MARS CAPITAL PARTNERS

Weekly Macro Review

w/c 5 November 2018

Key Themes

As expected, the FOMC kept rates on hold. There was little change to the accompanying statement. US data out this week confirmed the continued strength of economic activity. Growth in services activity remains close to near term highs and the services PMI grew at a faster pace. JOLTS data pulled back slightly, but job openings and hires remain close to all-time highs. Producer prices for final demand accelerated higher on the back of higher growth in energy, food and services prices.

US consumer credit growth was lower in the current month, but higher overall in the third quarter. Non-revolving credit drove overall consumer credit growth higher on the back of a pick up in both motor vehicle and student loan growth.

The EU has rejected the UK compromise to resolve the Irish border backstop issue – both sides have not agreed on the implementation. There is still some possibility for negotiation, but its becoming unlikely that a deal will be ready in time to call a special EC meeting in Nov. Despite the uncertainty, UK data remains resilient. UK Q3 GDP grew at a faster pace driven by higher export growth and continued growth in household and government consumption. Some underlying signs of growth slowing throughout the quarter. This was also highlighted by the slower growth in the UK services PMI. New orders and some areas of consumer spending were weaker.

German industrial production was somewhat stronger than the manufacturing PMI had suggested – with production growing ahead of last year in the latest month. But slower growth/declines in new manufacturing orders, especially from overseas and the decline in manufacturing turnover were in line with the weaker momentum outlined in the Sep and Oct PMI's.

Mixed data on Japan. Services PMI improved in Oct. The Japanese trade balance improved in the Sep month, but that was due to declining exports and mostly due to a larger slow-down in imports. Slightly different on a quarterly basis as the trade surplus shifted to deficit in Q3 (Yen basis) – export growth slowed and imports grew at a faster rate. Machinery orders for Sep fell very hard – it's also a volatile dataset. Will need to see how industrial output/activity responds in Oct and Nov, given the improvements in PMI's.

The data on Aus housing continues to deteriorate. Overall lending for housing was down 14% from a year ago. The weekly auction clearance rates continue to fall. The RBA kept rates on hold as expected. Despite the likelihood of further falls in house prices, the RBA increased growth projections for 2018/19.

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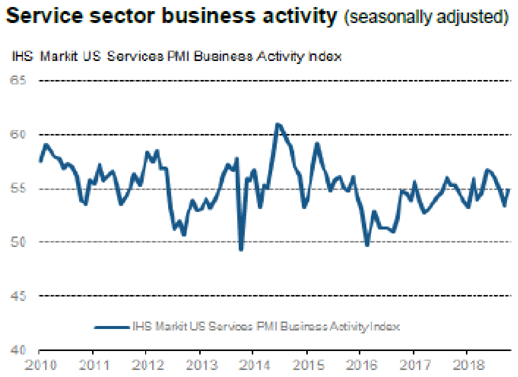
US Data

Services PMI (Oct)

Private sector services activity expanded at a faster rate in the latest month, rebounding from the recent low recorded in Sep;

Oct 54.8 versus Sep 53.5



Source: IHS Markit.

New business/orders expanded at a faster rate, 'above the series LT average and close to the rates seen earlier in the year'.

Employment continued to grow, albeit at a slower rate – reaching a nine-month low. At the same time, order backlogs continued to increase.

Input prices continued to increase, the fastest rate of increase in five years. Input prices, wages and increased borrowing costs were cited.

"Expectations of future business growth spiked higher, suggesting companies are expecting a strong end to the year for the economy"

https://www.markiteconomics.com/Survey/PressRelease.mvc/7402d1264e114708a0663c4d13c11f35

ISM Non-Manufacturing Index (Oct)

The ISM index of non-manufacturing activity continued to expand in the latest month – slowing slightly, but remaining close to the twelve-month high reached in Sep;

Oct 60.3 versus Sep 61.6

Expansion in the business activity index slowed in Oct but remains elevated. There was a shift back to a higher proportion of firms recording lower business activity and slightly less firms recording an increase in business activity.

New orders were little changed at an index reading of 61.5 – remaining at the near term high. Similarly, there was an increase in the number of firms recording a lower level of new orders and declines the proportion of firms recording 'higher' and 'unchanged' levels of new orders.

New export orders remained unchanged at 61 (note that 62% of indicated they either do not perform, or do not separately measure, orders for work outside of the U.S).

Employment expanded, but at a slower pace.

The increase in input prices slowed but remains elevated.

https://www.instituteforsupplymanagement.org/ISMReport/NonMfgROB.cfm?SSO=1

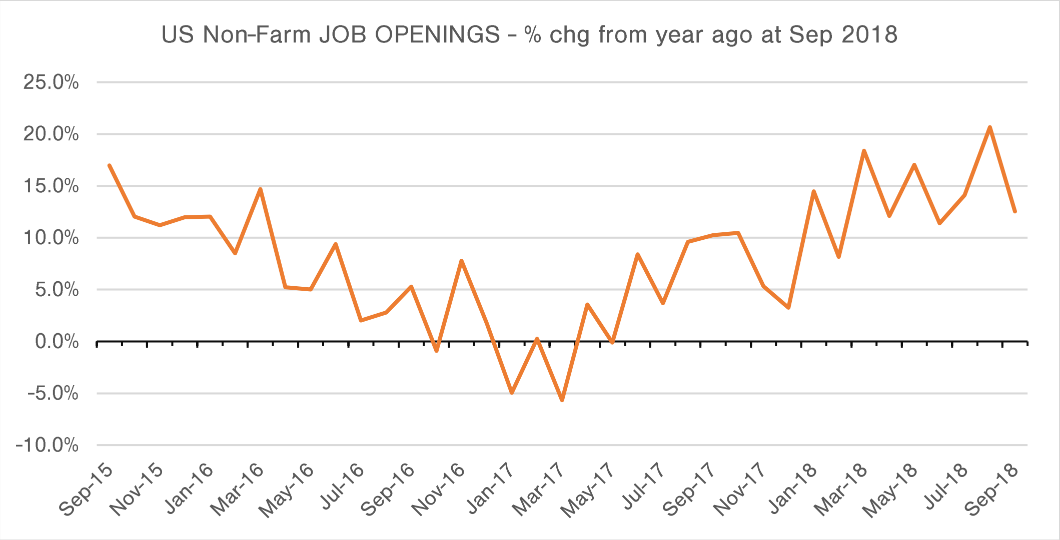
JOLTS (Sep)

There was only a small pullback in the levels of job openings and hires. The level of quits remains close to the series high, while layoffs and discharges remains well below the series high reached in Feb 2009.

Job openings

Sep 7m versus Aug 7.3m (Aug revised higher from 7.13m – Aug remains the series all time high)

The % chg from year ago remains high, but slowed from the month prior; Sep +12.5%

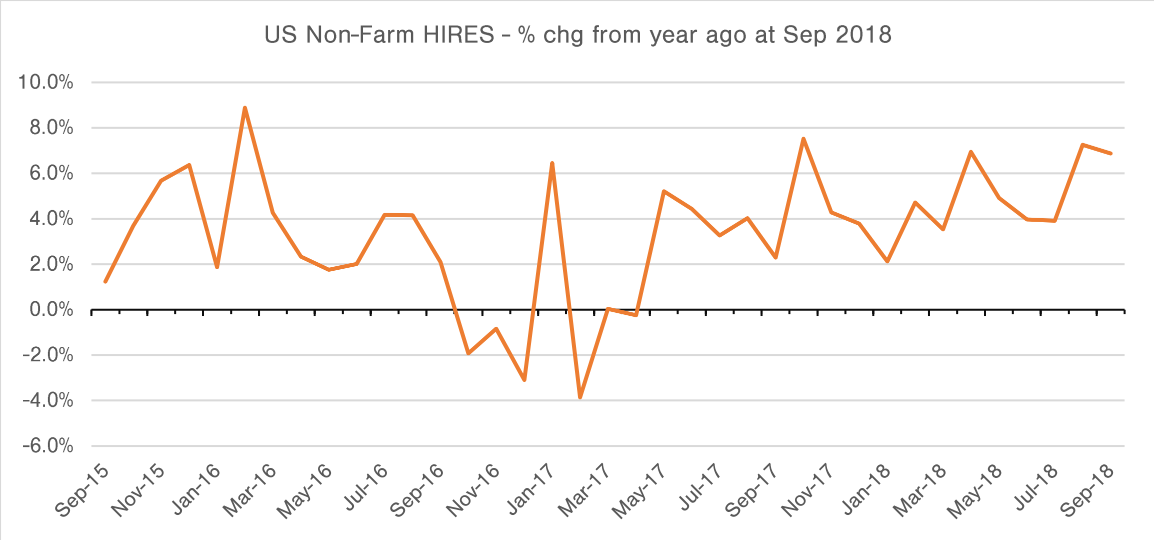


The job opening rate pulled back in the South, the Midwest and the West. The job opening rate increased in the Northeast. The job opening rate in the Northeast and the South are now almost on par – 4.3 and 4.4 respectively.

Hires

Sep 5.7m versus Aug 5.9m (Aug revised higher from 5.8m which was the series all time high)

The % chg from a year ago remains unchanged at 7%;

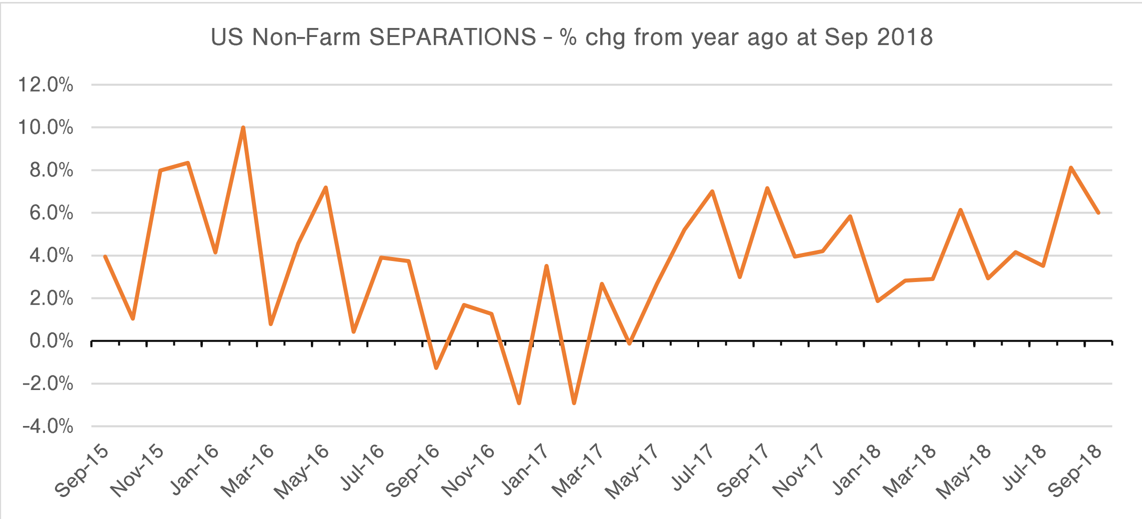


The hire rate fell in the Northeast and the West, was unchanged in the South and increased in the Midwest. The hire rate in the Northeast is now 2.9%.

<u>Separations</u>

Sep 5.7m versus Aug 5.8m

The % chg from year ago slowed to 6% in Sep but the growth rate remains elevated;



The main reasons for separations;

<u>Quits were little changed at 3.6m</u>. The level of quits reached in Aug was the series all time high level. The % chg from a year ago was 10%. The quit rate is highest in the South and the lowest quit rate is in the Northeast. The quite rate increased in the North east and the South and declined in the Midwest and the West.

<u>Lay-offs and discharges were also little changed at 1.7m</u>. The % chg from a year ago was -4%. The level of layoffs and discharges remains well below the series all time high of 2.6m in Feb 2009. The layoff and discharge rate decreased in the Northeast and the West and remained unchanged in the South and Midwest.

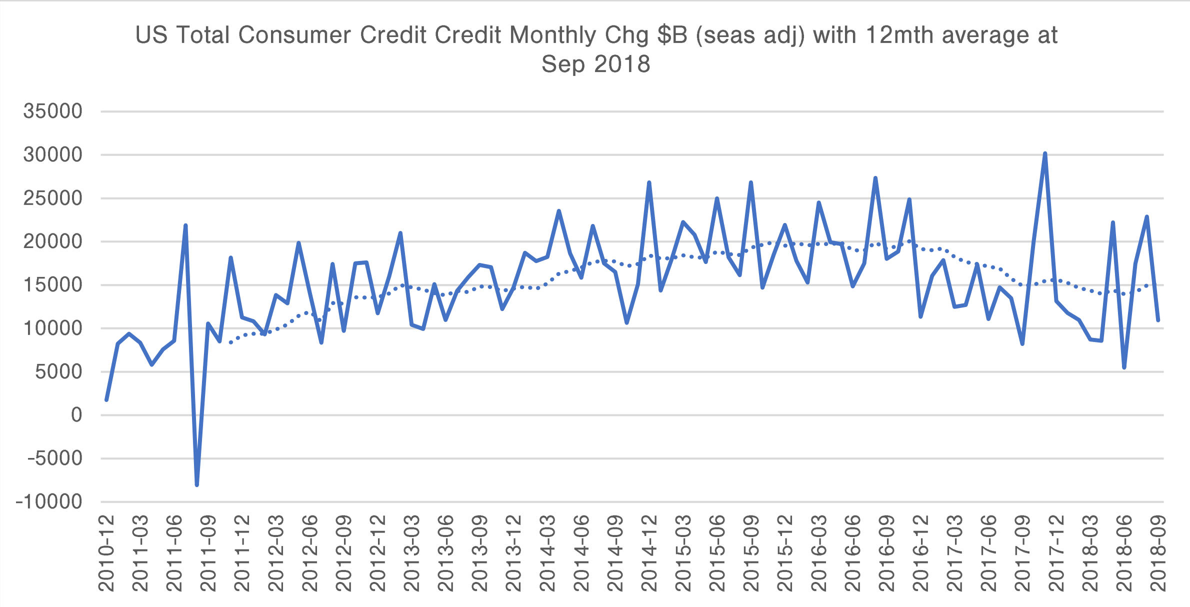
https://www.bls.gov/news.release/pdf/jolts.pdf

Consumer Credit (Sep)

Growth in consumer credit slowed in the latest month but grew overall in the latest quarter. In Q3, the slower growth in revolving credit was offset by the higher growth in non-revolving credit.

Total Consumer Credit chg from prior month; Sep +$10.9b versus Aug +$22.9b

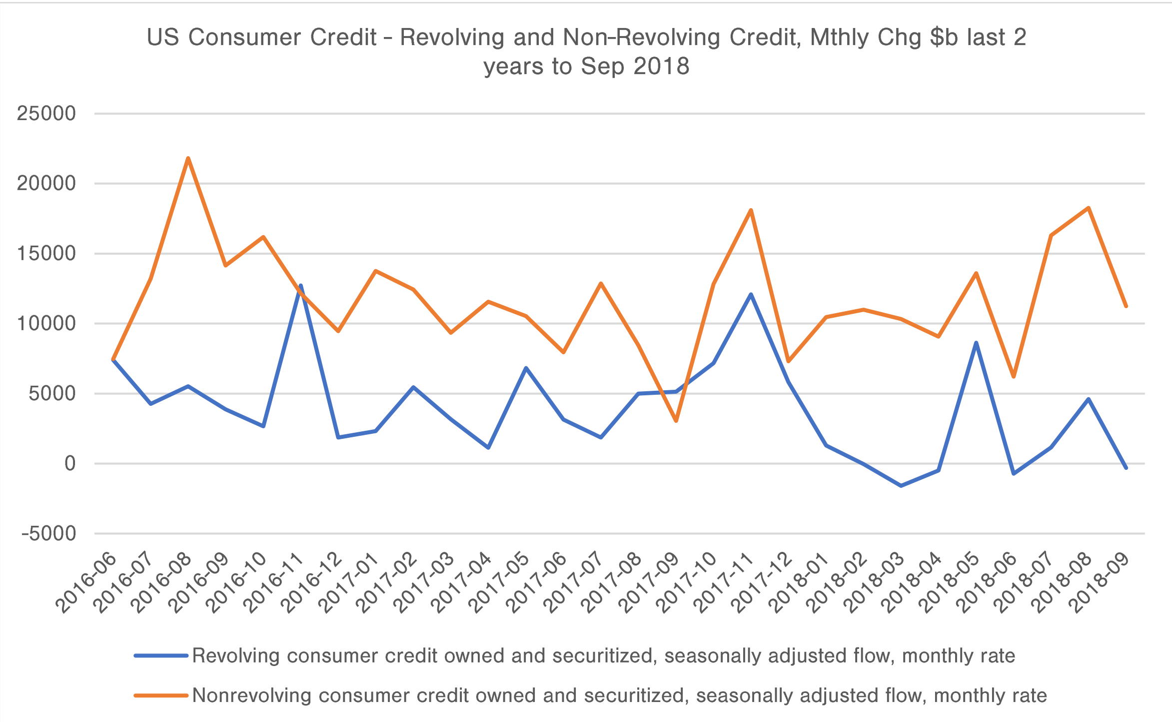
This is now below the 12mth average growth.



The slower growth in the latest month was the result of;

A decline in revolving credit for the month; Sep -$0.3b versus Aug +$4.6b

Slower growth in non-revolving credit for the month; Sep +$11.2b versus Aug +$18.2b

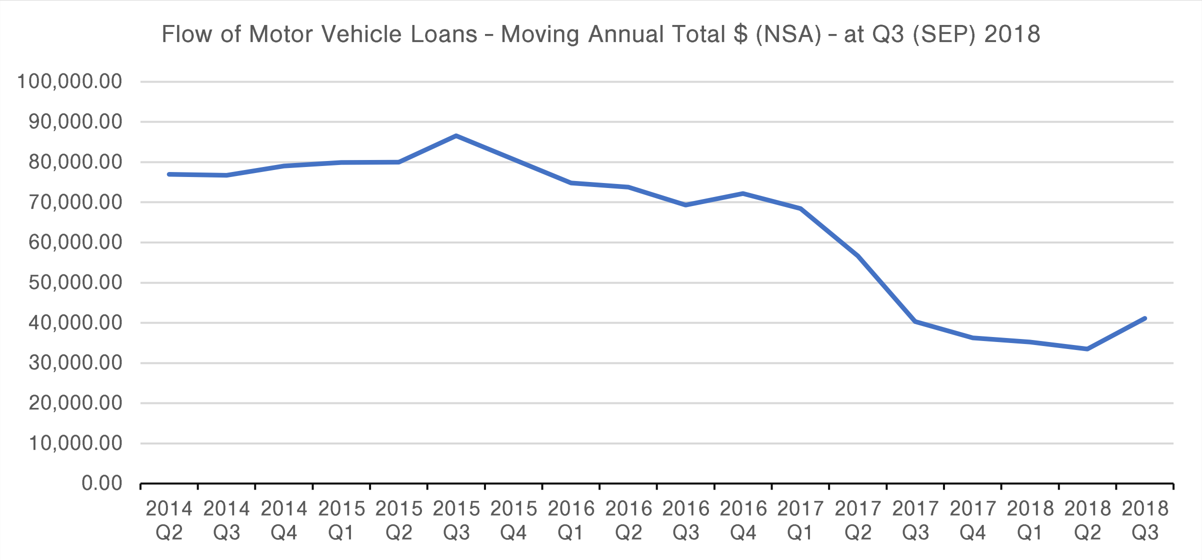


For the Sep qtr, revolving credit was $1.9b lower than quarter prior and non-revolving credit was +$16.9b higher.

The two biggest parts of non-revolving credit are Student Loans and Motor Vehicle Loans. The quarterly data for these two groups was reported this month and it is not seasonally adjusted.

<u>Motor Vehicle Loans</u>

The flow of new motor vehicle loans has been increasing over the last three quarters to record the first annual growth (measured as a moving annual total) in ten quarters of +1.9%.

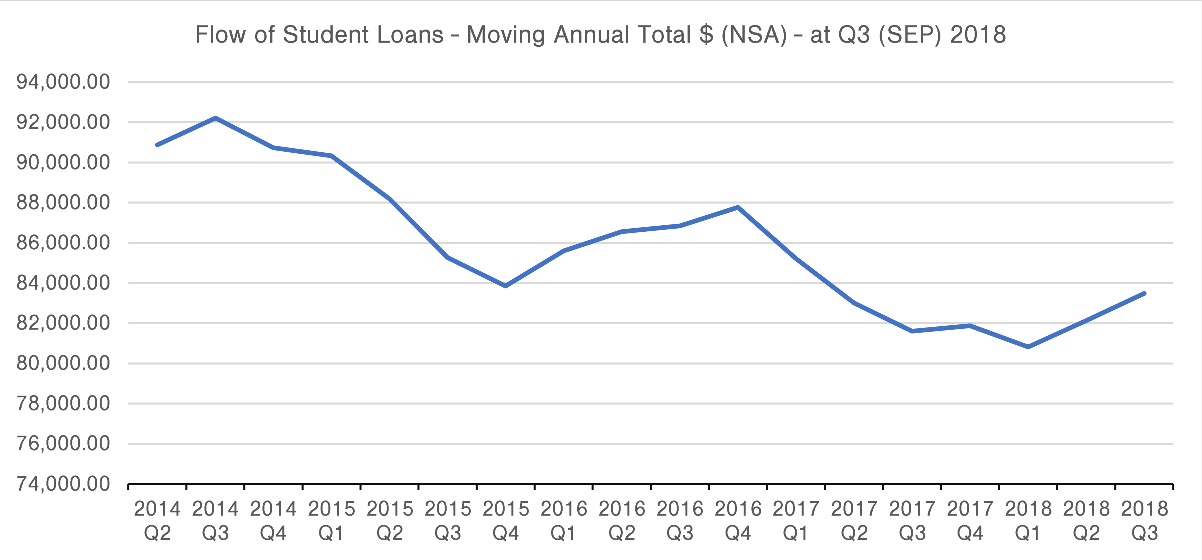


The Q3 2018 growth from the year prior was also higher. The value of new motor vehicle loans in Q3 2018 +$18.5b versus Q3 2017 +$10.9b or +69%.

Note that this is still well below the Q3 2016 value of $27.2b in motor vehicle loans.

<u>Student Loans</u>

The annual growth in student loans at Q3 2018 was +2.3%.



The % chg in Q3 from a year ago was +4.2%.

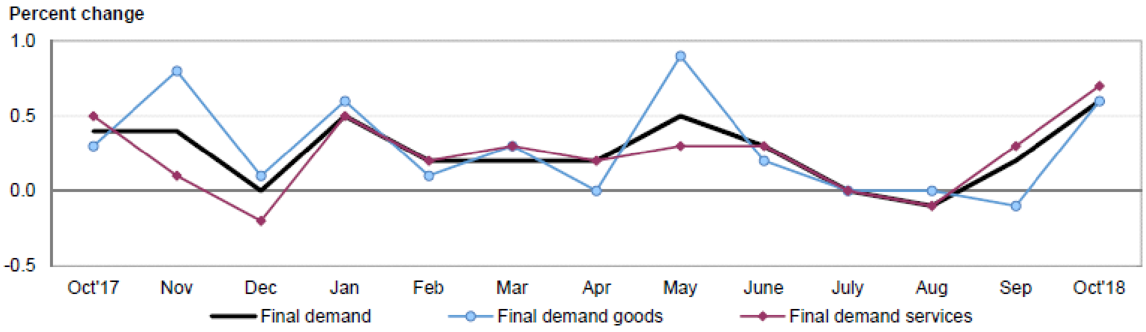
https://www.federalreserve.gov/releases/g19/current/

PPI (Oct)

The growth in producer prices accelerated in the latest month as a result of higher growth in services and (mostly) goods prices. The change from the month year ago also increased and remains below the higher growth rates recorded during May to Aug.

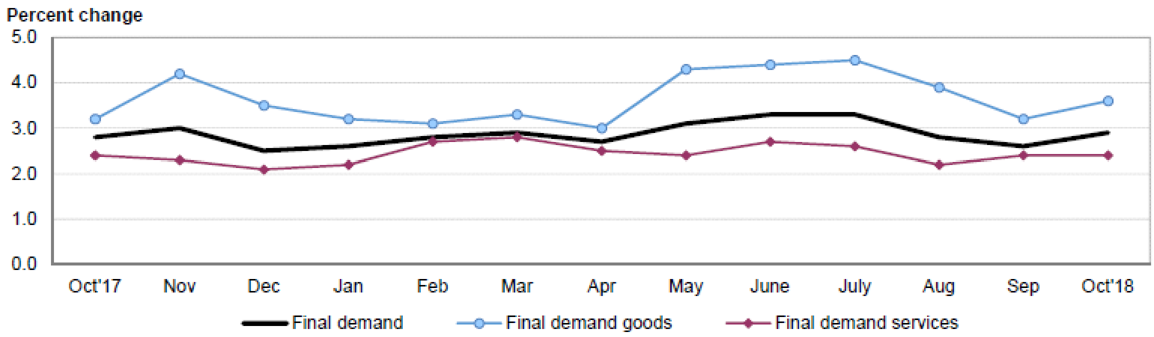
Month chg – producer prices for total final demand; Oct +0.6% versus Sep +0.2%. Excluding food and energy, the growth in final demand prices is slower; Oct +0.2% versus Sep +0.4%.

Chart 1. One-month percent changes in selected PPI final demand price indexes, seasonally adjusted



12month %chg (versus same month from a year ago) – producer prices; Oct +2.9% versus Sep +2.6%

Chart 2. Twelve-month percent changes in selected PPI final demand price indexes, not seasonally adjusted



Change in final demand prices

Both goods and services contributed to the higher growth in the latest month.

Goods; Oct +0.6% versus Sep -0.1%. The growth in goods final demand prices were led higher by food and by much higher growth in energy prices.

Services; Oct +0.7% versus Sep +0.3%. Growth in trade prices was higher, while growth in transport and warehousing prices halved after higher growth in Sep.

Change in intermediate demand prices

Processed and unprocessed goods prices accelerated in the latest month – over half of the increase in Oct was attributed to the 5.8% increase in unprocessed foodstuffs and feedstuffs.

Goods – processed for intermediate demand; Oct +0.8% versus Sep 0%. Oct versus 12mths ago +5.9%. Foods and feeds and energy goods both contributed to the higher prices.

Goods – unprocessed for intermediate demand; Oct +3.6% versus Sep +1.7%. Oct versus 12mths ago +7.8%. Led higher by food stuffs and feedstuffs. Energy materials grew at a slightly slower pace but remains elevated.

Services for intermediate demand; Oct +0.4% versus Sep +0.5%. Oct versus 12 mths ago +3.2%. About a quarter of the increase in the index for service prices for intermediate demand can be traced back to the increase in margins for metals, minerals and ores wholesaling which increased +7.8% in Oct.

https://www.bls.gov/ppi/

Wholesale Sales and Inventories (Sep)

Growth in total US wholesale sales and inventories slowed in Sep. Slower wholesale sales and inventory of durable goods were the main driver of this months' result.

Total US Wholesale sales month chg; Sep +0.2% versus Aug +0.7%

> Durable goods - Wholesale sales month chg; Sep 0% versus Aug +1.1%. This was mostly led lower by wholesale sales of computer equipment, but also lower was automotive, lumber, furniture metals, and electrical.
>
> Non-durable goods – wholesale sales month chg; Sep +0.3% versus Aug +0.3%. A large decline in farm products was more than offset by higher wholesale sales of petroleum and drugs.

Total US Inventories month chg: Sep +0.4% versus Aug +0.9%

> Durable goods – inventories month chg: Sep +0.8% versus Aug +1%. The inventory sales ratio increased to 1.59 from 1.58 in Aug, but still below 1.61 a year ago. Inventory value increased across every category this month, led by automotive and machinery.
>
> Automotive inventory to sales ratio increased from 1.57 in Aug to 1.6 in Sep (Sep 2017; 1.63)
>
> Other categories were the inventory to sales ratio increased in the month and is now ahead of last year; lumber, computer equipment and metals.

Non-durable goods – inventory month chg; Sep -0.4% versus Aug +0.8%. The inventory to sales ratio declined from 0.96 in Aug to 0.95 in Sep (Sep 2017 1.0)

> The increase in petroleum inventory was offset by a decline in inventory for drugs and farm products (related to lower wholesale sales?).

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

FOMC Meeting – Nov

Rates remained on hold at this meeting and there was no change to other monetary policy settings.

There was little change to the statement itself between the Sept and Nov meetings:

The unemployment rate had declined

Household spending had continued to grow strongly while business fixed investment has moderated from its rapid pace earlier in the year.

https://www.federalreserve.gov/monetarypolicy/fomccalendars.htm

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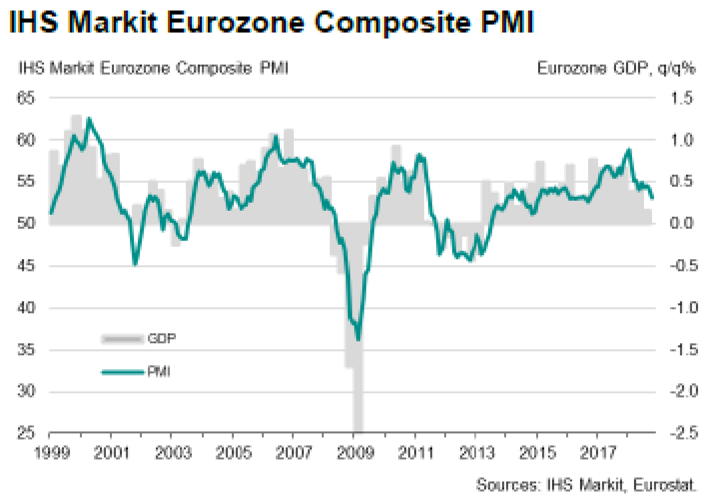
Europe

Eurozone Services PMI (Oct)

Private sector service activity throughout the Eurozone expanded at a slower pace in the latest month;

Oct 53.7 (revised up from prelim 53.3) versus Sep 54.7



Activity grew at a slower pace in Germany, Ireland (7mth low) and Italy fell into contraction for the first time since May 2016. Activity expanded at a faster pace in Spain and France but remains well below the recent peaks.

Growth in new business was slower – the lowest rate since May. At the same time, work backlogs increased. Employment expanded at a slightly slower pace now just below the peak reached in Sep.

Input costs continued to increase on the back of higher energy, fuel and wages. Output charges increased at a faster rate.

https://www.markiteconomics.com/Survey/PressRelease.mvc/086f9e6f394e47e7bbd53a460ea2b9b6

Eurozone Retail Sales (Sep)

The volume of retail sales was unchanged in the Euro area in latest month and growth has halved on a year ago basis;

In the latest month;

Euro area; Sep 0% versus Aug +0.3%

EU 28; Sep -0.1% versus Aug +0.3%

Retail sales were lower across a range of larger economies in the latest month; Spain (-0.6%), France (+0.1%), Portugal (-1.7%) and UK (-0.8%), Switzerland (-1.6%). Growth was stronger than the month prior in; Ireland (+2.9%) and Germany (+0.1%).

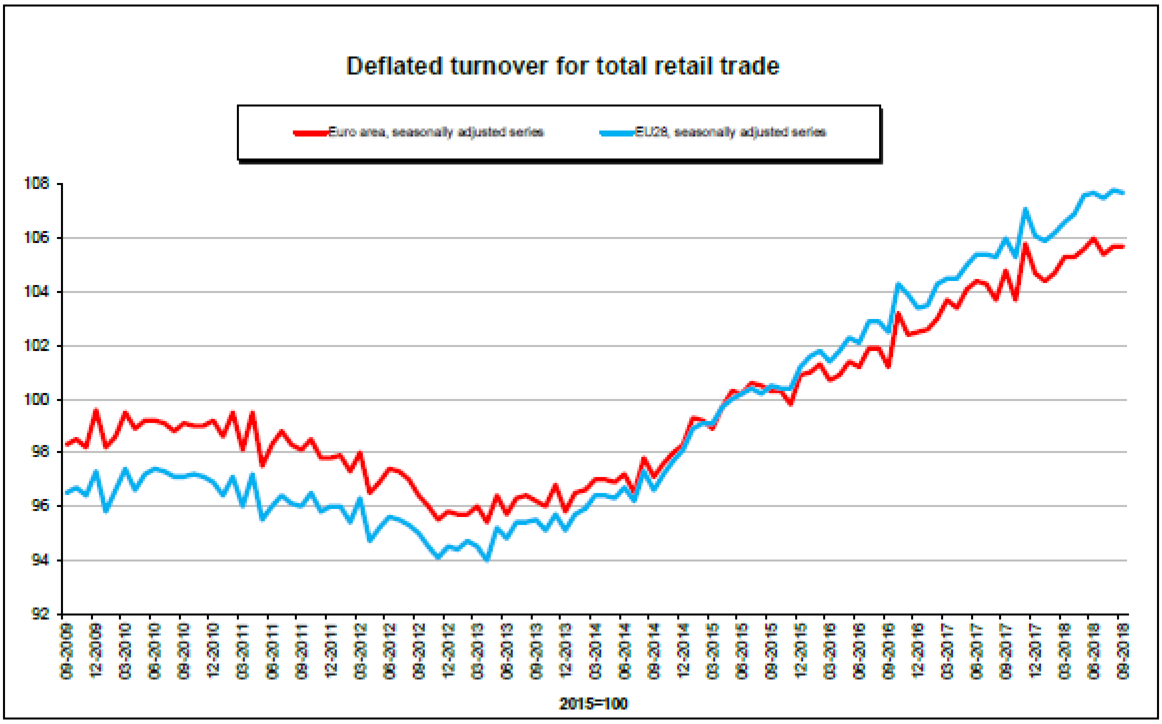
In the Euro area, growth in food/drink/tobacco and automotive fuel was offset by a decline in non-food products.

In the EU28 group, growth in food/drink/tobacco was unchanged and the growth in automotive fuel was offset by the decline in non-food products.

On a year ago basis, retail sales growth slowed quickly across the Eurozone in the latest month;

Euro area; Sep +0.8% versus Aug +2.2%

EU 28; Sep +1.5% versus Aug +2.7%



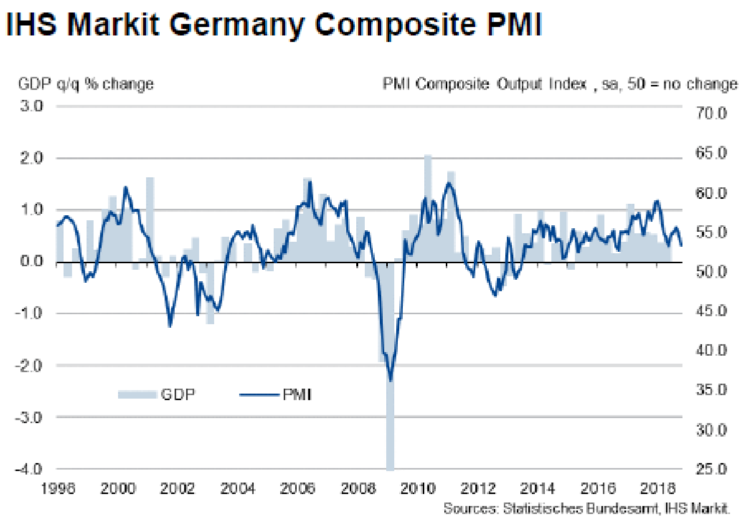
In the Euro area and EU 28 group, growth across most categories has slowed on a year ago basis. The only exceptions are for electrical goods and furniture and automotive fuel.

https://ec.europa.eu/eurostat/documents/2995521/9360121/4-07112018-AP-EN.pdf/fa00f6ee-7934-40af-9e16-a1c7465c4a81

Germany Services PMI (Oct)

Private sector services activity in Germany continued to expand at a slower rate in the latest month;

Oct 54.7 versus Sep 55.9 – this is the joint lowest reading for two years



New orders expanded at the slowest rate in five months. But despite this, order backlogs increased. Employment expanded at a slightly slower pace but remains elevated and close to the peak reached in Sep.

Input prices continued to grow – the second fastest rate in the survey history. Fuel and wages costs were cited as the key cost drivers.

https://www.markiteconomics.com/Survey/PressRelease.mvc/e52476c8be344a749a1ffa12b3ab48e5

Germany Manufacturing New Orders (Sep)

The provisional data for Sep indicates new orders in manufacturing increased in the latest month but remain below a year ago. At best, growth in overall new orders is stagnating after stronger momentum throughout 2016/17. This is broadly in line with the slowing/stagnating growth in new orders seen in the PMI over the last two months.

Month chg total Manufacturing New Orders; Sep +0.3% versus Aug +2.5% (Aug revised higher; provisional result +2%) - price, seas and calendar adjusted.

Growth in domestic new orders offset the decline in foreign (non Euro-area) new orders for the month (versus month prior);

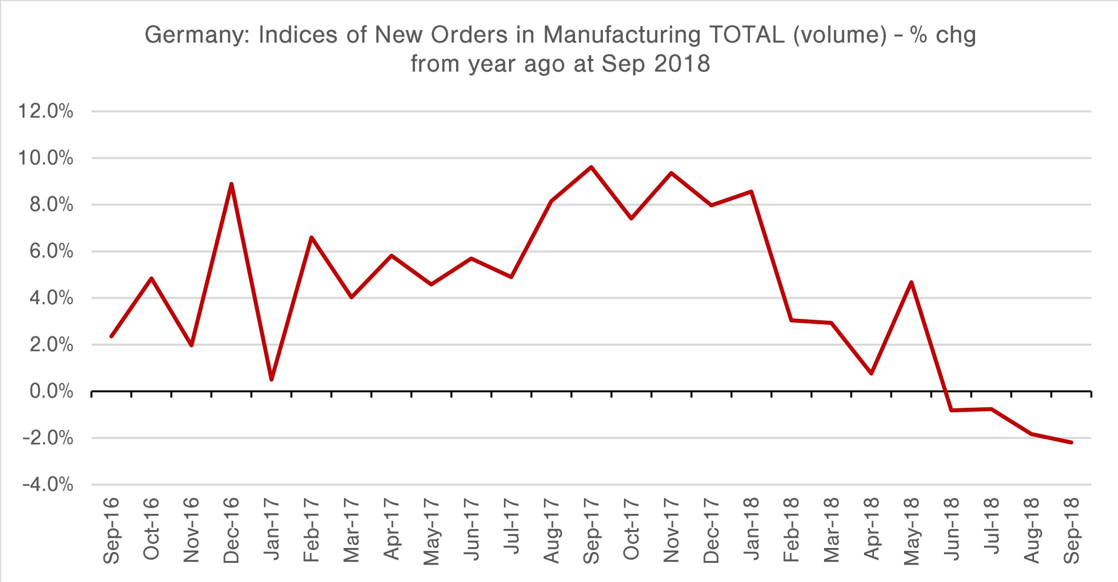
Domestic orders; Sep +2.8%

New orders from the Euro area; Sep +2.4%

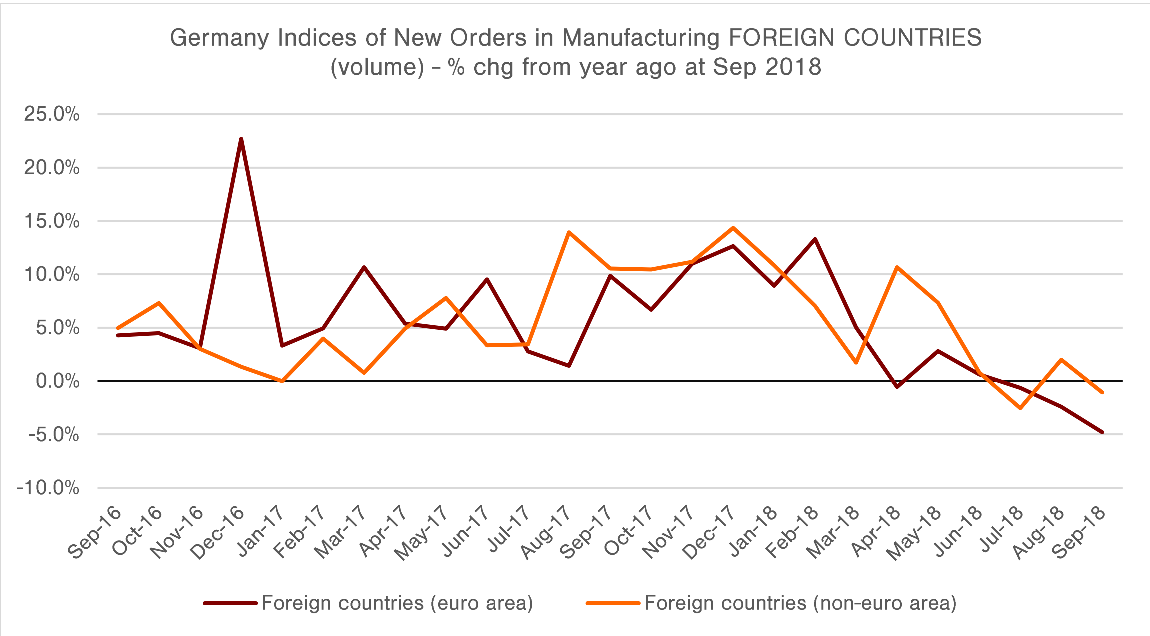
New orders from other countries; Sep -3.7%

Chg on same month year ago total Manufacturing New Orders; Sep -2.2% versus Aug -1.8% (Aug revised higher, provisional result was -2.1%)

The trend versus year ago shows that the growth momentum in new orders has been slowing throughout 2018 – after stronger momentum through 2016 and 2017. Over the last four months, new orders have been below that of a year ago;



How this compares to the PMI; This is directionally in line with the Sept German manufacturing PMI. The headline index slowed to 53.7 – a 25 month low. New orders 'rose only fractionally' and was 'the weakest growth in 46 months'. The slow-down was the result of a drop in new orders from abroad – which fell for the first time in three years;



The volume of new orders from foreign countries has fallen below a year ago in two of the last three months. The larger fall in the index of new orders from foreign countries was in June/July 2018 - the new orders index has been mixed since then.

https://www.destatis.de/EN/PressServices/Press/pr/2018/11/PE18_429_421.html

Germany Manufacturing Turnover (Sep)

The turnover index is based on the total of final invoice amounts of the reference month and deflated. These volume indices are used to measure the price-adjusted development of demand.

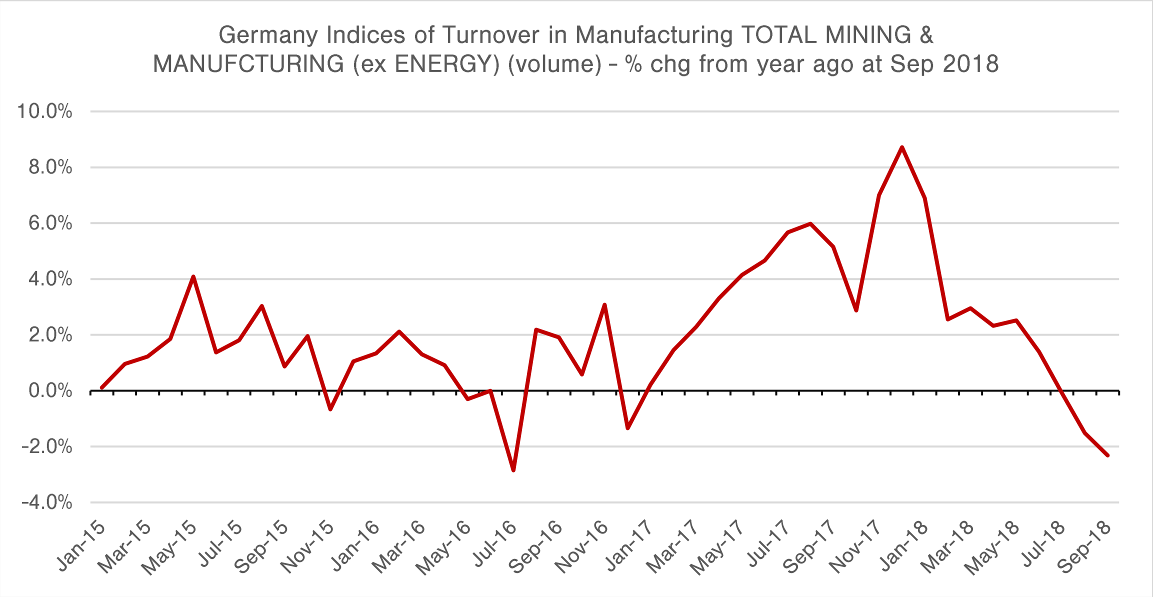
The month on month change for Sep shows total manufacturing turnover (volume) declined by -1.1% and was +0.3% in Aug (Aug revised higher from the provisional result of +0.1%)

The decline in the monthly turnover was the result of declines across domestic and foreign turnover;

Domestic turnover mth on mth change; Sep -1.9%

Foreign Countries turnover mth on mth chg; Sep -0.6% (Euro area countries +0.3% versus the mth prior)

Manufacturing turnover % chg from a year ago; Sep -2.5%



https://www.destatis.de/EN/PressServices/Press/pr/2018/11/PE18_429_421.html

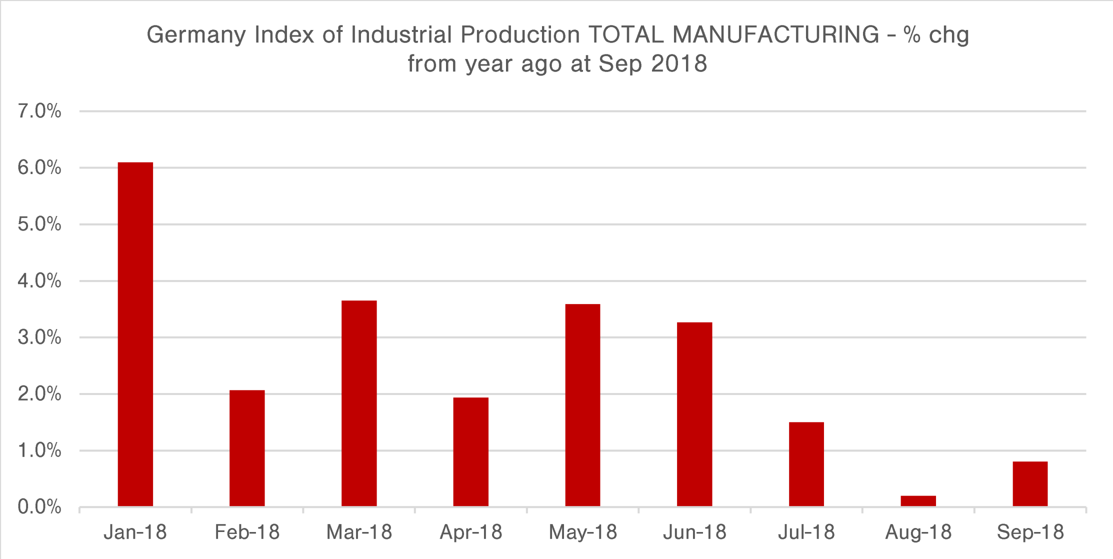
Germany Industrial Production (Sep)

Industrial production (output) growth increased in the latest month and was higher than a year ago.

Industrial production (provisional) for Sept;

Month on month chg; Sep +0.2% (Aug +0.1%) (Aug revised higher from the provisional result of -0.3%)

% chg from year ago; Sep +0.8% (Aug +0.2%) (Aug revised higher from the provisional result of -0.1%)



This remains somewhat directionally in line with the Sep PMI for Germany regarding weaker growth; 'Growth in output was faster than that of new orders, but still slowed to 'the weakest in nearly two and a half years'. In the latest manufacturing PMI for Oct, output continued to increase but at a slower pace; 'The rise in production in October was only marginal and the weakest seen since November 2014'.

Latest month growth in key areas of industrial production;

Production in industry excluding energy and construction; Sep 0% (+0.2% chg from year ago)

Production of intermediate goods; Sep -1.0% (-1.5% chg from year ago)

Production of consumer goods; Sep -0.3% (+5.3% chg from year ago)

Production of capital goods; Sep +0.9% (-0.4% chg from year ago)

Outside industry, energy production; Sep -3.3% (+1.3% chg from year ago)

Construction; Sep +2.2% (+3.8% chg from year ago)

https://www.destatis.de/EN/PressServices/Press/pr/2018/11/PE18_430_421.html

Germany Trade Balance (Sep)

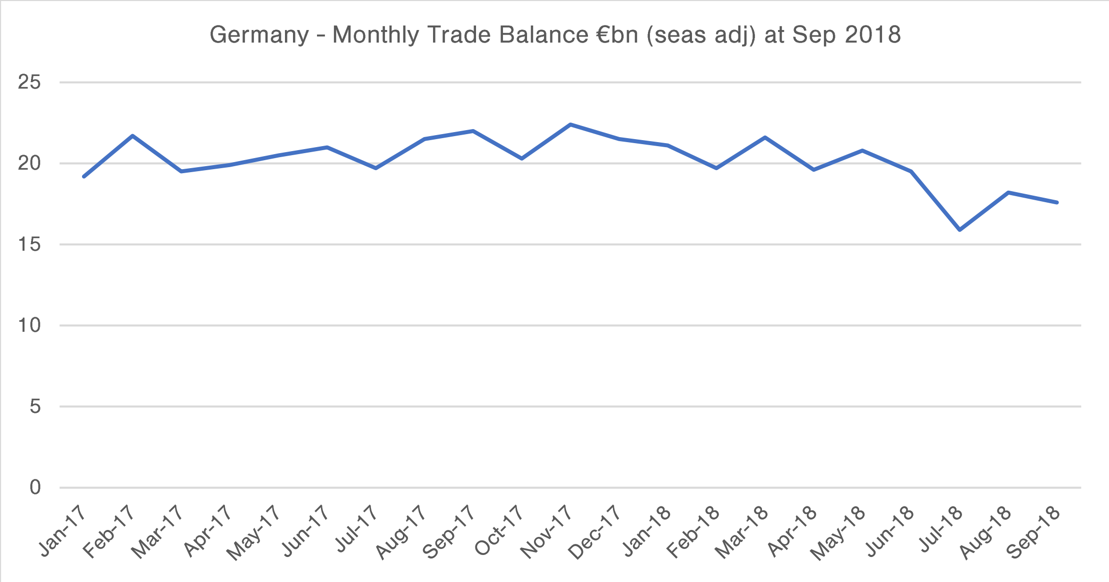
The value of the German trade balance (net exports) narrowed in the latest month. Both exports and imports declined but exports declined by a greater value;

Exports; Sep -0.8% on the month prior and -1.2% on the same month a year ago (and +3.5% YTD v YTD year ago)

Imports; Sep -0.4% on the month prior and +5.3% on the same month a year ago (and +6% YTD v YTD year ago)

The trade balance for Sep was €17.6b (Aug €18.2b)

On a value basis, net exports declined by -€8.2b between Q3 and Q2 – which would detract from GDP value growth in Q3.



The decline in German exports in Sep versus year ago of -1.2% was the result of declines in exports to non-Eurozone but EU member states of -2% and third countries -2.2%. Exports to Eurozone member states increased by +0.6%.

German imports year on year are much higher for Eurozone member states +9.3%, but -0.3% for EU member states but non-Eurozone. Imports from third countries +4.7%.

https://www.destatis.de/EN/PressServices/Press/pr/2018/11/PE18_431_51.html;jsessionid=AE204B8D8F798C8EF3993B8BB36BD5AE.InternetLive2

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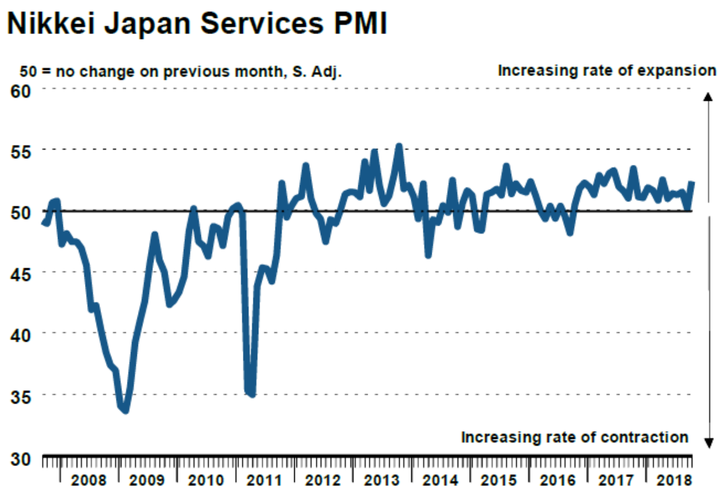
Japan

Services PMI (Oct)

Private sector services activity grew at a faster pace in the latest month;

Oct 52.4 versus Sep 50.2



Sources: Nikkei, IHS Markit

The more upbeat results were supported by improved demand conditions (some linked this to recovering from shortfalls from the typhoon/storms in Sep).

New business expanded at a faster rate. Despite the higher growth in demand, backlogs of orders were cleared.

Employment grew at a slower pace.

Input costs (food, fuel, labour) grew at a faster pace, while output charges grew at the slowest pace since June.

Sentiment of service providers remained optimistic that activity levels would increase over the coming year.

> "growth in Japan's crucial services economy rebounded at the beginning of Q4. Business activity expanded at the fastest pace in six months as firms observed the best monthly improvement in demand conditions since May 2013".

https://www.markiteconomics.com/Survey/PressRelease.mvc/0df8bd61cab84a3388a364d60242a8f3

Trade Balance (Sep)

The provisional data for Sep shows that the trade balance improved in Sep versus Aug. This was the result of slower import growth and despite a decline in exports in the month (from a year ago).

Exports; Sep -1.3% from a year ago (Aug +6.6%)

Imports; Sep +7% from a year ago (Aug +15.5%)

Trade balance; Sep +¥131bn versus Aug -¥448bn

The quarterly result is slightly different;

In Q3 (Jul-Sep) export growth slowed to +2.9% from +7.5% in Q2, while import growth increased from 7.5% in Q2 to +12.4% in Q3.

The Q3 trade balance -¥552bn versus Q2 +¥755bn. This change in the value of net exports will likely detract from Q3 GDP value growth.

Japanese exports to major destinations Sep growth (from year ago);

Asia +0.9% (this is the bulk of Japanese export value) (China -1.7%)

Oceania (Aus/NZ) -9.5%

Nth America -1.7% (US -0.5%, Canada -19%)

Western Europe -9.7%

Middle East -5.3%

Japanese exports by major commodity group;

Of note; All transport equipment (23% shr of export value/mth) -2.2%. Within that group, motor vehicles (cars) exports -8.3% on a volume basis (Cars represent 13% share of export value in the month).

Exports of most of the larger categories declined in the month. The exception was Machinery (20%) of export value) and exports were +0.1% on a year ago.

http://www.customs.go.jp/toukei/shinbun/trade-st_e/2018/2018095e.pdf

http://www.customs.go.jp/toukei/shinbun/trade-st_e/2018/2018_415e.pdf

Machinery Orders (Sep)

There was a near record slow-down in machinery orders for the month of Sep.

Total machinery orders; Sep -17.8%

Machinery orders for the private sector ex volatile items;

Sep; -18.9% versus month prior

Q3 v Q2; +0.9%. The Oct-Dec (Q4) forecast is for +3.6% growth

Orders were lower or weaker across all sectors in the latest month;

Private sector; -20.4%

Manufacturing -17.3%

Non-Manufacturing -17.1%

Govt +2.4% after a -21.2% decline in Aug

From overseas -12.5%

The forecast for Q4 total machinery orders at this stage sees growth slow further from +2.7% in Q3 to +1.7% in Q4.

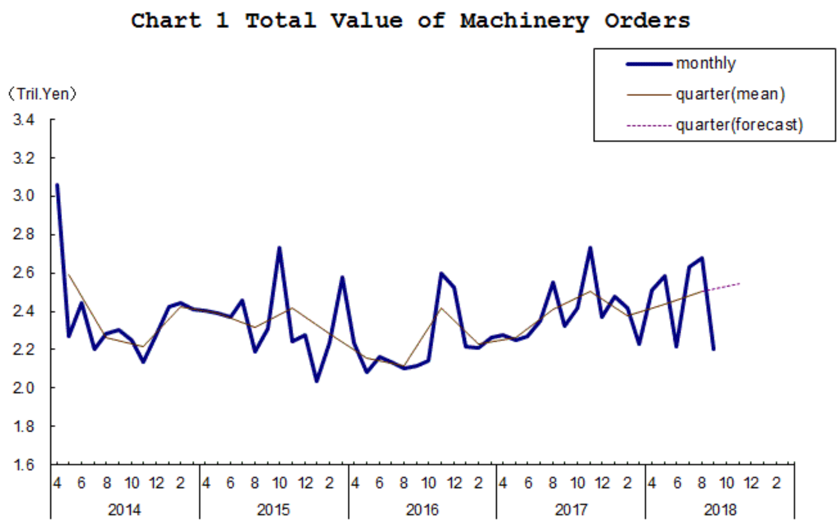
Percentage change from previous quarter (month)

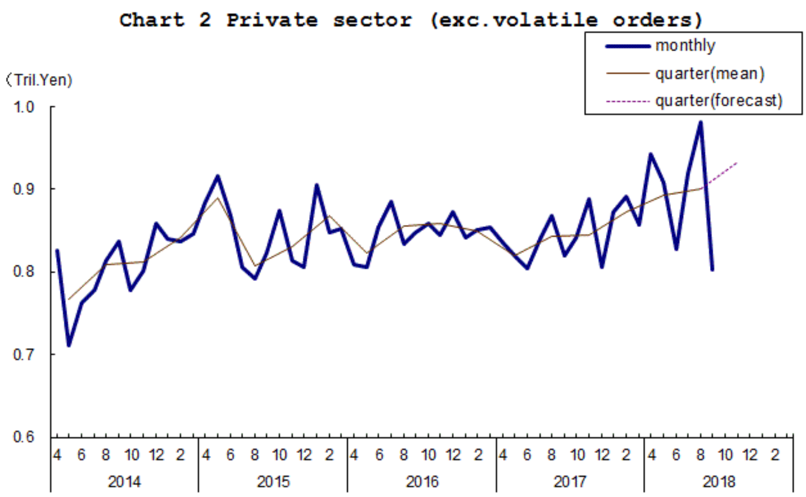
(%)

	2017 Oct-Dec	2018 Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec (forecast)	2018 Jun	Jul	Aug	Sep
Total	4.0	-5.3	2.6	2.7	1.7	-14.4	18.8	1.8	-17.8
Private sector	3.1	-3.5	4.7	3.1	2.5	-5.9	11.1	3.9	-20.4
(exc. volatile orders)	0.3	3.3	2.2	0.9	3.6	-8.8	11.0	6.8	-18.3
Manufacturing	3.5	2.5	5.5	-2.0	9.9	-15.9	11.8	6.6	-17.3
Non-manufacturing (exc. volatile orders)	-2.1	3.4	-0.4	3.5	-3.6	-7.0	10.9	6.0	-17.1
Governments	-5.0	-6.4	7.5	22.4	-18.5	-16.7	57.0	-21.1	2.4
From overseas	0.6	-1.7	-1.3	-1.6	4.3	-12.0	6.0	7.8	-12.5
Through agencies	-1.4	0.3	4.9	-2.2	4.7	-15.8	11.0	-5.2	2.4

(Note)

1. Seasonally adjusted series.As all series are seasonally adjusted individually, a sum of seasonally adjusted individual/component series does not equal to seasonally adjusted totals.
2. Volatile orders :Orders for ships and those from electric power companies.





Quarterly result v forecast

In the July-September Q3 period, machinery orders increased by 2.7% compared with the previous quarter. Machinery orders had been forecasted to increase by 2.8% and private-sector orders, excluding volatile ones, were forecasted to decrease by 0.3% from the previous quarter.

http://www.esri.cao.go.jp/en/stat/juchu/1809juchu-e.html

http://www.esri.cao.go.jp/en/stat/juchu/1806juchu-e.html

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United Kingdom

Brexit

Negotiations on the final aspects of the withdrawal agreement are ongoing. The details surrounding the implementation of a temporary customs arrangement have now been rejected by the EU.

> 'It is envisaged as a way to provide reassurance that a hard border in Northern Ireland will not be needed once the stand-alone transition period comes to an end. The key point of disagreement is over how to ensure the arrangement is temporary. EU officials have said the U.K. would not be able to exit unilaterally because that would not constitute a true "backstop" solution to avoid the need for border checks'.

UK ministers were demanding unilateral power to end the backstop. The compromise of creating a single customs union to avoid the Northern Ireland backstop issue was also contentious within the UK (and not likely to be supported by the cabinet), seen as 'not the will of the people' and not in the spirit of exiting the EU, to be tied to the EU in a customs union after Brexit and unable to sign its own trade deals.

https://www.politico.eu/article/brexit-customs-uk-minister-lock-in-not-will-of-the-people/

A special UK cabinet meeting had been pencilled in for Monday this week to approve a final withdrawal agreement. The usual Tuesday cabinet meeting will go ahead and unless there is a last-minute change, then it's not likely that the withdrawal agreement will be approved.

The timings are now such that;

1) It seems less likely that a complete withdrawal agreement will be finalised in time to schedule a special EU summit in November as hoped. The final EC meeting in the calendar is 12-13 Dec 2018. Both sides need enough time to approve the agreement in their respective parliaments before the 29 Mar 2019 deadline.
2) The UK govt will need to commence preparations for a 'no deal' Brexit so legislation can pass on time before the March deadline.

https://www.independent.co.uk/news/uk/politics/brexit-deal-latest-theresa-may-abandon-emergency-cabinet-meeting-opposition-eu-negotiations-a8628926.html

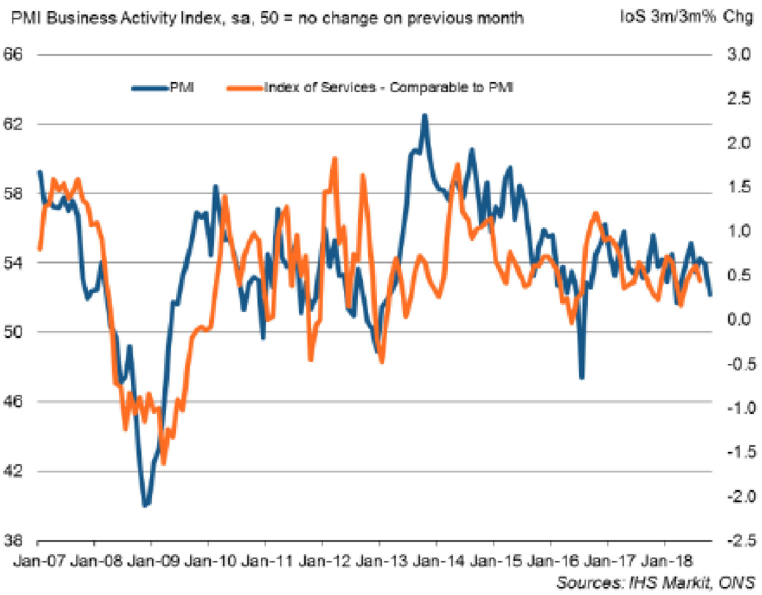
There have been no official updates provided on the EC Brexit site at this stage.
https://ec.europa.eu/commission/brexit-negotiations_en

Services PMI (Oct)

Private sector services activity in the UK continued to expand at a slower rate with a further loss of momentum;

Oct 52.2 versus Sep 53.9

This was the second lowest reading since July 2016;



The main area of concern was the weaker growth in new orders – the latest increase was 'only modest and the weakest recorded since July 2016'. Of note were reports of more subdued consumer spending in Oct – hotels, restaurants and leisure reporting weakest performance. Despite Brexit uncertainty, consumer spending had remained resilient to this point, so this is something to watch.

Order backlogs declined for the first time since Apr.

Employment growth remained moderate.

Input prices continued to grow at a faster pace due to transport costs and wages. In response, service firms increased prices.

Sentiment remains weak, but optimistic on balance. Concerns about Brexit and the general economic outlook persist.

https://www.markiteconomics.com/Survey/PressRelease.mvc/4bd2775d31cb4bd4b9d72cd7274f7c02

Q3 GDP (prelim)

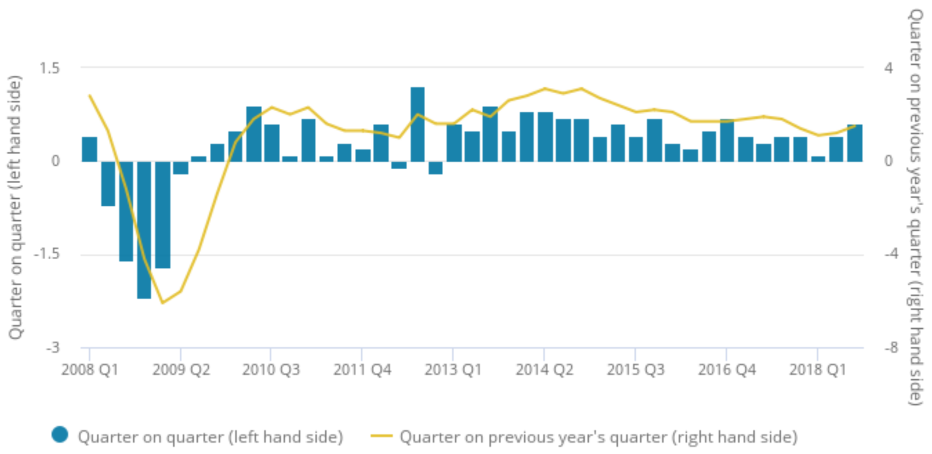
UK GDP grew at a faster pace in Q3 versus Q2 in real terms. This was led by higher growth in exports and continued growth in household and government consumption. Business investment declined for the third quarter in a row.

Real GDP growth; Q3 +0.6% versus Q2 +0.4%

GDP growth in Q3 versus the same quarter in the previous year was also higher in Q3; +1.5% versus +1.2% in Q2.

Figure 1: Real GDP increases by 0.6% in Quarter 3 2018

UK, Quarter 1 (Jan to Mar) 2008 to Quarter 3 (July to Sept) 2018



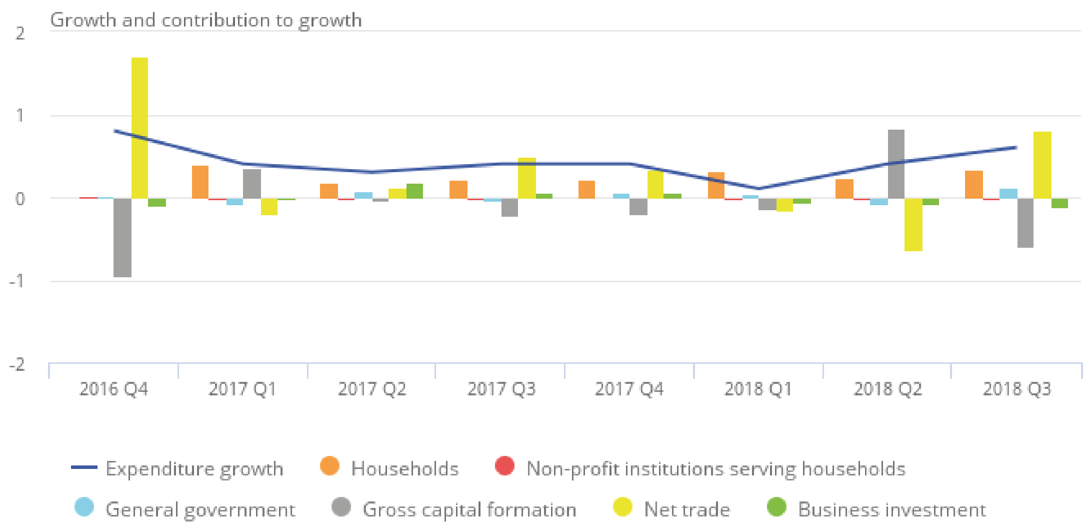
Source: Office for National Statistics

<u>Q3 GDP – expenditure view</u>

The two largest changes to GDP growth in Q3 were net trade and gross capital formation.

Figure 9: Gross capital formation was the only negative contribution to growth in Quarter 3 2018

Growth and contribution to growth, Quarter 4 (Oct to Dec) 2016 to Quarter 3 (July to Sept) 2018



Source: Office for National Statistics, GDP: first quarterly estimate

Net trade made a much larger contribution to growth in the latest quarter – led by an increase in the export of goods and services; Q3 +0.8%pts versus detracting -0.6%pts from GDP growth in Q2.

Gross capital formation detracted -0.6%pts from growth in Q3 versus a positive contribution of +0.8%pts in Q2. Gross capital formation includes the change in inventories and gross fixed capital formation (GFCF). The GFCF component made a positive contribution to overall growth but was offset by the (continued) decline in business investment. Business investment has declined in each of the last three quarters.

Household consumption made a slightly larger contribution to growth in Q3; +0.3%pts versus +0.2%pts in Q2.

Government consumption also made a positive contribution to growth in Q3 of +0.6%pts.

Q3 GDP – production view

All main sectors contributed to the 0.6% GDP growth in the latest quarter.

Services made the largest contribution to growth in Q3 of +0.33%pts – this was lower than in Q2 but in line/on par with growth during 2017.

Production contributed +0.11%pts to Q3 growth after detracting from growth in the prior quarter. This was led higher in the quarter by all areas of production including manufacturing.

Construction growth was stronger in Q3 and contributed +0.13%pts to quarterly growth.

On a monthly basis, overall GDP growth was strongest in July (+0.3% versus the mth prior). In Aug and Sep, the monthly change in GDP has been 0%;

Table 1: Breakdown of GDP growth rates by month

	Jul-18	Aug-18	Sep-18	Quarter 3 2018
GDP	0.3%	0.0%	0.0%	0.6%
Index of Services	0.3%	0.0%	-0.1%	0.4%
Index of Production	0.4%	0.0%	0.0%	0.8%
Manufacturing	-0.2%	-0.1%	0.2%	0.6%
Construction	0.2%	-0.3%	1.7%	2.1%
Agriculture	0.1%	0.1%	0.1%	0.2%

Source: Office for National Statistics

Services growth has weakened throughout Q3

Production growth has stagnated after a strong July – but within that, manufacturing growth has improved.

Growth of construction was more consistent throughout Q3

https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpfirstquarterlyestimateuk/julytoseptember2018

https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpmonthlyestimateuk/september2018

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Australia

RBA Interest Rate Decision – Nov

The RBA kept rates on hold – the overnight cash rate remains at 1.5%.

This was a surprisingly hawkish statement. Considering the slow-down in the housing market, growth forecasts have been upgraded.

The RBA has increased growth forecasts for 2018 and 2019. Growth forecasts were changed from ‘a bit above 3%’ to ‘around 3.5% over these two years’. Growth will slow in 2020 due to slower growth in resources exports. But resources prices are forecast to remain at ‘a relatively high level’.

One continuing source of uncertainty is the outlook for household consumption – growth in household income remains low, debt levels are high and ‘some asset prices have declined’.

Unemployment is expected to fall to 4.75% in 2020 (its currently 5% on a seasonally adj basis).

Inflation is expected to pick up gradually over the next few years 2.25% in 2019 and a bit higher in the following year.

Some acknowledgement of tighter financial conditions – globally and locally rates have been increasing but ‘rates remain low’.

Little change to the statement regarding the housing markets in Sydney and Melbourne – although some recognition that ‘the dynamics of the housing market have changed’.

https://www.rba.gov.au/media-releases/2018/mr-18-27.html

APRA Announcement

APRA is proposing to increase Australian bank capital requirements. Likely 4-5%pts of risk weighted assets within five years. This is expected to;

> ‘increase each of the four major banks cost of funding, incrementally over four years, by up to 5 basis points, based on current pricing’.

https://www.afr.com/business/banking-and-finance/financial-services/apra-proposes-lifting-major-bank-capital-levels-to-protect-from-any-shock-20181107-h17n5x

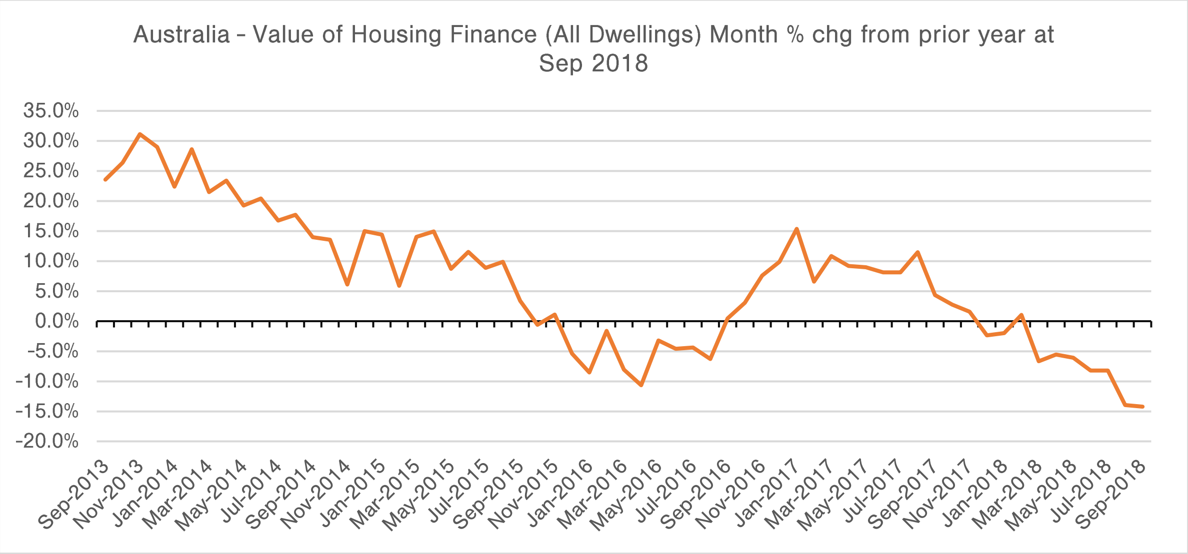
Housing Lending (Sep)

Across all measures, housing lending finance has continued to fall in Sep – this is indicating likely further house price falls. The overall decline in Sep was led by owner occupiers, which accelerated in the current month versus year ago. The decline for investment property lending slowed very slightly but continues to record double digit declines.

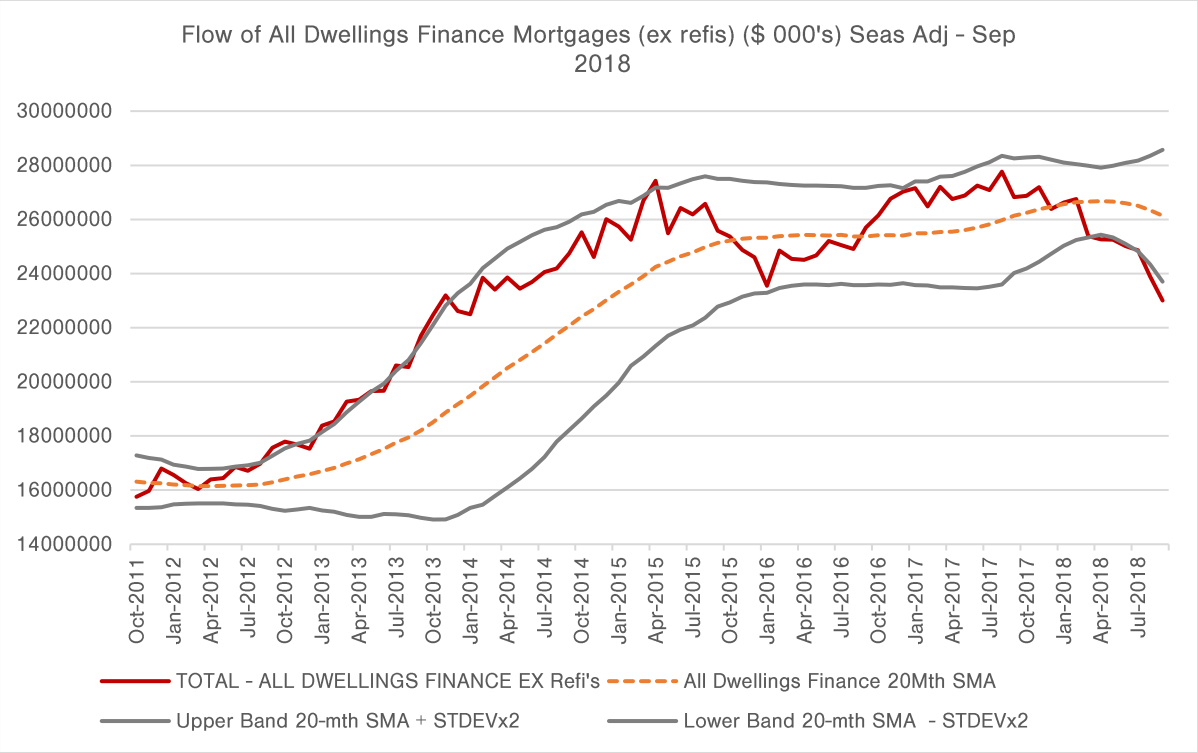
<u>All Dwellings Finance (ex refi's) (this is the sum of owner occupier and investment property mortgage finance)</u>

Month chg; Sep -3.7% versus Aug -3.9%

Monthly % chg from prior year; Sep -14.2% versus Aug -14%



The current flow of the value of housing finance ex-refi's is outside of the -2SD of the 20month moving average – this has been a very fast fall in lending.

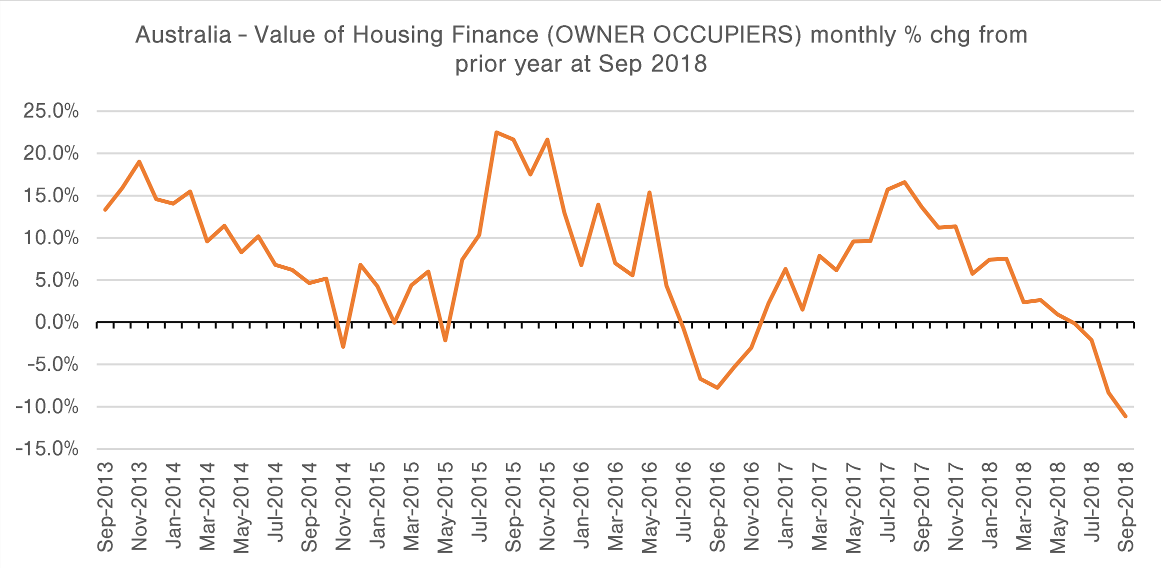


Owner Occupier Housing Finance (ex refi's)

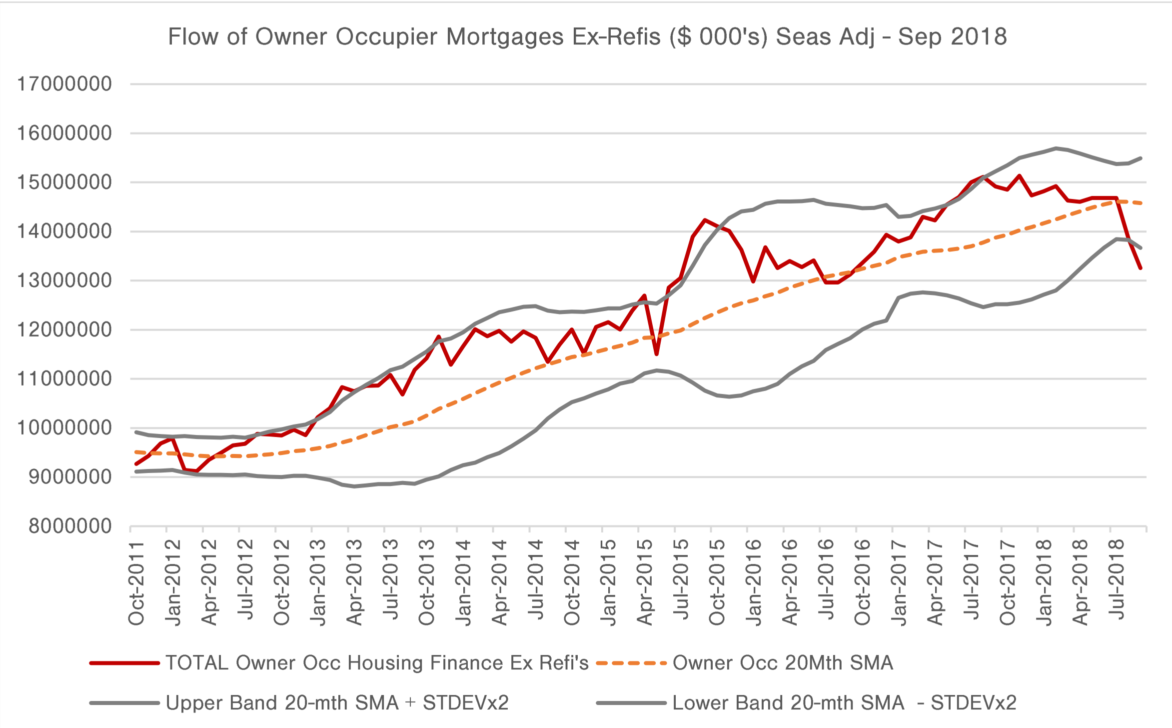
Whilst slowing, this area of housing finance had been a little more resilient – but the slow-down has accelerated over the last two months.

Month chg; Sep -4.3% versus Aug -5.6%

Monthly % chg from prior year; Sep -11.1% versus Aug -8.4%



The fall in the value of new owner occupier mortgage finance remains below -2SD of the 20month moving average. The change in the current month is a 1.3 SD decline. The Aug decline was 2.1 SD's.



At this stage, the fall in the number of new lending commitments has been just as fast on a 'year ago' basis.

Mth chg; Sep -1% versus Aug -2.2%

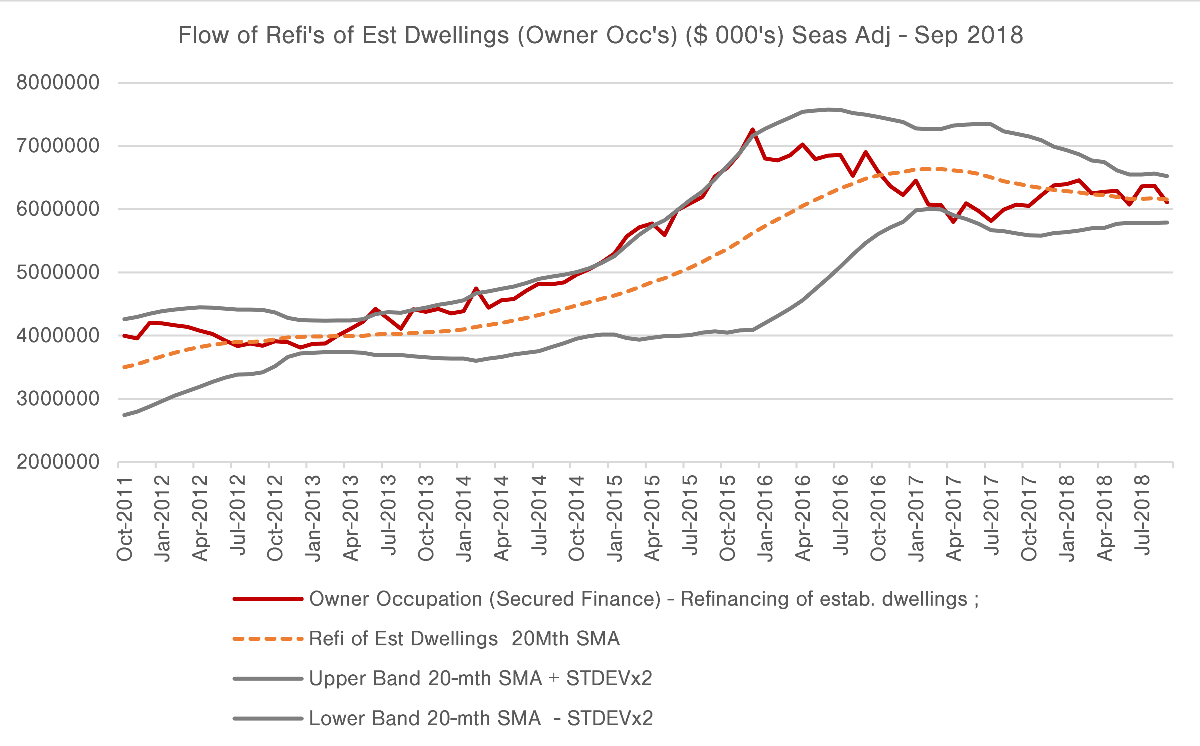
Monthly % chg from prior year; Sep -9.7% versus Aug -10.2%

The most notable result this month was in Victoria, one of the key markets; the number of owner occupier housing finance commitments fell by 4.3% versus Aug (this is a 1SD fall).

The current number of new owner occupier housing finance commitments has also slowed to the -2SD level.

Refinancing of Established Dwellings (Owner Occupiers)

The value of refi's for owner occupiers has been trending lower, but remains around the 20mth moving average;



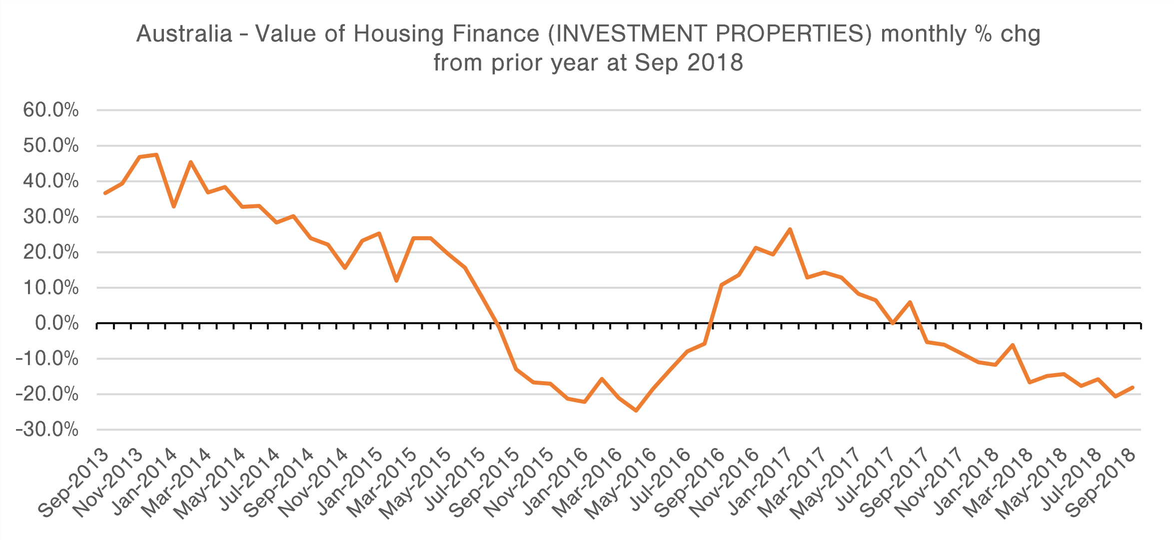
Most importantly, it appears that refis for owner occupiers has not been increasing.

Investment Housing Mortgages

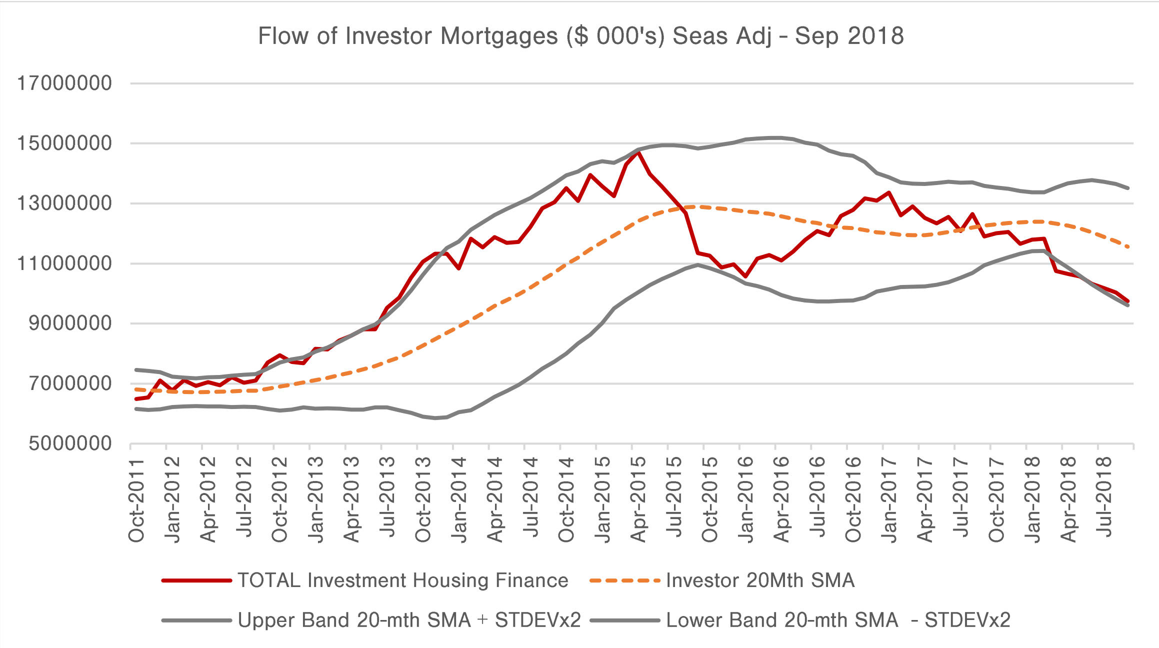
The value of investment housing lending has fallen for the seventh consecutive month;

Month chg; Sep -2.8% versus Aug -1.4%

Monthly % chg from prior year; Sep 18.1% versus Aug -20.7%



The flow of new lending for investment properties continues to fall quickly and has remained around the -2SD level since March;



http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/5609.0Main+Features1September%202018?OpenDocument

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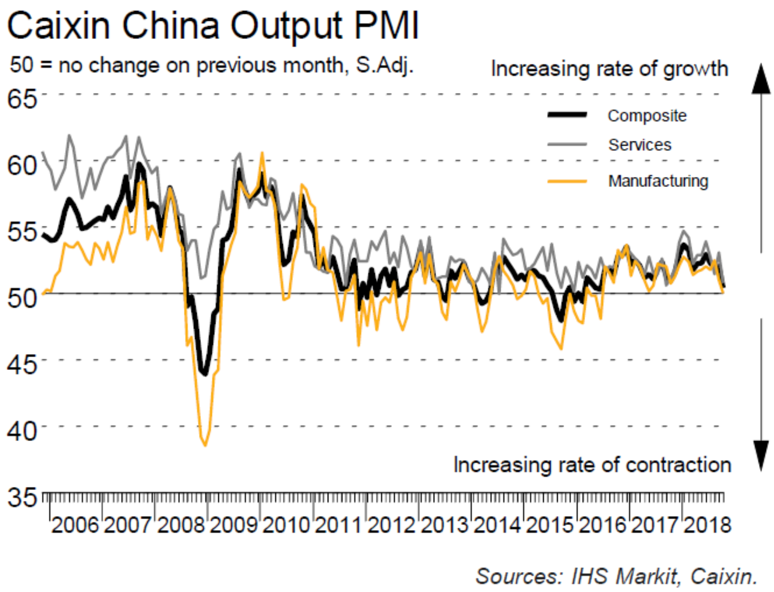
China

Services PMI (Oct)

The PMI of services activity in China slowed further in the latest month;

Oct 50.87 versus Sep 53.1



"First stagnation of new business in nearly 10 years"

Despite the more subdued demand conditions, employment increased, offsetting the decline from the prior month.

Unfinished work continued to decrease.

Input prices increased at a slower pace and output charges also increased.

Whilst still positive, the sentiment of service providers for the next twelve months fell. Subdued demand conditions and the US-China trade dispute were cited as key reasons.

https://www.markiteconomics.com/Survey/PressRelease.mvc/ab0293da45c3413bb1ee1909ea592061

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Trade

US-China Trade Negotiations

A possible fourth round of tariffs may be implemented by the US on $267b of Chinese imports after China retaliated. It's unclear how/whether mid-term results will alter the direction of negotiations.

It appears confirmed that Presidents Trump and Xi will meet on the sidelines of the G20 in November.

NAFTA/USMCA

U.S. officials intend to sign the agreement with Canada and Mexico most likely at the G-20 meeting on 30 November. https://www.politico.com/newsletters/morning-trade/2018/11/09/g-20-to-be-site-of-usmca-signing-406899

After which it would be submitted to the U.S. Congress for approval. Given mid-term election results, the deal is still likely to gain approval in Congress.

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

A hearing is now scheduled to take place on 10 Dec 2018 on the negotiating objectives for a US-Japan trade agreement. Talks likely to start in Jan 2019.

https://www.federalregister.gov/documents/2018/10/26/2018-23569/request-for-comments-on-negotiating-objectives-for-a-us-japan-trade-agreement

Section 232 – Car and Truck Imports

Awaiting the outcome of the public hearings.

US-Europe Trade Talks

Official notification of trade talks was sent to the US Congress three weeks ago (also notifying the US Congress of the intention to commence trade talks with Japan and the UK).

As noted in the announcement, the USTR will publish objectives for the negotiations at least 30 days before negotiations begin.

No formal consultation for the US-EU negotiations has been announced on the US Federal Register (only for US-Japan trade talks at this stage). https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/october/trump-administration-announces

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