Weekly Macro Review

w/c 8 October 2018

Key Themes

Inflation reports in the US were somewhat mixed. Growth in producer prices in Aug was higher, due to transport and warehouse prices. The annual core PPI growth remains at its highest level of the last 12months at +2.9%. In September, consumer price growth was slower – with a lower impact from energy prices, but continued pressure from shelter. Annual growth in core CPI remained at 2.2%, while the headline CPI slowed to +2.3%.

An important speech by the NY Fed President/CEO and Vice Chairman of the FOMC – John Williams. The Fed will review its current framework for managing interest rates over the coming months. Will either continue using the current system or go back to the pre-crisis system – possible implications for the value of excess bank reserves held at the Fed. Also, re-iterated that the Fed is nearing the end of the normalization process – less role for forward guidance and a shift away from using the 'neutral' rate benchmark.

European industrial production rebounded in August. But within that, German industrial production continued to decline, albeit to a lesser degree than the prior month.

German CPI reached its highest level in seven years at +2.3% on the back of higher energy prices – core CPI growth remains lower at +1.5%.

Australian housing - new lending for housing continued to fall in Aug. This time, the decline included owner occupier housing credit, notably in the two key states of NSW and to a lesser degree Vic. This data is prior to the out-of-cycle mortgage rate hikes taken by several of the major banks back at the start of September. Auction clearance rates remain at their lows (NSW & Vic). The data suggests further falls in house/apartment prices.

Brexit – at this stage, no further progress has been made on resolving the key issues of the Brexit withdrawal agreement. Unless progress is made over the next few days, its not likely that an additional EU summit will be announced for November. This leaves the final summit for the year in December to present and finalize the agreement ahead of the 29 March 2019 deadline.

It now looks likely that US President Trump and Chinese President Xi will meet on the sidelines of the G20 in late November.

Contents

US Data

PPI (Sep)

The PPI for final demand increased in the latest month, reversing the prior month decline:

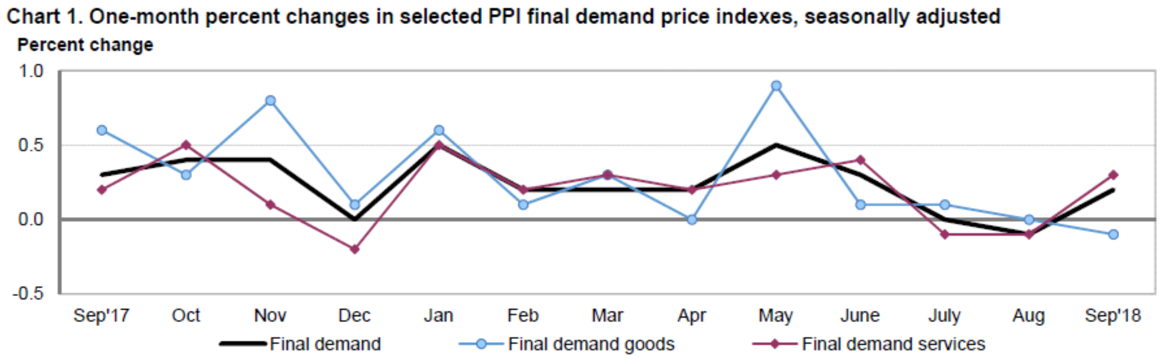
Monthly change; Sep +0.2% versus Aug -0.1%

Annual change slowed slightly; Sep +2.6% versus Aug +2.8%. The goods component slowed to +3.2% and services increased to +2.4%.

"Core" PPI ex food, energy and trade accelerated in the latest month;

Sep +0.4% versus Aug +0.1% - the acceleration was the result of declines in food and energy prices and higher growth in transportation and warehousing prices.

Annual growth in core PPI remains at +2.9% - the highest for last 12 months.



Final demand prices were led high by services;

Services; Sep +0.3% versus Aug -0.1%. In Sept transportation and warehousing services prices accelerated; +1.8% versus -0.6% in Aug.

Goods; Sep -0.1% versus Aug 0%. Both food and energy prices declined in the latest month.

Intermediate demand;

Processed goods for intermediate demand was again unchanged in the latest month; Sep 0% versus Aug 0%. Foods and feed and energy goods declined in the latest month. The 12mth change slowed to +5.8% (from +6.3% in Aug).

Unprocessed goods for intermediate demand partly reversed last months' declines; Sep +1.7% versus Aug -5.8%. The annual rate accelerated to +4.3%. Food stuffs and feed stuffs and energy materials grew in the latest month.

Services for intermediate demand accelerated higher; Sep +0.5% versus Aug +0.1%. The annual rate accelerated to +3.3%. Trade and transportation and warehousing all increased in the latest month.

https://www.bls.gov/news.release/pdf/ppi.pdf

US CPI (Sep)

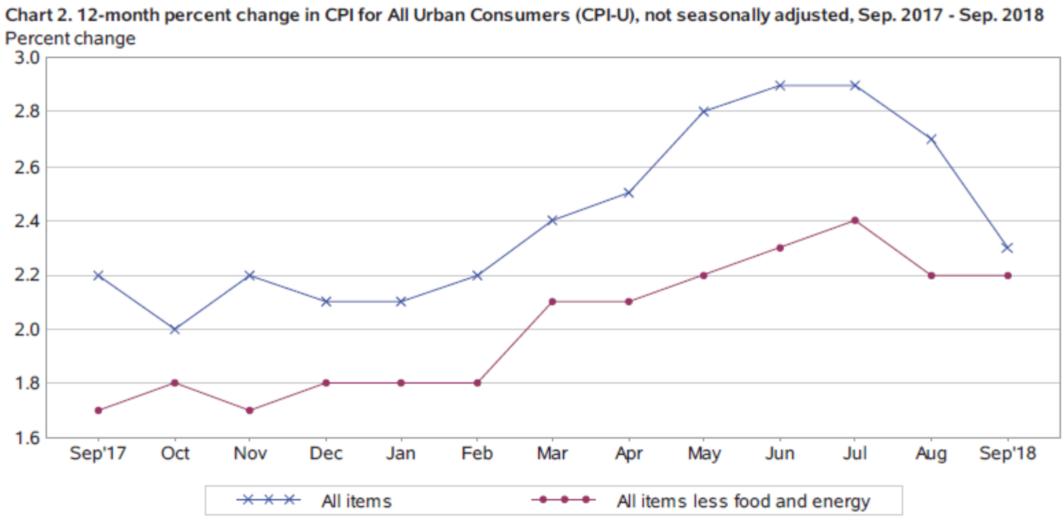
Growth in the headline CPI was lower in the latest month and lower on an annual basis;

Headline CPI: Sep +0.1% versus Aug +0.2%

Annual growth in headline CPI +2.3%, slowing from +2.7% in Aug

Core CPI ex food and energy grew at a constant pace in the month; Sep +0.1% versus Aug +0.1%

Annual growth in core CPI in Sep was +2.2% versus +2.2% in Aug – headline and core CPI growth are almost on par.



The main contributors to the slower growth in headline CPI were;

Energy; In Aug, growth in energy prices contributed over 30% of the increase in CPI, but in Sep only contributed 17% of the increase. Energy prices declined by -0.5% in Sep after +1.9% in Aug.

Growth in food prices slowed from +0.1% in Aug to 0% in Sep, and contributed approx. 7% of the increase in the index (same as last month)

Looking at the main components of core CPI;

Commodities less food and energy commodities; despite accounting for 20% of the weight of the index, was responsible for -3% of the change in CPI. The annual change in commodities less energy and food commodities is -0.3%. Growth in the latest month was also -0.3%. In the latest month, used cars and trucks made the largest negative contribution

Services less energy services; accounts for 60% of the CPI by weight and contributed 77% of the increase in the CPI in latest month (last month it was 65% of the increase). Annual growth +3%. Shelter and transportation services were the two main contributors.

> Shelter accounts for 32% of the total CPI index weight and contributed nearly 50% of the increase for the month on its own. Annual growth of +3.3%.
>
> Transportation services is a smaller part of the index (6% weight) and growing at 4% annual, well above the headline annual rate.

https://www.bls.gov/cpi/

US Wholesale Trade and Inventories (Aug)

Wholesale sales and inventories both grew at an accelerated rate in the latest month. Wholesale sales were higher across some of the larger durable goods categories, while inventories were higher mostly due to automotive.

Wholesale sales

Aug +0.8% versus Jul +0.2%

Wholesale sales of durable goods for Aug +1.3% - professional equipment, electrical and machinery (to a lesser degree) all contributed to the higher growth. Non-durable goods grew by +0.5% - half of that value growth was due to petroleum.

Inventories

Growth in inventories increased; Aug +1% versus Jul +0.6%. At the total level though, the inventory to sales ratio remained unchanged between Aug and Jul: both 1.26 days.

About one third of the of the overall growth in inventories was due to automotive, which grew by 3.5% in Aug versus -1.6% in Jul. This could possibly be some restocking, but Aug growth of wholesale sales of automotive underperformed (compared to total wholesale trade); Aug +0.2%. The other telling signal was the inventory to sales ratio for automotive increased from Jul 1.53 days to 1.58 days in Aug – but this is still well below Aug 2017 of 1.65 days.

There were two other notable increase in inventories; Drugs and Farm Products. The inventory to sales ratio for drugs increased slightly to 1.09 days. The inventory to sales ratio for farm products increased by a larger amount; from 1.33 days in Jul to 1.41 days in Aug (1.32 days in Aug 2017). Wholesale sales of farm products declined by -1.7% in Aug versus -2.6% in Jul.

https://www.census.gov/wholesale/index.html

US Fed Speeches

NY Fed President and CEO and Vice Chairman of the FOMC John Williams – Moving Toward 'Normal' US Monetary Policy

Several important points from this speech.

The first, is that the Fed will be looking at its operating framework for managing interest rates in the coming months;

Normalization in relation to the Fed balance sheet – will shrink the balance sheet, envisage that the asset side of the balance sheet will consist primarily of treasuries.

> "That's our strategy, but its execution will depend on the operating framework of monetary policy, among other factors."

Two choices for the Fed in relation to operation of monetary policy;

1. Return to a system similar to that of before the crisis – supply of reserves were kept scarce and the interest rate was set by adjusting those reserves via open market operations.

OR

2. Continue with the current system whereby reserves are abundant and the FFR target is achieved via administered rates (IOER and O/N RRP)

[Currently the Fed sets a target range for the FFR – the ceiling rate/upper bound of the range is the rate for interest on excess reserves (IOER) for banks and the floor rate/lower bound of the range is the O/N RRP rate, the facility which is open to a wider range of counterparties. The IOER was recently tweaked and set 5bps below the upper end of the FFR target range.]

> "The second system is working well, is easy to communicate and adaptable"

> "The Fed will be looking closely at these options in the coming months and will subsequently make a decision on the future operating framework"

Some further reading; http://libertystreeteconomics.newyorkfed.org/2017/09/why-pay-interest-on-excess-reserve-balances.html

As of the end of Aug, the total reserve balances maintained at the Fed totalled US$1.9t (H.3), down from the peak of $2.7t in Sep 2014.

The use of the O/N RRP facility has been declining significantly through 2018.

The second, which re-iterated the points from the latest FOMC statement, is that the Fed believes that it is close to reaching 'nomalized' monetary policy;

The Fed has been 'slimming' its statements, using less forward guidance about future path of policy. This doesn't signify a shift in policy approach. The changes in communication;

> "are a sign that we are nearing the end of the process of normalizing monetary policy and are inching closer to conducting normal monetary policy."

"Normal policy" - The policy process wont change, but the communication will. Forward guidance not as useful as rates start going up. When rates were closer to zero, it was clear that the most likely direction for rates would be up (based on some set conditions). As rates move to higher levels, the future direction of rates won't always be as clear (could be either up or down), hence forward guidance about the future path of policy will not be appropriate.

Also start to shift away from the 'neutral' rate benchmark – more useful for direction when rates were very close to zero.

https://www.newyorkfed.org/newsevents/speeches/2018/wil181009

Return to top

Europe

Eurozone Industrial Production (Aug)

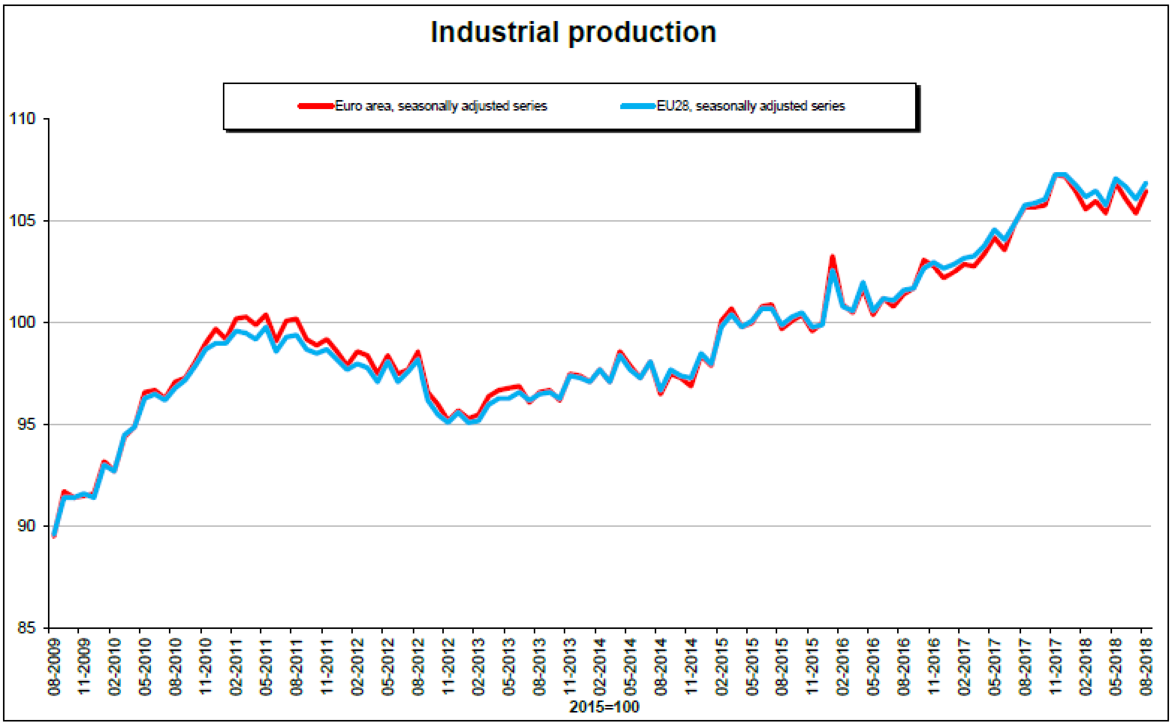
There was a welcomed rebound in Eurozone industrial production in August;

The core EA19 group; Aug +1% versus Jul -0.7%

Annual growth in industrial production increased to +0.9% in Aug, up from +0.3% in Jul – back in Mar2018 annual growth in industrial production was +3.2%. On an annual basis, industrial production in intermediate goods, energy and durable consumer goods is still negative.

The broader EU28 group; Aug +0.8% versus Jul -0.6%

Annual growth in industrial production increased to +1.2% in Aug versus +1% in Jul. In mar 2018, annual growth in industrial production was 3%.



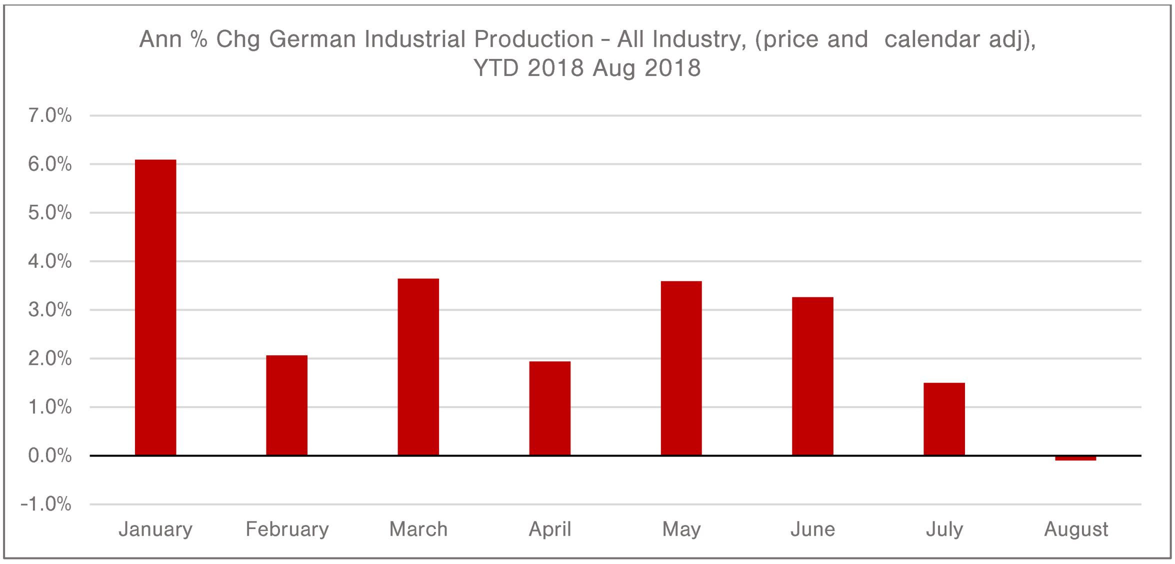
https://ec.europa.eu/eurostat/documents/2995521/9298852/4-12102018-AP-EN.pdf/7a4a12eb-8d24-4e1e-96b4-e39a32d6784d

German Industrial Production (Provisional - Aug)

The index of production in manufacturing in Germany, declined again in the latest month, but not to the same degree as the month prior;

Aug -0.3% versus Jul -1.3% (revised lower from the provisional result of -1.1%)

On an annual basis (current month versus the same month prior year), growth in industrial production has been slowing and declined by 0.1% Aug;



Key areas:

Production in industry excluding energy and construction; Aug -0.1% versus Jul -1.9%. Annual -0.7%

Within industry, production of capital goods; Aug -0.7% versus Jul -2.5%. Annual; -3.1%

Production of consumer goods; Aug +1.4% versus Jul -0.7%. Annual: +6%

Production of intermediate goods; Aug +0.1% versus Jul -1.6%. Annual -0.9%

Production in construction; Aug -1.8% versus Jul +1.2%. Annual +2.2%

https://www.destatis.de/EN/PressServices/Press/pr/2018/10/PE18_381_421.html

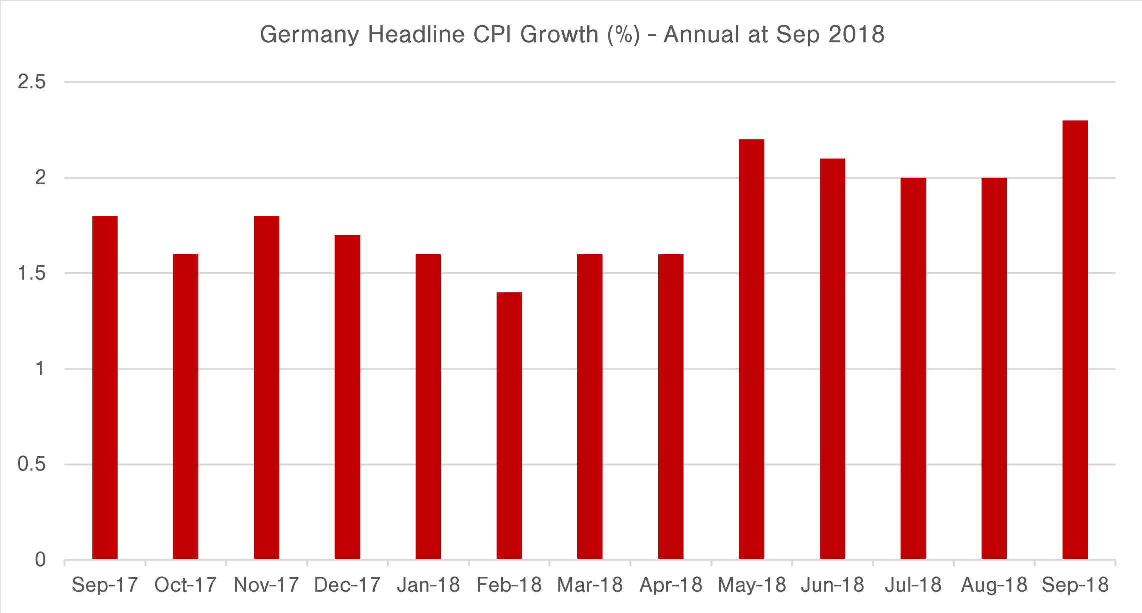
German CPI (Sep)

Consumer price growth accelerated in the latest month;

Monthly headline CPI growth; Sep +0.4% versus Aug +0.1%

Annual headline CPI growth; Sep 2.3% versus Aug +2% (v Sep 2017 +1.8%)

This was the largest increase in consumer prices in the last seven years. Headline CPI is higher due to the growth in prices for energy and goods.



Core CPI (ex food and energy) grew at a slower pace in the month; Sep +0.1% and annual +1.5%.

Energy prices; month change in Sep +2% and annual change at Sep +7.7%.

Goods prices; month change in Sep +1.4% and the annual change at Sep +3.1%. Growth in prices for vegetables, food generally, and clothing & footwear was notably higher in Sep.

Services prices; month change in Sep -0.5% and the annual change +1.5%. Growth in net rents exclusive of heating expense was notably lower growing at +0.1% in Sep and +1.5% annual at Sep.

https://www.destatis.de/EN/PressServices/Press/pr/2018/10/PE18_392_611.html;jsessionid=72DA8A6A2EFE100C574C86B3D3998095.InternetLive1

German Trade Balance (Provisional - Aug)

The provisional German trade balance/surplus increased in Aug versus Jul and narrowed in the YTD 2018 v 2017.

Flows of commodities and services in EUR bn					
Item	August	January to August	July	August	January to August
	2018			2017	

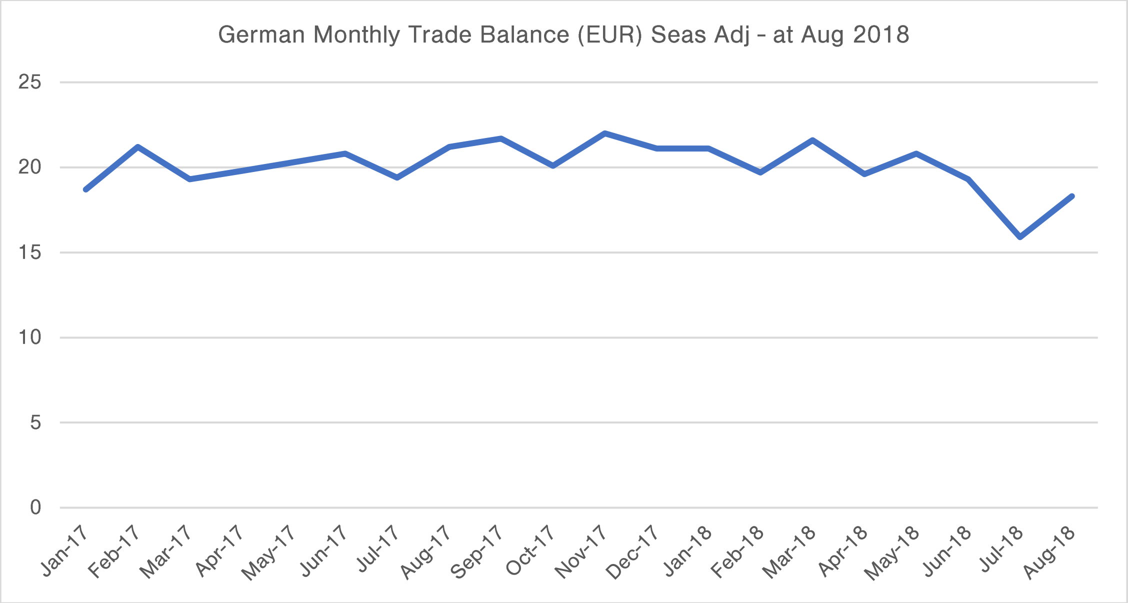
[1] According to calculations of the Deutsche Bundesbank

Foreign trade

Flows of commodities and services in EUR bn					
Item	August	January to August	July	August	January to August
	2018			2017	
1 Exports (f.o.b.)	105.2	879.0	111.0	103.0	843.8
2 Imports (c.i.f.)	88.1	723.1	94.5	83.0	683.7
3 Foreign trade balance (1-2)	**17.2**	**155.9**	**16.5**	20.0	**160.1**
Transition to trade in goods [1]					
4 Supplementary trade items	1.0	14.7	1.9	1.5	15.6
Current account balances [1]					
5 Trade in goods (3+4)	18.2	170.6	18.4	21.5	175.7
6 Services	-5.6	-14.1	-4.3	-5.4	-17.1
7 Primary income	6.5	37.5	5.6	5.2	35.7
8 Secondary income	-3.8	-28.3	-4.7	-3.5	-36.5
Current account (5+6+7+8)	15.3	165.7	15.1	17.8	157.7

Note; data in table is unadjusted

The increase in the trade surplus/balance in the latest month was the result of a larger contraction in imports and a smaller decline in exports. But over the last few months, the trade surplus has become smaller due to imports growing faster than exports;



Exports;

The seasonally adjusted decline in exports for Aug -EUR0.1b versus Jul -EUR2.5b (the unadjusted decline in exports for the month of Aug was -EUR5.8b)

YTD 2018 v YTD 2017 (unadjusted); +4.2%

Imports;

The seasonally adjusted decrease in imports for Aug -EUR2.5b versus Jul +EUR2.5b (unadjusted decline in imports for the month of Aug was -EUR6.4b)

YTD 2018 v YTD 2017 (unadjusted); +5.8%

https://www.destatis.de/EN/PressServices/Press/pr/2018/10/PE18_383_51.html;jsessionid=2CA0E1B0DB4081542D0000217E89DF6A.InternetLive2

Return to top

United Kingdom

Brexit

Despite last minute meetings, there has been no/little progress made on the Brexit withdrawal agreement this week

As tweeted by Michel Barnier (early Monday morning AEST);

> "We met today @DominicRaab and UK negotiating team. Despite intense efforts, some key issues are still open, including the backstop for IE/NI to avoid a hard border. I will debrief the EU27 and @Europarl_EN on the #Brexit negotiations."

Others are reporting that the Irish backstop agreement is 'back to square one'. The UK lead negotiator has returned to the UK.

At the EU summit this week - on 17-18 Oct – it will be decided this week whether enough progress has been made on the withdrawal agreement to schedule the additional EU meeting in November to approve the deal. The decision will be announced on 18 Oct whether to schedule the additional meeting – which would likely be the 17-18 Nov.

Speech by Michel Barnier late last week – at the closing session of Eurochambre's European Parliament of Enterprises 2018

http://europa.eu/rapid/press-release_SPEECH-18-6089_en.htm

BRC Like for Like Retail Sales (Sep)

Weaker overall retail sales result for Sep;

On a like for like basis; Sep 2018 -0.2% versus Sep 2017 +1.9%

On a total basis; Sep 2018 +0.7% versus Sep 2017 +2.3%

Current 3mth average growth; +1.2%

Current 12month average growth; +1.3%

Non-food sales (in-store) continued to disappoint;

On a like for like basis; 3mths to Sep -4.0%

On a total basis; 3mths to Sep -2.7% - the 12mth average -2.7%

Online sales of Non-Food products were higher, but underperformed recent averages;

Sep 2018; +5.4% versus Sep 2017 +10.7%. This is the lowest growth since January 2018.

3-month average +6.7% and 12-month average +7.1%

Online penetration rate increased from 22.7% to 24.2% in Sep 2018

Food sales underperformed compared to the 12mth average;

on a like-for-like basis increased 2.3%

on a total basis - 3.4%. below the 12-month Total average growth of 3.7%

https://home.kpmg.com/uk/en/home/media/press-releases/2018/10/brc-kpmg-retail-sales-monitor-for-the-month-of-september-2018.html

UK Monthly GDP (Aug)

The growth rate so far for the current rolling quarter remains higher than Q2 GDP growth;

Jun-Aug; +0.7% versus Q2 GDP +0.4%

Underlying that data though was a weaker August month result – with GDP growing at 0%. The monthly data is volatile, with the June and July results revised slightly higher.

Table 1: Breakdown of GDP growth rates by month

UK GDP growth, June 2018, July 2018 and August 2018

			Growth (%)
	Jun-18	Jul-18	Aug-18
GDP	0.2%	0.4%	0.0%
Index of Services	0.0%	0.3%	0.0%
Index of Production	0.9%	0.4%	0.2%
Manufacturing	1.0%	0.0%	-0.2%
Construction	0.9%	0.5%	-0.7%
Agriculture	-0.2%	-0.2%	-0.2%

Source: Office for National Statistics

https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpmonthlyestimateuk/august2018

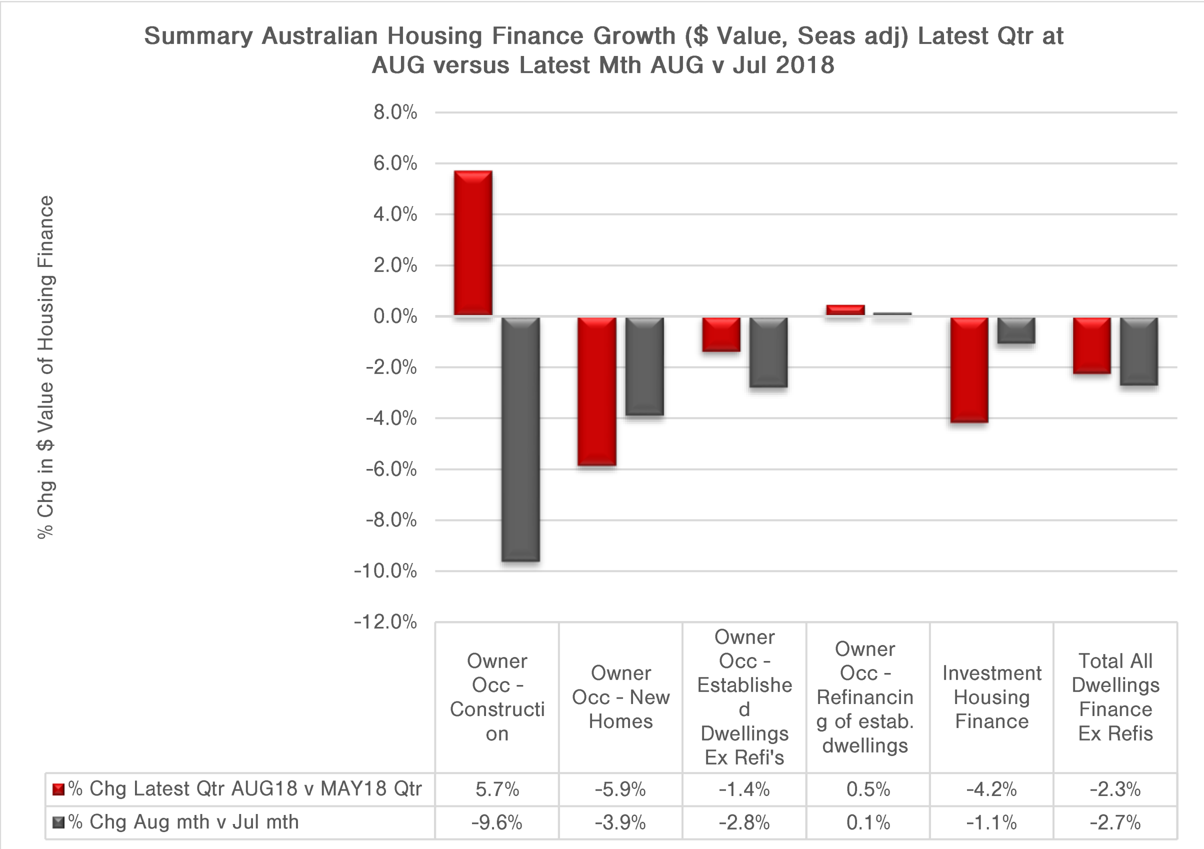
Return to top

Australia

Aus Housing Credit (Aug)

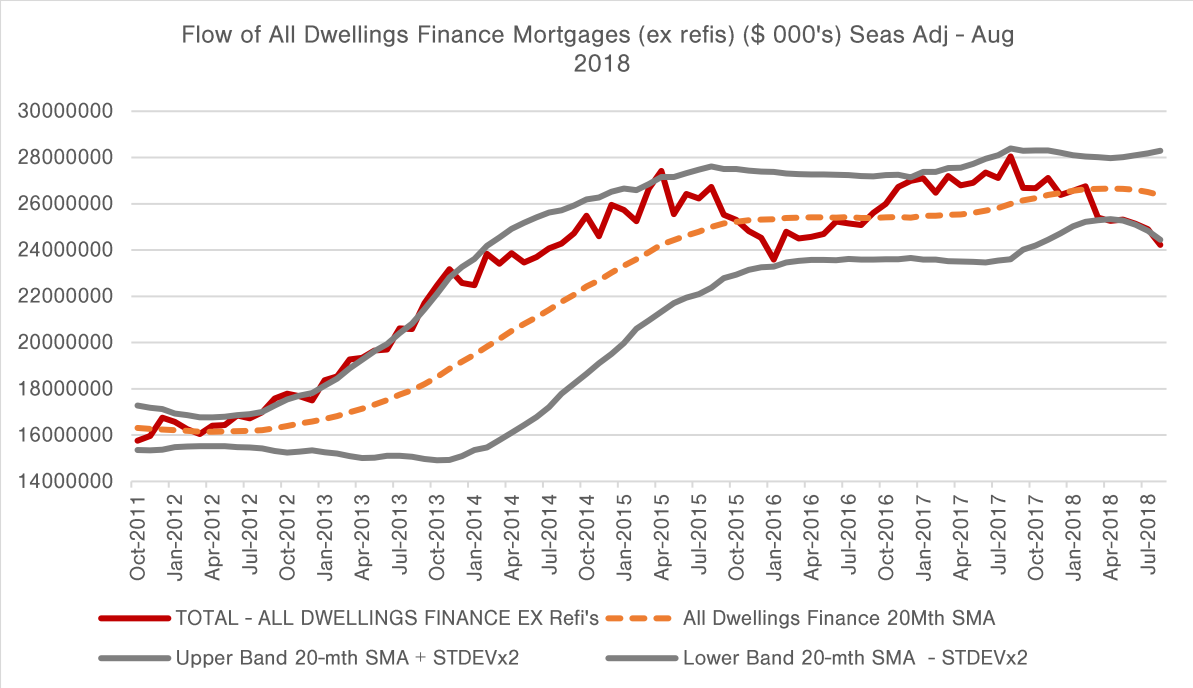
Housing credit continued to decline in the latest month. Whilst the declines <u>had</u> been more focused on investor property lending, this month, there was a larger decline in lending for owner occupiers. <u>Note that this data/report is for the month BEFORE three of the four major banks increased variable mortgages rates out of the RBA cycle.</u>

The following chart perfectly captures the concerning report for August;



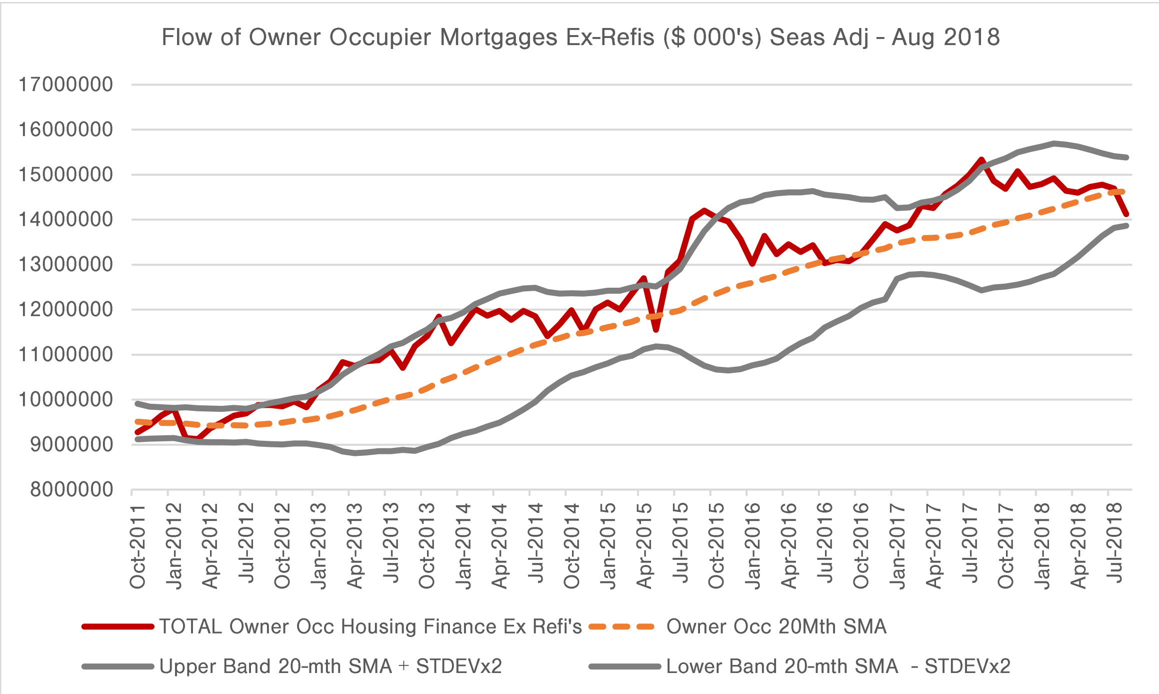
The only increase in the latest month was refinancing of established dwellings.

Th total value of all dwellings finance declined below 2SD's of the 20mthSMA in the latest month;



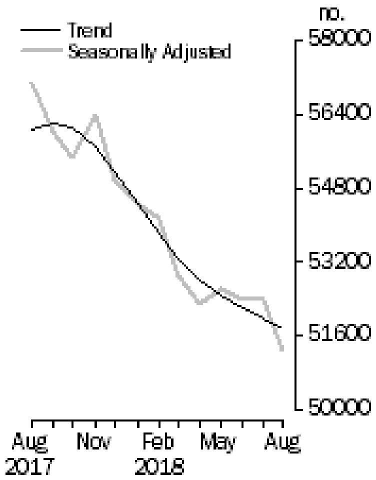
All dwellings finance, ex refi's declined by 2.7% in the month and is 13% below the same month a year ago.

The big declines this month were for owner occupier housing finance. Owner occupiers had been 'holding up' total lending growth (at least growing at the 20mth SMA) until this month;

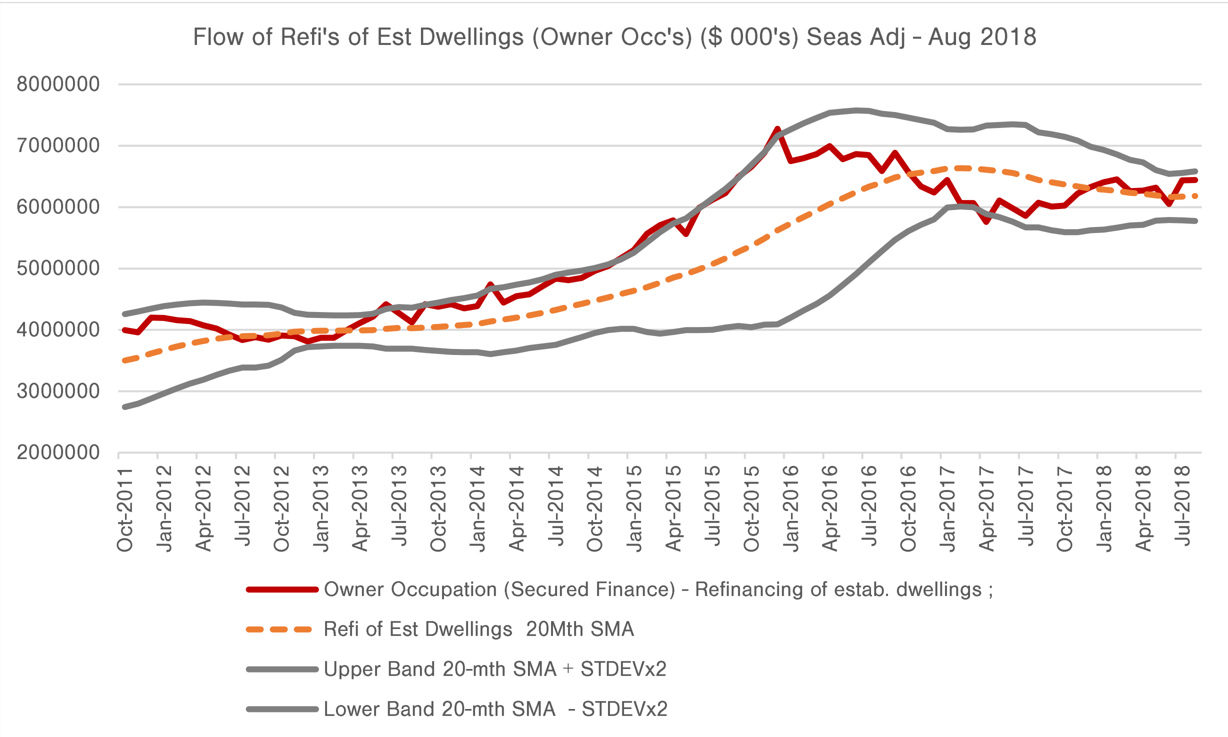


Owner occupier lending (ex refis) declined by 2.7% in the month and is 7.6% down on the same month the year prior.

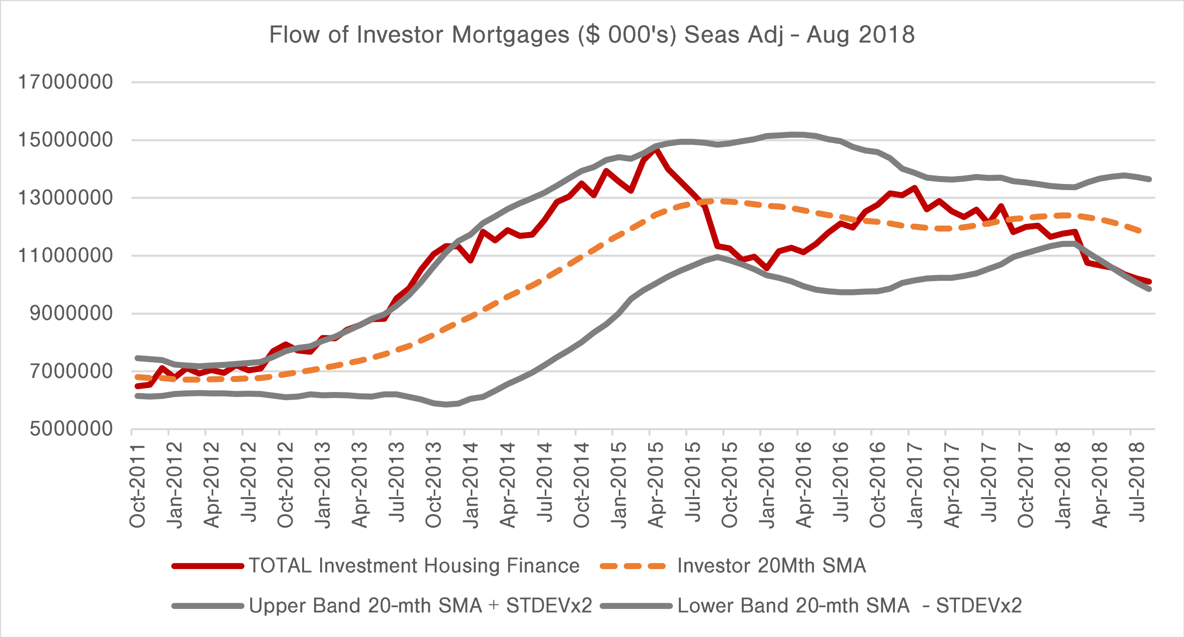
The number of owner occupier dwelling commitments also continues to fall;



Refinancing for owner occupiers has been increasing; +0.1% for the month and up +6% versus the year prior;



Investor lending continues to fall; -1.1% in the month and down 20% on the same month the year prior.

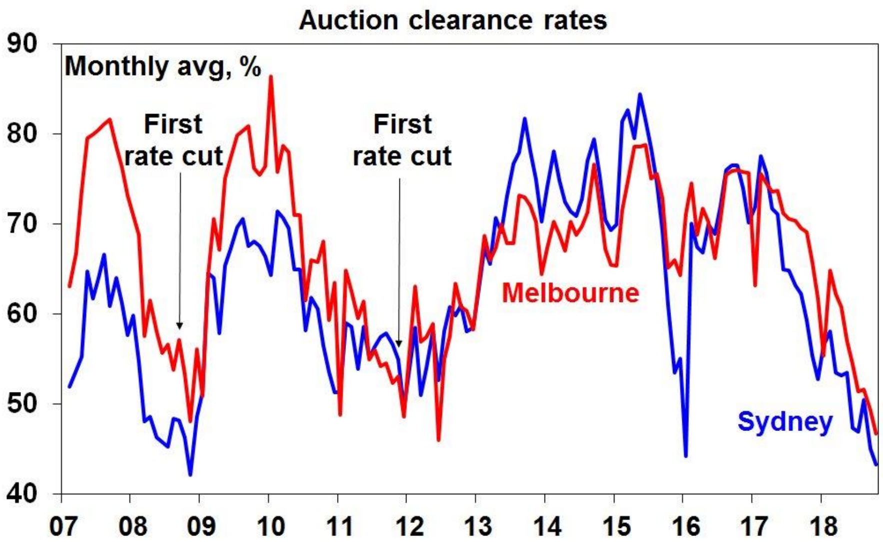


Without growth in new lending finance, house price growth will remain under pressure.

Next month data will be interesting to see the impact of the out-of-cycle mortgage rate increases.

http://www.abs.gov.au/ausstats/abs@.nsf/mf/5609.0?OpenDocument

Auction clearance rates in the key markets of Melbourne and Sydney have been falling and this is consistent with further price falls. Via AMP;



Return to top

China

Exports increased by more than expected in Sep +14.5% (forecast +8.9%) - the fastest pace since Feb 2018. Aug export growth was +9.8%. Front loading shipments and a weaker Yuan may be at play.

> “With global growth likely to cool further in the coming quarters and US tariffs set to become more punishing, the recent resilience of exports is unlikely to be sustained.”

> “China’s politically-sensitive surplus with the U.S. was $34.13 billion in September, surpassing the record of $31.05 billion in August.”

Imports on the other hand slowed further. In Aug imports grew by +14.3% versus +19.9% in Aug.

China has announced it will increase export tax rebates and will cut import tariffs on a range of goods from 1 Nov.

https://www.reuters.com/article/us-china-economy-trade/chinas-september-export-growth-tops-forecasts-surplus-with-u-s-record-high-idUSKCN1MM080

Return to top

Trade

US-China Trade Negotiations

The US Treasury secretary met with the PBoC Governor Yi Gang during the week. It now looks likely that Trump and Xi will meet on the sidelines of the G20 in Buenos Aires in November.

President Trump has again raised the threat of the fourth round of tariffs on $267b of Chinese imports. The worsening trade balance with China in the Sept data probably didn't help.

The latest efforts to restart trade talks comes amid rising tensions between the two countries;

> "The bilateral ties are also deteriorating in other ways. Military talks between the two nations have halted and both sides have blamed the other for a recent close encounter between their warships in the South China Sea."

> "Secretary of State Mike Pompeo exchanged testy words with China's Foreign Minister Wang Yi in Beijing, which risked complicating an anticipated summit meeting between Mr. Trump and North Korean leader Kim Jong Un"

> "a major speech last week in which Vice President Mike Pence outlined a shift in U.S. strategy from engagement to confrontation with China, accusing Beijing of undermining American interests on several fronts, including meddling in U.S. elections."

https://www.wsj.com/articles/trump-and-xi-plan-to-meet-amid-trade-tension-1539266715

USMCA

U.S. officials intend to sign the agreement with Canada and Mexico at the end of November, after which it would be submitted to the U.S. Congress for approval.

The joint statement can be found on the USTR website; https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/september/joint-statement-united-states

US-Japan Trade Talks

Awaiting details now of a schedule/timeline for talks between the US and Japan on a bilateral trade deal.

The US wants to include provisions in all trade deals, including the USMCA, to prevent currency manipulation. This raised some concerns in Japan, with upcoming trade negotiations, as to whether the BoJ could be labelled a currency manipulator.

> "Along with fears of being slapped with higher tariffs on its auto exports to the United States, Japan worries about having its hands tied on addressing sharp yen rises that hurts its export-reliant economy."

https://www.reuters.com/article/us-imf-worldbank-us-japan/us-to-seek-currency-chapters-in-trade-talks-with-japan-others-mnuchin-idUSKCN1MO00W

Section 232 Car and Truck Imports

Awaiting the outcome of the public hearings.

Return to top