanied by faster growth in incomes than we have seen over recent times. In this sense, it will be a sign that things are returning to normal."

Not a strong case for near term rate changes.

https://www.rba.gov.au/speeches/2018/sp-gov-2018-08-17.html

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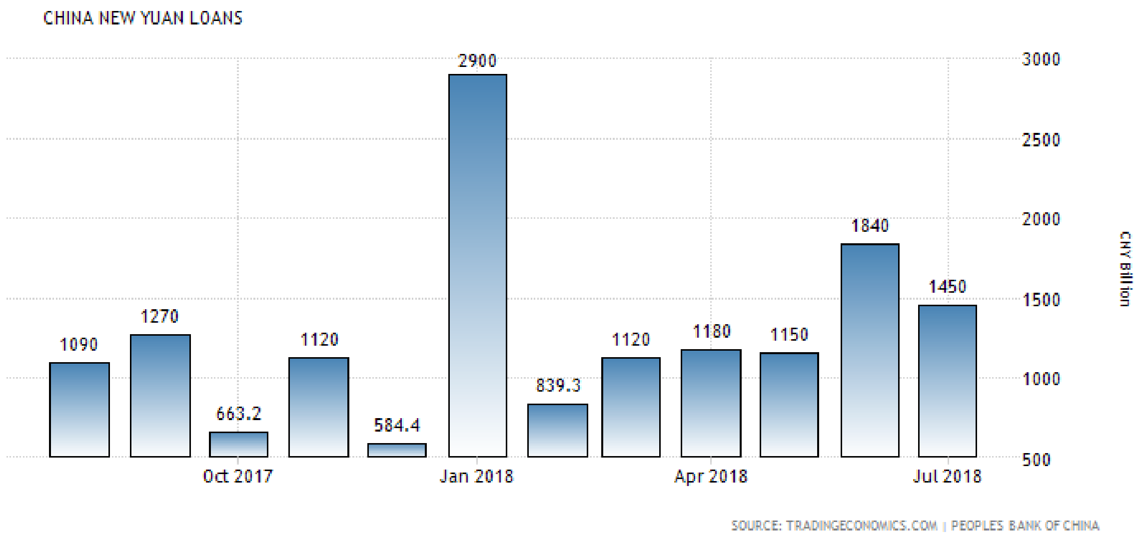
Other

China – New Loans (Jul)

New loans in China grew more than expected;

July +1.45 trillion yuan versus June +1.84 trillion yuan (July 2017 +825 billion yuan)



One of the drivers of higher loans versus last year was due to 'policy support' via PBoC liquidity support, directed lending for small firms and infrastructure and tax cuts.

The total stock of outstanding loans grew by +13.2% in July versus the year prior, accelerating from +12.7% recorded in June. Note according to the National Bureau of Statistics of China, GDP growth is currently running at +6.6%.

Amid the new loan growth has been a reported rise in non-performing loans (NPLS's). Commercial bank NPL's increased to 1.96 trillion yuan at the end of June up from 183 billion yuan at the end of March. The increase was the result of Beijing's crackdown on riskier lending.

Chinese authorities have been focused on reducing leverage of the shadow banking sector, while providing support to the broader economy in the midst of the US-China trade dispute. Total Social Financing (TSF) – the broadest definition of credit and liquidity in China, which includes the shadow banking sector, fell to 1.04 trillion yuan in July versus 1.18 trillion in June. Combined trust loans, entrusted loans and undiscounted bankers' acceptances, which are common forms of shadow banking finance, fell by 488.6 billion yuan in July, following a slide of 1.26 trillion yuan in the first six months.

https://www.reuters.com/article/us-china-economy-loans/china-july-new-loans-stronger-than-expected-money-supply-picks-up-idUSKBN1KY1C8

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Trade

US-China Trade Dispute

The big news this week was the announcement of the resumption of talks between the two countries. The talks will be between the US Vice Treasury Secretary and China Commerce Ministry. The Chinese delegation is to visit the US at the invitation of the US. A firm date has yet to be set but will be during August.

The second tranche of tariffs will go into effect on 23 August. https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/august/ustr-finalizes-second-tranche

Public hearings take place this week for the third tranche of tariffs on approx. $200b worth Chinese products. - https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/august/public-hearings-proposed-section-301

NAFTA

Continued positive news coming out of negotiations this week between US and Mexico - sources familiar with the discussions say the two sides have largely agreed to new rules on auto trade. Latest news is that the US has also withdrawn previous proposals for seasonal curbs on agricultural imports from Mexico.

https://www.reuters.com/article/us-trade-nafta/u-s-drops-agriculture-demand-from-nafta-talks-mexico-farm-lobby-idUSKCN1L40OA

There is more of a sense of urgency for the US and Mexico to finalise a deal by the end of August. That way, the new deal can be approved by the outgoing Mexican president which might be a more favourable outcome than the new Mexican president. The US congressional rules required there be 90 days between the notification of a deal and the signing of an agreement and the new Mexican president is sworn in on 1 December.

Recent comments by President Trump suggest that Canada has been left out of the negotiations;

> “We’re not negotiating with Canada right now,” said Trump, who has frequently complained about Canada’s supply-managed dairy sector.
>
> “Their tariffs are too high, their barriers are too strong, so we’re not even talking to them right now. But we’ll see how that works out. It will only work out to our favour.”

https://business.financialpost.com/news/economy/trump-suggests-canada-has-been-sidelined-from-latest-nafta-negotiations

https://www.politico.com/newsletters/morning-agriculture/2018/08/16/mexico-us-keep-moving-to-wrap-up-nafta-20-319106

BREXIT

No official outcomes from the ‘technical” level talks 16-17 August have been published on the EC’s Brexit Negotiations website at this stage.

Unofficial reports are not positive – that progress is not being made on the important issues of the Irish border.

The next official meeting will be with the key UK and EU negotiators – Dominic Raab and Michel Barnier on Tuesday 21 August.

There is an increasing focus on preparedness for a 'no deal' Brexit - the UK government will commence release of 'no deal' contingency plans starting next Thursday.

https://www.express.co.uk/news/uk/1004586/Brexit-news-UK-EU-negotiations-Northern-Ireland-Republic-border-no-deal-warning

There is a possibility that Brexit will be discussed at an informal summit of EU leaders in Salzburg on 20 Sept.

The Salzburg meeting is 4 weeks before the formal EU summit in Brussels 18 Oct – where it is hoped a deal can be struck. If not then, the next time will be 13/14 EU Council meeting.

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