MARS CAPITAL PARTNERS

Weekly Macro Review

w/c 9 September 2019

Key Themes

The ECB eased this week due to the continued shortfall of inflation linked to the 'more protracted weakness in the Euro area economy'. Easing measures included a further cut into negative territory for the deposit facility, the reintroduction of QE at €20bn a month, continued reinvestments and changes to TLRTO III operations. Guidance now is that low rates and QE will be applied indefinitely.

The other important news in the announcement/decision was the introduction of the two-tier system of remunerating bank excess liquidity holdings from 30 Oct. It's been suggested that this was a somewhat 'historic' shift in the implementation of monetary policy – the following is worth a read; https://www.philosophyofmoney.net/draghis-historic-farewell/.

News leaked late last week that the WTO ruled in favour of the US regarding illegal EU subsidies for Airbus. The ruling has not yet been made public as both parties review the decision over the next few weeks. The WTO panel will then adopt the decision and make the ruling public. The US has been reviewing the possible list of tariffs in preparation of the ruling. Depending on the details of the ruling, tariffs in EU imports will most likely be implemented. The EU has a similar case outstanding regarding Boeing.

US consumer credit growth accelerated in Jul in line with the much stronger retail sales in that month. The Aug retail sales growth slowed, and, ex autos, growth was 0% versus the month prior. Consumer sentiment rebounded only slightly in the prelim Sep reading, after the larger drop in Aug (linked mostly to negative tariff news).

JOLTs data indicated that while hiring continued to grow, job openings growth slowed further. Layoffs and discharges (involuntary separations) contributed to the increase in total separations. The number of quits (voluntary separations) increased at a faster pace, reaching a new all-time high number of quits, suggesting that workers were more confident in conditions to change jobs.

The growth in the headline all-items CPI slowed slightly on an annual basis to +1.7%. But the core CPI ex food and energy prices accelerated to +2.4%. Both core goods and services contributed to this acceleration. It will be important to see how the FOMC will view this at the upcoming meeting where rates are expected to be cut again.

There has been some optimism emerging regarding progress on an alternative to the current backstop agreement for Brexit. UK rolling GDP data for May-Jul was lackluster with growth at zero % after the prior three-month decline. The labour market remains resilient – somewhat slower annual employment growth was offset by a lower increase in participation which helped reduce total unemployment further.

Australian lending for housing increased at a much faster pace in Aug as easing of lending restrictions and rate cuts continued to take effect. Business confidence eased back again, and business conditions continued to decline in August. There is some indication that conditions may be firming across selected industries.

Contents

US Data

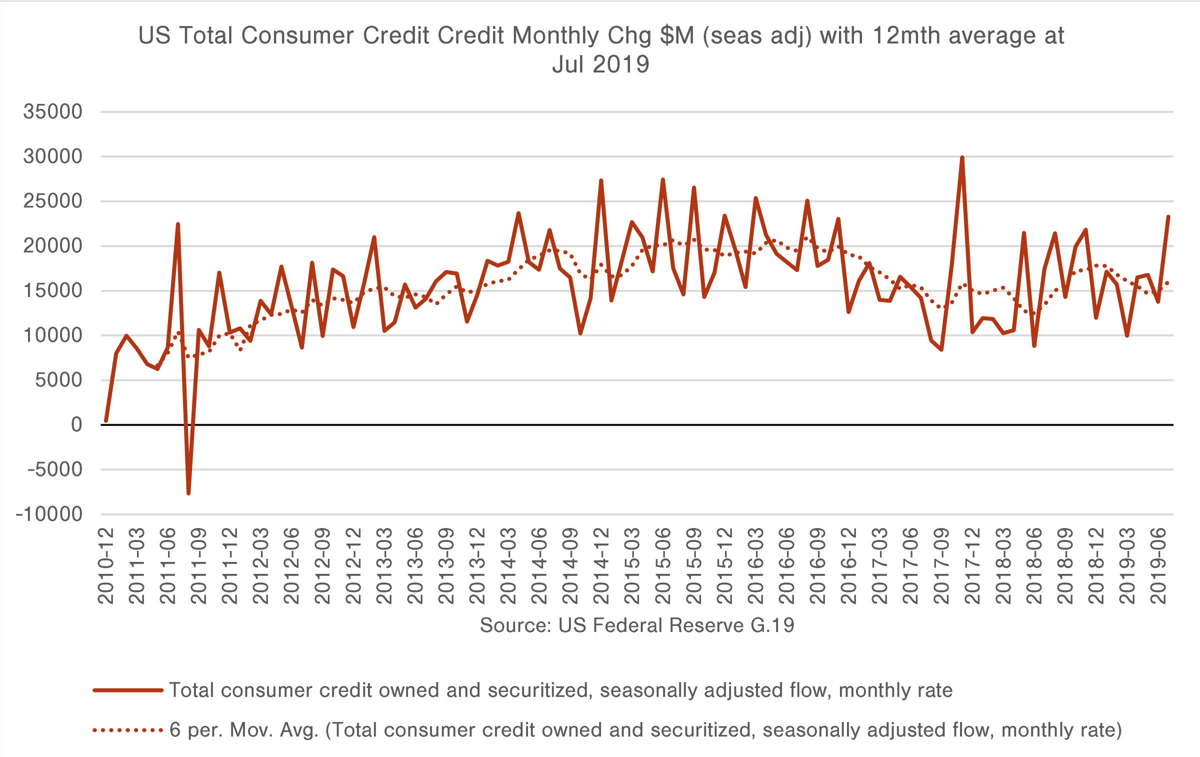
Consumer Credit (Jul)

Total consumer credit increased at an accelerated pace in Jul. Both revolving and non-revolving credit contributed to the increase in the month – but there was a much larger increase in revolving (credit card) credit growth versus the month prior. The growth in non-revolving credit was slightly slower than in the month prior.

The faster increase in flow of new revolving credit is consistent with the much stronger growth in retail sales in Jul – the pace of retail sales growth doubled versus the month prior. The single largest contributor to the growth in retail sales that month was non-store retailers – which accounted for at least half of the headline growth in retail sales. The pace of growth of revolving credit has been 'trending' upwards since Mar 2019 – and the monthly Personal Income and Consumption data indicates that the saving rate has been falling.

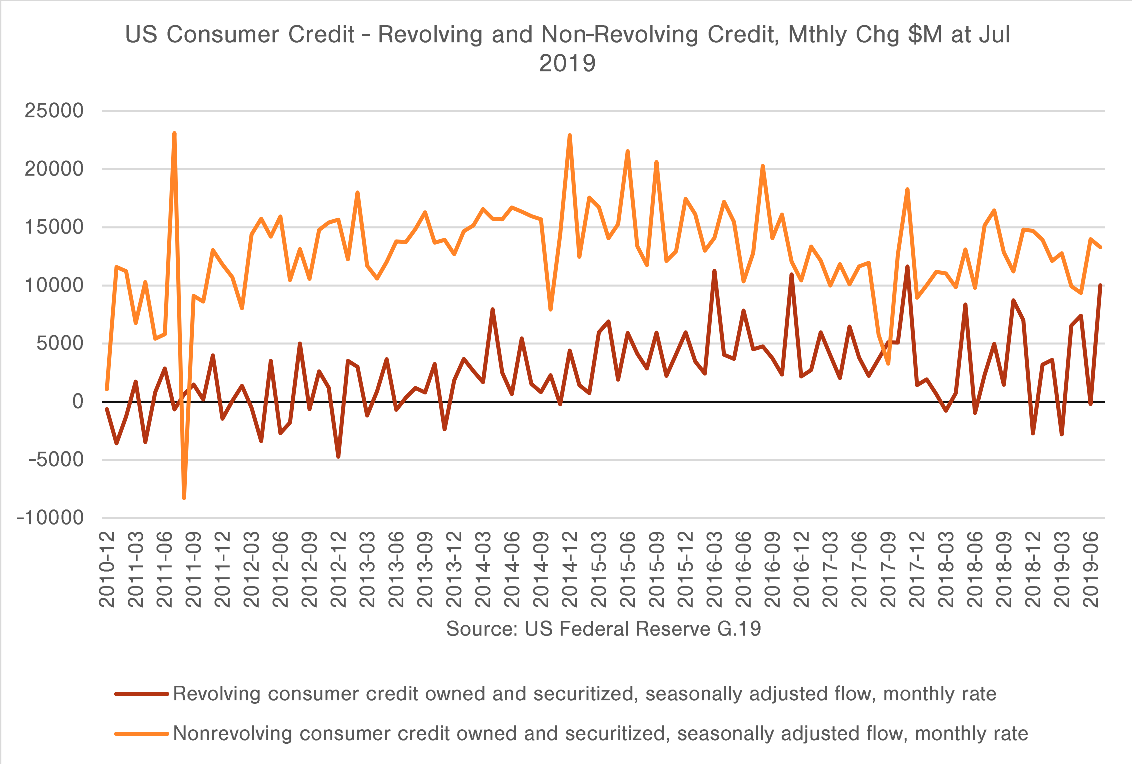
<u>Total Consumer Credit</u>

Month change; Jul +$23.3bn versus Jun +$13.8bn



The total of outstanding consumer credit increased by +6.8% in Jul versus Jun and is +5.2% higher than in Jul 2018.

The largest contributor to the increase in credit for the month was revolving credit;



<u>Revolving Credit</u>

The flow of revolving credit increased at a much faster pace; Jul +$10bn versus Jun -$0.2bn.

The growth in the total outstanding revolving credit increased by +11.2% versus Jun and remains +4.6% ahead of a year ago.

<u>Non-Revolving Credit</u>

The flow of non-revolving credit increased at a slightly slower pace than in the month prior; Jul +$13.3bn versus Jun +$14bn.

The growth in the total outstanding non-revolving credit increased by +5.3% in Jul versus Jun, which is just slightly behind the annual pace of growth of +5.4%.

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

JOLTS (Jul)

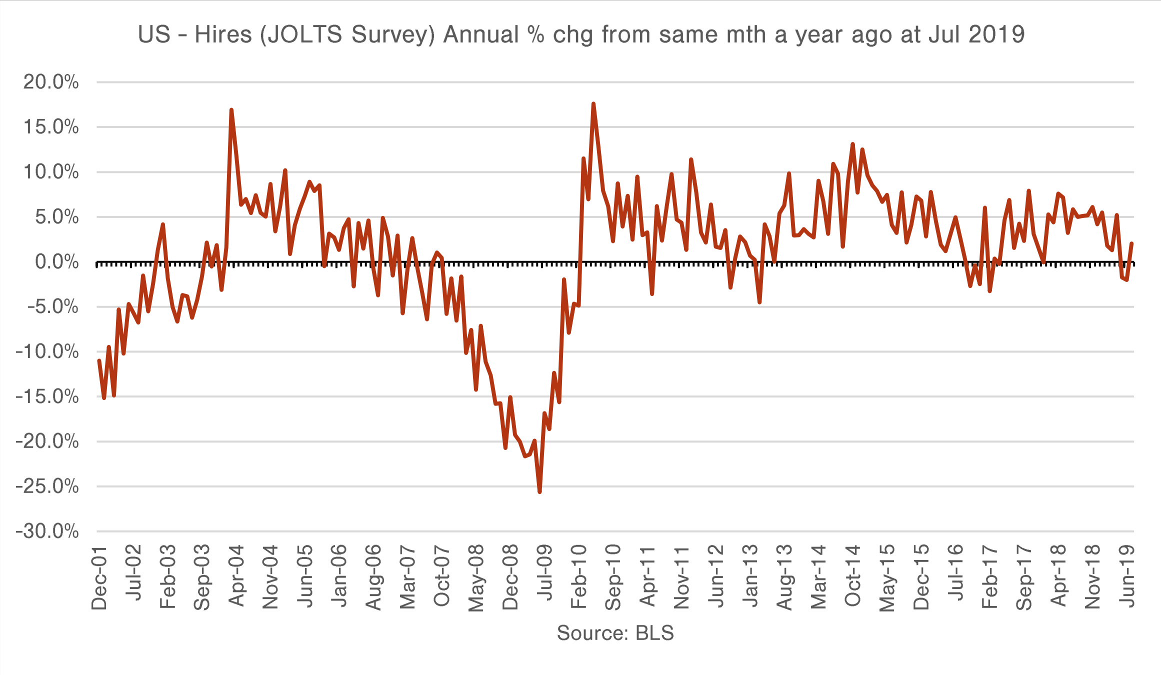
The Jul JOLTs data was somewhat mixed. The growth in job openings continued to slow on a monthly and annual basis. Job hires though increased at a much faster pace in the month, reversing the annual decline recorded in the month prior.

Separations increased at a much faster pace. Layoffs and discharges (involuntary separations) contributed to the increase, and despite the increase in the month, layoffs remain below that of a year ago. At the same time, the number of quits increased at a faster pace (reaching a new all-time high number of quits), suggesting that workers were more confident in conditions to change jobs.

Total Hires

The pace of hires increased at a much faster pace; Jul +5.95m persons (+4%) versus Jul +5.7m persons. The increase in Jul was +2SD's (based on the last 12months).

The faster pace of growth in hiring in the month resulted in the annual rate of growth shifting from a decline in Jun to positive growth in Jul;

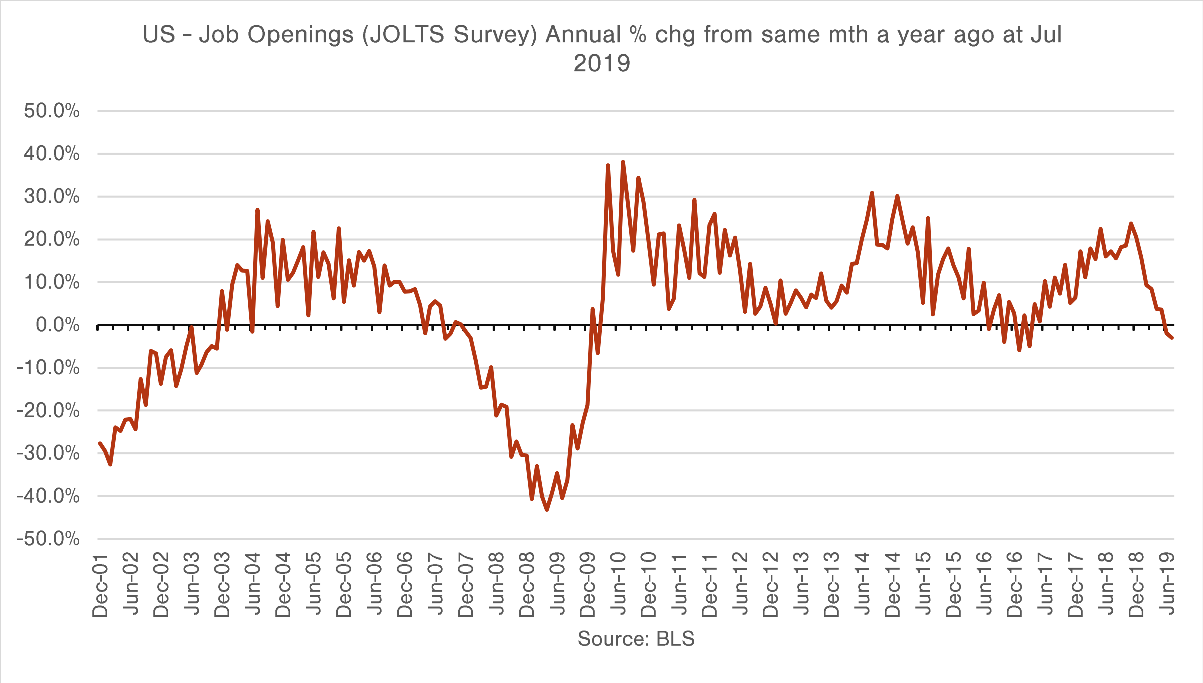


The hiring rate also increased from 3.8 in Jun to 3.9 in Jul. The 12-month average is 3.9.

JOB OPENINGS

While hires grew strongly in Jul, the number of job openings decreased slightly; Jul +7.22m versus Jun +7.25m openings.

On an annual basis, the pace of job openings growth has been slowing since Nov 2018 (+23%)



The job opening rate also slowed further from 4.6 in Jun to 4.5 in Jul – and remains below the 12-month average of 4.7.

TOTAL SEPARATIONS

There was a large increase in the number of separations in Jul – both layoffs & discharges and quits contributed to the increase in the month.

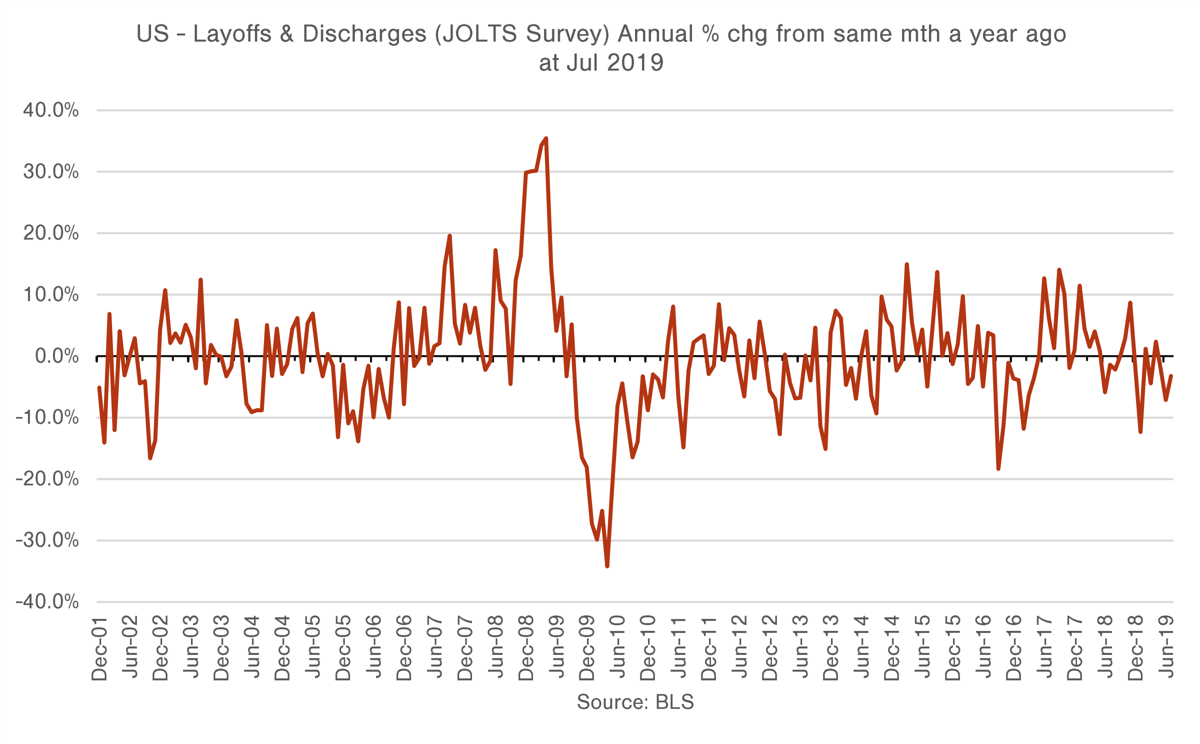
Total Separations – month change; Jul +5.76m persons versus Jun +5.5m. The month change was +3SD's.

Layoffs and Discharges

This is an indicator of involuntary separations – firms increasing the number of layoffs, generally suggest a weakening of the labour market. While there was an increase in the month, the pace of layoffs remains 3% below the same time last year.

Month change; Jul +1.8m persons versus Jun +1.7m persons.

On an annual basis, layoffs and discharges remain below a year ago;



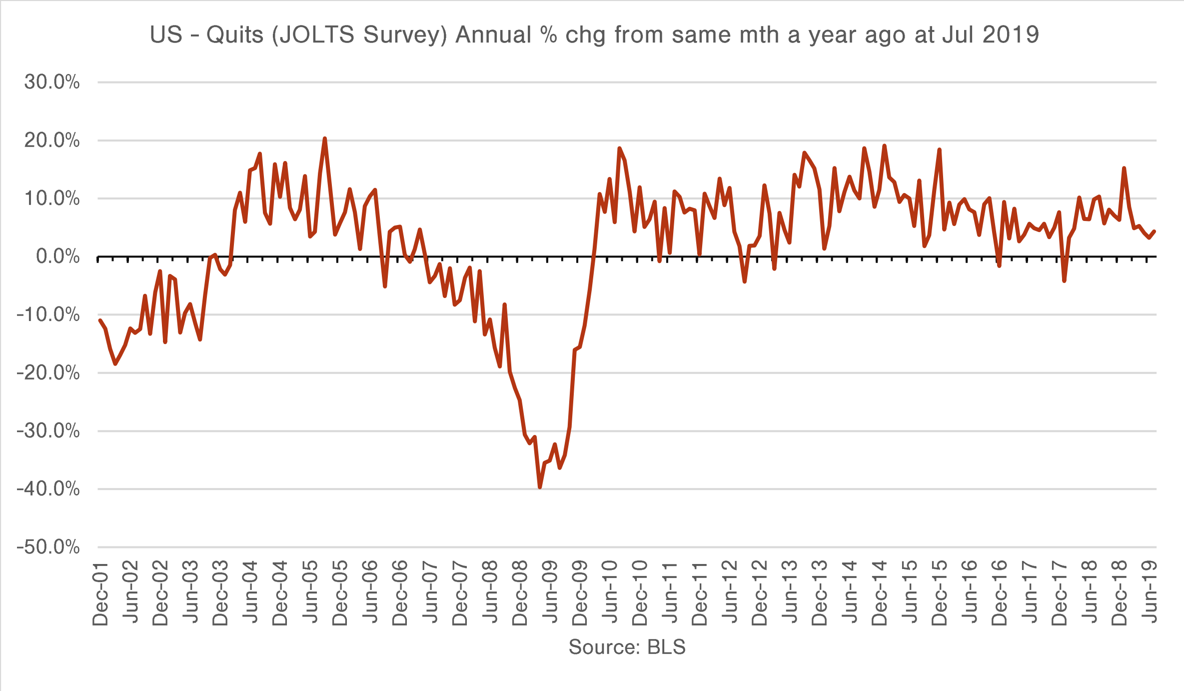
Quits

This is an indicator of voluntary separations. As quits increase, it generally suggests a stronger labour market as workers are more confident in the labour market to change jobs.

Of note this month is the large jump in the number of quits – reaching a new all time high (the quit rate remains below the all-time largest rate though).

Month change; Jul +3.6m versus Jun +3.46m. The increase in the month was a +2SD increase (based on the last 12-months).

The annual pace of quits had been slowing since the start of the year (suggesting some weakening of conditions) and, despite the increase in the month, the annual pace of quits still ticked up slightly, but remains below the pace of a year ago;



https://www.bls.gov/news.release/jolts.nr0.htm

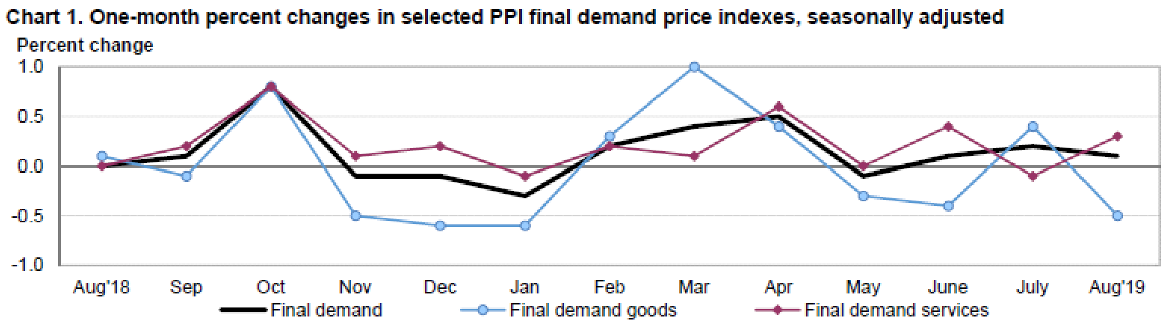
PPI (Aug)

Producer selling price growth continued to slow in the latest month – this was led by a decline in final demand goods prices (most of which was due to the decline in gasoline prices) while services shifted to an increase after declining in the month prior.

On an annual basis, producer price growth increased at a slightly faster pace – due to a small increase in final demand services price growth. Price growth remains well below the peak reached in mid-2018.

PPI FINAL DEMAND – MONTH CHANGE; Aug +0.1% versus Jul +0.2%

The slower growth was the result of a decline in goods prices, while services prices increased in the month.



Final demand goods – month change; Aug -0.5% versus Jul +0.4%

Contributing to the decline was both food and energy prices for the month. Excluding food and energy, goods prices were unchanged from the month prior - 0% growth.

Almost two-thirds of the August decline in the index for final demand goods can be traced to prices for gasoline, which dropped 6.6 percent. The indexes for fresh and dry vegetables, diesel fuel, corn, home heating oil, and ethanol also moved lower.

Final demand services – month change; Aug +0.3% versus Jul -0.1%

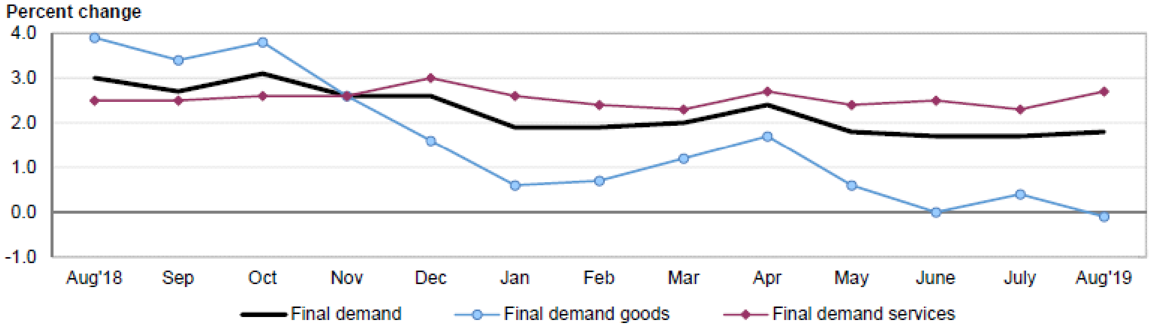
Prices for services were generally stronger this month across all categories.

A major factor in the increase in prices for final demand services was the index for guestroom rental, which moved up 6.4 percent. The indexes for fuels and lubricants retailing; apparel, footwear, and accessories retailing; chemicals and allied products wholesaling; gaming receipts (partial); and insurance also advanced.

PPI FINAL DEMAND – ANNUAL CHANGE; Aug +1.8% versus Jul +1.7%

The annual pace of producer prices increased slightly in Aug – as services prices increased at a faster pace and goods prices declined on an annual basis.

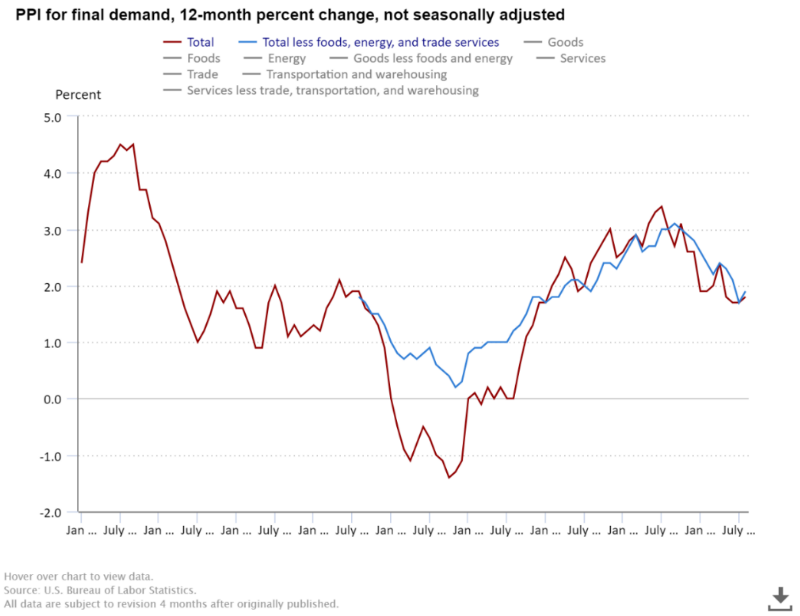
Chart 2. Twelve-month percent changes in selected PPI final demand price indexes, not seasonally adjusted



Excluding food, energy and trade, the annual growth in final demand PPI increased at a faster pace of +1.9% versus Jul +1.7%.

Despite the lift in the annual growth in the latest month, growth in both headline and core producer prices has been slowing on an annual basis since mid-2018;

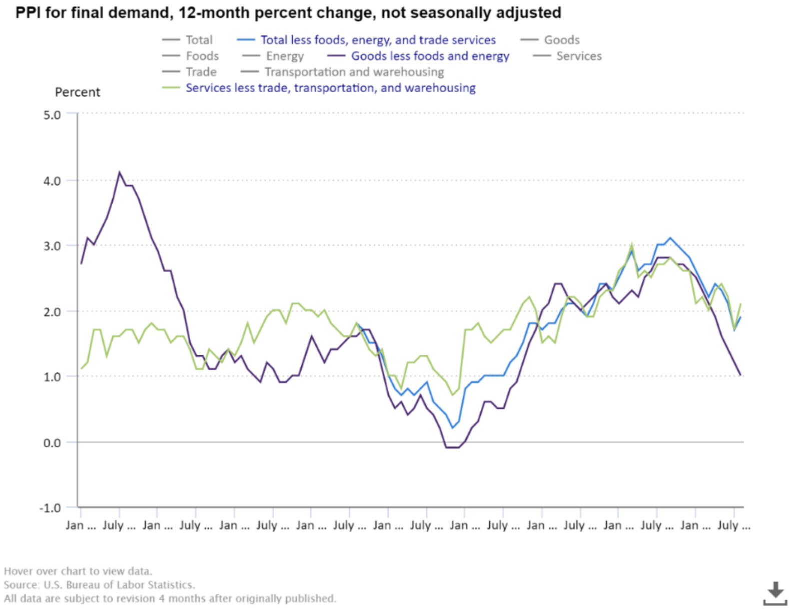
Chart; PPI Annual Change; Headline PPI and Core PPI (ex food, energy and trade services) – 2011-2019



The annual decline in core goods prices continues to accelerate while the annual pace of core services prices increased in Aug.

Both core goods and services price growth remain well below the recent peak in mid-2018 – indicative of slower growth in demand.

Chart; Annual Change Core PPI Goods and Services (2011-2019)



https://www.bls.gov/news.release/ppi.nr0.htm

CPI (Aug)

Growth of the headline all-items CPI slowed slightly on an annual basis but core CPI (ex food and energy) continued to grow at an accelerated pace. Both commodities less food & energy commodities and services less energy services contributed to the acceleration in core CPI.

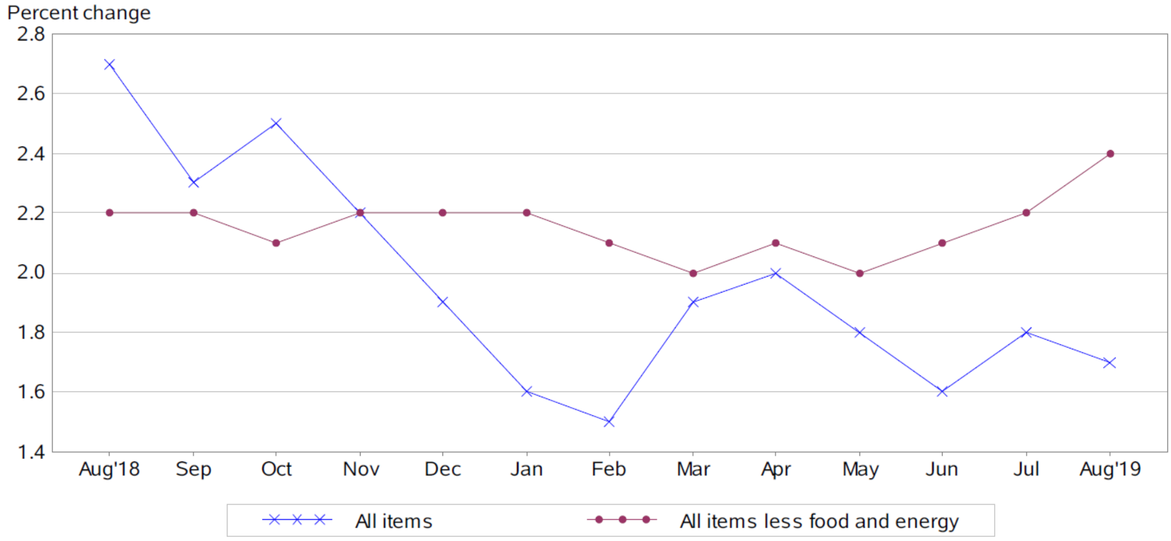
Headline CPI-all items – month change; Aug +0.1% versus Jul +0.3%

The slow down in the monthly CPI was the result of no change in food prices and a -1.9% decline in energy prices (after increasing +1.3% in the month prior).

Core CPI (less food and energy) on a monthly basis continued to grow at a constant pace; Aug +0.3% versus Jul +0.3%.

Annual Change – All-items CPI; Aug +1.7% versus Jul +1.8%

Chart 2. 12-month percent change in CPI for All Urban Consumers (CPI-U), not seasonally adjusted, Aug. 2018 - Aug. 2019



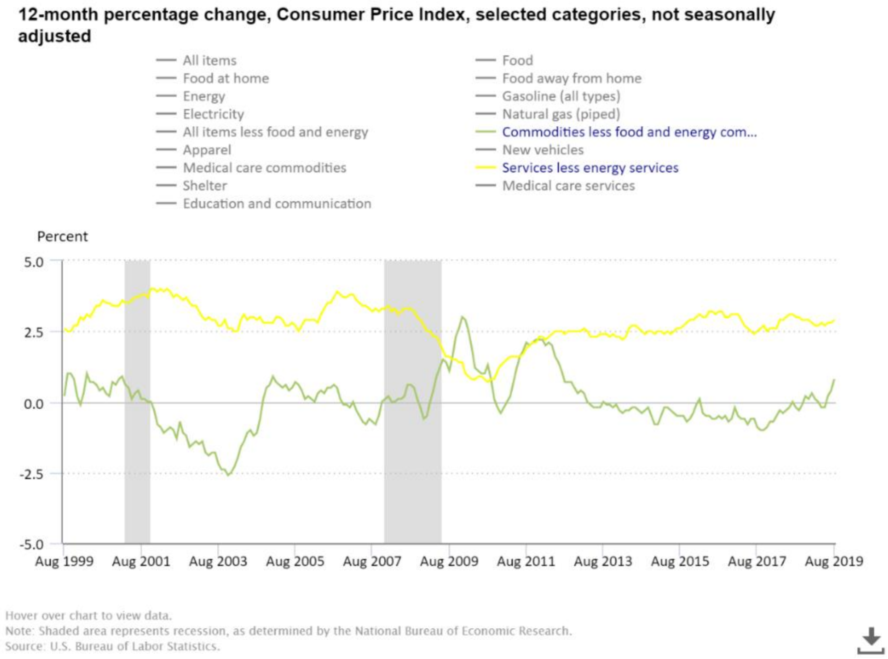
On an annual basis, food prices increased at a slower pace and the decline in energy prices subtracted from the headline CPI growth.

But the core CPI growth (ex food and energy) continued to accelerate for the third month in a row. All-item less food and energy represent approx. 80% of the total CPI weight.

Annual change – Core CPI (ex Food & Energy); Aug +2.4% versus Jul +2.2%

Both core goods and services contributed to the acceleration in the annual underlying CPI growth between Jul and Aug;

Chart: Annual % Chg – Core Goods and Core Services



Core goods (commodities less food and energy commodities) – annual change; Aug +0.8% versus Jul +0.4%. Annual growth, although low, has still been accelerating over the last three months.

The contribution from core goods to annual CPI growth doubled from +0.08%pts in Jul to +0.16%pts in Aug.

Core services (services less energy services) – annual change; Aug +2.9% versus Jul +2.8%.

Annual growth in services is running much higher than the headline growth. The contribution (to the headline CPI growth) from core services increased from +1.67%pts in Jul to +1.73%pts in Aug. Growth in shelter and (mostly) medical care services is running well ahead of the core CPI rate.

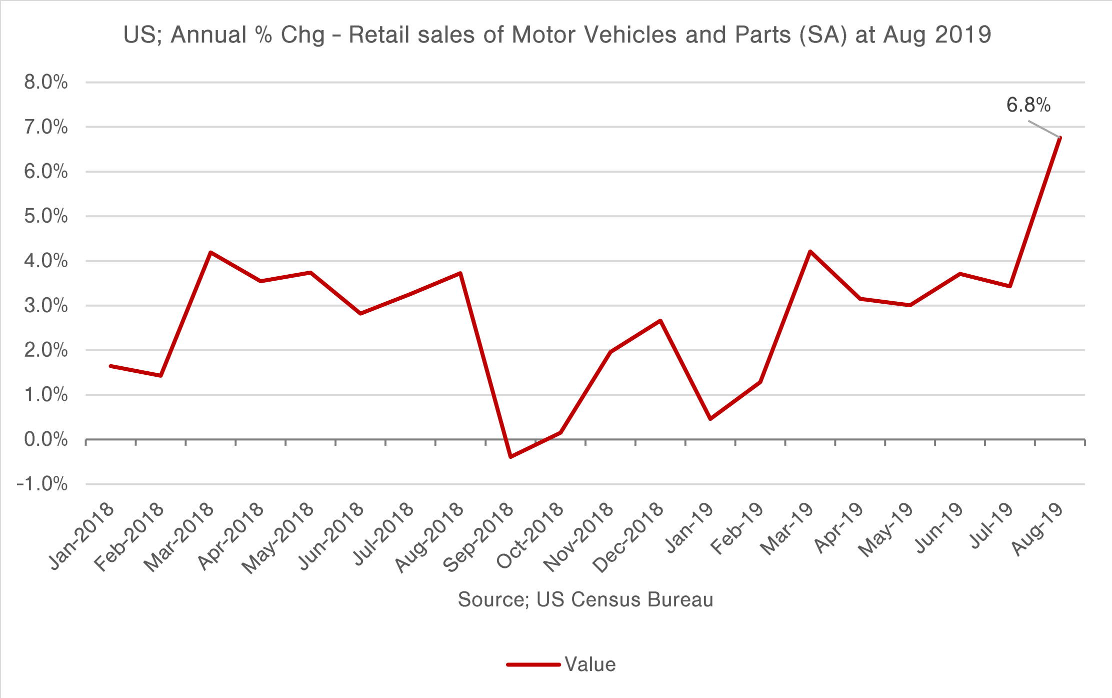
https://www.bls.gov/cpi/home.htm

Retail Sales (Aug)

The headline Aug retail sales growth slowed versus the month prior. It was a strong month for Auto sales which accounted for most of the growth in total retail sales in the month – in fact the annual growth in motor vehicle retail sales has been accelerating throughout 2019 and increased at a much faster pace in Aug (partly a base-effect too). Excluding Auto sales, retail sales growth was flat in the month. Stronger non-store retail sales continued into Aug but was offset by declines across food & bev, gasoline stations and food service.

Retail Sales ($) – month change; Aug +0.4% (+$1.8bn) versus Jul +0.8% (Jul growth was revised higher from +0.7%).

The single largest contributor to sales growth in the month was Auto sales; Aug +1.8% (+$1.83bn) versus Jul +0.1% (which was also revised higher from a -0.6% decline in Jul). The annual growth of retail sales of Motor Vehicles and Parts has been accelerating in the YTD 2019;



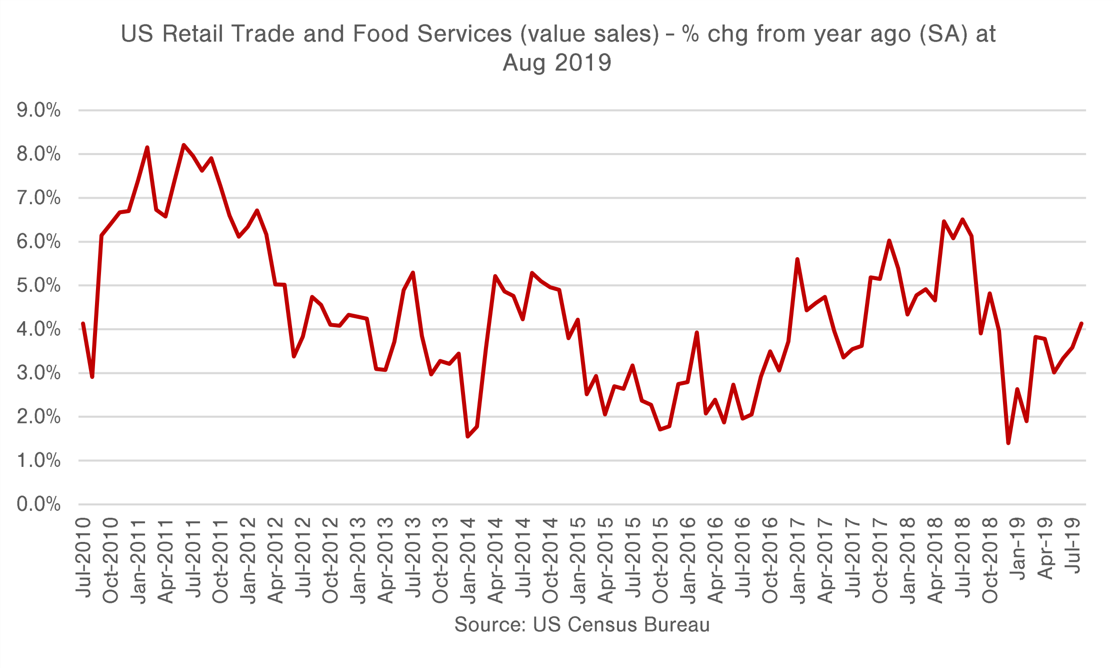
Excluding Autos, retail sales growth was flat (0%) versus the month prior.

Other contributors to growth in the month were; building and garden materials, health and personal care stores and another strong performance from non-store retailers (growth remained on par with the month prior; Aug +1.6% versus Jul +1.7%).

Sales declined in several categories; furniture, food & beverage stores, gasoline stations, clothing stores, general merchandise and a relatively large decline in food services & drinking place sales.

<u>Retail Sales ($) – annual change</u>; Aug +4.1% versus Jul +3.6%

Annual retail sales continue to accelerate – and this is an identical trend even excluding the value of gasoline sales;



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

Uni of Michigan Consumer Sentiment – Prelim (Sep)

There was a small rebound in consumer sentiment in the prelim Sep data after the larger decline in the month prior. Underlying commentary suggests continued concerns from consumers, but sentiment levels are still consistent with (slower) growth in personal consumption expenditures.

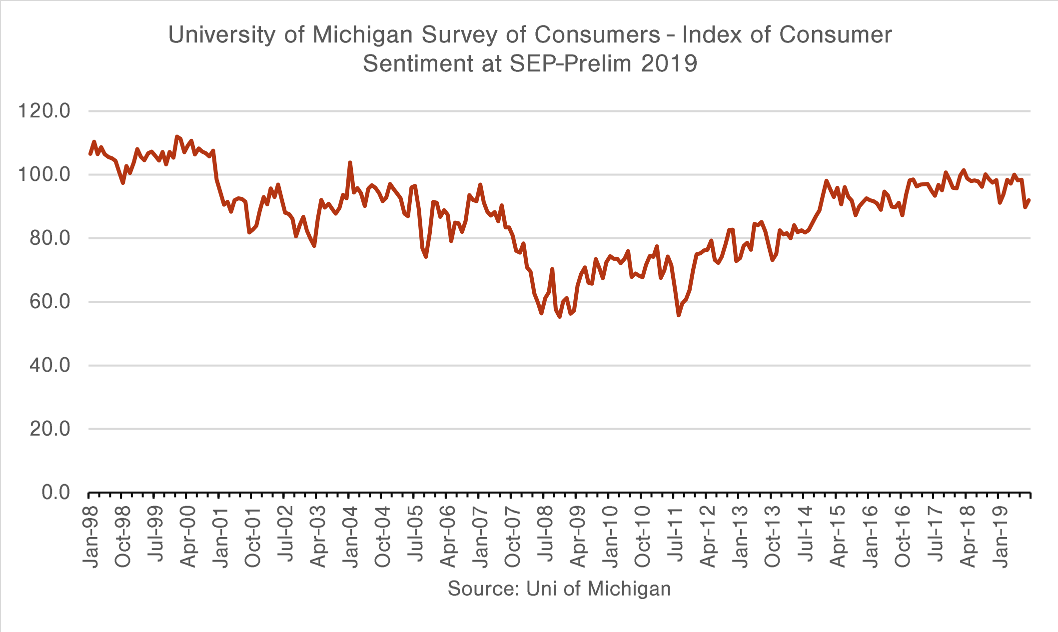
> While the uptick was across both current and expected economic conditions, the early September rebound was not widespread across age or income subgroups as it only fell among consumers under age 45 and among households with incomes in the top third---these two groups account for about half of all spending.

Consumers are currently expecting another cut in interest rates next week. Concerns about tariffs continued to increase – 38% of consumers in the study made a spontaneous reference to the negative impact of tariffs.

> Those who negatively mentioned tariffs also held more negative views on the overall outlook for the economy as well as anticipated higher inflation and unemployment in the year ahead.

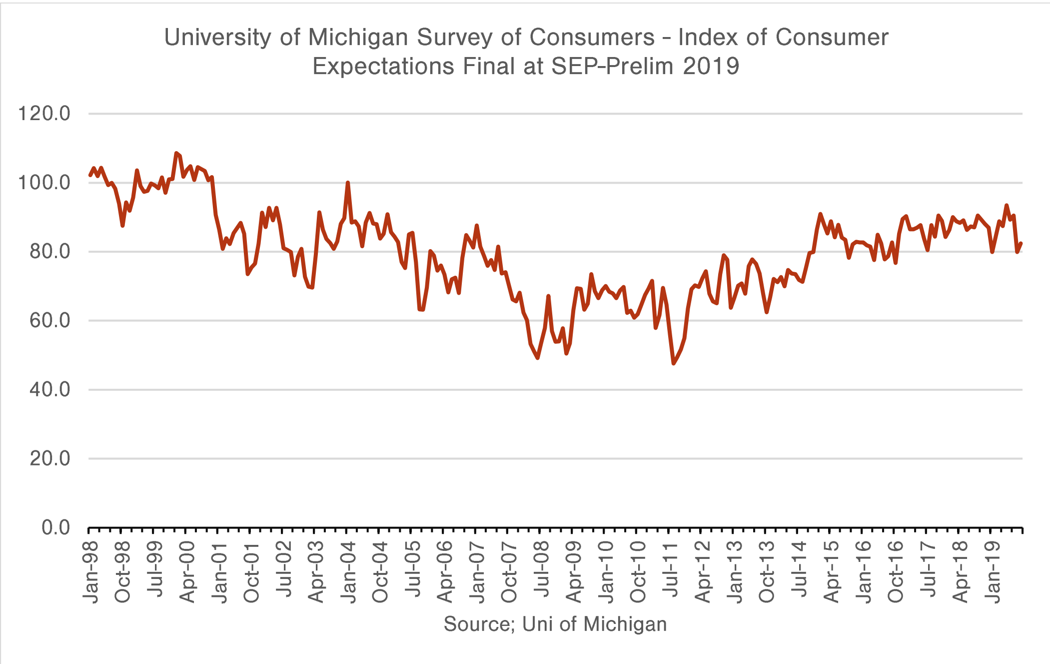
Index of Consumer Sentiment

Sep-prelim 92 versus Aug 89.9



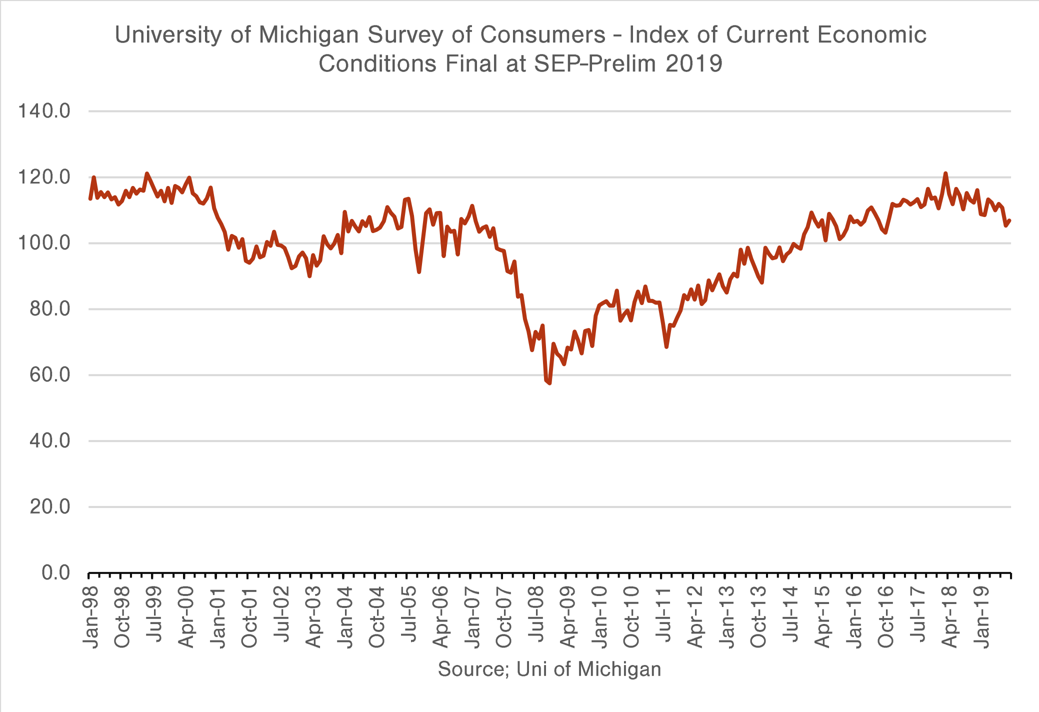
Index of Consumer Expectations

Sep-prelim 82.4 versus Aug 79.9



Index of Current Conditions

Sep-prelim 106.9 versus Aug 105.3



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

[Return to top](#)

Europe

ECB Rates Decision – 12 Sep 2019

As telegraphed, the ECB eased monetary policy further at the latest meeting. Aside from the nature of the easing measures, a key feature of the policy change is that reference to a timing for rates (and other policy measures) to change has been removed. Low rates and QE are to remain in place indefinitely.

The less covered aspect of the decision was the iintroduction of the two-tier system of remunerating bank excess liquidity holdings.

This was Mario Draghi's final meeting before his term as President of the ECB is over at the end of Oct.

Details from the announcement;

<u>Developments</u>

The decision to ease policy was based on the continued shortfall of inflation, linked to the 'more protracted weakness in the Euro area economy'.

<u>Policy Changes - Rates</u>

Interest rate on the deposit facility was lowered by 10bps to -0.5%

Interest rate on the main refinancing operation remained unchanged at 0%

Interest rate on the marginal lending facility remained unchanged at 0.25%

<u>Policy Changes – Net Purchases</u>

The asset purchase program will restart at a pace of €20bn a month from 1 Nov.

> The Governing Council expects them to run for as long as necessary to reinforce the accommodative impact of its policy rates, and to end shortly before it starts raising the key ECB interest rates.

Reinvestments of maturing securities on the ECB balance sheet will continue;

> for an extended period of time past the date when the Governing Council starts raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

<u>TLTRO III</u>

The interest rate in each of the quarterly operations will now be set at the average rate applied in the Eurosystem's main refinancing operations. For banks whose eligible net lending exceeds a benchmark, the rate applied in TLTRO III operations will be lower, and can be as low as the average interest rate on the deposit facility prevailing over the life of the operation. The maturity of the operations will be extended from two to three years.

Introduction of the two-tier system of remunerating excess liquidity holdings

This has been the least covered aspect of the decision. But the implications are important.

> The two-tier system will first be applied in the seventh maintenance period of 2019 starting on 30 October 2019. The multiplier that will be applicable as of that maintenance period will be set at 6. The remuneration rate of the exempt tier and the multiplier can be changed over time.

Source document;
https://www.ecb.europa.eu/press/pr/date/2019/html/ecb.pr190912_2~a0b47cd62a.en.html

Some further reading on the ECB decision indicates a far more intricate and 'historic' shift in monetary policy took place here. This from The Philosophy of Money;

> Specifically, the ECB has moved to a zero-interest rate on excess reserves up to 6x required reserves. Banks with excess reserves below this level can now borrow reserves at negative rates and deposit with ECB, generating positive carry. Furthermore, using TLTROs banks will be able to borrow from the ECB itself at -0.5% under certain conditions and earn positive carry if these transactions result in them holding higher excess reserves, but less than 6x required reserves. The distributional consequences between northern and southern Europe are not completely clear, but my initial thoughts are that it creates an incentive for banks in Northern Europe holding reserves in excess of 6x their required holdings to effectively lend these reserves to banks in Southern Europe.
>
> Be in no doubt. Dual rates is monetary rocket-fuel. In contrast to standard negative rates, to forward guidance, or QE, the marginal effects of these policies are increasingly powerful. I am not convinced that this specific combination of measures will suffice to generate enough demand to create an acceleration in Eurozone activity – but it will help. But further move along these lines will have increasingly impact. For example, cutting the TLTRO rate further and paying zero interest on a larger share of reserves, would have an even greater effect.

https://www.philosophyofmoney.net/draghis-historic-farewell/

Rates Guidance

The important change is that reference to a timing for rates (and other policy measures) to change has been removed. In the Jul statement, rates were expected to remain at current or lower levels at least until the first half of 2020. This has now changed to refer only to the achievement of an inflation outcome;

> The Governing Council now expects the key ECB interest rates to remain at their present or lower levels until it has seen the inflation outlook **robustly converge** to a level sufficiently close to, but below, 2% within its projection horizon, and such convergence has been consistently reflected in underlying inflation dynamics.

https://www.ecb.europa.eu/press/pr/date/2019/html/ecb.mp190912~08de50b4d2.en.html

Eurozone Industrial Production (Jul)

Industrial production declined across the Eurozone in Jul at a slower pace than the month prior. In the Euro Area, there were further declines in production across intermediate goods, energy and non-durable consumer goods. Production of capital goods and durable goods rebounded.

Production levels remain below the same month a year ago.

Euro Area Industrial Production – month change; Jul -0.4% versus Jun -1.4%

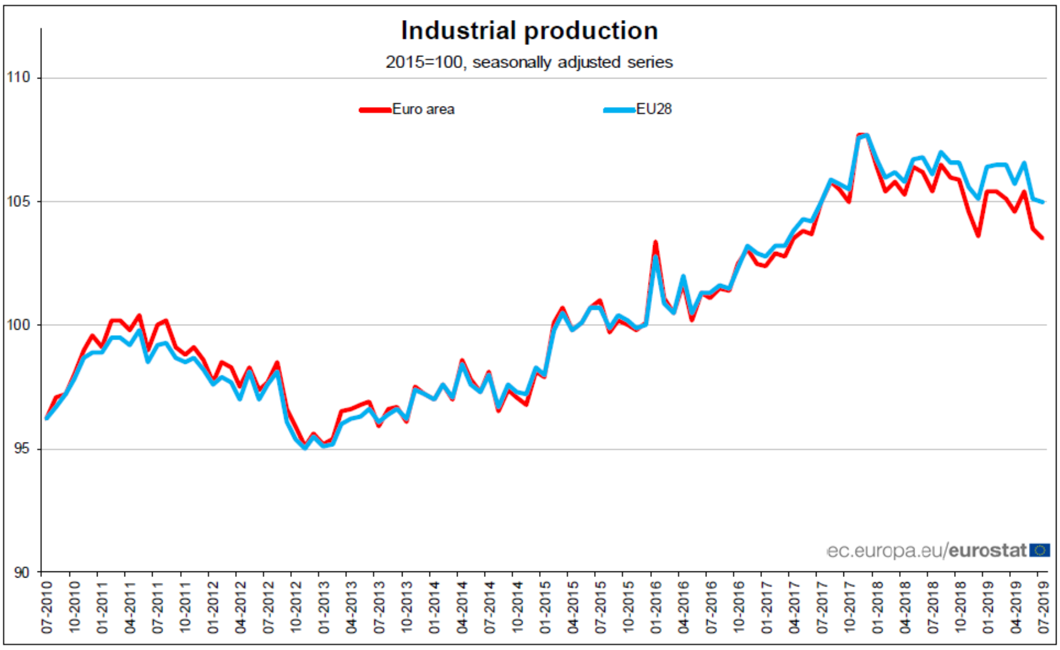
The categories contributing to the decline were; intermediate goods (-0.3%), energy (-0.7%) and non-durable consumer goods (-0.8%).

Rebounding somewhat in the month was production of capital goods (+1.8% in Jul versus -3.6% in Jun) and durable consumer goods (+1.2% in Jul versus -1.3% in Jun)

Euro Area Industrial Production – annual change; Jul -2% versus Jun -2.4%

Production continues to decline (on an annual basis) across intermediate goods, energy and capital goods. Durable consumer goods returned to annual growth in Jul (+1.8% versus -1.2% in Jun). Annual growth in non-durable consumer goods continued to slow.

Production growth remains weaker across some of the larger economies within the Eurozone; Germany (-5.3%), Ireland (-2.9%), France (-0.3%), Italy (-0.7%) and UK (-0.7%).



https://ec.europa.eu/eurostat/documents/2995521/10059795/4-12092019-AP-EN.pdf/6d63846e-7864-68db-9599-7cd75bc4964c

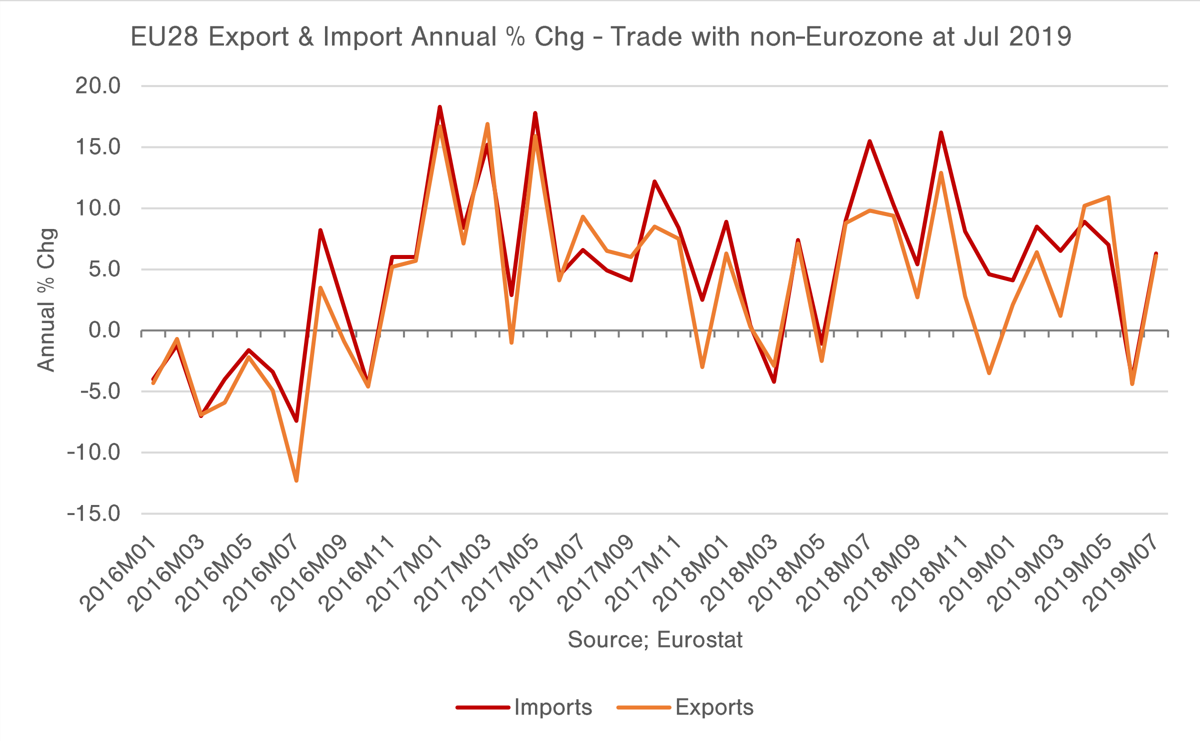
Eurozone Trade Balance (Jul)

The broader Eurozone trade balance (trade with non-EU members) shifted into a -10bn (EU) deficit in Jul. This was the result of faster growth in imports than exports versus the month prior. A year ago, the trade balance was somewhat higher at +20bn (EU).

The annual growth in both exports and imports rebounded in Jul;

Exports; Jul +6.3% versus Jun -4%

Imports; Jul +6.1% versus Jun -4.4%



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Return to top

Japan

GDP – second prelim estimate Q2 2019

GDP growth was revised slightly lower in the second prelim estimate. Annual growth was also revised slightly lower. Overall, higher public expenditure was mostly offset by revised lower private investment expenditure.

Real GDP - Quarter Change; Q2 +0.3% (revised lower from +0.4%) versus Q1 +0.5% (also revised lower from +0.7%).

GDP Revisions – Expenditure Perspective

Private residential investment spending was revised lower in Q2 from +0.2% growth to +0.1%

Private non-residential expenditure was revised much lower from +1.5% to +0.2%

The change in inventories was revised higher (a smaller decline versus Q1)

Government consumption expenditure was revised higher from +0.9% growth to +1.2% growth

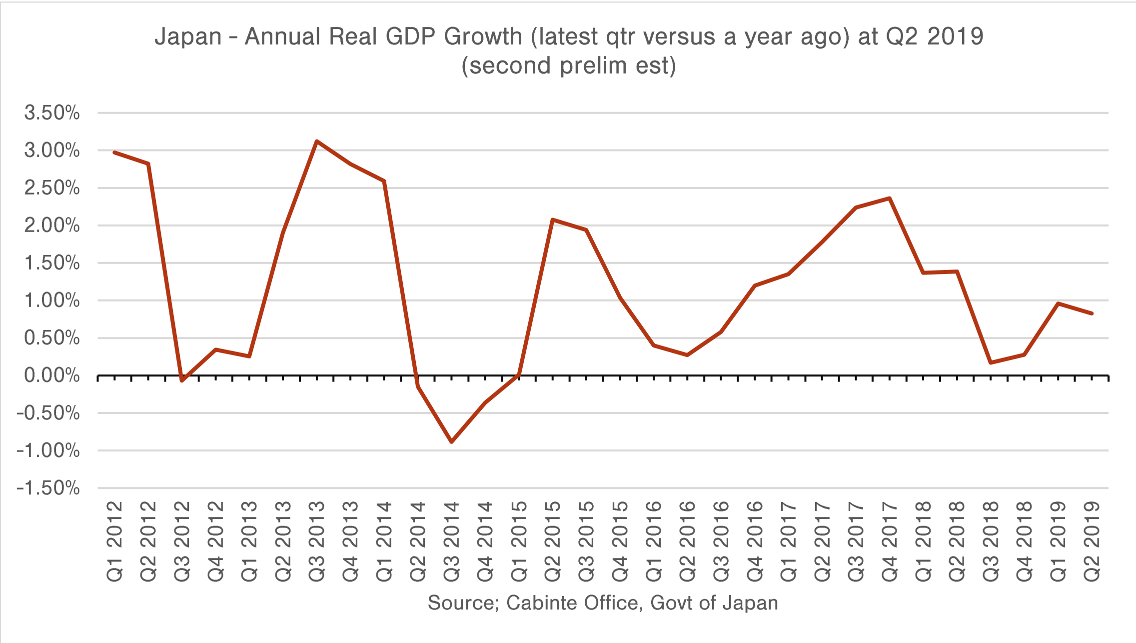
Public investment expenditure was revised higher from +1% growth to +1.8% growth

Real exports were revised from -0.1% decline to 0% change

Real import growth increased slightly also

There was no change from the contribution by household consumption.

Real GDP – Annual Growth; Q2 +0.8% (revised lower from +1%)



https://www.esri.cao.go.jp/en/sna/data/sokuhou/files/2019/qe192_2/gdemenuea.html

Industrial Production – Final (Jul)

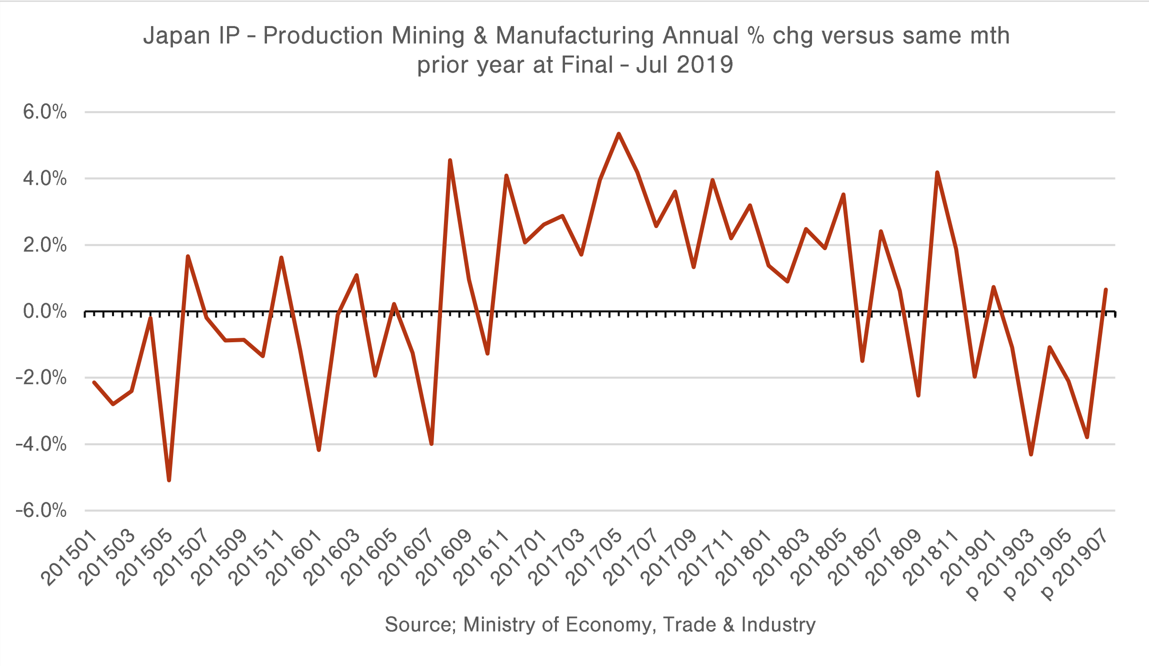
There was little change between the prelim and final industrial production data. Production growth was unchanged between releases. Shipment growth was revised only slightly higher. The decline in inventories was also revised slightly higher.

Overall, it was a stronger month for production and shipments – across most industry categories. Total shipments and production have now shifted to growth on an annual basis. Inventory growth and levels remain elevated.

Production

Month change; Jul +1.3% versus Jun -3.3%

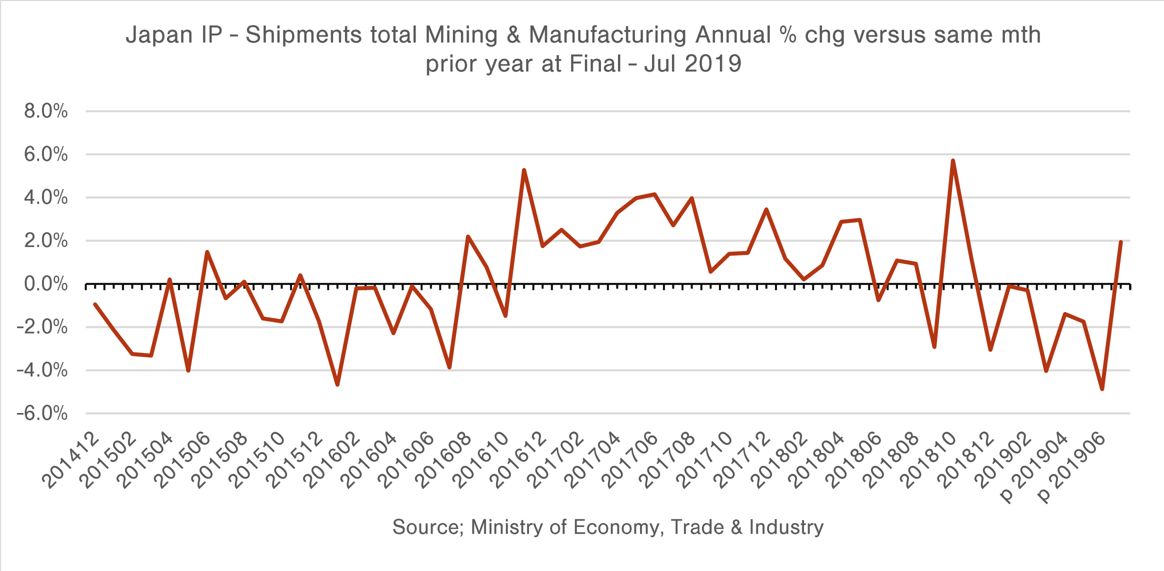
Annual change; Jul +0.7% versus Jun -3.8%



Shipments

Month change; Jul +2.7% versus Jun -4%

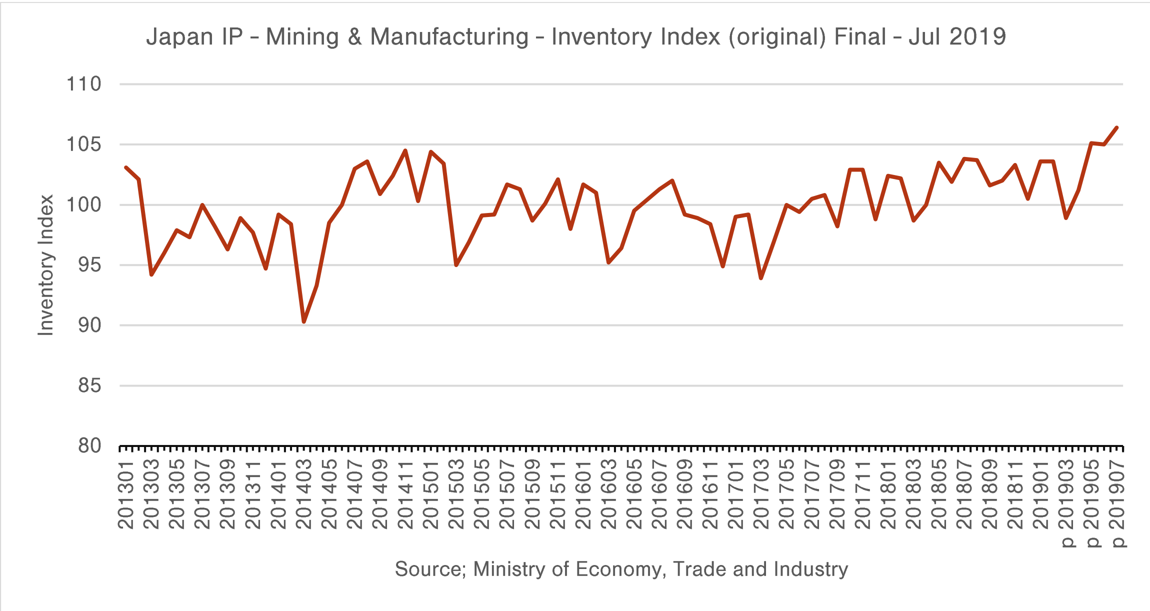
Annual change; Jul +1.9% (revised higher from +1.8%) versus Jun -4.9%



Inventory

Month change; Jul -0.2% versus Jun +0.4%

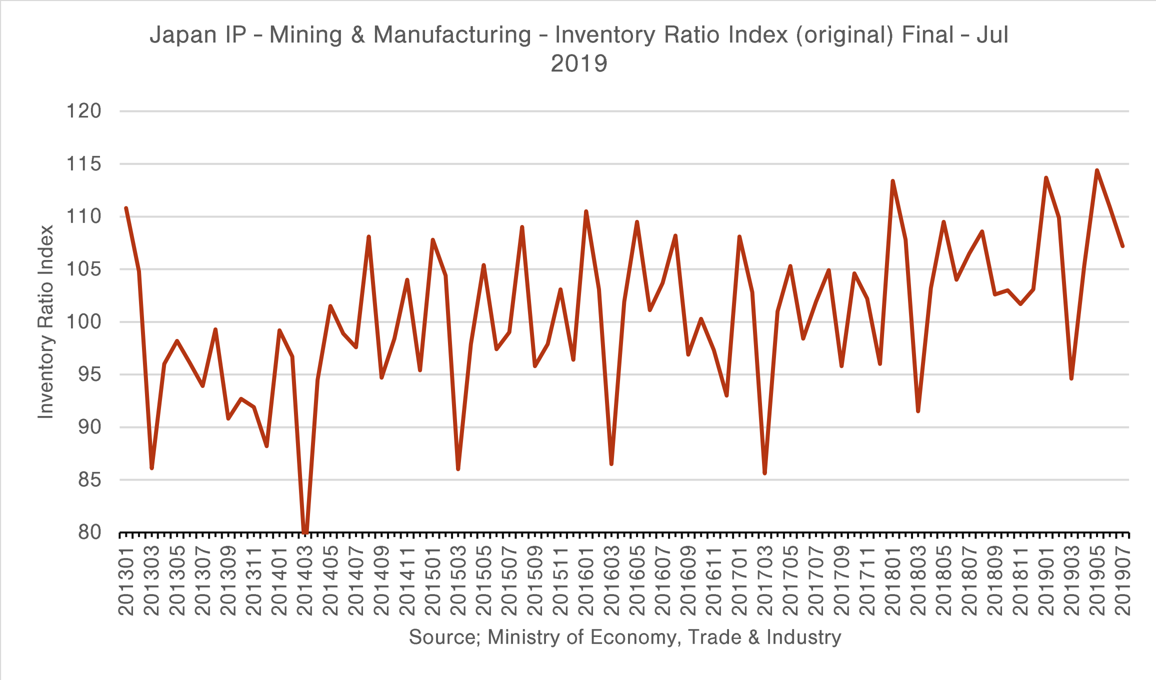
Annual change; Jul +2.5% (revised higher from +2.4%) versus +3%



Inventory Ratio

Month change; Jul -2.1% versus +3.2%

Annual change; Jul +0.7% (revised higher from +0.6%) versus Jun +6.6%



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

Return to top

United Kingdom

Brexit

Talks continue this week across most levels of the UK government and the EU on Brexit. There is some indication that the UK government may consider an option/alternative to the Irish border backstop that is in the current (and rejected) withdrawal agreement.

The option is an 'all Ireland backstop'. Details remain unclear but the indication is that the UK government is willing to make some compromises;

> "Mr Johnson has made a proposal in the last few days talking about an all-Ireland food zone," Hogan told The Irish Times in an interview after his nomination. "That is certainly a clear indication of divergence between Northern Ireland and the Republic of Ireland, the EU and the rest of the UK. This is the first time that this has been spoken about by a British prime minister where **they are prepared to accept some level of divergence between Northern Ireland and the rest of the UK**.
> https://www.irishtimes.com/news/world/europe/penny-finally-dropping-for-uk-on-brexit-says-phil-hogan-1.4013645?mode=amp

There is some optimism emerging that an alternative could be developed in the coming weeks;

> "The prime minister will be seeing President Juncker tomorrow, I'll be meeting with Michel Barnier tomorrow, so there's extensive talks been happening both at a technical level but also at a political level. So there has been a huge amount of work going on behind the scenes. We can see a landing zone in terms of a future deal but there is significant work still to do."
> https://www.theguardian.com/politics/2019/sep/15/brexit-uk-ministers-talk-up-irish-border-compromise-as-key-to-deal

> "With Johnson vehemently committed to leaving the EU on 31 October but bound by law to seek an extension if a deal is not in place by the time of the European council summit on 17 October, **there has been intense focus on ways he could find a plan acceptable to Brussels but which would not be seen by Conservative MPs as a betrayal**."
> https://www.theguardian.com/politics/2019/sep/15/brexit-uk-ministers-talk-up-irish-border-compromise-as-key-to-deal

Monthly GDP (May-Jul)

The rolling 3month GDP growth was flat in the May-Jul quarter. Over the three-month period, slower growth in services was offset by declines in construction and production. While the breakdown of the three-month period by month is more volatile, all sectors returned to growth in Jul after a much weaker Jun. It is likely that activity will continue to pick up as the UK again prepares for the next Brexit deadline in Oct.

Rolling three-month GDP Growth; May-Jul 0% versus Apr-Jun -0.2%

Services activity increased by +0.2% in the May-Jul quarter.

Production decreased by -0.5% in the May-Jul quarter. The data is still cycling over the effects of the original Brexit deadline where production in manufacturing especially, was bought forward.

Construction activity decreased by -0.8% over the May-Jul period.

The monthly growth breakdown suggests that there was some improvement across all three sectors most recently in the Jul month – the monthly breakdown is more volatile though;

Table 1: Breakdown of GDP and its components' growth rates by month

	May 2019	**June 2019**	**July 2019**
GDP	0.2%	0.0%	0.3%
Index of Services	0.0%	0.0%	0.3%
Index of Production	1.2%	-0.1%	0.1%
Manufacturing	1.4%	-0.2%	0.3%
Construction	0.3%	-0.7%	0.5%
Agriculture	0.0%	0.0%	-0.1%

Source: Office for National Statistics – GDP monthly estimate

https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpmonthlyestimateuk/july2019

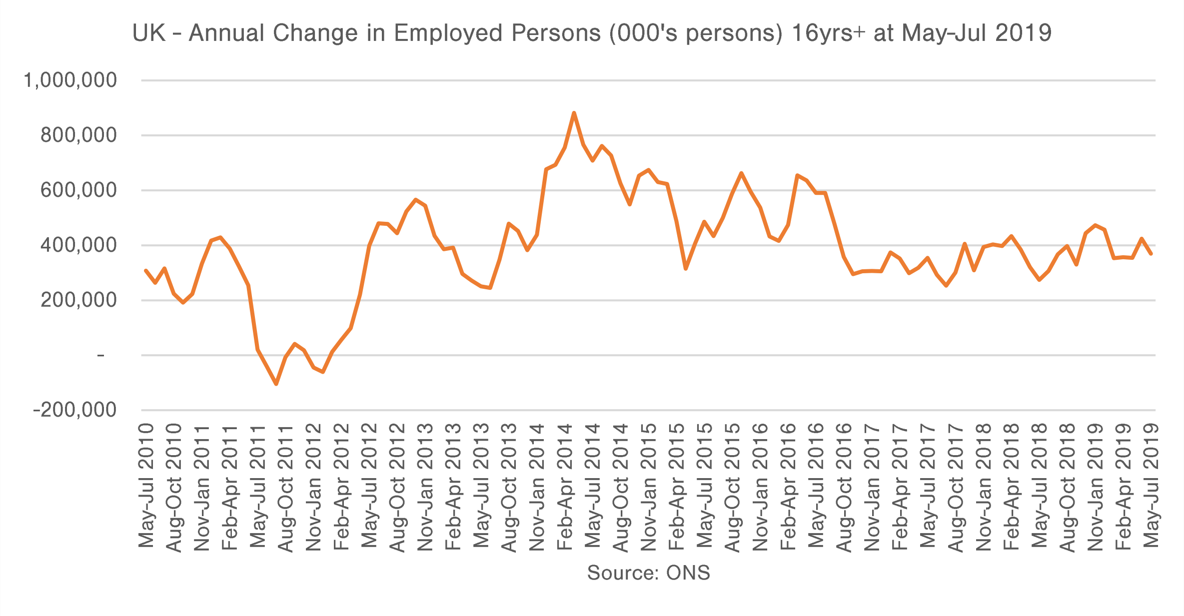
Employment and Labour Market Survey (May-Jul)

The main feature of the labour force and employment situation was slower growth in employed persons – on both an annual and quarterly basis. Despite the slower growth in employed persons, total unemployed persons continued to decline at a faster pace on an annual basis due to a smaller increase in participation. While on a quarterly basis, total unemployed persons declined due to the fall in participation.

<u>Employment</u>

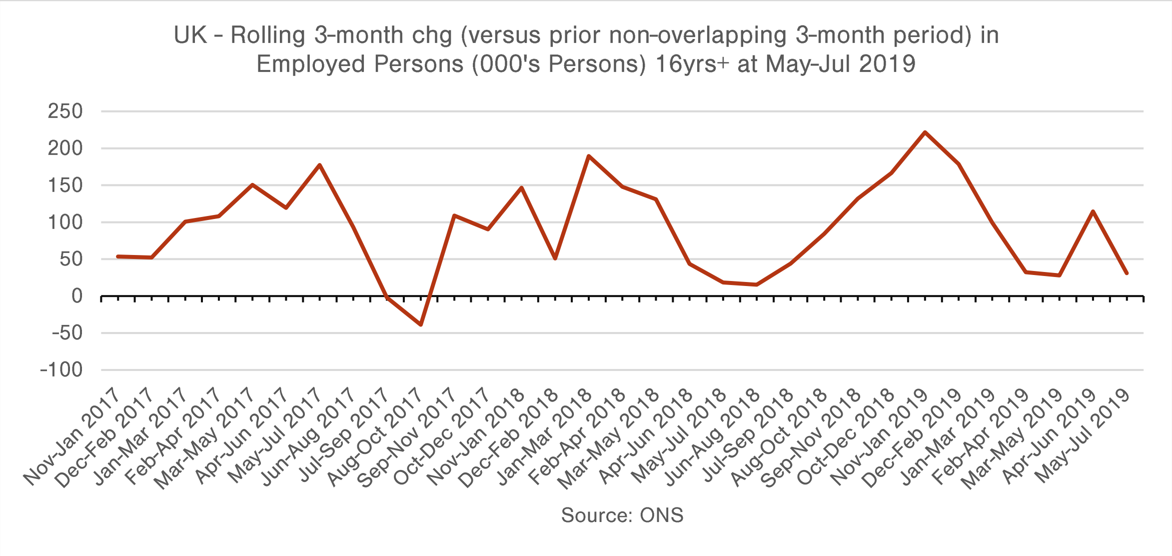
Annual change; May-Jul +369k persons versus Apr Jun +424k persons

While annual growth slowed slightly, it remained in line with recent growth



The qtr change in employed persons slowed back down to recent lows;

Qtr chg; May-Jul +31k persons versus Apr-Jul +115k persons

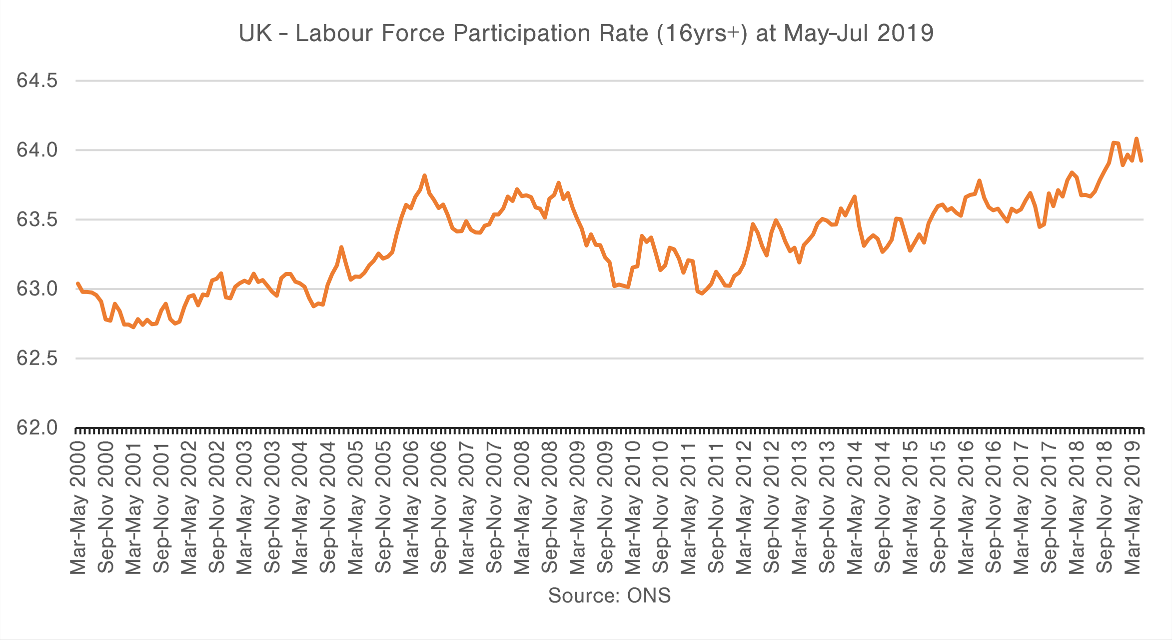


Labour Force

On an annual basis, growth in the labour force also slowed over the last year;

Annual change; May-Jul +305k persons versus Apr-Jun +391k persons

The slower growth in the labour force was the result of a smaller increase in participation. The labour force participation rate (LFPR) in May-Jul was still higher than that of a year ago by +0.2%pts (the annual change in Apr-Jun was +0.4%pts);



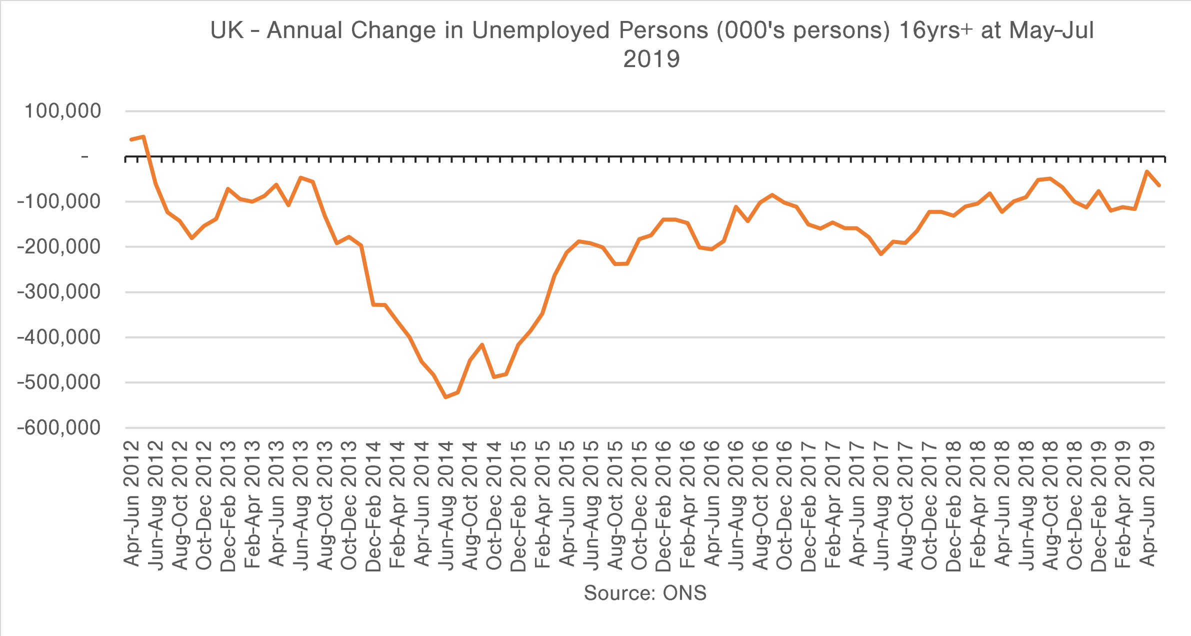
Overall, employment growth slowed by less than the labour force, which meant that total unemployed persons declined at a faster pace.

On a quarterly basis, employment growth was higher than that of the labour force – but only because there was a -0.04%pts decline in participation. This meant that total unemployed persons also declined on a quarterly basis.

Total Unemployed Persons

Annual change; May-Jul -64k persons versus Apr-Jun -33k persons

The larger annual decline was the result of employment growth that slowed by less than the growth in total labour force.



On a quarterly basis, unemployed persons declined by -11k persons (versus the increase of +31k in the Apr-Jun quarter). The decline in participation for the quarter was the main reason for the decline in total unemployed persons – given that employment growth had slowed.

The unemployment rate declined from 3.9% in Apr-Jun to 3.8% in May-Jul.

Summary of they main labour market indicators;

	16yrs+ (000's of persons)		16-64yrs (000's of persons)	
	Latest Qtr Chg May-Jul 2019	ANN Chg May-Jul 2019	Latest Qtr Chg May-Jul 2019	ANN Chg May-Jul 2019
Estimated change in the Labour Force due to pop growth (1)	43.657	173.636	15.809	62.120
How many jobs available for them? (employment growth) (2)	30.979	369.469	20.637	310.743
Difference; employment less est chg in labour force due to pop (3) (if positive, then employment growing faster than pop)	-12.678	195.834	4.828	248.623
Change in the labour force due to the change in participation (4)	-23.216	131.745	-1.992	187.416
The remainder is the chg in total unemployed persons (4) less (3) - if neg, then unemployment decreasing	-10.537	-64.089	-6.821	-61.207
Different views of the Labour Force;				
Double check - change in total economically active (pop + participation)	20.441	305.380	13.817	249.536
Double check - change in total economically active (employ + unemp)	20.441	305.380	13.817	249.536
Actual economically active ann chg (as reported)	20.441	305.380	13.817	249.536

https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/uklabourmarket/september2019

Return to top

Australia

Housing Finance (Jul)

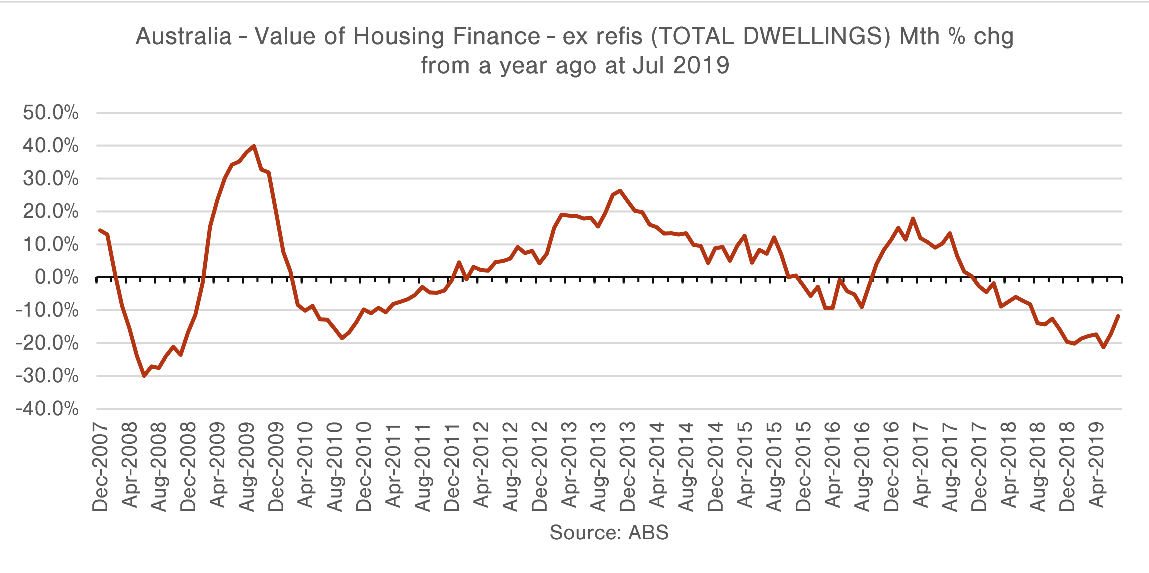
Lending to households for housing recorded a large % increase in the latest month. The bulk of the growth was for lending to owner occupiers but lending for investors also increased at a faster pace. The jump in the month comes as APRA (the Aus banking regulator) eased some of the restrictions on lending in Jul – shifting from a 7% interest rate serviceability benchmark to a +2.5% buffer above the borrowers' interest rate (mostly allowing the banks to determine this level). This month of data also captures both RBA interest rate decreases.

The increase in lending will continue to support growth in house prices in the near term. By the end of the year, APRA has advised that it will implement 'responsible lending' changes after it lost a benchmark case against Westpac (claiming that Westpac had breached responsible lending laws (Source: https://www.afr.com/companies/financial-services/asic-plans-responsible-lending-changes-by-end-of-year-20190814-p52gyp)). The result could be a further curb placed on lending again, limiting mortgage sizes going forward.

Total Lending for Housing

Lending for dwellings ex-refi's - month change; Jul +5.1% versus Jun +3.2%

Lending in Jul remains 12% below a year ago;



Most of the increase in the month was the result of more lending for owner occupiers.

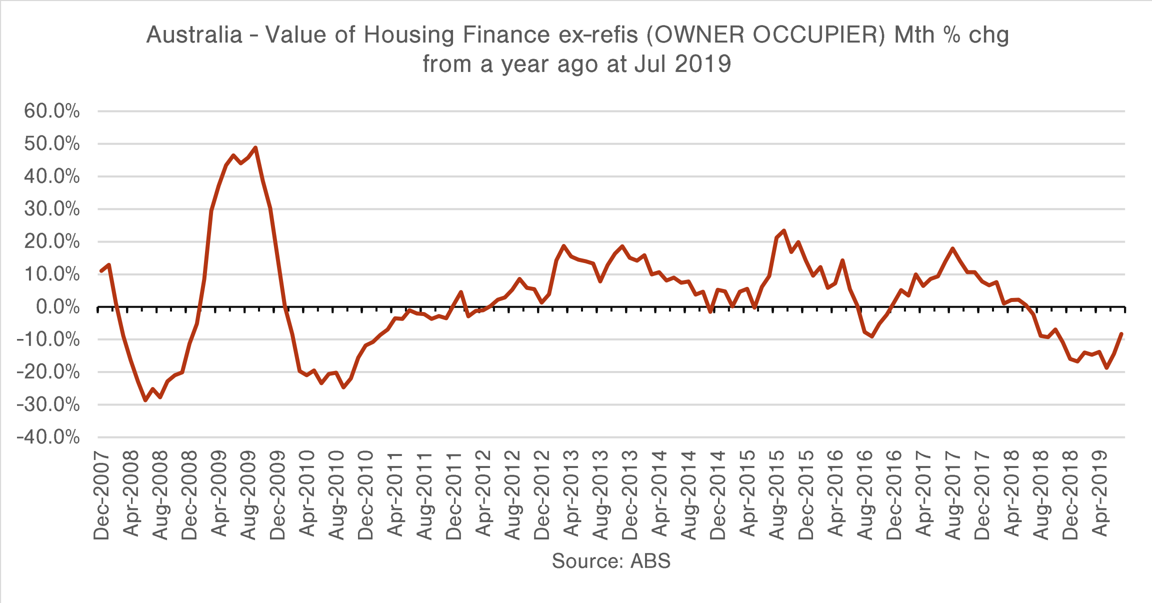
Lending for Owner Occupier Housing

Owner occupier housing finance ex-refis – month change; Jul +5.3% versus Jun +4.1%

The increase in the month was only a 1.4SD increase (based on the last 12 months). Most of the growth was for borrowers purchasing established dwellings, but there was also a +20% increase in lending for the purchase of new dwellings.

The annual decline in lending for owner occupiers has slowed considerably over the last two months, now declining by 8% in Jul (in May lending for owner occupiers was down 19%).

Lending for owner-occupiers remains 13% below the max.



The number of housing finance commitments for owner occupiers also increased at a similar rate this month;

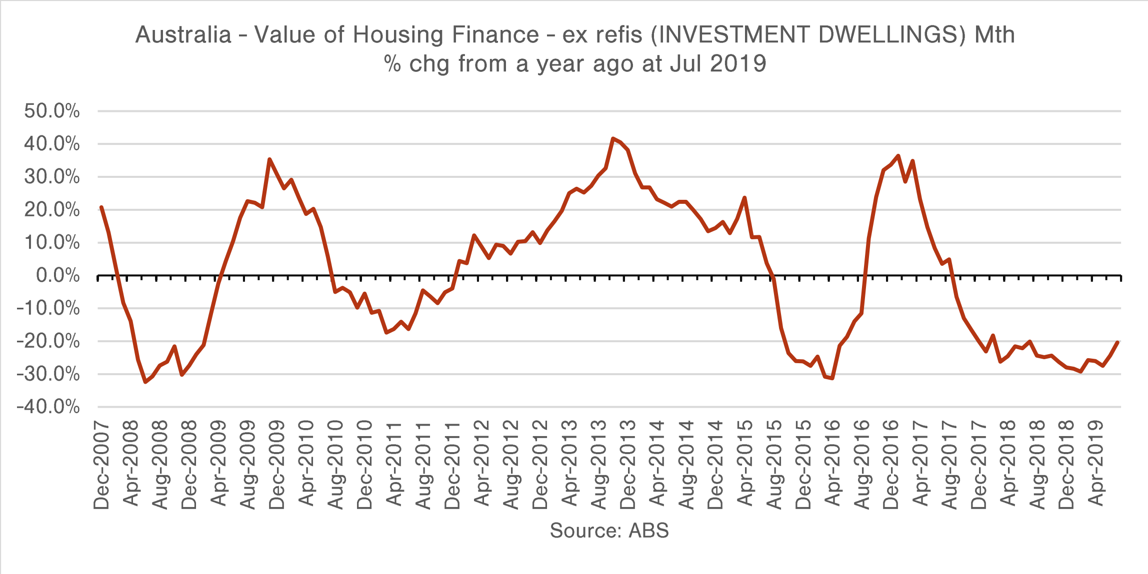
Month change; Jul +5% versus Jun -0.8%

The increase in the number of commitments was mixed among the states; NSW and VIC accounted for over half of the increase in the month. The increase in the ACT was relatively large. The increase in SA and WA lagged the broader market. The number of commitments declined in TAS.

<u>Lending for Investment Properties</u>

Lending for investment properties ex-refi's – month change; Jul +4.7% versus Jun +0.9%

The increase in the month was only a 0.5SD increase (based on the last 12-months). The value of lending for investment properties remains 20% below the same month a year ago. Part of the reason that investment lending is lagging is due to previous curbs on investor lending (differential pricing of mortgages - higher rates for investment properties).



https://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/5601.0Main+Features1Jul%202019?OpenDocument

NAB Business Conditions and Confidence (Aug)

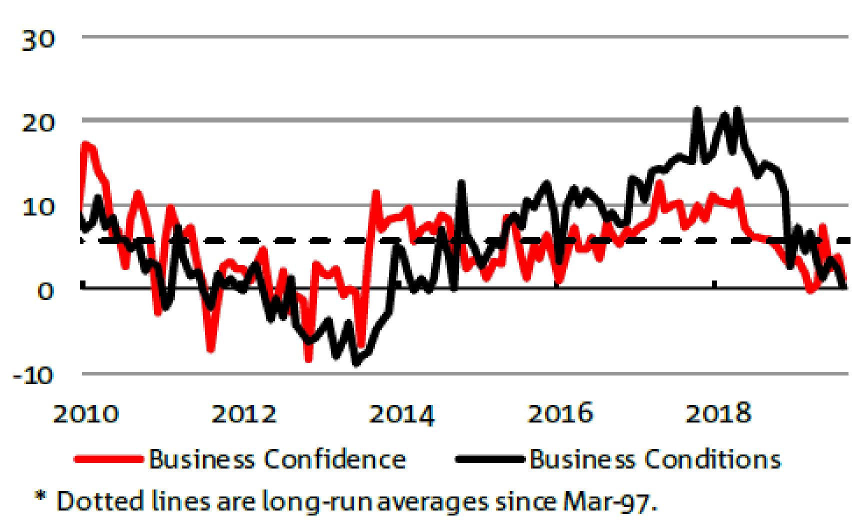
Business confidence and conditions were weaker this month with both measures recording slower growth. Confidence dropped back after a recent improvement based on expectations of stimulus and election results. The impact of these stimulus measures is only just starting to filter through to firmer conditions across selected industries and, business conditions overall continued to weaken, slowing to a new near-term low.

Business Confidence; Aug 1 versus Jul 4

Business Conditions; Aug 1 versus Jul 3

Both measures remain below the long-run average and are only just above the threshold of zero of improving versus deteriorating conditions/confidence;

CHART 1: CONFIDENCE AND CONDITIONS BOTH DECLINE



Business Confidence

Confidence was lower in Aug across all of the main industry sectors. Most sectors remain above the recent low in confidence measures. But in Aug some of recent improvement was reversed in business confidence across mining, retail and finance/bus/property. The latter two were likely impacted positively in Jun/Jul by recent rate cuts, stimulus measures and election results.

Confidence is now negative for wholesale trade and confidence has fallen to around neutral across manufacturing, construction and recreation & personal services.

CHART 24: BUSINESS CONFIDENCE BY INDUSTRY (NET BALANCE)

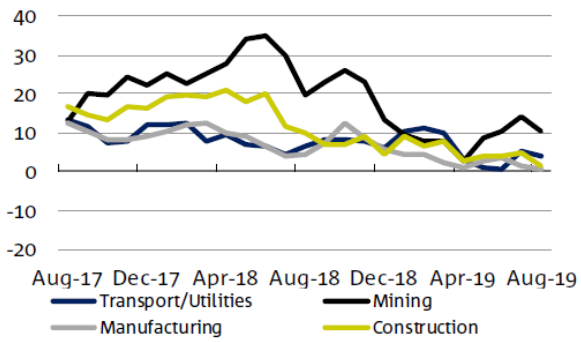
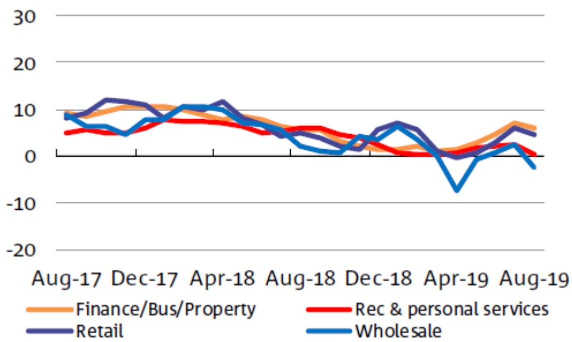


CHART 25: BUSINESS CONFIDENCE BY INDUSTRY (NET BALANCE)

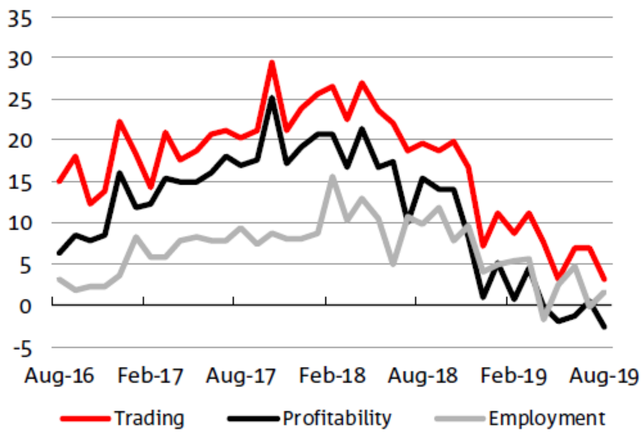


Business confidence also fell across the states except for Tas, where confidence shifted back into positive territory.

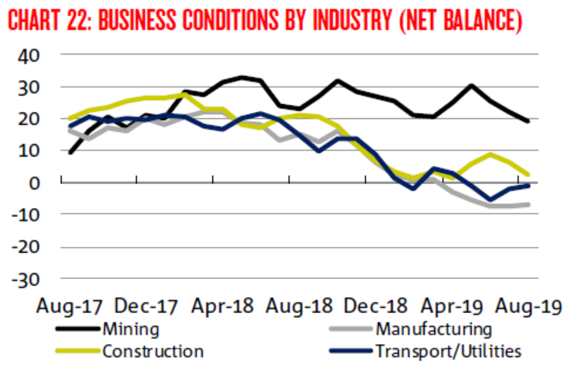
Business Conditions

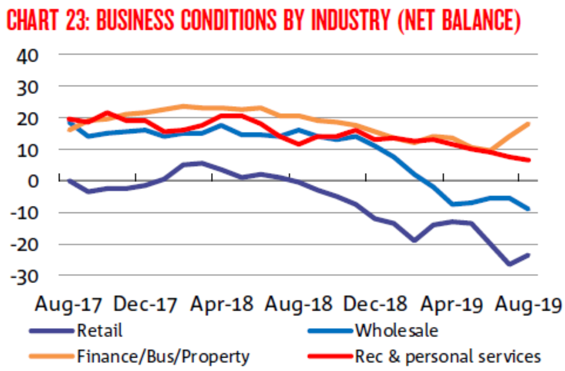
Overall business conditions fell to a new low in Aug. This was led by a further fall in trading (growing at a slower pace) and a decline in profitability. Employment growth increased in Aug. But forward orders became more negative, suggesting little improvement in activity in the near term.

CHART 6: COMPONENTS OF BUSINESS CONDITIONS, NET BALANCE, S.A.



Conditions improved somewhat across several industries; transport/utilities, finance/bus/property, and retail (but retail remains in negative territory). So, despite firmer conditions across finance/bus/property and retail, business confidence in these industries was weaker this month.





WA has been the only state to see a marked improvement in business conditions.

https://business.nab.com.au/nab-monthly-business-survey-august-2019-36493/

Return to top

China

Trade Balance, Exports and Imports (Aug)

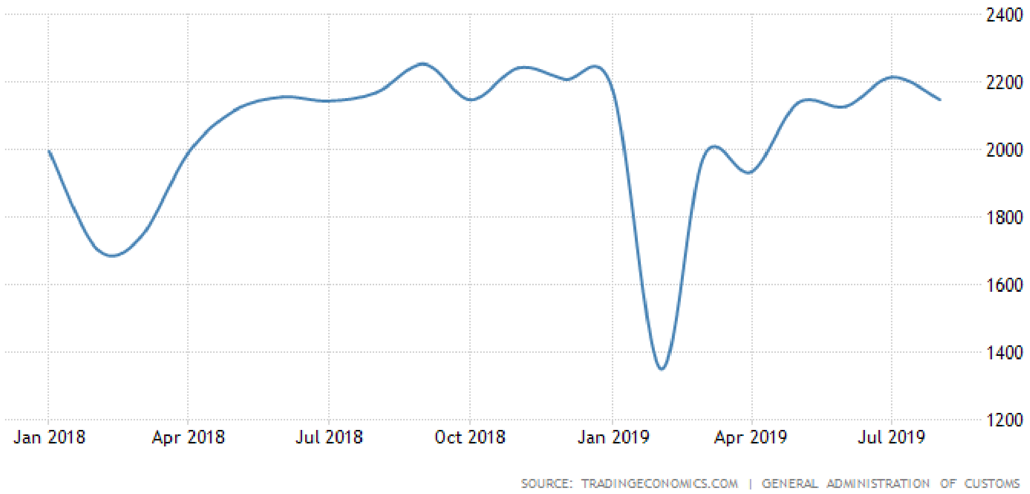
The trade balance increased versus a year ago. While exports declined slightly, imports declined by a faster pace.

Trade Balance; Aug US$34.8bn versus a year ago US$26bn

Exports

The value of exports declined in Aug by -1% versus a year ago after increasing by +3.3% in Jul.

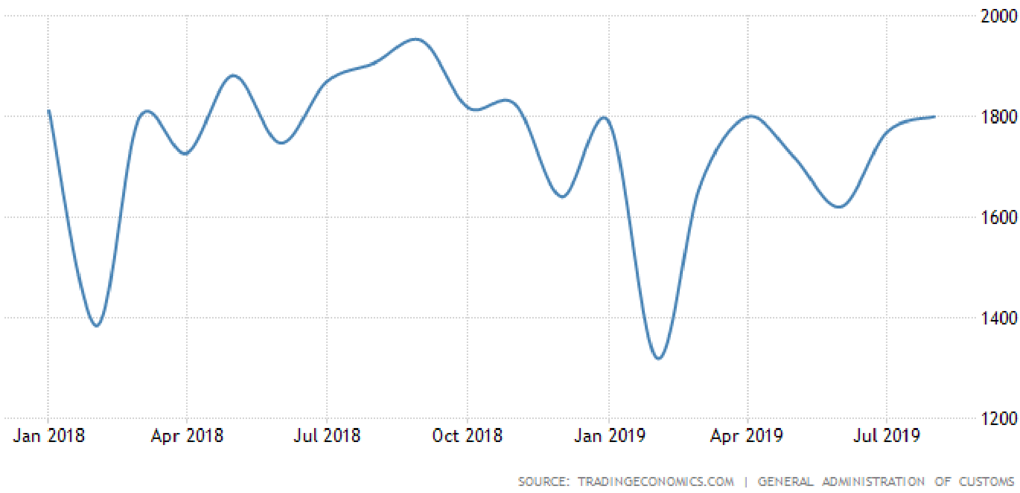
Chart: China Aug Exports (USD)



Imports

The value of imports continued to decline, and this has been the main source of the increase in the trade surplus. In Aug imports declined by 5.6% versus a year ago, somewhat faster than the 5.3% decline in Jul;

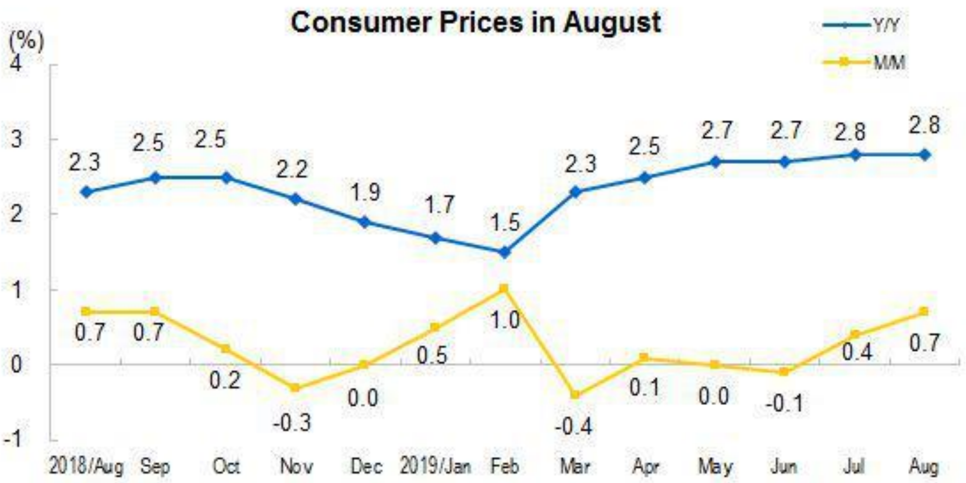
Chart; China Aug Imports (USD)



https://tradingeconomics.com/china/balance-of-trade

CPI (Aug)

Consumer price growth continued to accelerate on a monthly basis while the annual growth in consumer remained constant. The growth in food prices (especially pork/livestock) continues to make a larger contribution to the monthly change;



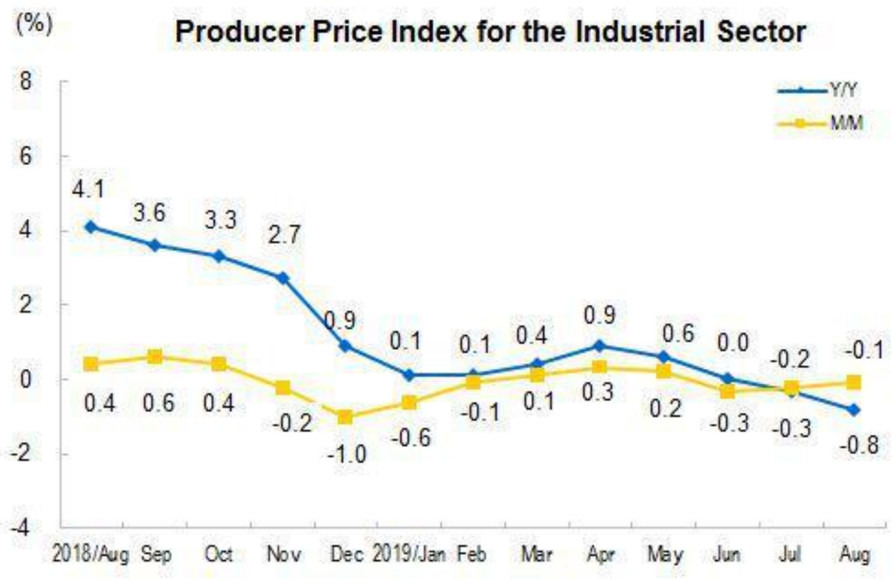
http://www.stats.gov.cn/english/PressRelease/201909/t20190911_1697184.html

Producer Price Index (Aug)

The annual decline in producer prices for the industrial sector accelerated in Aug. Prices received by producers declined again in the month but at a slower pace than in the month prior – and the shorter-term trend appears to be improving. The overall decline in selling prices continues to reflect the weaker demand environment.

Month change; Aug -0.1% versus Jul -0.3%

Annual change; Aug -0.8% versus Jul -0.2%



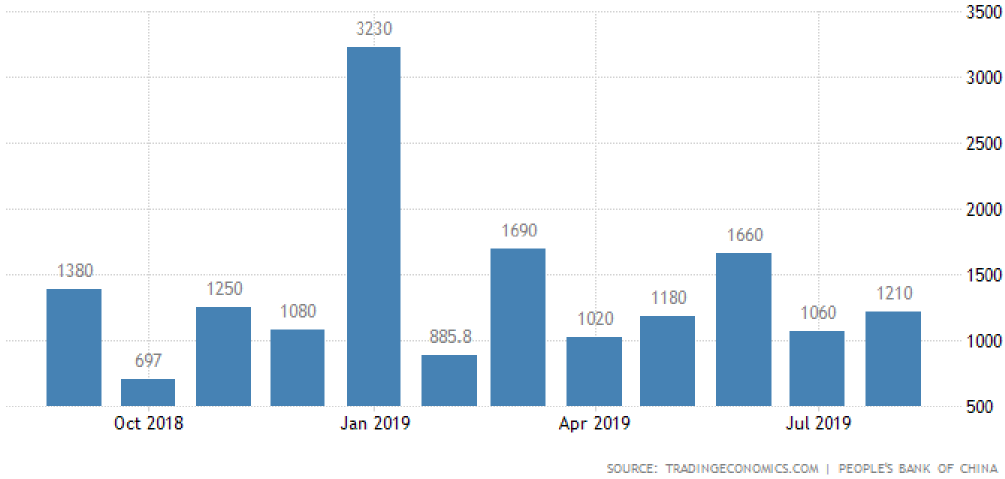
http://www.stats.gov.cn/english/PressRelease/201909/t20190911_1697194.html

New Loans (Aug)

Net new loans in China totalled CNY 1.21tr versus the 1.06tr in the month prior. The increase in the month was slightly ahead of the forecast for 1.20tr in CNY loans

Household loans, mostly mortgages; Aug CNY 653.8bn versus Jul CNY 511.2bn

Corporate loans; Aug CNY 651.3bn versus CNY 297.4bn



https://tradingeconomics.com/china/banks-balance-sheet

Return to top

Trade

US-China Trade Talks

During the week, US President Trump announced a two-week delay to the implementation of the tariff increase on $250bn of imports from China originally planned for 1 Oct. The delay was in observance to the PRC's 70th anniversary on 1 Oct.

Last week, it was announced that USTR Lighthizer and Vice Premier Lui He will meet in Washington in early Oct – no further details regarding dates at this stage.

Talks will take place later in Sep in the lead up to, and in preparation for, the meeting in Oct.

Some new tariff rates went into effect as of 1 Sep.

China; imposed a 5% tariff on crude oil imports as well as further duties on an unspecified range of imports from the US;

> "In retaliation, China started to impose additional tariffs on some of the US goods on a $US75 billion ($111 billion) target list. Beijing did not specify the value of the goods that face higher tariffs from Sunday. The extra tariffs of five per cent and 10 per cent were levied on 1,717 items from a total of 5,078 products originating from the United States."
> https://www.abc.net.au/news/2019-09-01/us-china-trade-war-escalates-with-additional-tariffs/11468922

US; tariffs were increased to 15% on approx. $125bn of imports from China (Annex A) and increasing the planned 10% tariff on the remaining of $300bn of imports to a 15% tariff from 15 Dec (Annex C).https://www.federalregister.gov/documents/2019/08/30/2019-18838/notice-of-modification-of-section-301-action-chinas-acts-policies-and-practices-related-to

The USTR made a request for comments on increasing the original 25% tariff on $250bn of imports to 30% from 1 Oct (now postponed by 2 weeks). https://www.federalregister.gov/documents/2019/09/03/2019-18946/request-for-comments-concerning-proposed-modification-of-action-pursuant-to-section-301-chinas-acts

On 23 Aug, Reuters reported that the US was still planning face to face meetings with Chinese officials regarding trade – dates in Sep are yet to be confirmed;

> ""The deputies' call [with Chinese officials] **was quite constructive** and this may lead to a meeting of the principals here in Washington, D.C.," Kudlow said, referring to a teleconference involving deputy-level officials on Wednesday."
> https://www.reuters.com/article/us-usa-trade-china/us-chinese-officials-held-productive-trade-call-white-house-adviser-idUSKCN1VC2NR

The issue of intellectual property remains a key obstacle to the deal;

> "Indeed, China's Vice Premier Liu He has only reiterated Beijing's position that a deal must be balanced and "expressed in terms that are acceptable to the Chinese people and do not undermine the sovereignty and dignity of the

country." https://www.cnbc.com/2019/06/29/g20-summit-trump-and-xi-agree-to-talks-but-offer-no-clear-path-to-end-the-trade-war.html

Reconfirming what a 'win' in the negotiations with China looks like – a statement of the key negotiating goals as outlined by the USTR (emphasis added);

> The meetings were held as part of the agreement reached by President Donald J. Trump and President Xi Jinping in Buenos Aires to engage in 90 days of negotiations **with a view to achieving needed structural changes in China with respect to forced technology transfer, intellectual property protection, non-tariff barriers, cyber intrusions and cyber theft of trade secrets for commercial purposes, services, and agriculture**.

https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/january/statement-united-states-trade

US-Japan Trade Talks

On the sidelines of the G7 summit, the US President and the Japanese PM announced a trade deal on 'core principles.

Both sides are now working through the detail of the deal - with a very tight deadline of having the deal ready to sign on the sidelines of the UN General Assembly later this month (Sep).

The Japan Times reported last week that the original announcement at the G7 had surprised Japanese officials and that the "core principles" didn't include the more contentious issue – namely auto tariffs;

> "Japanese officials were caught by surprise when Trump called a news conference at the G7 to announce a deal in principle, people close to the talks said. The situation moved so quickly that the Japanese government didn't even have time to invite journalists to attend the briefing."

> "The announcement also came before a firm agreement on the most contentious issue on the bargaining table, the people said. While Trump told reporters that the U.S. wouldn't impose new tariffs on autos and auto parts imported from Japan "at this moment," the president wasn't clear on whether he'd agreed to that as a concession. And Trump kept the tariff threat alive by saying he could still impose the levies at a later date." https://www.japantimes.co.jp/news/2019/09/06/business/u-s-japan-trade-deal-trump-deadline/#.XXXQAygzaUk

The summary of US negotiating objectives for the US-Japan trade talks;

https://ustr.gov/sites/default/files/2018.12.21_Summary_of_U.S.-Japan_Negotiating_Objectives.pdf

US-Europe Trade Talks

News late last week was that the WTO had provided a confidential ruling in favour of the US for illegal subsidies provided to Airbus.

> "The decision means that U.S. President Donald Trump will almost certainly soon announce tariffs on European products ranging from cheeses to Airbus planes. One official said Trump had won the right to collect a total of between €5 billion and €8 billion. Another said the maximum sum was close to $10 billion." https://www.politico.eu/article/trump-poised-to-hit-eu-with-billions-in-tariffs-after-airbus-win/

Amid the current negotiations, the EU is now starting to transition to new leadership including a new lead trade negotiator;

> "The decision sets the stage for a showdown between Europe and Washington just as the EU is transitioning to new leadership under incoming Commission President Ursula von der Leyen and Trade Commissioner-designate Phil Hogan. In unveiling her team on Tuesday, von der Leyen signaled **a robust approach to transatlantic disputes on trade and other issues with the Trump administration**" https://www.politico.eu/article/trump-poised-to-hit-eu-with-billions-in-tariffs-after-airbus-win/

The WTO ruling, together with new EU leadership, could see escalation in trade and tariff tensions between the EU and the US over the next few weeks once the ruling has been made official and public.

There are several fronts to the US-EU trade discussions.

Airline Subsidies

The WTO has now ruled in favour of the US (confidential judgement) over illegal European subsidies to Airbus. The EU also has a similar case pending related to Boeing.

Both sides have already identified potential areas for further sanctions if matters escalate and the US has already instigated a second process to identify further targets for tariffs.

The USTR has commenced another review; "Additional Products for Tariff Countermeasures in Response to Harm Caused by EU Aircraft Subsidies" (1 Jul 2019) https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/july/ustr-proposes-additional-products#

According to the Federal Register announcement;

> "A number of public comments submitted in response to the April 12 notice requested that the U.S. Trade Representative consider additional products that were not included in the April 12 list for possible inclusion on the final list of products to be subject to additional duties." https://ustr.gov/sites/default/files/enforcement/301Investigations/Notice_for_Additional_Products.pdf

The process for the latest review has now been completed – with no final announcement.

"In the event the Arbitrator issues its decision prior to completion of the public comment process on the supplemental list, the USTR may immediately impose increased duties on the products included in the initial list, and take further possible actions with respect to products on the supplemental list."

Also hanging over the negotiations are the US threats of tariffs on auto imports from Europe.

Trade Negotiations

One of the main issues standing in the way of a trade deal is that agriculture has been exempt from the negotiations by the EU.

The key sticking point remains agriculture. The EC authorised negotiations to commence between the EU and the US – but excluding agriculture. Emphasis added;

"Today's adoption of the EU negotiating directives gives a clear signal of the EU's commitment to a positive trade agenda with the US and the implementation of the strictly defined work programme agreed by Presidents Trump and Juncker on 25 July 2018. **But let me be clear: we will not speak about agriculture** or public procurement."

https://www.consilium.europa.eu/en/press/press-releases/2019/04/15/trade-with-the-united-states-council-authorises-negotiations-on-elimination-of-tariffs-for-industrial-goods-and-on-conformity-assessment/?utm_source=dsms-auto&utm_medium=email&utm_campaign=Trade+with+the+United+States%3a+Council+authorises+negotiations+on+elimination+of+tariffs+for+industrial+goods+and+on+conformity+assessment

""I do not think we will reach an agreement if agriculture is not included," McKinney told reporters on a teleconference during his visit to Brussels, citing concerns raised by U.S. lawmakers and Trump."
https://www.reuters.com/article/us-usa-trade-eu/no-u-s-eu-trade-deal-without-agriculture-u-s-official-idUSKCN1TS2SH

Instex

The EU confirmed that Britain, France and Germany had established a special trade channel (Instex) that would enable trade with Iran that circumvents the US sanctions. It was announced last year that the EU would work on developing the channel.
https://www.reuters.com/article/us-iran-nuclear-talks-statement/europe-says-iran-trade-channel-operational-statement-idUSKCN1TT2RL

President Trump made some mention of this development at the G-20;

"President Donald Trump said there was "absolutely no time pressure" in dealing with Iran as European nations pushed to salvage what remains of the 2015 nuclear accord and avert a slide toward war."
https://finance.yahoo.com/news/trump-chats-putin-shakes-hands-081017994.html

The Instex system enables trade with Iran without the use of U.S. dollars or US banks. The US has previously stated opposition to this;

> "According to Bloomberg, the Treasury Department's undersecretary for terrorism and financial intelligence, Sigal Mandelker, sent a letter on May 7 warning that Instex, the European SPV to sustain trade with Tehran, and anyone associated with it could be barred from the U.S. financial system if it goes into effect."
>
> "Separately, during a visit to London on May 8, Mike Pompeo also warned that there was no need for Instex because the U.S. allows for humanitarian and medical products to get into Iran without sanction."
>
> ""When transactions move beyond that, it doesn't matter what vehicle's out there, if the transaction is sanctionable, we will evaluate it, review it, and if appropriate, levy sanctions against those that were involved in that transaction," Pompeo said. "It's very straightforward.""

Digital Services

Undeterred by the USTR investigation into the digital services tax to be approved by the Govt of France, the EU has opened its own investigation into possible anti-competitive conduct of Amazon;

> "The European Commission has opened a formal antitrust investigation to assess whether Amazon's use of sensitive data from independent retailers who sell on its marketplace is in breach of EU competition rules."
> https://ec.europa.eu/commission/presscorner/detail/en/ip_19_4291

Further to the USTR S.301 investigation into the digital services tax approved by the French government, a public hearing on the tax implications has been held in the US;

> "The French DST law imposes a 3% tax on annual revenues generated by some companies that provide certain digital services to, or aimed at, French users. The tax applies only to companies with annual revenues from the covered services of at least €750 million globally and €25 million in France. The services covered are ones where U.S. firms are global leaders."
> https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/august/public-hearing-section-301

Background

The summary of US negotiating objectives for the US-EU trade talks have been published;

https://ustr.gov/sites/default/files/01.11.2019_Summary_of_U.S.-EU_Negotiating_Objectives.pdf

Section 232 – Car and Truck Imports

President Trump has agreed to delay the decision to impose tariffs on auto imports as a part of the s.232 investigation on car and truck imports on national security grounds. But he has **stated that he agrees with the conclusion of the Commerce Dept report that imports harmed national security by causing declining market share for US-owned carmakers.**

“"I concur in [Commerce Secretary Wilbur Ross'] finding that automobiles and certain automobile parts are being imported into the United States in such quantities and under such circumstances as to threaten to impair the national security of the United States," Trump said in a proclamation outlining his decision.” https://www.politico.com/story/2019/05/17/donald-trump-auto-tariffs-1330014

As a part of the announcement, US President Trump also…

“directed U.S. Trade Representative Robert Lighthizer to pursue the negotiation of agreements with the EU, Japan and other countries that address the alleged national security threat posed by auto imports.

Lighthizer was directed to update the president on the status of those talks within 180 days.” https://www.politico.com/story/2019/05/17/donald-trump-auto-tariffs-1330014

The tariffs remain as negotiating leverage between the US and Japan and the EU. The S.232 report has not been made public, but President Trump’s statement provided some insight as to how the Commerce Dept justified the ‘national security’ grounds;

“The rapid application of commercial breakthroughs in automobile technology is necessary for the United States to retain competitive military advantage and meet new defense requirements,” the proclamation said.

The proclamation added that the U.S. defense industrial base depends on the “American-owned automotive sector” for development of technologies essential to military superiority. Foreign imports have eroded the ability of U.S. companies to compete and research and develop new technologies, the proclamation said.

“The lag in R&D expenditures by American-owned producers is weakening innovation and, accordingly, threatening to impair our national security,” the proclamation stated. https://www.politico.com/story/2019/05/17/donald-trump-auto-tariffs-1330014

NAFTA/USMCA

The US Congress was back last week, and given the increased volatility around trade, there is even more pressure on both sides to approve the USMCA. Both sides appear to be making moves to progress the approval.

During the week USTR Lighthizer provided formal responses to address concerns over labor, environment, enforcement and prescription drug provisions.

House Democrats said Thursday they believe they are making progress with the Trump administration over how to fix their concerns with the new North American trade agreement, indicating a congressional vote on the measure is still possible this year.

The two sides are likely to spend the next several weeks exchanging texts as the Trump administration continues to push for Congress to pass the agreement before the end of the year.

White House trade adviser Peter Navarro said earlier this week that the administration wants to "get this thing done within the next 30 to 60 days," — a timeline House Agriculture Chairman Collin Peterson (D-Minn.) also embraced on Thursday. https://www.politico.com/story/2019/09/12/democrats-nafta-usmca-talks-1729037

The Democrats continue to work with USTR Lighthizer on changes required to the USMCA before the deal can go to Congress for approval.

"The end of 2019 has become an informal deadline to get the deal approved amid concerns that it will get lost in the noise of the presidential election if it bleeds into 2020. But the campaign itself could add to pressure for action sometime over the fall, as Democrats seek to defend their House majority." https://www.politico.com/story/2019/08/31/democrats-trade-trump-1691486

Once the US approves/ratifies the USMCA, Canada will take steps to approve the USMCA in parliament.

US-UK Trade Talks

During his visit to the UK, President Trump announced that the US would begin talks with the UK on a trade deal as soon as Brexit was completed.

The USTR has now published the summary of specific negotiating objectives for the US-UK trade negotiations; https://ustr.gov/sites/default/files/Summary_of_U.S.-UK_Negotiating_Objectives.pdf

Return to top