

Key Themes

Several central banks stepped in to calm the markets last week. First, US Fed Chairman Powell made it explicit that the Fed will be flexible and will adjust policy, and significantly, if required. Chairman Powell referenced the 'tension' between balancing the markets (and what the shift in bond yields is saying about future growth) and data on the economy. A continued or extended Government shutdown will hinder that data flow.

US data was very mixed. Further slowing in manufacturing activity, including the larger fall in the ISM manufacturing index, contrasted with the very strong non-farm payrolls number. The Dec Uni of Michigan Consumer sentiment survey highlighted that "consumers reported more negative than positive news about job prospects for the first time in two years, with the shift widespread". This is a one-month shift, but negative news may be starting to play a role.

Second, the PBoC cut the RRR for the fourth time since the start of 2018 on the back of continued weaker readings of economic activity. The PBoC's benchmark interest rate has remained unchanged since 2016.

The range of opinions in the BoJ summary of opinions report was skewed to a more positive view on the Japanese economy. More candid opinions stood out claiming that "it cannot be said that the actual condition of restoration-related demand and production stemming from natural disasters has been strong". The BoJ may also further downgrade its inflation forecasts. In Nov, Japanese industrial production declined in the month (expecting an increase) and retail sales also declined with annual growth more than halving. The Dec manufacturing PMI confirmed renewed falls in new export orders with "unfavourable workload growth" cited in markets such as Nth America, China and Taiwan.

The European PMI's for Dec continued to disappoint. To some degree, Eurozone results were lower on the back of ongoing French protests. But Italy and Germany PMI's (manufacturing and now services) slowed even further on the back weak/declining new orders. Production levels were maintained as firms worked through backlogs.

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US Data – Case Shiller House Price Index (Oct), Richmond Fed Manufacturing Index (Dec), Chicago Fed PMI (Dec), Dallas Fed Manufacturing Survey (Dec), Manufacturing PMI (Dec), Services & Composite PMI (Dec), ISM Manufacturing Index (Dec), Challenger Job Cut Report (Dec), Non-Farm Payrolls (Dec), University of Michigan Consumer Sentiment (Dec)

Chairman Powell; panel on monetary policy and central banking at the American Economic Association in Atlanta, Georgia, incl former Fed Chair's Yellen and Bernanke.

Europe – Germany CPI – Prelim (Dec), Eurozone and Germany Manufacturing PMI (Dec), Germany Services PMI (Dec), Eurozone Services & Composite PMI (Dec), Eurozone CPI Prelim (Dec)

Japan – Industrial Production (Nov), Retail Trade (Nov), BoJ Summary of Opinions (Dec), Manufacturing PMI (Dec)

United Kingdom – Brexit, Manufacturing PMI (Dec), Services PMI (Dec)

Australia – Corelogic House Prices (Dec)

China – Manufacturing and Non-Manufacturing PMI (Dec) - China Federation of Logistics and Purchasing, Caixin Manufacturing PMI (Dec), Caixin Services PMI (Dec)

Trade – US-China Trade Negotiations, Special 2019 Section 301 Review (new), NAFTA-USMCA, US-Japan Trade Talks, Section 232 Car & Truck Imports, US-Europe Trade Talks, US-UK Trade Talks

US Data

Case Shiller House Price Index (Oct)

Annual growth in US house prices continued to slow in the latest report. The month change (seas adj) was mostly on par or slightly lower than in the month prior.

Monthly Change – Seas Adj

US National House Price Index; Oct +0.5% versus Sep +0.4%

US Composite 20 Price Index; Oct +0.4% versus Sep +0.7%

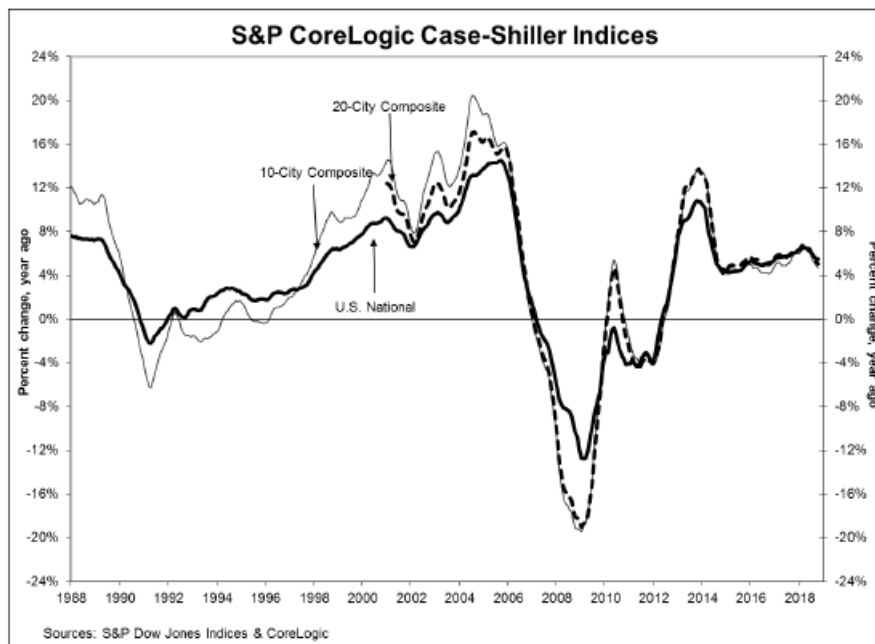
US Composite 10 Price Index; Oct +0.5% versus Sep +0.4%

Annual change – Not Seas Adj

US National House Price Index; Oct +5.5% versus Sep +5.5%

US Composite 20 Price Index; Oct +5% versus Sep 5.2%

US Composite 10 Price Index; Oct +4.7% versus Sep +4.9%

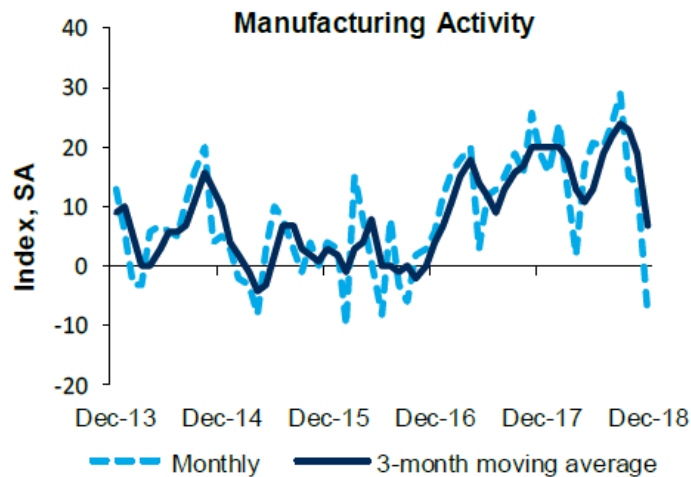


https://www.spice-indices.com/idpfiles/spice-assets/resources/public/documents/843358_cshomeprice-release-1226.pdf?force_download=true

Richmond Fed Manufacturing Index (Dec)

The headline index of manufacturing activity slipped into contraction in the latest month. Shipments and new orders declined while employment continued to grow.

Headline Manufacturing Index; Dec -8 versus Nov +14



Shipments declined to the lowest reading since Apr 2009; Dec -25 versus Nov 12

The volume of new orders also declined; Dec -9 versus Nov 17

The backlog of orders and capacity utilization both fell into contraction.

Capex remained unchanged.

Finished goods and raw materials inventories both increased at a faster pace.

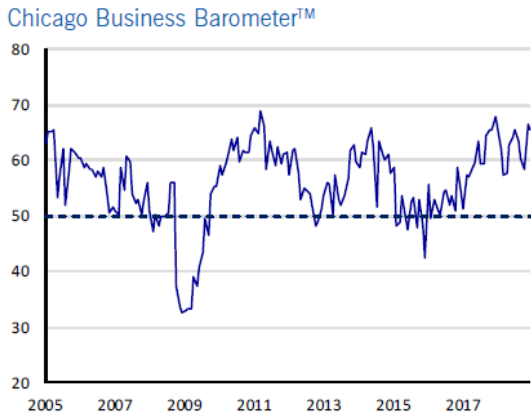
The number of employees continued to grow at a faster pace, while wage growth slowed, and the average workweek also slowed to a virtually unchanged level. Finding workers with the necessary skills remained a problem for firms.

https://www.richmondfed.org/-/media/richmondfedorg/research/regional_economy/surveys_of_business_conditions/manufacturing/2018/pdf/mfg_12_26_18.pdf

Chicago Fed PMI (Dec)

The Chicago PMI bucked the regional trend as the headline business barometer index continued to grow, slowing only slightly versus the month prior.

Business Barometer; Dec 65.4 versus Nov 66.4



Production increased to an 11-mth high. Order backlogs also increased at a faster pace. Inventories increased in response to increased orders. But the higher inventory may be indicating possible demand issues;

For others, however, inventories remained high by virtue of an unanticipated quietening in demand.

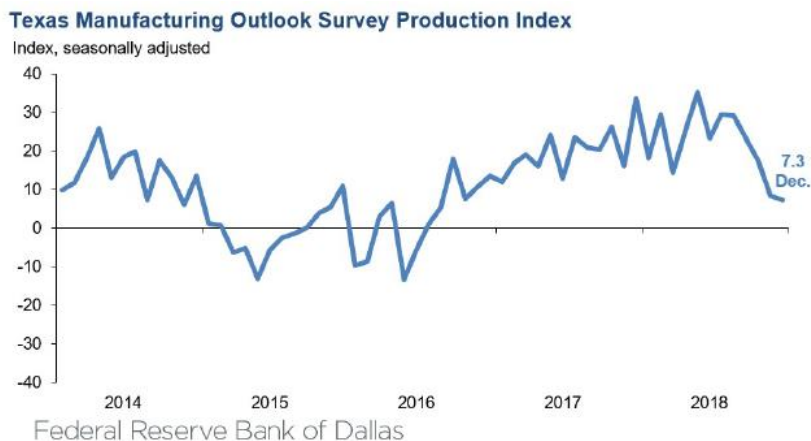
Employment growth slowed to a 3-mth low but remains above the 50-neutral mark.

<https://s3.amazonaws.com/images.chaptermanager.com/chapters/b742ccc3-ff70-8eca-4cf5-ab93a6c8ab97/files/mni-chicago-press-release-2018-12.pdf>

Dallas Fed Manufacturing Survey (Dec)

Manufacturing activity within the region continued to grow at a slower pace. While production growth slowed, new orders grew at a faster pace. The company and general business activity outlook show conditions worsening with both measures declining/contracting.

Production; Dec 7.3 versus Nov 8.4



New orders grew at a faster pace and the growth in production also resulted in unfilled orders falling into contraction (as firms worked through unfilled orders/order backlogs). Finished goods inventory grew at a slower pace and growth remained low.

Employment growth slowed, and the hours worked was unchanged.

The company outlook and general business activity show a worsening of conditions, with both falling into contraction.

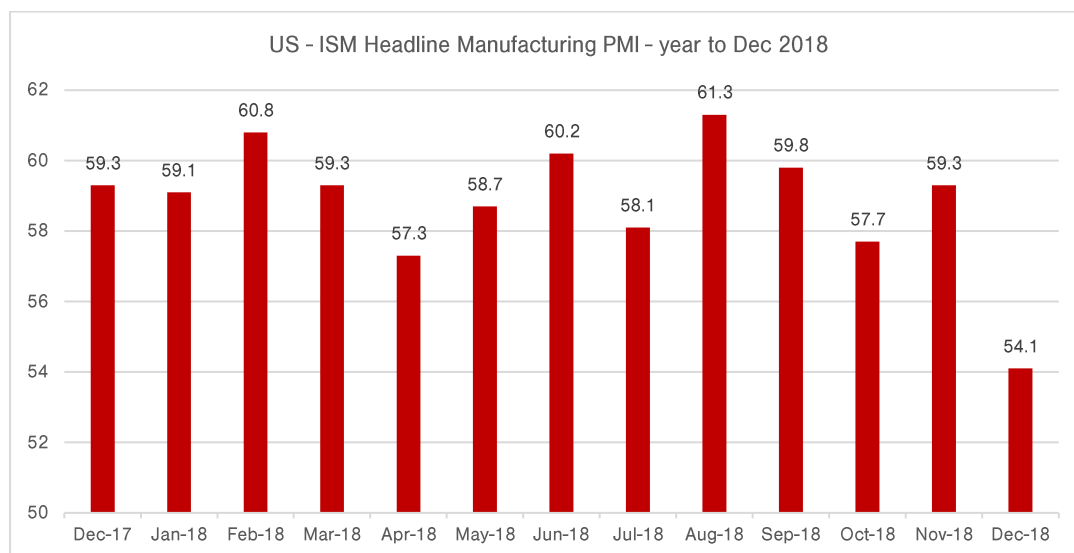
That said, capex still increasing at a faster rate in Dec (+5pts).

<https://www.dallasfed.org/-/media/Documents/research/surveys/tmos/2018/1812/tmos1812.pdf>

US ISM Manufacturing Index (Dec)

The headline ISM index showed continued growth in private sector manufacturing activity but at a much slower pace. The decline in the PMI for the month was significant (compared to the last 12 mths). The slowdown in the headline PMI was the result of weaker growth in key demand measures of new orders and production. Slowing by a lesser degree was employment, inventories and prices.

Dec 54.1 versus Nov 59.3 (-5.2pts)



New orders fell by 11pts from 62.1 in Nov to 51.1 in Dec. The internal make-up of that index shows that the proportion of firms recording 'lower' new orders is now larger than the proportion of firms recording 'higher' new orders.

Production fell by 6.3pts from 60.6 in Nov to 54.3 in Dec. The internals are not quite as negative as for new orders, but there was a large drop in the proportion of firms recording 'higher' production (-9%pts). The proportion of firms recording 'lower' production increased by 7%pts.

Like other reports, order backlogs have also declined and is now at a neutral '50' reading. The proportion of firms recording higher and lower backlogs are now at the same level.

Inventories grew at a slightly slower pace.

Employment growth was also slightly lower but still expanding at a similar pace as recent months; Dec 56.2 versus Nov 58.4. Most firms (70.7%) report the 'same' levels of employment.

Price growth slowed sharply, falling by 5.8pts. Since Oct, the expansion/growth in prices has slowed from a reading of 71.6 in Oct to 54.9 in Dec. While there was a large shift in the

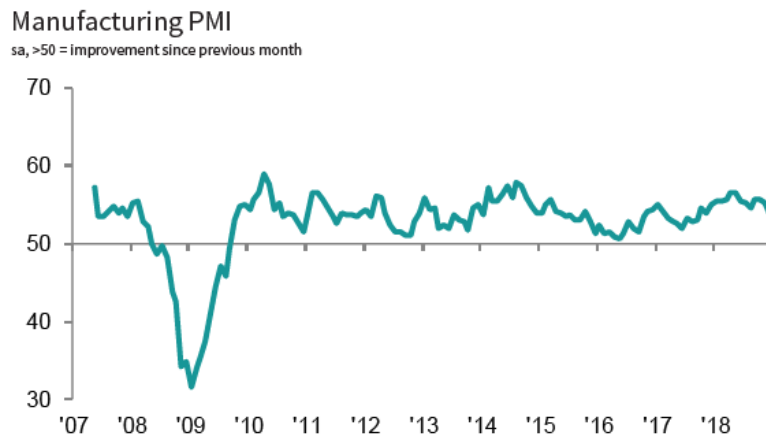
proportion firms now reporting 'lower' input prices, the overall proportion of firms reporting higher input prices is still larger.

<https://www.instituteforsupplymanagement.org/ismreport/mfgrob.cfm?SSO=1>

US Manufacturing PMI (Dec)

The headline index showed that manufacturing activity slowed further in the latest month.

Dec 53.8 versus Nov 55.3 (-1.5pts)



Production/output growth was unchanged from Nov – remaining at the lowest level in 15-months.

New order growth slowed (on par with that of Sep 2017). Some firms cited new orders from new clients but there were also concerns about a 'drop' in client demand compared to a year ago. New export orders increased at a faster pace.

Order backlogs increased 'moderately'.

The slower increase in new orders (overall) led to lower optimism, below the LR avg.

Employment growth slowed to an 18-month low.

Input price growth eased but "greater cost burdens were reportedly due to raw material stockpiling among manufacturers, shortages of electronics components and the ongoing impact of tariffs."

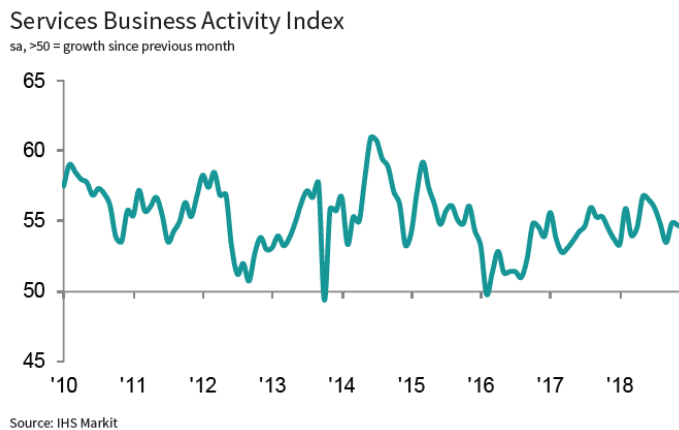
"A shift to inventory reduction was highlighted by purchasing activity in the manufacturing sector rising at the weakest rate for one and a half years in December, providing further evidence that companies have become increasingly cautious about spending amid rising uncertainty about the outlook."

<https://www.markiteconomics.com/Survey/PressRelease.mvc/05d9f578300847c99c422e6886c8f542>

US Services PMI (Dec)

Private sector services activity continued to expand but at a slightly slower rate in the latest month.

Dec 54.4 (revised up from the prelim 53.6 index) versus Nov 54.7



New orders continued to grow but growth slowed - this was the slowest increase in new orders since Oct 2017. New export business also fell into contraction.

Order backlogs declined as capacity pressures eased. Despite this fall in backlogs, employment continued to increase.

Input prices increased but the rate of increase was the lowest since Aug. Some cited higher wages, higher interest rates and higher transportation costs.

Service firms recorded lower levels of optimism towards future business activity in Dec.

<https://www.markiteconomics.com/Survey/PressRelease.mvc/ab3f68183e0947459ee08713c44f2275>

Challenger Job Cut Report (Dec)

The total number of US job cut announcements in 2018 was 28.6% higher than in 2017. At the same time, announced hiring plans ran 7% below the 2017 total.

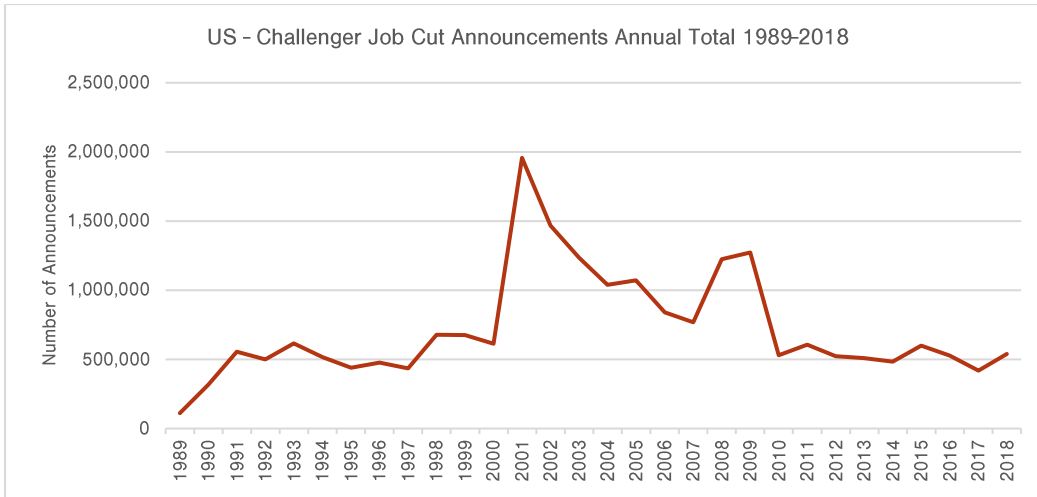
Job Cut Announcements

Month chg: Dec 43.8k versus Nov 53.1k announced job cuts

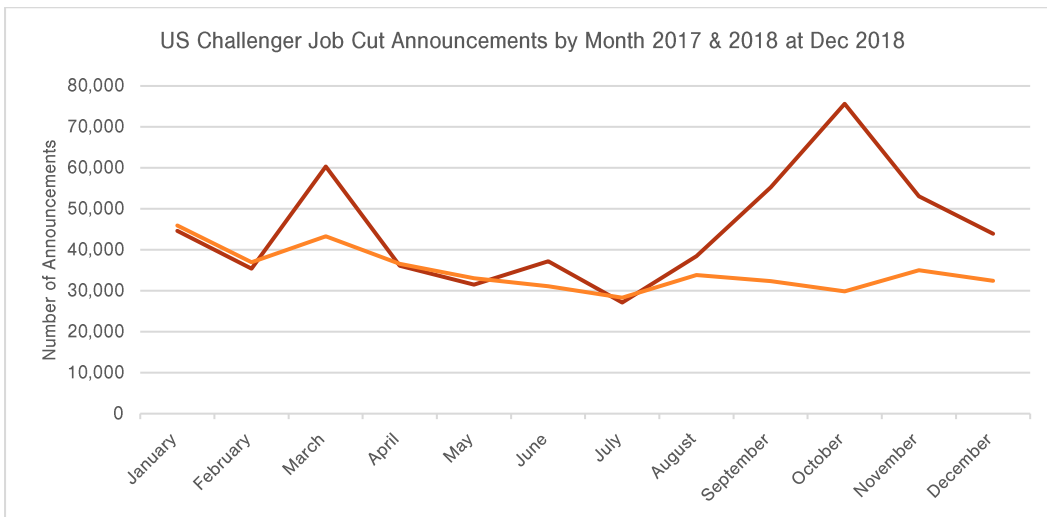
Annual chg 2018; +28.6%

This relatively high annual increase in 2018 was also a function of the very low number of job cut announcements in 2017 - the lowest since 1990.

The current annual total is on par with the average number of job cut announcements since 2010.



During 2018, job cut announcements reached a low in Jul and peaked in Oct and has been running higher than 2017 since Jul;



Job Hiring Announcements

The latest month of job hiring announcements were slightly higher; Dec 15.9k versus Nov 15.4k

The annual total number of job hire announcements decreased by 7% year on year;



Note: the moving annual total is used here due to the large seasonal fluctuation in Sep.

The total hiring announcements are influenced by the large increase in seasonal hiring announcements in Sep. In Sep 2018, seasonal job announcements reached the highest level of the last five years. But excluding Sep/seasonal announcements, the total hiring announcements in 2018 was much lower than the total 7% decline;

Total 2017 less Sep/seas announcements; 677.9k

Total 2018 less Sep/seas announcements; 422.4k (-37%)

<http://www.challengergray.com/press/press-releases/2018-challenger-report-annual-total-29-percent-highest-2015>

Non-Farm Payrolls and Household Labor Force Survey (Dec)

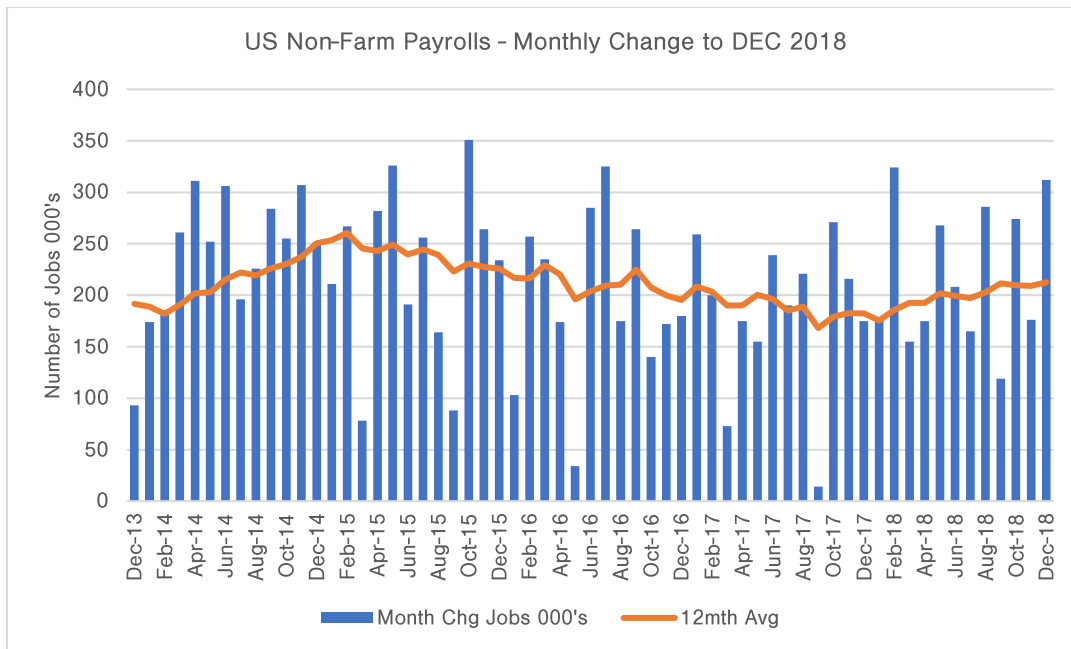
We measure both the household and establishment surveys; The **establishment** survey covers only wage and salary employees on the payrolls of nonfarm **establishments**. This includes multiple jobholding. The **household** survey provides information on the work status of the population without duplication, since each person is classified as employed, unemployed, or not in the labor force.

Non-Farm Payrolls

Growth in non-farm payrolls was very strong in Dec, exceeding expectations while the two prior months were revised higher;

Dec +312k jobs versus Nov +176k jobs (Nov revised higher from +155k jobs)

This result lifted the average monthly growth to the highest level for the year at +213k jobs;



Household Survey – Labour Force

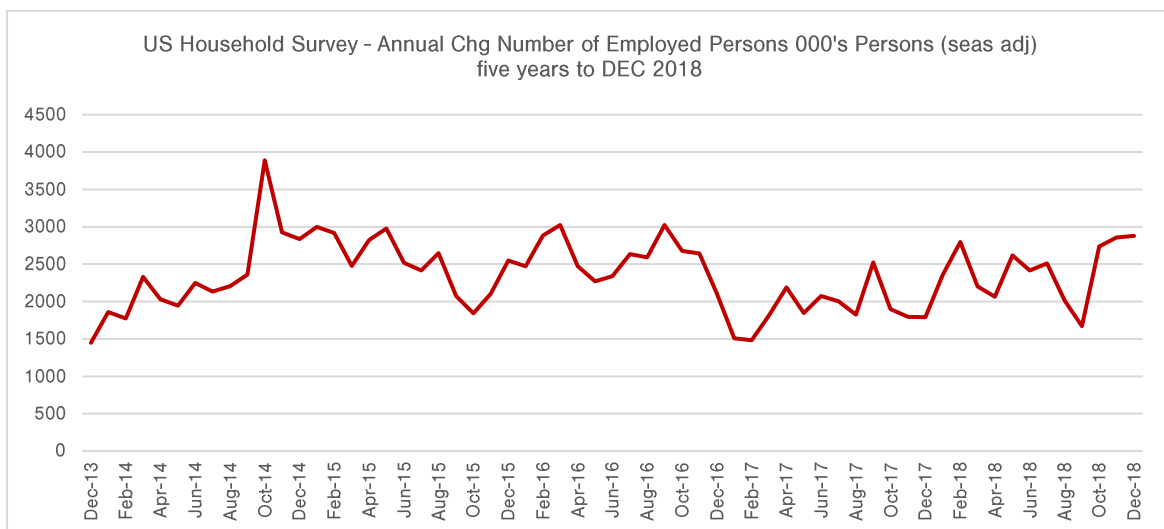
The main feature of the household survey this month was the large increase in labour force participation. Over half of the increase in participation in the last year was recorded outside of the core 25-54yr working age group.

Overall, annual employment continues to grow faster than the estimate of what population growth adds to the labour force. The larger increase in participation meant that total unemployed persons decreased at a slower pace. Importantly, employment growth has still been large enough to absorb workers back into the labor force and reduce total unemployed persons.

Employment

Annual employment growth remained steady but the monthly change in employment continued to slow.

Annual employment growth (16yrs+); Dec 2.88m persons versus Nov 2.86m persons



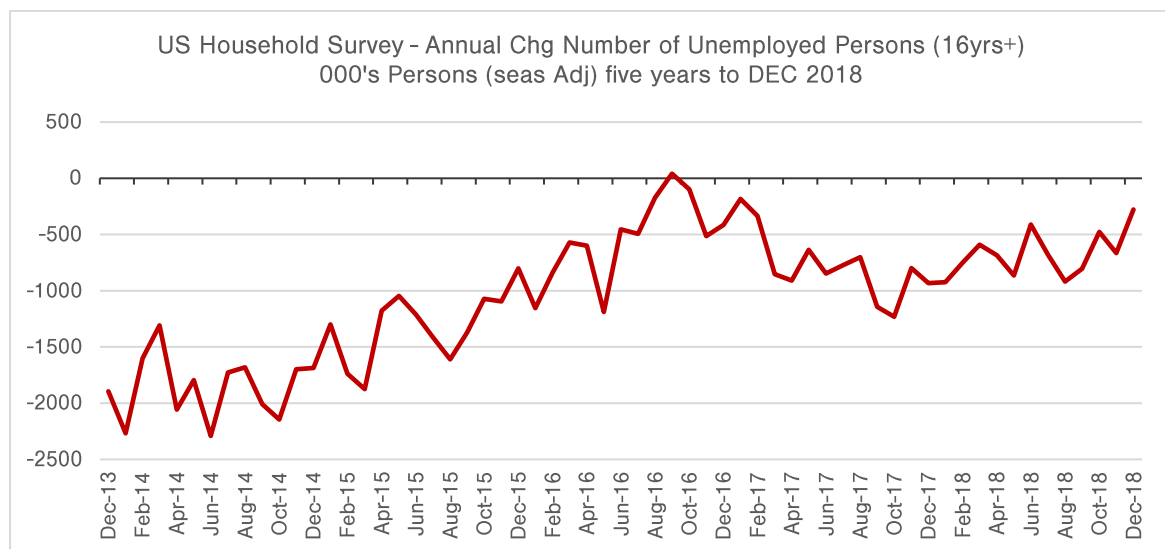
Latest month employment growth; Dec +142k persons versus Nov +221k persons

Its also worth noting the slow down in the annual employment growth for the core working age group 25-54yrs; Annual employment growth slowed from +1.43m persons in Nov to +1.28m persons in Dec. In the latest month, total employed persons 25-54yrs declined slightly by -11k persons.

Unemployment

The total number of unemployed persons continued to fall in the latest year, but that decline has slowed;

Dec -278k persons versus Nov -664k persons



In the latest month, total unemployed persons increased; Dec +276k persons versus Nov -94k persons. The trend is similar for those in the 25-54yr age group.

The unemployment rate ticked up to +3.9% in Dec.

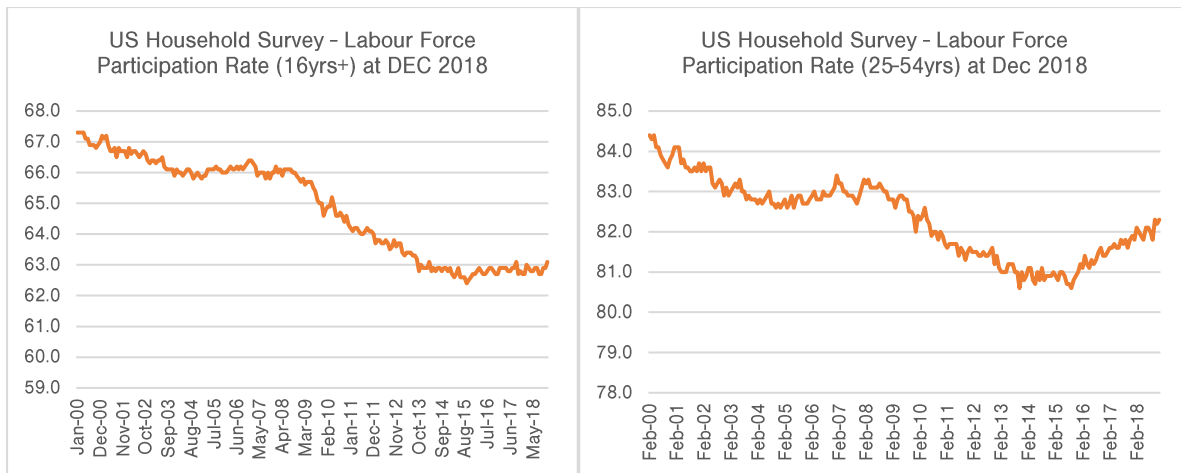
The reason for the slower decline in total unemployed persons is the change in the participation rate.

Participation

In the latest year, participation for those 16yrs+ increased by +0.4%pts. This equates to approx. 1,034m persons returning to the labour force. For the core working age population (25-54yrs) participation also increased by +0.4%pts or approx. +506k persons.

Put another way, half of the increase in participation was the result of people outside of the core working age group to enter/re-enter the labour force in the last year. Most of this has occurred in the last 3-4 months.

Both charts below highlight just how much slack remains in the labor force with participation rates still well below pre-GFC levels:



To summarise; For the 16yrs+ age group, employment continues to grow faster than the estimated change in what population adds to the labour force. The relatively large increase in participation has resulted in a slower decline in total unemployed persons.

Annual chg 000's people (16yrs+) - DEC 2018	
The estimated change in the Labour Force due to pop growth (1)	1569.20
How many jobs available for them? (annual employment growth) (2)	2880.00
Difference (if negative, then employment growing faster than what pop adds to the labour force) (3)	-1310.80
Change labour force participation - people entering/returning to the labour force (4)	1034.80
The remainder is the reduction in total unemployed persons - (4) plus (3)	-276.00
Two views of annual growth in the labour force;	
Total employed persons plus total unemployed persons	2604.00
Est of what population adds to the labor force plus change in participation	2604.00
BLS reported change in the size of the labor force	2604.00

For the 25-54yr age group, employment also continues to grow faster than what population adds to the labor force. Similarly, the relatively large increase in participation has meant that the decline in total unemployed persons has slowed.

Annual chg 000's people (25-54yrs) - DEC 2018	
The estimated change in the Labour Force due to pop growth (1)	639.51
How many jobs available for them? (annual employment growth) (2)	1282.00
Difference (if negative, then employment growing faster than what pop adds to the labour force) (3)	-642.49
Change labour force participation - people entering/returning to the labour force (4)	506.49
The remainder is the reduction in total unemployed persons - (4) plus (3)	-136.00
Two views of annual growth in the labour force;	
Total employed persons plus total unemployed persons	1146.00
Est of what population adds to the labor force plus change in participation	1146.00
BLS reported change in the size of the labor force	1146.00

Earnings

Average weekly earnings continue to grow; Dec +3%

Average hourly earnings; Dec +3.3%

<https://www.bls.gov/news.release/empsit.nr0.htm>

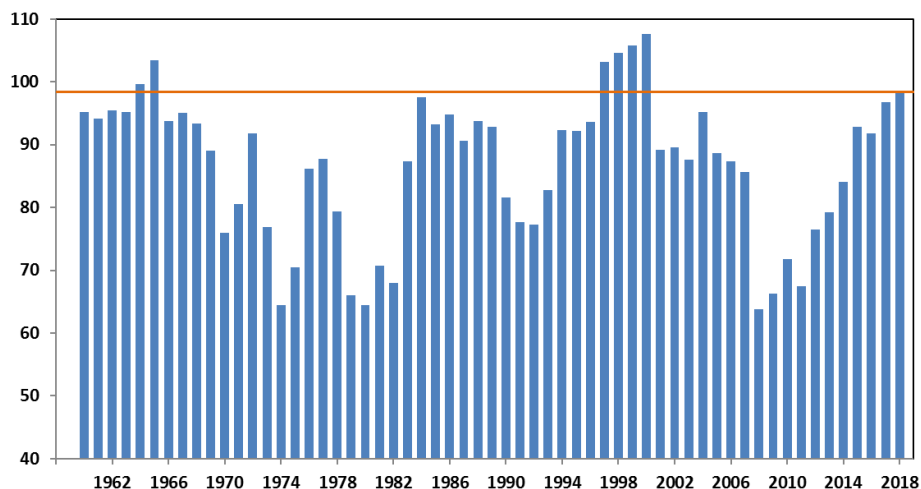
University of Michigan – Surveys of Consumers Dec 2018

The Dec results highlight some interesting insights – especially related to the stock market and employment.

Consumer sentiment in the US has remained close to high levels throughout the year;

“The Sentiment Index averaged 98.4 in 2018, the best year since 107.6 in 2000”

The Index of Consumer Sentiment



© University of Michigan 2018

From the final Dec results for 2018;

While the plunge in stock prices has recently garnered the most attention in the national press, consumers have focused more on their concerns about income and job prospects. **Consumers reported more negative than positive news about job prospects for the first time in two years, with the shift widespread across socioeconomic subgroups. When asked about prospects for the national unemployment rate, 30% expected increases, up from last month's 22% and the highest percentage in two years. Importantly, this still meant that 70% anticipated no increase in unemployment in the year ahead.** Surprisingly, even in the last week of the survey, falling stock prices were reported by just 12% as a primary concern about recent economic developments. This may reflect their initial dismissal as another indication of the heightened volatility of stock prices, and not signal an emerging downtrend. While next month's data may reflect increased concerns, it has been news of changing job and income prospects that have been of the greatest concern to consumers.

<http://www.sca.isr.umich.edu/>

The early Dec report also had similar references;

In the early December survey, however, consumers did mention hearing much more negative news about future job prospects.

When specifically asked how they expected the unemployment rate to change in the year ahead, the balance of opinion turned negative for the first time in the past eighteen months. While one month's results must be treated with caution, if it is confirmed in the months ahead, it will act to diminish consumer spending in 2019.

<https://data.sca.isr.umich.edu/fetchdoc.php?docid=61696>

US FED/FOMC

Chairman Powell's comments calmed the markets last week. While he didn't shift the policy approach, he did shift his messaging making more explicit the willingness of the Fed/FOMC to adjust either rates and/or balance sheet run-off.

"IF we came to the view that the balance sheet normalisation plan, or any other aspect of normalisation was part of the problem, we wouldn't hesitate to make a change".

Prior comments, especially related to balance sheet run-off, have been quite decisive, i.e. 'will run on autopilot'. Based on Chairman Powell's comments on this panel, balance sheet runoff is likely to continue – for the moment, Powell believes that "the amounts are not that big" (when compared to the new US Treasury issuance).

Further quotes;

"There is no pre-set path" for policy. Inflation is muted, so will be "patient" in its approach to monetary policy.

“Always prepared to shift policy and shift it significantly if necessary”

Will this year be like 2016? (also a soft patch);

“We will be prepared to adjust policy quickly and flexibly, and to use all of our tools to support the economy should that be appropriate”

Markets expressing concerns about the future (growth and trade negotiations) and pricing in "downside risks" that aren't visible yet.

Listening carefully to what those signals are saying and taking that into account.

<https://www.aeaweb.org/webcasts/2019/us-federal-reserve-joint-interview>

<https://www.stlouisfed.org/fomcspeak>

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Europe

Germany CPI – Prelim (Dec)

The prelim CPI for Dec shows consumer price growth abating on the back of lower oil/energy price growth.

Headline CPI – annual change; Dec +1.7% versus Nov +2.3%

The annual change in the prices of Goods slowed substantially; Dec +2% versus Nov +3.2%. This slower growth was led by energy price growth halving from +9.3% in Nov to +4.8% in Dec. While the growth has slowed, prices remain higher than year ago. Food prices growth also slowed somewhat.

The annual change in the prices of Services including Rents was unchanged; Dec +1.5% versus Nov +1.5%.

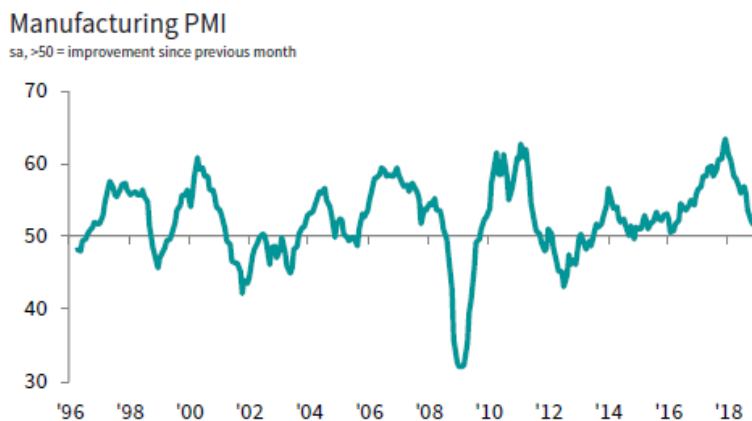
The final Dec results released 16 Jan 2019.

https://www.destatis.de/EN/PressServices/Press/pr/2018/12/PE18_518_611.html;jsessionid=B97D3C0E6C3A54715BC03075F6A51E5E.InternetLive2

Germany Manufacturing PMI (Dec)

The headline PMI indicated that manufacturing activity slowed further in the latest month. Production increased slightly, despite the drop in new orders, as firms reduced order backlogs.

Dec 51.5 versus Nov 51.8



Source: IHS Markit

The key issue remains the fall in new orders. In Dec, new orders continued to fall further into contraction, the steepest fall since Nov 2014. New export orders recorded the steepest fall for six years.

Production/output increased at a slightly faster pace than in Nov & Oct – due to consumer goods. Production of intermediate and capital goods contracted slightly. This is yet to show up in the German industrial production data.

Production increased slightly, despite the drop in new orders, as firms reduced order backlogs. Both the stock of finished goods and order backlogs declined by the most in six years.

Manufacturers reduced their purchases of raw materials and semi-finished goods – the third decline in three months.

Employment growth increased slightly after slowing to a 23month low in Nov.

Input cost growth slowed – firms cited lower oil prices.

“Business confidence towards the year-ahead outlook stayed close to last October's near six-year low. Sentiment was curbed by uncertainty relating to Brexit, trade frictions and the slowdown in the automotive industry”

<https://www.markiteconomics.com/Survey/PressRelease.mvc/96da18b3cfbc4e3f97424c53e1777ec1>

Germany Services PMI (Dec)

Private sector service activity in Germany grew at a much slower pace in Dec. This is the third month of slower growth led by a further slow down in the growth of new orders. Services output growth was supported by further declines in work backlogs.

Dec 51.8 (revised down from prelim 52.5) versus Nov 53.3 (-1.5pts)

Services Business Activity Index

sa, >50 = growth since previous month



Source: IHS Markit

While new work increased, the rate of expansion slowed to the lowest level in seven months. New export business recorded another fall in the month.

Firms worked through order backlogs resulting the first decline in outstanding business in ten months.

As backlogs fell, employment growth also slowed further after almost reaching an eleven-year high back in Sep.

Input prices increases slowed after reaching a seven-year peak in Nov.

December saw the degree of optimism among services firms drop to the lowest in over three years as concerns grew in relation to a slowdown in the economy, geopolitical uncertainties and volatility in financial markets.

<https://www.markiteconomics.com/Survey/PressRelease.mvc/23bd37c50cf4412ba572ebc1dbf5311b>

Eurozone Manufacturing PMI (Dec)

The manufacturing PMI indicated that private sector manufacturing activity continued to grow at a slower pace in Dec. New orders in the Eurozone fell for the third month, but production grew slightly as firms reduced order backlogs.

Dec 51.4 versus Nov 51.8

IHS Markit Eurozone Manufacturing PMI



The four largest manufacturing economies posted the lowest PMI readings; Italy remained in contraction, France PMI moved into contraction (admittedly amid a period of protests) and manufacturing growth was slower in Germany and Spain.

Slower growth in new orders was the main driver of the lower PMI. Total new orders in the Eurozone fell for the third month.

Output growth increased slightly as firms continued to work on order backlogs.

Inventories increased. Employment grew at a slightly faster pace but remains close to Nov lows. Input price inflation eased for firms.

“Business confidence regarding output in a year’s time was the lowest recorded by the survey since the end of 2012”

<https://www.markiteconomics.com/Survey/PressRelease.mvc/e35efd4d974d433a9c914419313231a5>

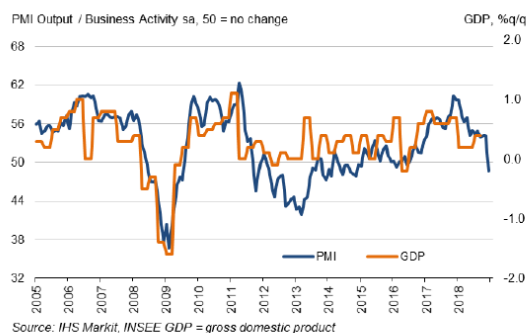
Eurozone Services PMI (Dec)

Growth in private sector services activity slowed further across the Eurozone in the latest month. One reason for the sharper slowdown were the protests in France. But growth in Germany and Italy service PMI's also slowed, while Spain was unchanged.

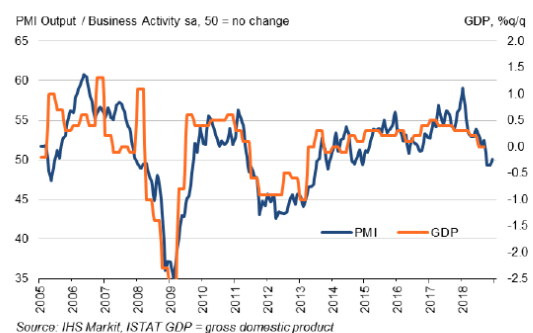
Dec 51.2 versus Nov 53.4 (-2.2pts)

Composite PMI Output measures across key Eurozone economies;

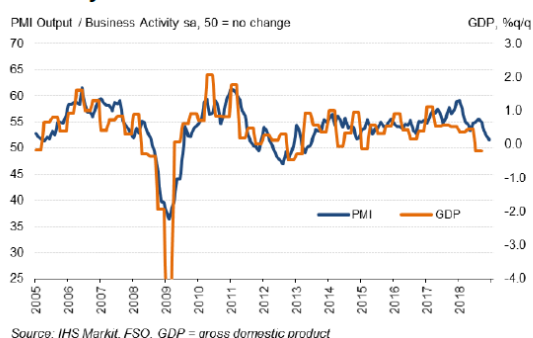
France



Italy



Germany



Spain



<https://www.markiteconomics.com/Survey/PressRelease.mvc/1b8bb14c90a04470a1768dafaeb8fc079>

Eurozone CPI Prelim (Dec)

The Dec CPI indicated that annual growth in consumer prices had slowed further across the Eurozone. The slowdown in growth was mostly the result of lower growth in energy prices. Growth in processed food, alcohol and tobacco prices also slowed somewhat.

Annual All-items HICP growth; Dec +1.6% versus Nov +1.9%

This is now well below the ECB target of 'below, but close to 2% over the medium term'.

Annual core CPI growth (less food energy alcohol and tobacco); Dec +1% versus Nov +1% (using this measure, CPI growth hasn't changed much since Dec 2017 CPI growth of +0.9%).

Annual energy price growth has slowed in the latest month but is still well ahead of the annual rate recorded last year; Dec +5.5% versus Nov +9.1% (Dec 2017 +2.9%).

Services prices continue to growth a constant pace; Dec +1.3% versus Nov +1.3%. A year ago, the annual growth was +1.2%.

<https://ec.europa.eu/eurostat/documents/2995521/9473029/2-04012019-AP-EN/44cdf5df-7dd7-47a8-add2-98ddf2611c4a>

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Japan

Industrial Production – Prelim (Nov)

On a monthly, seas adj basis, Japanese industrial production declined by -1.1% in Nov after the much stronger growth rebound in Oct. The survey of monthly production had forecast a +0.6% increase in industrial production in Nov.

Annual growth slowed after the strong rebound in Oct but remains higher than year ago. The Oct and Nov results appear to have broken the trend of slower growth.

Monthly % chg (seas adj)

Production; Nov -1.1% versus Oct +2.9%

The decline in production was led by general-purpose and business-oriented machinery, electrical machinery, and information and communication electronics equipment and electronic parts and devices.

Shipments; Nov -1.4% versus Oct

The decline in shipments was led by; general-purpose and business-oriented machinery, motor vehicles and electrical machinery & information and communication electronics equipment.

Inventories; Nov +0.2% versus Oct

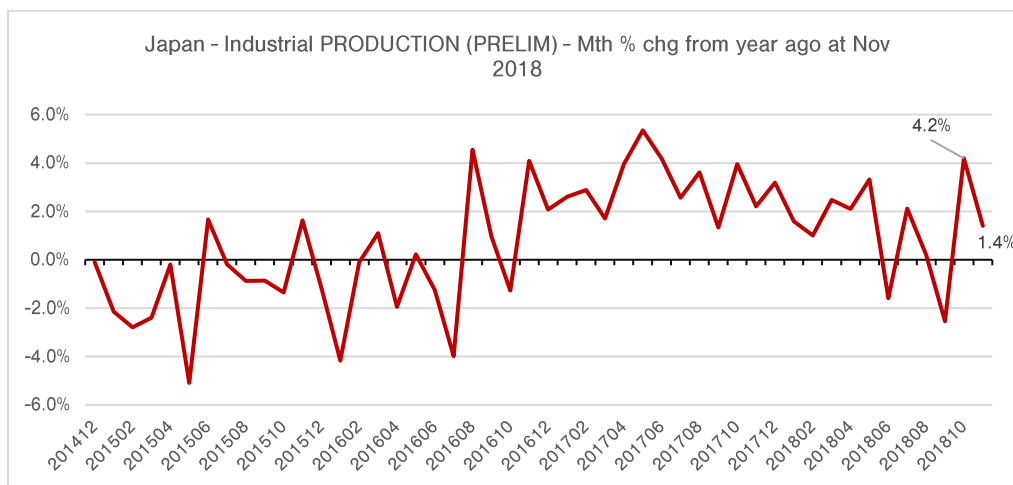
Growth in inventories was led by petroleum and coal products, motor vehicles and chemicals (excl. Inorganic, organic chemicals, and medicine).

Inventory Ratio; Nov -1.8% versus Oct

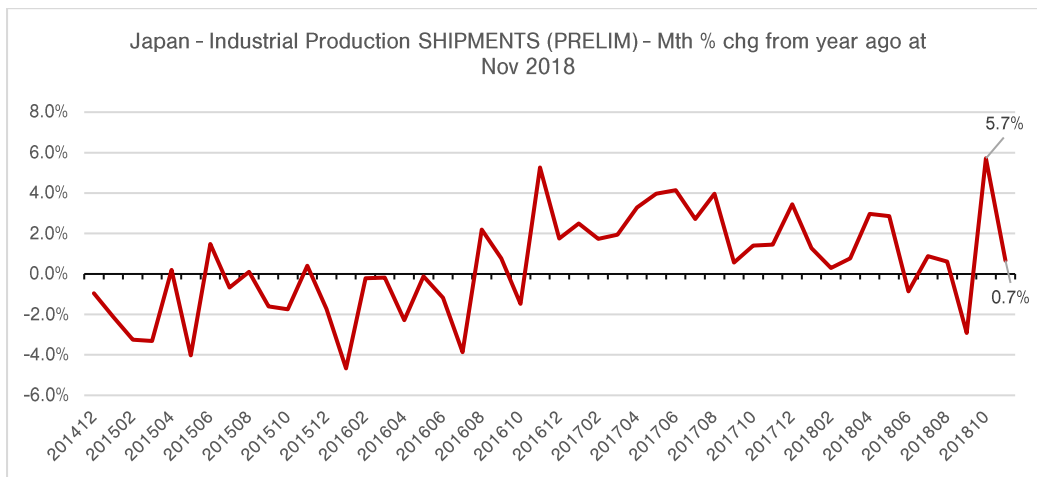
The forecast for Dec industrial production growth has remained unchanged at +2.2%. The forecast for Jan is -0.8%.

Annual % chg (non-seas adj)

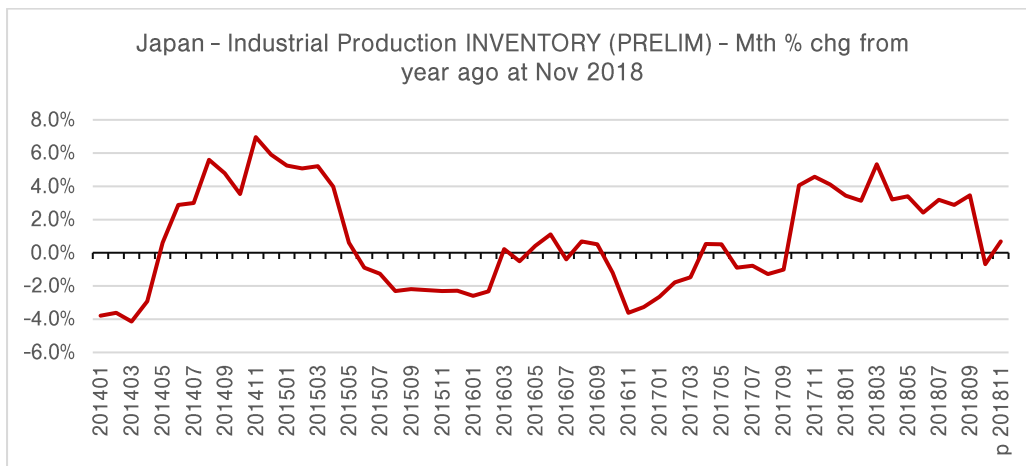
Production; Nov +1.4% versus Oct +4.2%



Shipments; Nov +0.7 versus Oct +5.7%



Inventories of finished goods; Nov +0.7% versus Oct -0.7%



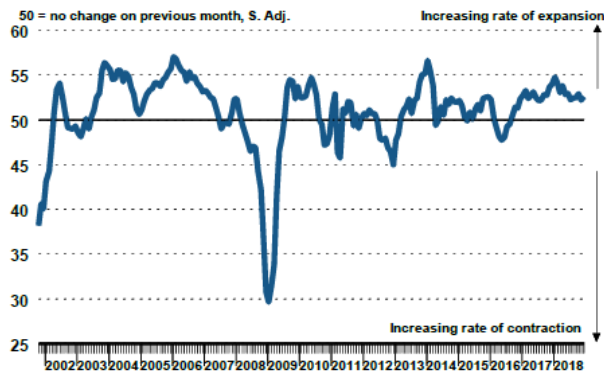
<http://www.meti.go.jp/english/statistics/tyo/iip/index.html>

Japan – Manufacturing PMI (Dec)

The headline PMI shows that private sector manufacturing activity continued to grow at a slightly faster pace in Dec. While new orders and production continued to grow, new export orders fell back into contraction, highlighting ongoing issues with slower trade growth.

Dec 52.6 versus Nov 52.2

Nikkei Japan Manufacturing PMI



Sources: Nikkei, IHS Markit

New orders increased, but growth was 'modest overall'. New export orders fell back into contraction. "Unfavourable workload growth" was cited in markets such as Nth America, China and Taiwan.

Production increased at the fastest level since Apr. Backlogs also increased – somewhat hampered by stock shortages and prolonged input delivery times.

Employment increased at a slower rate – the weakest in three months.

Input price inflation slowed somewhat during Dec.

Business confidence, while still increasing, fell to a 7-month low. Optimism regarding the 2020 Olympics was offset by concerns over the 2019 sales tax hike.

<https://www.markiteconomics.com/Survey/PressRelease.mvc/c41d751a58be49568d76e9b125589975>

Retail Trade – Prelim (Nov)

Retail sales declined in Nov and annual growth slowed on the back of slower growth and declines across all retail categories.

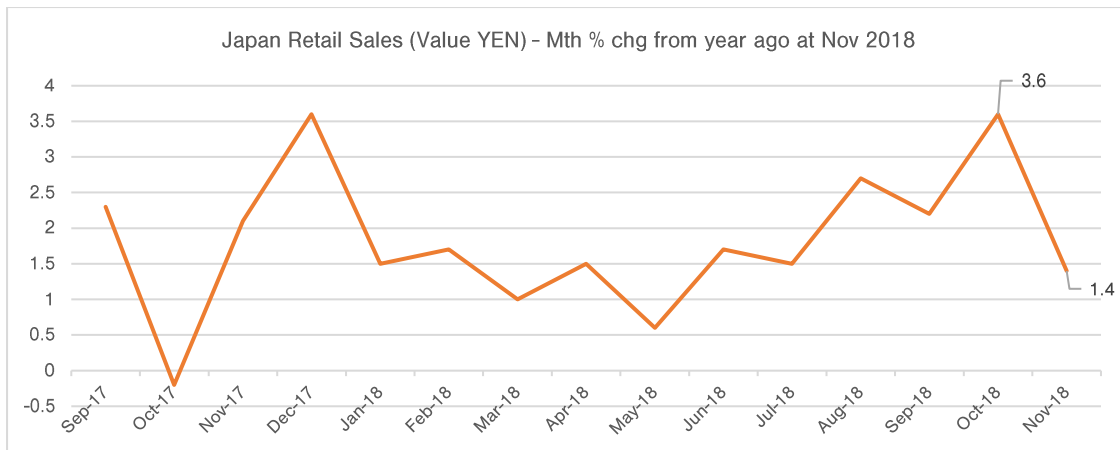
Retail Sales - Monthly chg: Nov -1% versus Oct +1.3%

On an annual basis, retail sales growth slowed by more than half.

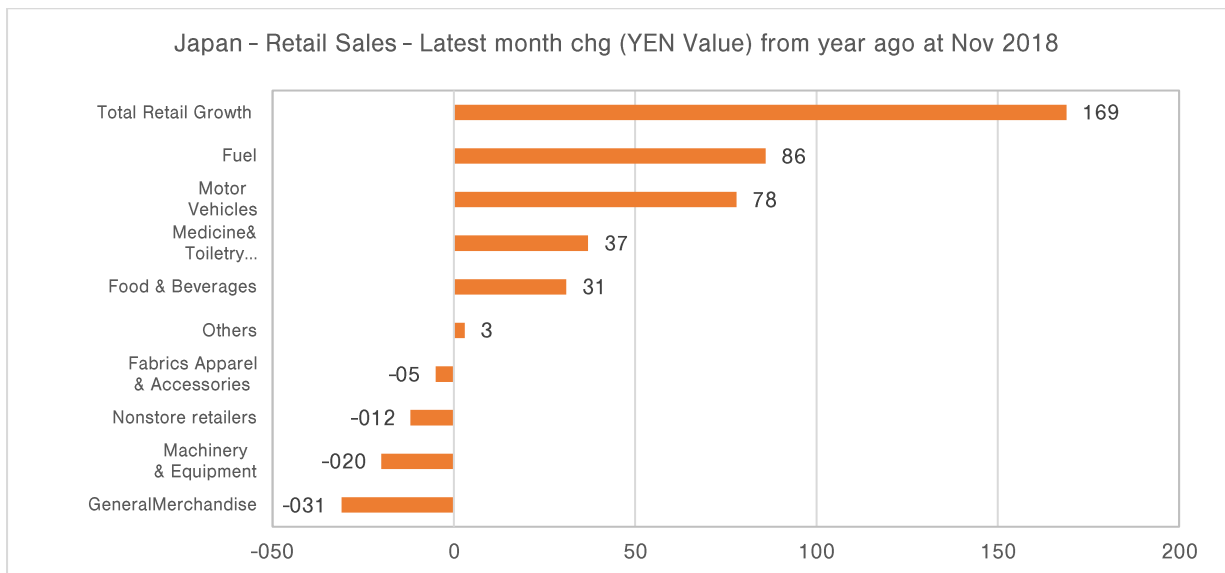
Retail Sales – Annual chg: Nov +1.4% versus Oct +3.6%

Excluding the value of fuel sales, annual retail sales growth was +0.8% in Nov versus +2.6% Oct.

This months' sales have put a hefty dint in the solid growth trend between May and Oct 2018;



This slower annual growth was the result of lower growth or faster declines across all categories (values in ¥);



<http://www.meti.go.jp/english/statistics/tyo/syoudou/index.html>

BoJ Summary of Opinions (Dec)

This is the BoJ meeting just after the prelim Q3 GDP decline was revised even lower, so I was expecting some elaboration on the BoJ view of conditions.

The range of opinions on economic and financial developments are very much skewed to a more positive view of the economy. The Q3 decline in GDP was attributed to temporary factors. Some possible downsides mentioned; uncertainties in the global economy incl the trade friction between the US and China. But the effects of trade frictions and global decline in stock prices on the Japanese economy had been limited so far.

Two opinions stand out as more candid, especially as related to trade (confirmed by data previously reported here);

Downside risks to economic activity have been heightening. Looking at the latest data on trade activities in China, both exports and imports marked negative growth on a month-on-month basis, which possibly indicates a deceleration in the Chinese economy. Turning to Japan's economy, it cannot be said that the actual condition of restoration-related demand and production stemming from natural disasters has been strong. In addition, the recovery in exports to China has been weak, and exports as a whole also have shown weak developments.

In China, defaults of private firms have been increasing, and authorities have been requesting that banks increase lending in order to resolve the difficulty in funding. Developments in private firms' funding under these circumstances warrant close attention.

On prices – most opinions expressed say that the positive output gap will remain in positive territory allowing inflation to gradually move towards the target rate. Again, there are several candid comments that reinforce that CPI growth is not on the path to the 2% target. The impact of the fall in oil prices is also cited;

There is a low possibility that the output gap will continue to widen within positive territory going forward, and a decline in crude oil prices also will contribute to further delaying the achievement of the price stability target.

On monetary policy – there was broad support for continued easy monetary policy.

Cabinet office opinions;

In the government's economic outlook -- approved by the Cabinet on December 18 -- the real GDP growth rates for fiscal 2018 and 2019 are projected to be about 0.9 percent and about 1.3 percent, respectively.

http://www.boj.or.jp/en/mopo/mpmsche_minu/opinion_2018/opi181220.pdf

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United Kingdom

Brexit

The Brexit vote in the UK Parliament on 15 Jan 2019 is under question. There are reports that PM May could further delay the vote. It is also being reported that the PM is possibly making approval of the deal conditional on the EU providing further concessions.

While the EU has stated that it will not change its stance on the deal, there appears to be some negotiation underway. Source: The Telegraph

One of the main issues for MP's is that Irish border backstop is not time-limited and that this could keep the UK in the customs union with the EU indefinitely.

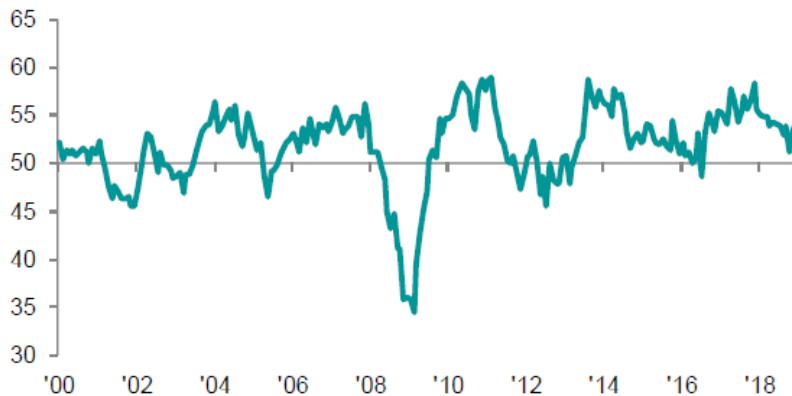
Manufacturing PMI (Dec)

The Manufacturing PMI tells an interesting story of firms preparing for Brexit. The UK Manufacturing PMI reached a new 6-month high in Dec, led by increases in stock holdings and new orders.

Dec 54.2 versus Nov 53.6

Manufacturing PMI

sa, >50 = improvement since previous month



New order growth increased to a 10-month high as clients (domestic and export) increased purchasing to build safety stock coming into Brexit. The weaker GBP was also cited as helping to win new export business.

Output also increased, but at a slower pace than in Nov.

The purchase of inputs and subsequent increase in inventories, was at the fourth fastest pace in the history of this report.

The stock of finished goods also increased at a faster rate, with the rate of increase the second-strongest since the survey began.

Input price growth slowed. Any increases in input prices were cited to be related to expectations of a further weaker GBP.

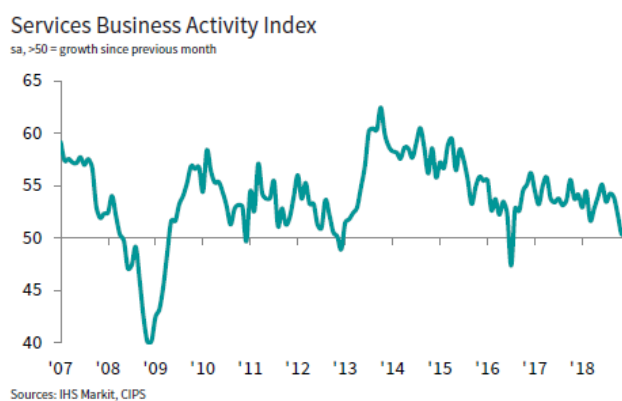
The telling part of this report is the outlook for 12 months' time. While still positive, confidence increased only slightly above the 2 year low reached in Nov.

<https://www.markiteconomics.com/Survey/PressRelease.mvc/73ab261ce1c449f885a9ec6b053c0fff>

Services PMI (Dec)

Growth of the UK services PMI bounced back in Dec off the very low level reached in the month prior. Activity expanded at a slightly faster pace on the back of slightly higher new orders and mostly due to further declines in order/work backlogs.

Dec 51.2 versus Nov 50.4



Overall, firms cited Brexit related concerns for the slowdown. Some firms also indicated that 'subdued' consumer demand had affected activity.

Growth in new work/orders increased slightly from the 28-month low reached in the month prior. Firms cited political uncertainty and lower projections for 2019 growth as reasons for the overall slowing growth.

Backlogs of work declined for the third month.

With less pressure on capacity, employment growth slowed in the latest month. The increase was 'marginal' and slowest pace of increase for over 2 years. Some firms still cited tight labour market conditions and difficulty finding skilled staff.

Input costs increased at a continued slower pace – a 6-month low. Costs were impacted by rising wages, food prices and imported goods.

“December data indicated a moderation in business optimism across the service economy for the third month running. Moreover, the degree of confidence towards business activity in the coming year is now the second-weakest recorded by the survey since March 2009.”

<https://www.markiteconomics.com/Survey/PressRelease.mvc/c56316eb27e248719e9464b7c8f67778>

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Australia

House Prices – CoreLogic at 31 Dec 2018

Dwelling prices continued to fall at a National level, led by further declines in the two major capital cities;

CoreLogic RP Data Daily Home Value Index: Monthly Values - 31 December 2018

City	All dwellings			Houses			Units		
	Month End Value	% Change Year on Year	% Change Month on Month	Month End Value	% Change Year on Year	% Change Month on Month	Month End Value	% Change Year on Year	% Change Month on Month
Sydney	158.31	-8.88▼	-1.82▼	159.97	-10.03▼	-1.86▼	153.93	-6.28▼	-1.73▼
Melbourne	145.82	-7.04▼	-1.50▼	155.10	-9.12▼	-1.95▼	128.49	-2.28▼	-0.53▼
Brisbane (inc Gold Coast)	108.30	0.02▲	-0.21▼	113.43	0.14▲	-0.34▼	93.95	-0.40▼	0.20▲
Adelaide	117.06	1.33▲	0.21▲	117.15	1.27▲	0.16▲	116.64	1.69▲	0.50▲
Perth	92.12	-4.73▼	-0.98▼	94.28	-4.32▼	-0.97▼	83.03	-6.46▼	-1.04▼
5 capital city aggregate	136.66	-6.42▼	-1.34▼	138.65	-7.16▼	-1.44▼	131.65	-4.44▼	-1.10▼
Brisbane	108.13	0.22▲	-0.18▼	112.94	0.42▲	-0.29▼	89.85	-0.67▼	0.30▲
Darwin	82.24	-1.54▼	-1.84▼	92.81	3.74▲	-1.77▼	66.68	-10.39▼	-1.98▼
Canberra	120.79	3.27▲	-0.02▼	127.88	3.66▲	-0.05▼	99.35	1.98▲	0.11▲
Hobart	133.81	8.66▲	0.43▲	134.58	8.31▲	0.50▲	130.75	10.17▲	0.12▲

Note: 5 capital city aggregate includes Sydney, Melbourne, Brisbane (inc. Gold Coast), Adelaide and Perth. Month and Year Changes are updated monthly and calculated as at the end of each calendar month respectively.

<https://www.corelogic.com.au/research/monthly-indices>

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China

Two sets of Chinese PMI data are reported here. The official PMI tracks large sized companies, mostly state owned. The Caixin PMI tracks mostly small sized companies. Both measures show manufacturing activity in contraction.

China – Official PMI (Dec)

NBS Manufacturing PMI; Dec 49.4 versus Nov 50

Non-Manufacturing PMI; Dec 53.8 versus Nov 53.4

Caixin General Manufacturing PMI (Dec)

The headline manufacturing PMI fell into contraction in the latest month.

Manufacturing PMI; Dec 49.7 versus Nov 50.2



Sources: IHS Markit, Caixin.

While production increased slightly in the latest month, new orders continued to fall. New export orders also fell for the ninth month in a row but at a slower pace than in Nov.



Note: Any reading over 50 suggests a sector is expanding

Source: FactSet

Employment continued to fall.

Inventories of inputs were little changed while stocks of finished goods increased slightly.

Firms decreased output charges (cut prices) for the second month in a row, partly due to further falls in input costs.

“In general, China’s manufacturing sector faced weakening domestic demand and subdued external demand in December. Companies had a stronger intention to destock and prices of industrial products were declining, which could further drag on production. It is looking increasingly likely that the Chinese economy may come under greater downward pressure.”

<https://www.markiteconomics.com/Survey/PressRelease.mvc/43505f4c1b3f489cb553cb84bdf d52ec>

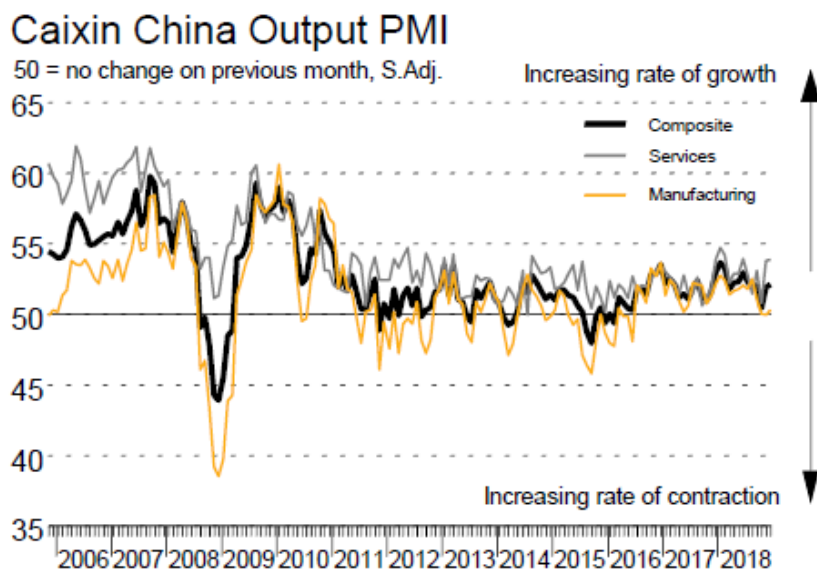
China General Services PMI (Dec)

The China Business Services activity index expanded at a slightly faster rate in the latest month and somehow offset the weaker manufacturing print. The overall composite index increased at a faster rate.

Total Composite PMI (Services & Manufacturing): Dec 52.2 versus Nov 51.9

Services Business Activity Index:

Dec 53.9 versus Nov 53.8



Sources: IHS Markit, Caixin.

New orders for services increased modestly.

Employment/job creation was marginal, with growth falling to a 3-month low.

Input prices fell for the second month. Services output charges increased only slightly in Dec.

“Overall business confidence remained relatively subdued in the context of historical data, with a number of surveyed firms citing concerns over relatively soft market conditions”

<https://www.markiteconomics.com/Survey/PressRelease.mvc/55fdee470bd64aa0a75420aab822aa04>

PBOC – Required Reserve Ratio

The Chinese central bank will cut the bank Required Reserve Ratio by 1ppt to release about 1.5tn Yuan (US\$210b) of liquidity. The People’s Bank of China will cut the reserve requirement ratio by 0.5 percentage point each on 15 Jan and 25 Jan.

On Wednesday, the PBOC changed the definition of a small business, meaning loans to an enterprise with a credit line of less than 10 million yuan will qualify for targeted RRR cuts, up from the previous standard of 5 million yuan. This will allow banks to lend more capital to enterprises now classed as small businesses, and therefore free up more reserves from the central bank, with estimates ranging from 400 billion yuan to as much as 700 billion yuan.

<https://www.scmp.com/economy/china-economy/article/2180758/china-prepares-testing-2019-freeing-us210-billion-latest-move>

This brings the total to four RRR cuts since the start of 2018:



<https://tradingeconomics.com/china/cash-reserve-ratio>

While the availability of cash/liquidity has been increasing, the PBoC's interest rate has remained unchanged (at Dec 2018):



<https://tradingeconomics.com/china/interest-rate>

The decreases in the RRR have not seemed to have had an impact on data coming out of China. Despite the RRR cuts, loans growth has only accelerated slightly mid-2018 and has remained constant through the back half of the year.



SOURCE: TRADINGECONOMICS.COM | PEOPLE'S BANK OF CHINA

<https://tradingeconomics.com/china/loan-growth>

Last week, the Chinese Government also announced plans to approve local government bond issues (1.39tr Yuan) to further stimulate growth.

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Trade

US-China Trade Negotiations

A US delegation will attend trade talks in China on 7-8 Jan. The USTR statement including attendee's, can be found here; <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/january/statement-regarding-united-states>

From last week's briefing document;

USTR Lighthizer is now leading the negotiations with China. The following article is recommended regarding the trade dispute and the perspective of Robert Lighthizer; <https://www.theatlantic.com/politics/archive/2018/12/robert-lighthizers-bid-cut-chinas-trade-influence/578611/>

<https://www.theatlantic.com/politics/archive/2018/12/robert-lighthizers-bid-cut-chinas-trade-influence/578611/>

A 'hard deadline' of 1 Mar 2019 has been established for both sides to reach an agreement. But given the perspective of the current US administration - that "the United States is currently engaged in a long-overdue reckoning with China over its predatory trade practices" – it would seem an enormous task to engineer a complete 'restructure' of the trade relationship between the two countries by this date.

<https://www.theatlantic.com/international/archive/2018/10/trump-china-trade/572122/>

At the same time, a positive outcome is something that could shift sentiment, especially regarding the business outlook in the US.

For the moment, uncertainty and headline risk around trade and tariffs remains as heightened as ever. Adding further strain to this deadline will be the Christmas and Chinese New Year breaks.

<https://www.federalregister.gov/documents/2018/12/19/2018-27458/notice-of-modification-of-section-301-action-chinas-acts-policies-and-practices-related-to>

Special 2019 Section 301 Review

Posted on the Federal Register by the USTR is a request for comments and a notification of a public hearing for the annual special S.301 review;

to identify countries that deny adequate and effective protection of intellectual property rights (IPR) or deny fair and equitable market access to U.S. persons who rely on intellectual property protection.

The special 301 subcommittee will hold a hearing on 27 Feb 2019.

On 26 Apr 2019, the USTR will publish the 2019 special 301 report within 30 days of the National Trade Estimate Report.

<https://www.federalregister.gov/documents/2018/12/28/2018-28319/request-for-comments-and-notice-of-a-public-hearing-regarding-the-2019-special-301-review>

NAFTA/USMCA

It's been reported that the Democrats support the new labor provisions of the agreement (they were consulted by the USTR in the negotiation process) but are concerned that provisions don't go far enough to protect workers.

Sen. Chuck Grassley (R-IA), who will chair the Senate Finance Committee that will usher the USMCA through the chamber in 2019, even gave a sort-of endorsement of the president's hardball strategy. "That's a hard-nosed approach, but sometimes the president has to use that if he wants to get things accomplished," Grassley said on a Monday radio show, according to the Washington Post.

<https://www.vox.com/2018/12/4/18123809/usmca-trump-nafta-withdrawal-congress>

US-Japan Trade Talks

Public hearings have been completed and talks are likely to start in Jan 2019.

As noted in the announcement, the USTR will publish objectives for the negotiations at least 30 days before negotiations begin. There are currently no announcements.

<https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/october/trump-administration-announces>

<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

The final report on the S232 has not yet been made public.

President Trump hinted that he is consider imposing steeper tariffs on imported passenger vehicles in response to the cost cutting announcement by GM.

"If Washington imposed a 25% tariff on cars as it long has with small trucks, "many more cars would be built here" and GM "would not be closing their plants in Ohio, Michigan & Maryland," Trump tweeted."

"The President has great power on this issue," he wrote."

<https://asia.nikkei.com/Economy/Trade-War/Trump-threatens-to-boost-auto-tariffs-on-GM-restructuring>

This is contrary to commitments made to Japan and Europe to hold off on any tariffs until trade negotiations get underway.

The White House has pledged not to move forward with imposing tariffs on the European Union or Japan as long as it is making constructive progress in trade talks.

<https://www.straitstimes.com/world/united-states/tariff-proposals-on-imported-cars-and-parts-given-to-white-house>

US-Europe Trade Talks

Public hearings for input into the negotiating objectives have been completed.

As noted in the announcement, the USTR will publish objectives for the negotiations at least 30 days before negotiations begin. No announcements have been made at this time.

(<https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/october/trump-administration-announces>)

US-UK Trade Talks

A formal request has now been posted on the US Federal Register for comments on the negotiating objectives for a US-UK trade agreement.

<https://www.federalregister.gov/documents/2018/11/16/2018-24987/request-for-comments-on-negotiating-objectives-for-a-us-united-kingdom-trade-agreement>

A public hearing has been scheduled for 29 Jan 2019 on the negotiating objectives for the US-UK trade talks.

As noted in the announcement, the USTR will publish objectives for the negotiations at least 30 days before negotiations begin. (<https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/october/trump-administration-announces>).

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