MARS CAPITAL PARTNERS

# Weekly Macro Review

w/c 29 June 2020

## Key Themes

Sectors within the US economy have, so far, been affected by the pandemic in different ways.

US durable goods manufacturing has been most affected within transport equipment, specifically, motor vehicles and non-defense aircraft (which was already declining prior to the pandemic). That's not to say that other durable goods sectors have not been affected by shutdowns, it's that the extent of the impact on transport equipment production has been most severe – and this is a large part of industry.

The May US factory orders data showed that transport orders rebounded strongly – but half of that growth was due to the change from -$8bn in aircraft orders in Apr (net cancelled orders) to $3bn in orders in May resulting in +$11bn contribution to the headline growth between the two months. Orders for transports are still 41% below a year ago. Yet, orders for durable goods ex transports is "only" 6.7% below a year ago (which is still a large decline, but not as extreme).

Motor vehicle retail sales rebounded in May – led by SUV's/light trucks. Sales of auto's also increased, but off an extremely low base, and to a lesser degree than SUV's. The pandemic appears to have accelerated the trend of the decline in auto/sedan sales - May auto sales on a SAAR basis was a mere 2.65m units, the second lowest on record after Apr 2020.

It is also worth noting that Japanese production of motor vehicles declined at an accelerated pace in May and production levels fell to 61% below a year ago. Retail sales of motor vehicles in Japan fell by 11% in May (and -34% compared to a year ago).

Non-durable goods shipments in May, excluding petroleum, are now only down 3.2% versus a year ago. Production across food and chemicals, especially, has been less affected throughout the pandemic. Petroleum production in the US has been impacted by severe price falls as well as a decline in demand. Petroleum shipments are 54% below a year ago (value). The Dallas Fed Survey for Jun noted that oil producers remained downbeat, despite a general improvement in manufacturing conditions in the region.

The broader forward view of manufacturing for Jun via the ISM manufacturing PMI highlighted that more manufacturing firms continue to recover across most industries. But within the detail of the ISM is that transportation equipment manufacture continued to worsen across every measure in the Jun PMI. Most concerning is the continued decline in orders for this segment as it suggest continued weaker output in the short-term.

Despite the improvements in shipments and orders, the ISM survey showed that firms, on net, continue to reduce employment.

We will cover services next week once the Jun data is released. For now, the non-farm payrolls for Jun increased by 4.8m jobs – of which 2.1m of the gains were in leisure and hospitality. The trend of improving payrolls is extremely positive – but there are another 14.5m jobs still to be recovered. Yet the weekly initial claims, continuing claims and pandemic unemployment assistance claims all remain extremely elevated and have been little changed. The concerning trend in the household employment survey was the continued rise in permanent layoffs (but temporary layoffs also declined).

The outbreak of infections across the US South and parts of the West and Midwest will likely derail some of this recovery, especially in the services hospitality sector. The unemployment claims data is likely to record further increases in these regions.

The global manufacturing PMI's were consistent. The pace of decline slowed notably as more firms started to record improving conditions especially across Europe and Australia. Japanese manufacturing was the exception - almost half of the survey panel (48% of firms) recorded lower production, compared to 13% of firms that expanded output in June.

In most cases, growth is just starting to rebound, so excess capacity is still an issue and firms are continuing to reduce employment. The improvement in sentiment for the next twelve months was universal.

## Contents

# US Data

## Initial (26 Jun) and Continuing Jobless Claims (19 Jun) and Pandemic Unemployment Assistance (PUA) Claims

Initial unemployment claims continued to increase in the latest week. The weekly increase is still well above 1,000,000 claims. For comparison, initial claims were tracking at approx. 217k a week throughout 2019.

The level of continuing claims, combining the total of all programs for the wk ending 13 Jun (NSA);

> The total number of people claiming benefits in all programs for the week ending June 13 was **31,491,627**, an increase of 916,722 from the previous week. There were 1,582,309 persons claiming benefits in all programs in the comparable week in 2019.

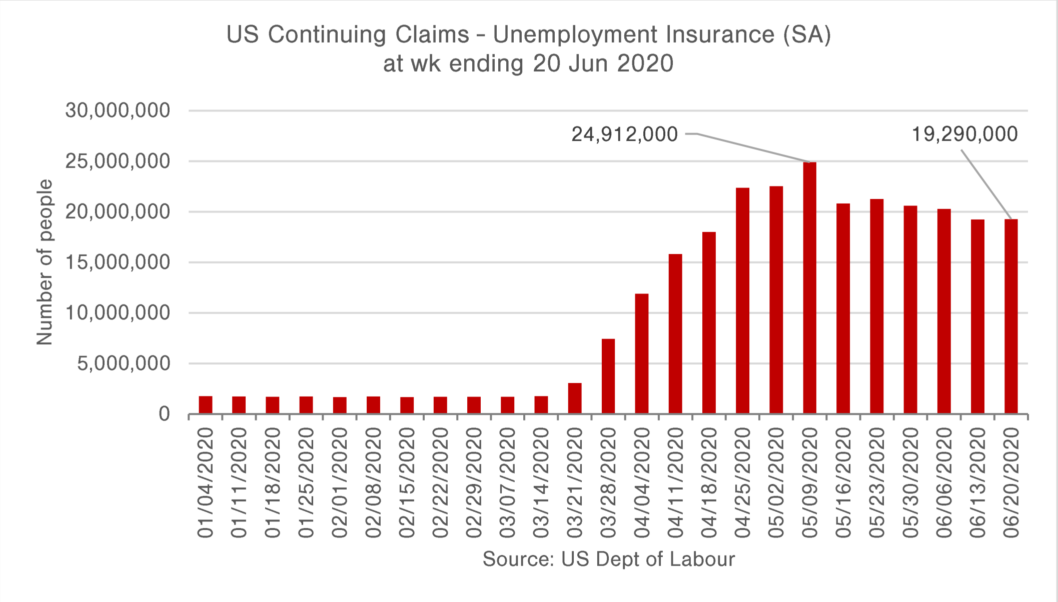
Advance initial unemployment claims wk ending 27 Jun (SA): 1,427,000 people

Prior week claims were revised higher by 2k claims.

Advance insured unemployment claims (continuing claims) wk ending 20 Jun 2020; 19,290,000 people

Prior week claims were revised lower to 19,231,000 claims.

That means that the level of continuing claims increased slightly week on week:




The insured unemployment rate was 13.2% in wk ending 20 Jun.

> The highest insured unemployment rates in the week ending June 13 were in Puerto Rico (23.0), Nevada (21.4), Hawaii (21.3), the Virgin Islands (17.8), New York (17.5), California (16.0), Louisiana (15.9), Massachusetts (15.9), Georgia (15.3), and Connecticut (15.2).

Pandemic Unemployment Assistance (PUA)

Advance claims for PUA wk ending 27 Jun 2020 (NSA); 839,000

The prior week initial claims were revised higher from 728k to 881k.

PUA Continuing Claims – wk ending 13 Jun 2020 (NSA); 12,853,163 people.

This is an increase on the total number reported for wk ending 6 Jun of 11,067,347 continuing PUA claims.

Pandemic Emergency Unemployment Compensation (PEUC) Benefits

The number of new claims for PEUC slowed this week.

New Claims PEUC wk ending 13 Jun 2020 (NSA); 749k persons (851k in the week prior)

> During the week ending June 13, 47 states reported 12,853,163 individuals claiming Pandemic Unemployment Assistance benefits and 39 states reported 749,703 individuals claiming Pandemic Emergency Unemployment Compensation benefits.

https://www.dol.gov/ui/data.pdf

## Non-Farm Payrolls (Jun) and Employment Survey (Jun)

Non-farm payrolls growth accelerated again this month. So far though, the cumulative total of jobs recovered in May and Jun (+7.5m) remain well below the Mar and Apr 2020 shock of losing -22m jobs.

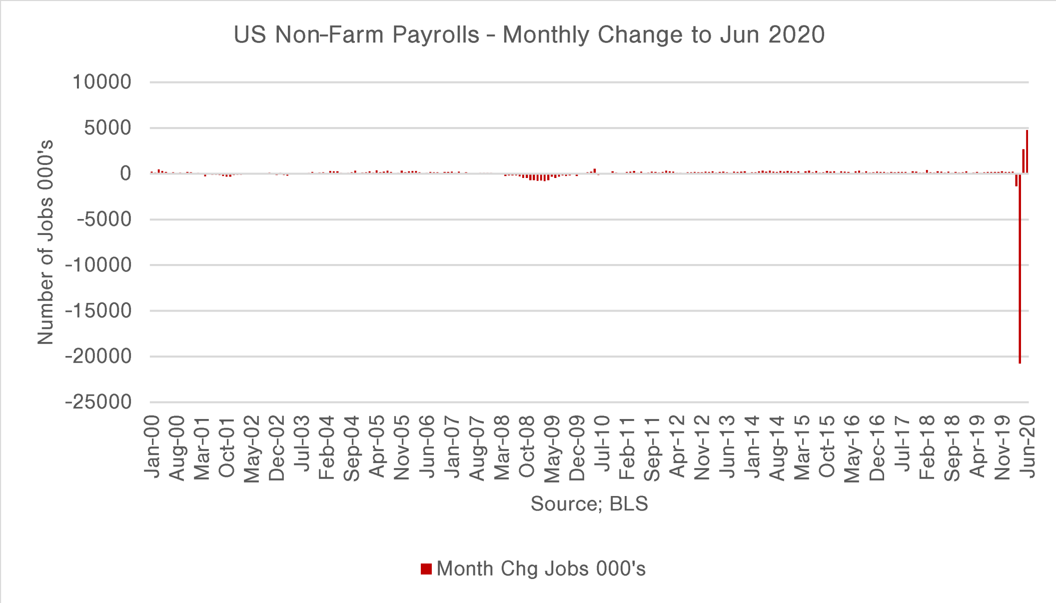
The survey reference week was 7 - 13 Jun.

Non-Farm Payrolls – month change; Jun +4.8m versus May +2.7m

The acceleration in jobs recovered is a welcomed development – the result of the resumption of business activity across most industries. There is obviously still a long way to go before the complete recovery of the jobs lost in Mar and Apr.

> In June, nonfarm employment was 14.7 million, or 9.6 percent, lower than its February level.

Most of the gains in payroll employment in the month were in leisure and hospitality, which added +2.1m jobs in Jun.




## US Employment – Household Survey (Jun)

A more positive change this month as employment growth was higher than what both population and participation added to the labour force. This resulted in a reduction in total unemployed persons in Jun.

While the direction of change is good, it is the level of employment and unemployment that is still a problem. Employment levels are down 15m people compared to a year ago and total unemployed persons is higher by 12m people compared to a year ago.

One of the more concerning developments this month was the increase (acceleration) in the number of job losers now on a permanent layoff (transitioning from a temporary layoff).

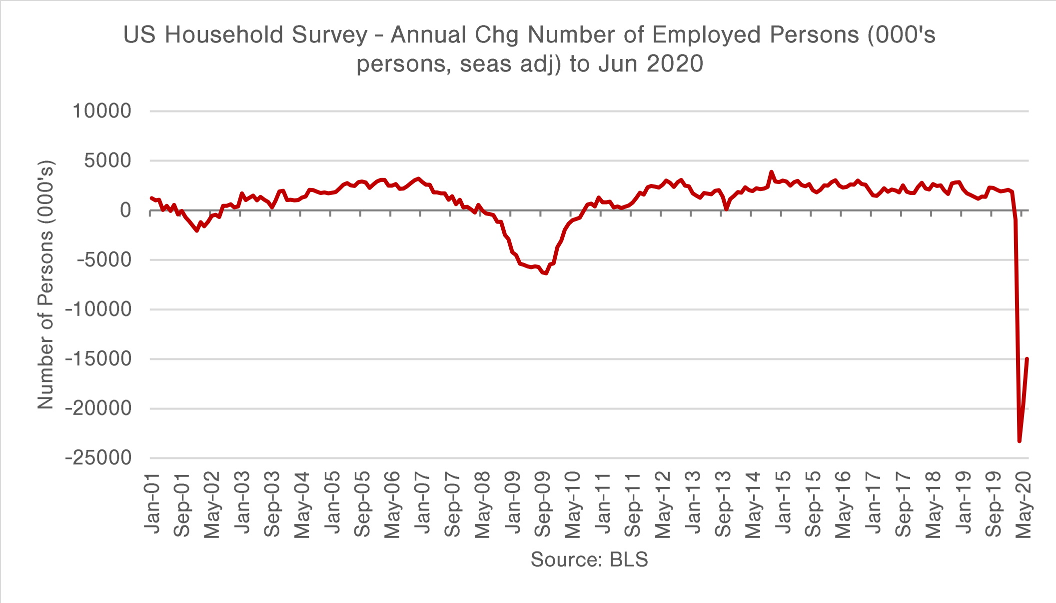
<u>Employment</u>

The total number of employed persons increased for the second month in a row.

<u>Total employed persons – month change</u>; Jun +4.9m versus May +3.8m

So far, the jobs recovered in May and Jun is approx. 8.8m – compared to the 25m jobs lost in Mar and Apr. There is still clearly a long way to go before employment growth recovers these losses.

On an annual basis, the current employment level is 15m people below the same month a year ago;



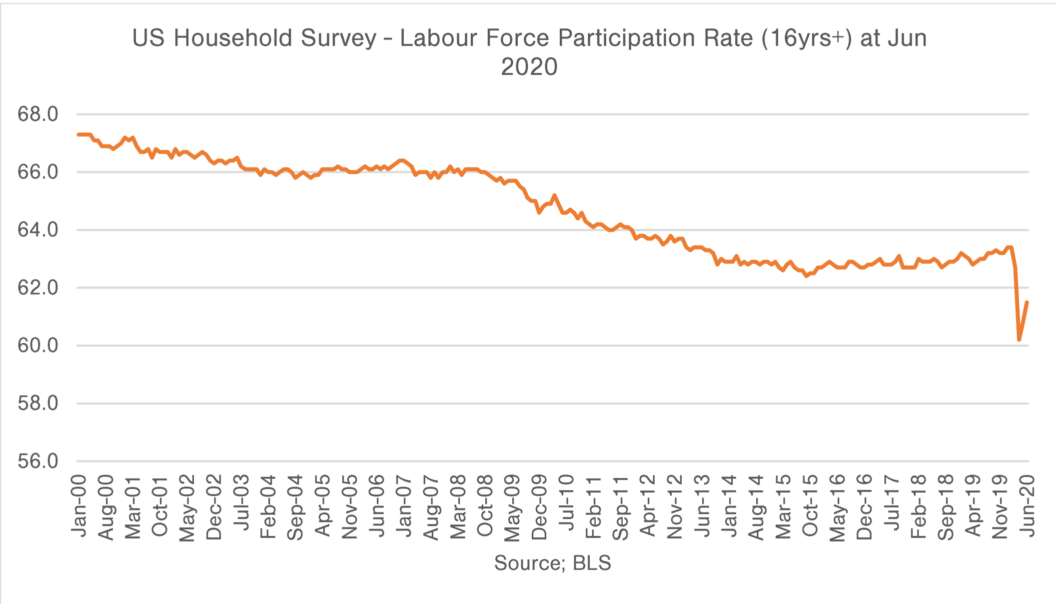

<u>Labour Force</u>

The size of the labour force increased for a second month in a row in Jun.

<u>Labour Force – month change</u>; Jun +1.7m persons versus May +1.7m persons

The increase in Jun was the result of an increase in the participation rate. In Jun, participation increased to 61.5% versus 60.8% in May. This added approx. 1.8m people back into the labour force.

Despite the monthly increase, there are still approx. 3.7m less people in the labour force compared to a year ago, due to the decline in the participation rate.



Total Unemployed Persons

The crucial point though is that employment growth of +4.9 people in Jun was greater than the +1.7m person increase in the size of the labour force. This means that total unemployed persons declined in Jun.

Total unemployed persons – month change; Jun -3.2m people versus May -2.1m people

While the two-month trend is positive, there is still a long way to go before total unemployment is back down to pre-pandemic levels. The declines in May and Jun total -5.3m people – compared to the +17.3m increase in total unemployed persons back in Mar and Apr.

The total number of unemployed persons is still 11.7m people above the same month from a year ago.

The unemployment rate fell to 11.1% in Jun (from 13.2% in May).

Temporary versus Permanent Layoff

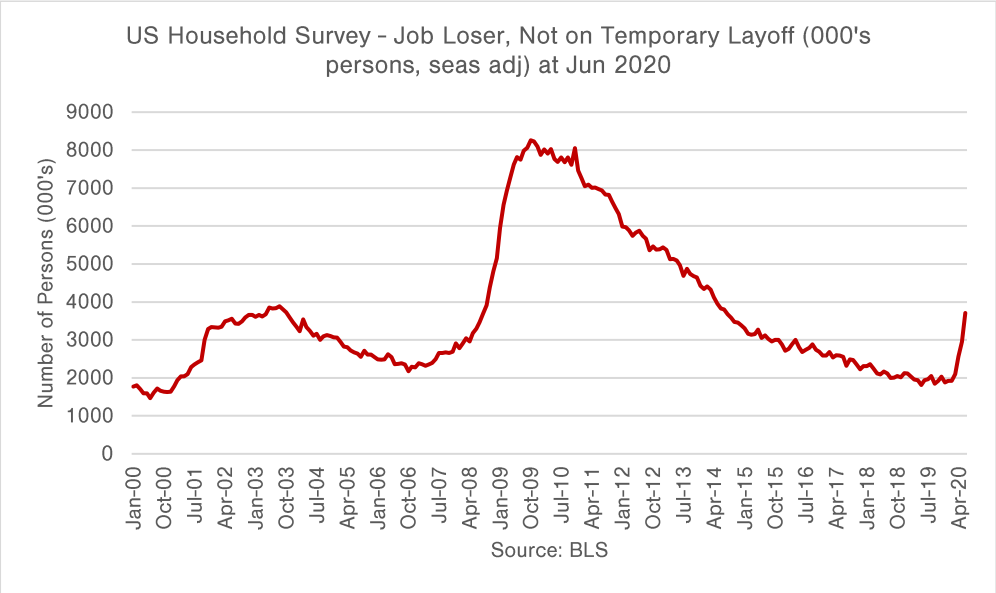
The nature of the pandemic shutdown was such that there was a higher proportion of unemployed persons classified as on a 'temporary layoff'.

This is a slightly different unemployment data series (seasonally adjusted independently). The data series provide an insight now into the shifts between those classified on 'temporary layoff' and those classified on 'permanent layoff'.

This month, the number of people classified as having lost a job, decreased by -4m people (a positive result). This total is the sum of those people on temporary layoff and permanent layoff.

Those on temporary layoff declined by -4.8m people in Jun to a total of 10.6m people still classified as on a temporary layoff.

But those on permanent layoff increased this month by 759k people, from 2.9m people in May to 3.7m people in Jun;




The number of people on permanent layoff is still well below the GFC peak but will be something to watch.

Summary of Labour Market Changes – Monthly and Annual at Jun 2020

| 000's people (16yrs+) | Annual chg - JUN 2020 | Monthly Chg - Jun |
|---|---|---|
| The estimated change in the Labour Force due to pop growth (1) | 700 | - 117 |
| How many jobs available for them? (employment growth) (2) | - 14,966 | 4940 |
| Difference (if negative, then employment growing faster than what pop adds to the labour force) (3) | 15,666 | -5057 |
| | | |
| Change labour force participation - (if positive, people entering/returning to the labour force) (4) | - 3,901 | 1820 |
| | | |
| The remainder is the chg in total unemployed persons (declining if negative) (4) plus (3) | 11,765 | -3236 |
| | | |
| **Two views of annual growth in the labour force;** | | |
| Total employed persons plus total unemployed persons | - 3,201 | 1704 |
| Est of what population adds to the labor force plus change in participation | - 3,201 | 1704 |
| BLS reported change in the size of the labour force | - 3,201 | 1705 |
| | | |

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

## ISM Manufacturing PMI (Jun)

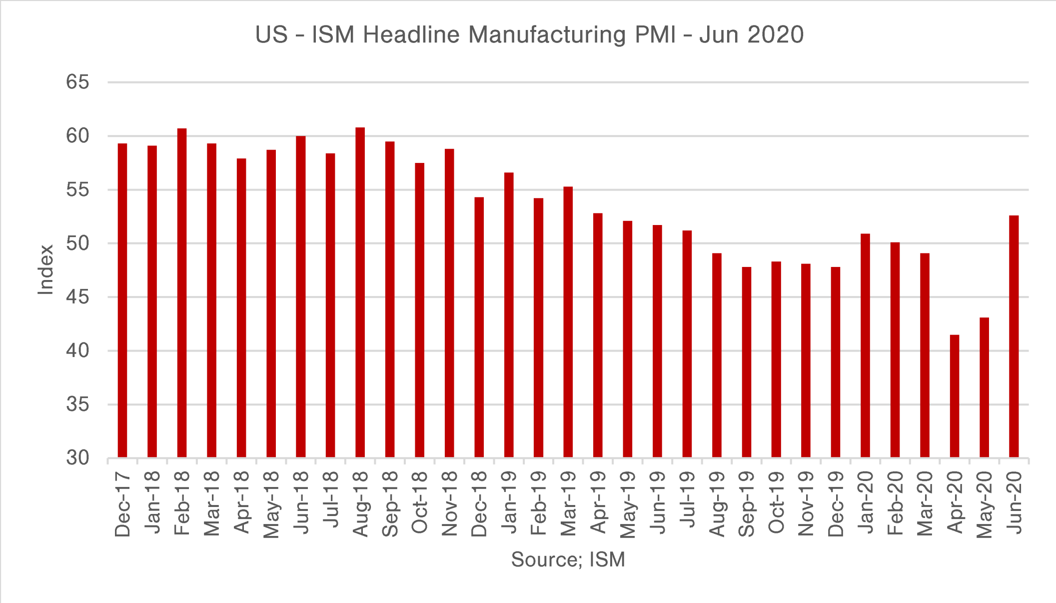
The ISM manufacturing PMI showed that manufacturing firms on net, reported an increase/growth in activity in Jun compared to May. Measures of demand such as production and new orders increased compared to the month prior. Comments were positive regarding activity in the month. Firms still appear cautious and continue to reduce employment on net – although at a slower pace than in May.

There is no indication though of how levels compare to a year ago, or how much production/shipments/orders need to grow in order to get back a pre-shut down level.

Of the eighteen manufacturing industries covered in the series, fourteen reported growth in Jun compared to May. Four industries continued to record declines, on net, in activity in Jun compared to May - Transportation Equipment; Primary Metals; Fabricated Metal Products; and Machinery.

Transportation equipment is one of the largest weight industries and the return to growth is taking longer than in other industries. On most dimensions, the transport equipment industry continued to record declining activity, including new orders.

Headline ISM Manufacturing PMI; Jun 52.6 versus May 43.1




New orders, on net, increased in Jun compared to the three prior months of decline. The proportion of firms reporting higher new orders now outnumbers the proportion of firms reporting lower new orders in Jun. In Jun, less firms reported lower new orders – 23.9% in Jun compared to 52.9% in May. Some of these firms instead recorded no change in orders – and this group increased from 26% of firms in May to 39% of firms in Jun. There was also an increase in the proportion of firms reporting higher new orders – from 21% of firms in May to 37.3% of firms in Jun.

On an industry basis, there were ‘only’ two of eighteen manufacturing industries reporting declines in new orders for the month; Fabricated Metal Products; and Transportation Equipment.

New export orders (75% of all firms in the survey) improved, with the pace of decline easing. But the underlying change was less positive. While less firms recorded lower/declining new export orders, most of those firms shifted into ‘no change’ from the month prior. Just over 50% of firms recorded no change in new export orders in May and this increased to 67% of firms in Jun. There was also a small decline in the number of firms reporting increasing new export orders, falling from 14.3% in May to 13.8% in Jun.

The production increase was stronger. The index increased from 33.2 in May to 57.3 in Jun. More firms reported increasing production and less firm reported declining production.

Only three industries continued to report a decrease in production in Jun (compared to the month prior) - Primary Metals; Transportation Equipment; and Fabricated Metal Products.

The growth in orders and the restart of production for many firms still resulted in little change in order backlogs this month. This likely indicates the level of spare capacity that still exists and how much further orders need to grow. Order backlogs continued to decline on net in Jun (45.3), but at a slower pace than in May (38.2).

More than half of all industries covered in this report still recorded declining order backlogs; In June, seven industries reported lower backlogs, in the following order: Food, Beverage & Tobacco Products; Transportation Equipment; Petroleum & Coal Products; Miscellaneous Manufacturing; Furniture & Related Products; Fabricated Metal Products; and Electrical Equipment, Appliances & Components.

The level of spare capacity was also evident in the employment change. The employment index showed that most firms, on net, continued to reduce employment in Jun (42.1) – also though at a slower pace than in May (32.1). Less firms reported declining employment (26% of firms in Jun versus 41% in May). Most firms instead shifted in the 'no change' category – 59% of firms reported no change in employment in Jun. There was an increase in the proportion of firms reporting higher employment, increasing from 7.6% in May to 14.6% of firms in Jun.

At an industry level, only five industries out of the eighteen total reported employment growth in Jun; Apparel, Leather & Allied Products; Nonmetallic Mineral Products; Computer & Electronic Products; Food, Beverage & Tobacco Products; and Chemical Products.

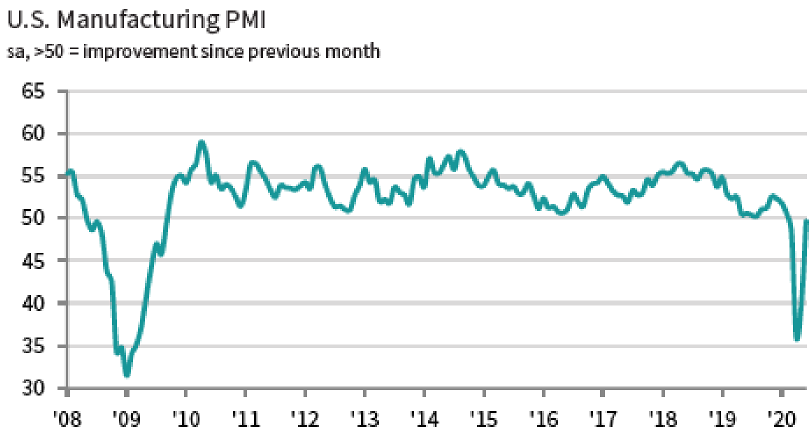
Eleven industries reported continued declines in employment; The 11 industries reporting a decrease in employment in June, in the following order, are: Printing & Related Support Activities; Petroleum & Coal Products; Transportation Equipment; Primary Metals; Electrical Equipment, Appliances & Components; Plastics & Rubber Products; Paper Products; Furniture & Related Products; Fabricated Metal Products; Machinery; and Miscellaneous Manufacturing.

https://www.instituteforsupplymanagement.org/ISMReport/MfgROB.cfm?SSO=1#:~:text=PMI,-%C2%AE&text=Manufacturing%20grew%20in%20June%2C%20as,May%20reading%20of%2043.1%20percent.&text=A%20reading%20above%2050%20percent,that%20it%20is%20generally%20contracting.

## US Markit Manufacturing PMI Final (Jun)

Manufacturing activity continued to rebound in Jun. The proportion of firms recording lower activity still outnumber those recording improving activity, but by a much smaller degree than in the month prior. In other words, more firms were starting to see improving conditions. Underlying that, new orders growth stabilized (no change overall) after several months of severe decline. Output continued to decline on net, albeit at a slower pace.

Headline Manufacturing PMI; Jun 49.8 versus May 39.8




Source: IHS Markit.

Demand started to improve this month with at least stabilization in new orders. New orders growth was unchanged this month – meaning, on net, there were (likely) equal number of firms reporting increases and decreases in orders.  Improvement in orders from the month prior was the result of customer reopening. New export orders continued to decline.

Despite the improvement in orders, production continued to decline, albeit at a slower pace (the slowest since Feb).

Despite improving demand conditions, employment continued to decline. The decline remained moderate. Backlogs of work continued to decline indicating the level of spare capacity, despite the improvement in orders.

> Goods producers also indicated renewed optimism that output would increase over the coming year. Positive sentiment stemmed from hopes of a sustained pick-up in client demand **and an end to the pandemic**.

This survey was taken between 12-25 Jun. With infection rates now reaching new highs again in the US, it will be interesting to see how sentiment responds and how this impacts demand.

Inventories continued to fall, and the pace of decline slowed. Firms continued to run down inventories of inputs and finished goods.

https://www.markiteconomics.com/Public/Home/PressRelease/92bddcb07e0447ffaf545a13bd6031d1

## Dallas Fed Manufacturing Survey (Jun)

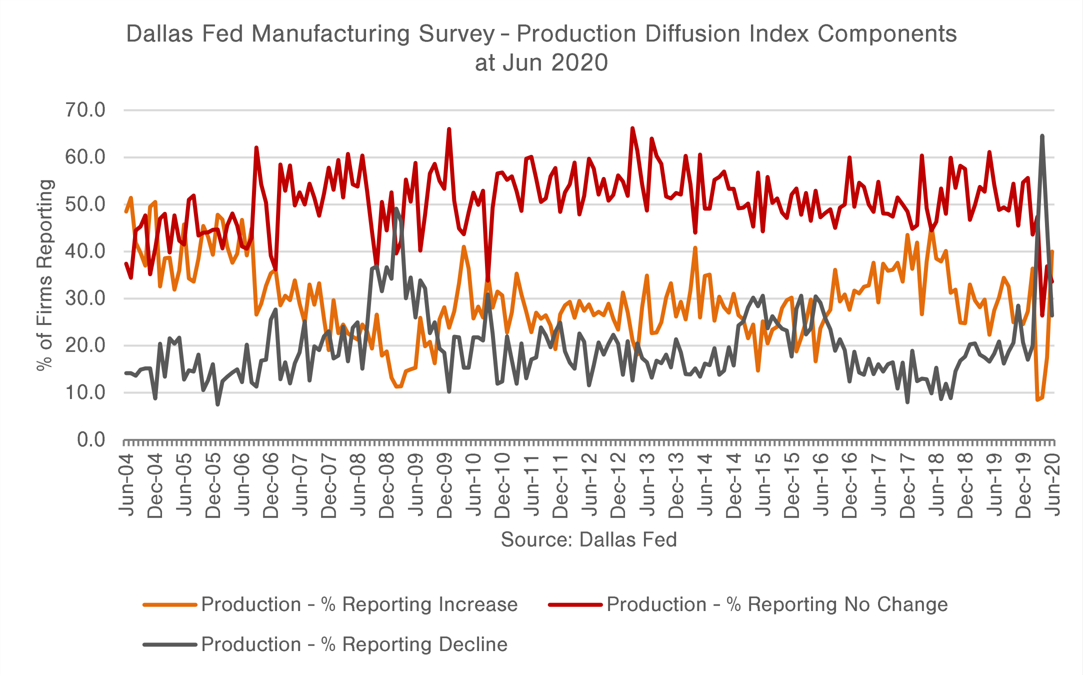
A positive rebound in demand this month – with production, orders, and shipments all moving into positive territory this month. Employment levels and the workweek continue to slowly improve but remain slightly negative.

Industry comments from the Dallas Fed report are mixed – and in fact, the choice of negative comments/anecdotes seems at odds with the stronger data. Overall; Oil producers remained downbeat. Homebuilder materials demand is stronger. Material for commercial construction (non-resi) is weak. Supply constraints remain. Some improvement in revenue this month, but from depressed levels.

Data collected 16-24 Jun.

Headline Production Index; Jun 13.6 versus May -28

This was a substantial improvement in the month and the underlying shifts were positive. More firms reported an increase in production (40% of firms) and less firms reported a decline in production levels (26.4% of firms) in Jun compared to the month prior.




New orders also shifted back into positive territory; Jun 2.9 versus the more severe decline of -30.6 in May. The Jun result shows that the number of firms reporting an increase in orders now outnumbers the firms reporting declines in orders. In fact, the number of firms reporting a decline in new orders fell from 51.7% of firms in May to 29.5% of firms in Jun.

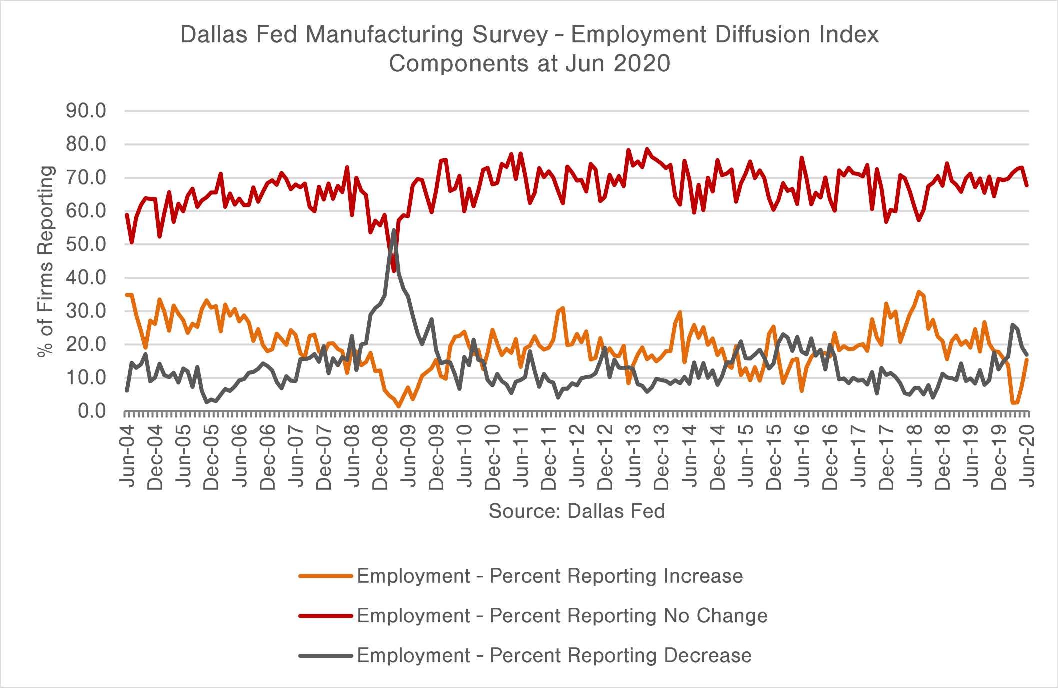
Similarly, shipments also shifted into positive territory.

Unfilled orders continued to decline, but at a much slower pace; Jun -2.3 versus May -17.4. The pace of growth in new orders is resulting in some pressure on backlogs.

Growth in capacity utilization increased this month – more firms reported an increase in capacity utilization this month (35.5% of firms) while less firms reported a decline in utilization this month (27.9% of firms) in Jun compared to May.

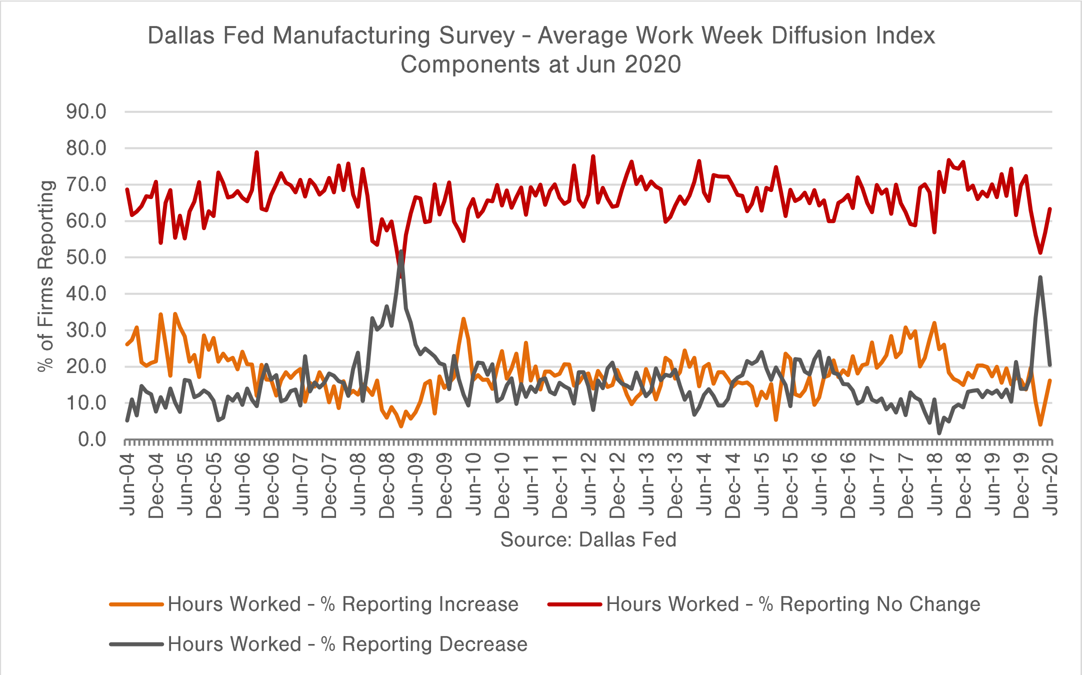
Employment levels remained in negative territory this month. But, as we noted previously, there was less change in employment levels throughout this shutdown – firms appeared to opt for a reduction in hours instead. That said, the proportion of firms reporting an increase in employment during the pandemic shutdown was the only metric that fell close to the GFC extreme. This reflects more of a hiring freeze – PPP support likely?

This month, there was still a positive change in employment though. Less firms reported no change in employment and less firms reported declining employment. This all shifted into more firms reporting higher employment. But note that most firms had left employment levels unchanged throughout this shutdown (in Jun 67.7% of firms).




Hours worked was where there had been more change throughout the initial lockdown. This month, hours worked remained in negative territory, but less so than in May. There was a larger decrease in the proportion of firms reporting further decreases in hours worked (20.5% of firms in Jun). There were subsequent increases in firms reporting no change in hours from the month prior (63.3% of firms in Jun) and firms reporting an increase in hours worked (16.2% of firms in Jun).

So, there is less emphasis on further contraction in hours worked, and at least some stability in the workweek, albeit likely at a lower level.



At the same time, firm's margins are likely to be under pressure. Prices paid for raw materials increased at an accelerated pace, while prices received for finished goods continued to decline. But note that most firms (75.7% of firms in Jun) reported no change in selling prices.

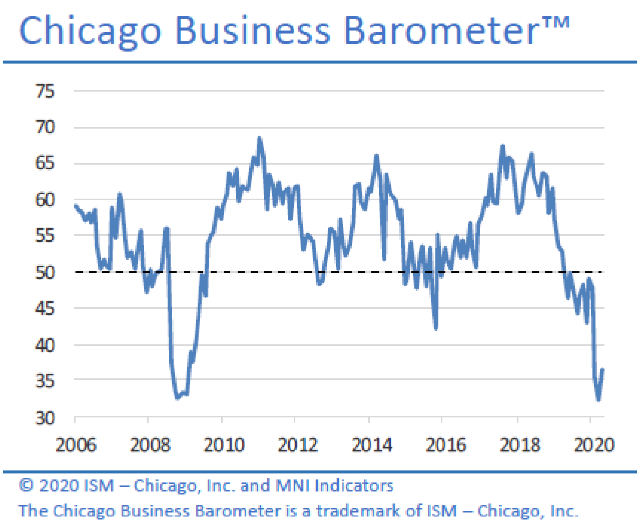
The company outlook improved and shifted into positive territory. More firms reported an improved outlook while less firms reported a worsening outlook.

https://www.dallasfed.org/research/surveys/tmos/2020/2006.aspx

## Chicago ISM Business Barometer (Jun)

Business activity remained firmly in contraction in the Chicago area in Jun. The pace of decline was only slightly slower than in May.

Headline Business Barometer Index; Jun 36.6 versus May 32.3




The change in production improved this month, but the quarter two result was the lowest on record. Similarly, new orders also improved, while the quarter two result was the lowest in forty years.

Inventories fell back into contraction in Jun.

The employment index fell five points in Jun compared to May. This is the twelfth consecutive month where employment has declined.

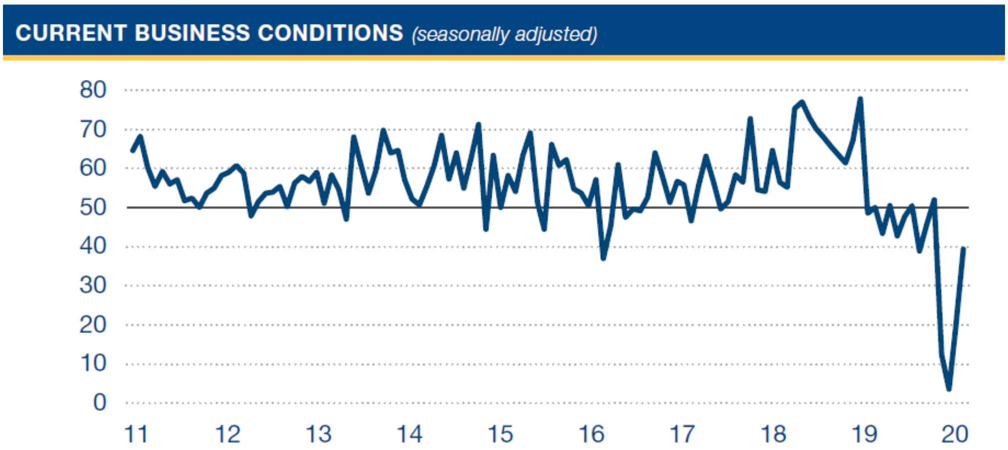
This month's special question asked: "What are your personnel plans for the rest of the year?". The majority (55.8%) plan a hiring freeze, while 23.3% expect to lay off employees. Only 18.6% of respondents projected expanding their workforce.

https://s3.amazonaws.com/images.chaptermanager.com/chapters/b742ccc3-ff70-8eca-4cf5-ab93a6c8ab97/files/mni-chicago-press-release-2020-06.pdf

## ISM NY Business Conditions (Jun)

As the region starts to reopen and infections continued to fall, business conditions improved – in that the pace of decline slowed notably.

<u>Current Conditions Index;</u> Jun 39.5 versus May 19.5




The outlook for six months' time improved notably, with most respondent seeing growth rebound; Jun 67.1 versus the May outlook of 48.

Employment is yet to catch up to expectations. The employment index continued to decline, and at a slightly faster pace; Jun 33.5 versus May 33.9

http://www.ismny.com/wp-content/uploads/2020/07/2020_ISM-New-York_June-ROB_v01.pdf

## US Factory Orders (May)

The factory orders data enables us to look at more detail of the composition and level (value only) of orders and shipments across manufacturing industries – rather than just the broad direction provided by the PMI's (which is useful as a leading indicator).

At the top-line, orders and shipments returned to growth ($ value terms) in May – but are yet to bridge the gap in terms of prior month declines. The increase in orders was much stronger than the increase in shipments in May. This was due to the change from -$8bn in aircraft orders in Apr (net cancelled orders) to $3bn in orders in May resulting in +$11bn contribution to the headline growth in orders between the two months.

The key issues are that orders (and shipments) for transports (motor vehicles and non-defense aircraft) are still 41% below a year ago. This is masking the better performance of order growth across other durable goods industries (ex-transports) – which is "only" 7% below a year ago.

The other factor is the impact of the value of petroleum shipments on non-durable goods shipments. Because these data are in value, the fall in oil prices impacts the value of shipments. Shipments for petroleum refineries is 54% below a year ago as of May. Shipments of non-durable goods ex petroleum refineries is only down by 3% on a year ago basis. The largest non-durable goods industries such as Food and Chemicals recorded YTD growth in shipments as of May.

NEW ORDERS (DURABLE GOODS ONLY) – MONTH CHANGE; May +15.7% (+$26.3bn) versus Apr -18.3% (-$37.5bn)

The new orders data covers only durable goods. The total manufacturing new orders data is the sum of shipments for non-durable goods and the sum of orders for durable goods. In this analysis, the focus will be on the durable goods data – so numbers will differ to the headline reports.

At the industry level, all durable goods industries recorded growth in orders in May versus Apr – but that growth did not make up for the decline in Apr.

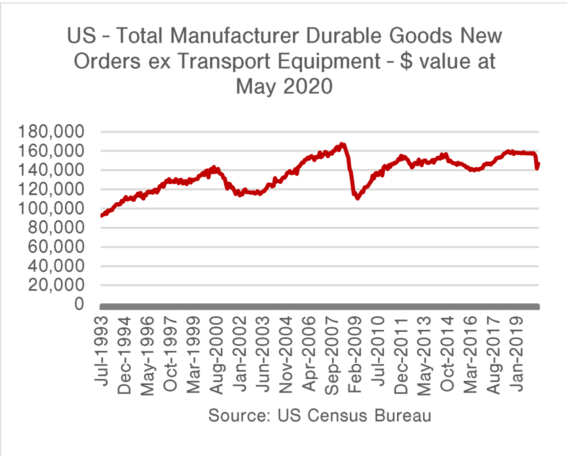
The single largest contributor to the growth in orders in May was transport equipment; May +82% (+$21.1bn) versus Apr -49% (-$24.6bn). Within transport equipment, most of the growth in orders was from one group – non-defense aircraft and parts.

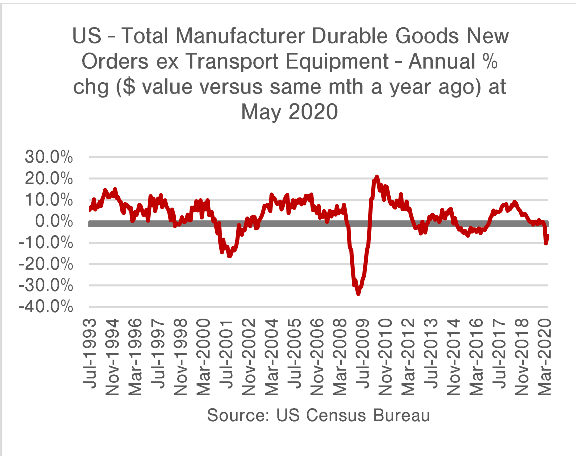
Orders for non-defense aircraft and parts were negative in Mar and Apr (net cancelled orders) and turned positive in May. The change from -$8bn in aircraft orders in Apr (net cancelled orders) to $3bn in orders in May resulted in +$11bn contribution to the headline growth in orders between the two months. Non-defense aircraft orders are still down -40% versus a year ago.

Orders for Motor vehicles and parts orders also increased by +$6bn in May but remain 52% below the same month a year ago (up from 62% in Apr). This is a case of where the month increase sounds impressive (+28%), but its off a low base. There has been little appreciation of the fact that motor vehicle production/orders are one of the hardest hit industries in this pandemic.

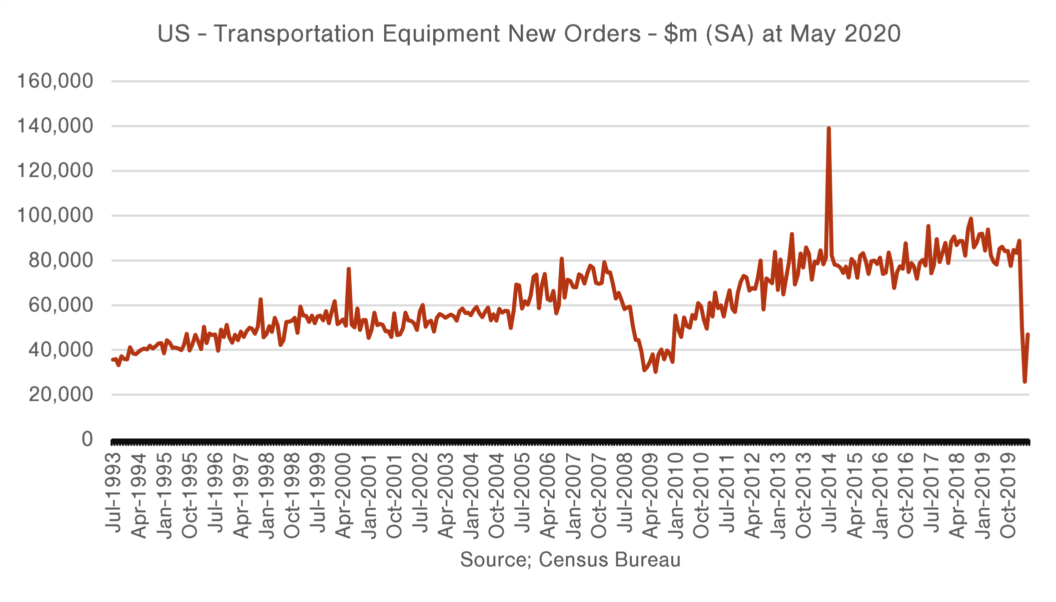
On a year ago basis, total durable goods orders were still 18% below the same month a year ago. The fall in transport orders is a large part of this.

Excluding transportation orders, durable goods orders are 6.7% below the same month a year ago. The value of new orders (chart on left) indicates that levels never really fell by the extremes as indicated by the PMI's. This might be different on a volume basis.




The more extreme declines in new orders have been recorded in transport equipment – at its worst level in Apr, the value of orders fell below the worst month of the GFC (over ten years ago on a non-price adjusted basis);




<u>SHIPMENTS – MONTH CHANGE</u>; May +3.1% (+$12.5bn) versus Apr -14% (-$65.8bn)

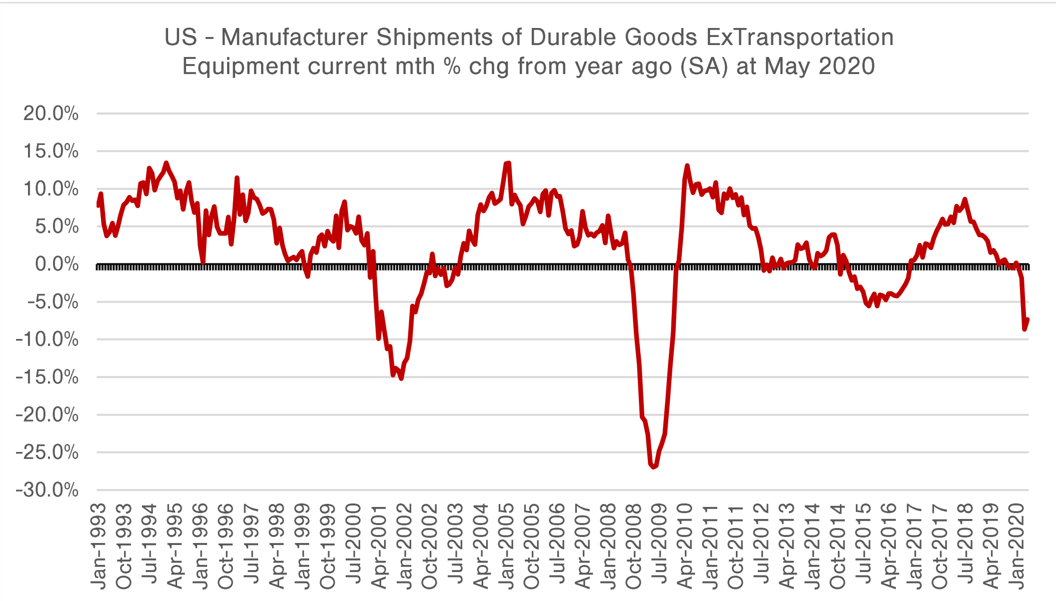
Shipments were higher across both durable and non-durable goods.

<u>Durable goods shipments – month chg</u>; May +4.4% (+$8.2bn) versus Apr -18.8% (-$43.8bn)

There is still a lot of ground to make up after the falls in shipments of the last several months. Most durable goods industries recorded growth in May versus Apr. The largest contributor was growth in transport equipment – but off a low base. Shipments of non-defense aircraft and parts declined again in May (-20% versus Apr).

Durable goods shipments are still down 20% on a year ago. Again, a large part of that decline is transport equipment shipments, which is still down 45% on a year ago.

Excluding transports, durable goods shipments are "only" 7% below a year ago – not close to the extremes highlighted by other reports.

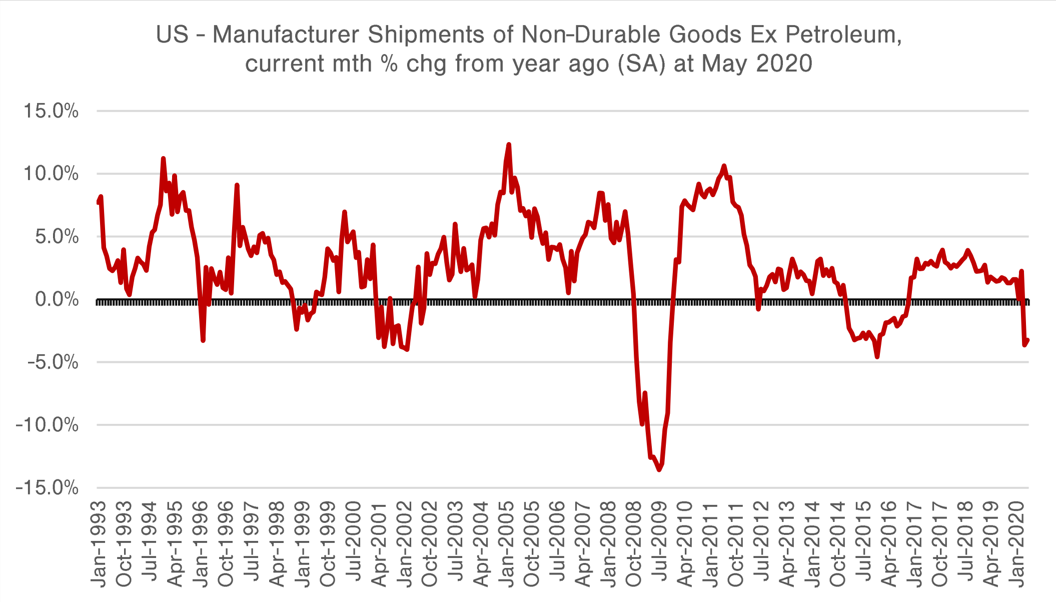


Non-durable goods shipments – month chg; May +2% (+$4.3bn) versus Apr -9.3% (-$22bn)

Most of the improvement this month was the result of the value of petroleum shipments increasing by 12% in May after falling 32% in Apr.

On an annual basis, non-durable goods shipments are down 13.7% on a year ago. Most of this decline is due to the fall in the value of petroleum shipments (-53% versus a year ago). Given lock-down restrictions, there will also be a volume impact on petroleum shipments.

Excluding the performance of petroleum, highlights that other non-durable goods shipments are performing quite well – in relative terms. Non-durable goods ex petroleum shipments are only down 3.2% on a year ago, up slightly from the annual -3.6% decline in Apr. The pace of decline during the pandemic was not even on par with the weakness of 2015/16;




UNFILLED ORDERS (DURABLE GOODS ONLY) – MONTH CHANGE; May +0.1% (+$0.7bn) versus Apr -1.5% (-$17.6bn).

The severe Apr decline in orders was the result of a fall in order backlogs for non-defense aircraft (due to the net cancellation in orders). Ex-transports, unfilled orders were down only - 0.5% in Apr (-$1.7bn). The rebound this month was still smaller than the decline in the month prior and this suggests that order growth is too low to result in growing backlogs.

Fabricated metals and primary metals unfilled orders were most affected in Apr, with declines of -1.6% and -2.8% respectively in Apr. Fabricated metals unfilled orders continued to decline in May (-$0.1bn), but primary metals orders increased slightly.

The other decline in unfilled orders this month was non-defense aircraft -0.1% (-$0.4bn)

INVENTORIES – MONTH CHANGE; May +0.2% (+$1.1bn) versus Apr -0.5% (-$3.2bn)

Most of the increase in inventory this month was due to +1.6% increase in non-defense aircraft inventory (+$1.1bn) and a +0.3% increase in non-durable goods inventory. The +6.5% increase in petroleum and coal products inventory was offset partly by declines across most other non-durable goods industries.

https://www.census.gov/manufacturing/m3/index.html

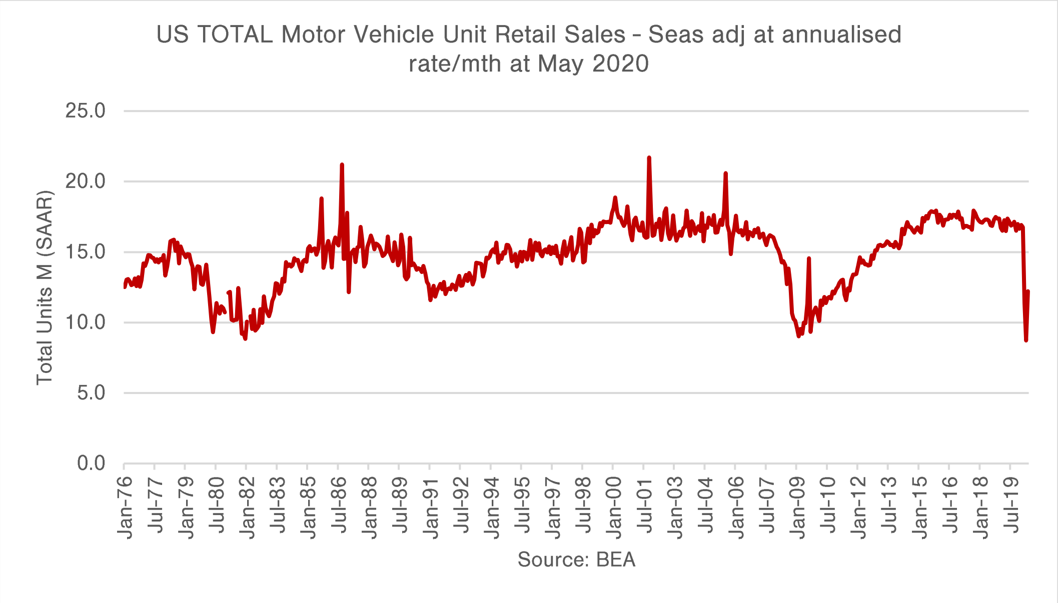
## US Motor Vehicle Sales (May)

The rebound in motor vehicle sales (retail) in May was the largest contributor to overall retail sales growth in the month. While there was a stronger rebound in motor vehicle sales in May, the SAAR is still well below a year ago.

Growth was recorded across Autos and light trucks/SUV's in the month, but the overall rebound was led by sales of light trucks/SUV's.

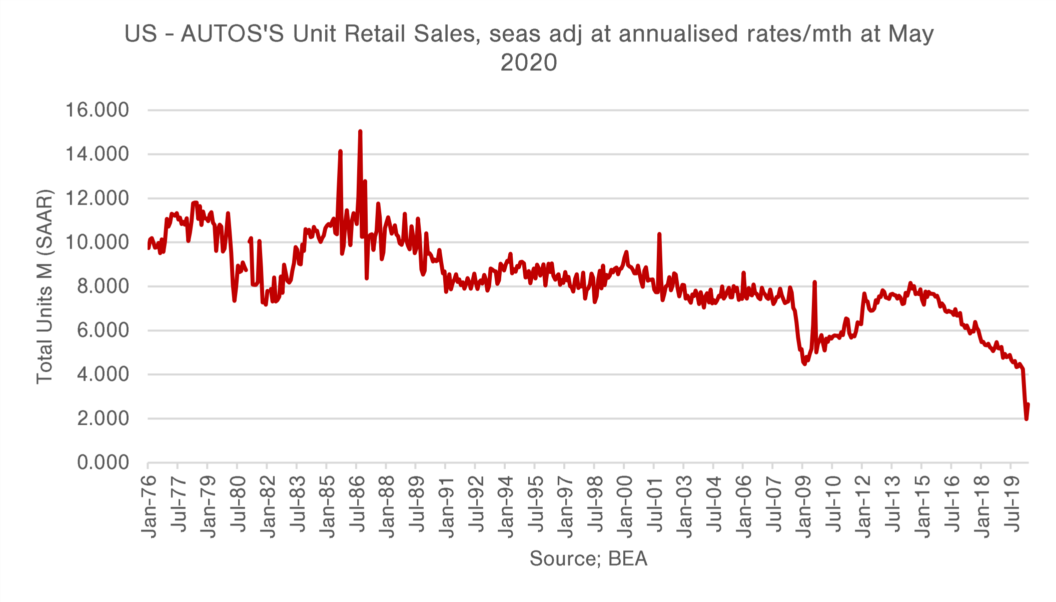
Total Motor Vehicle Sales (SAAR) – month; May 12.2m versus Apr 8.7m units

While this is +37% growth in the month, the May SAAR of sale is still 30% below the same month a year ago.




Autos Retail Sales (SAAR) – month; May 2.65m versus Apr 1.98m units

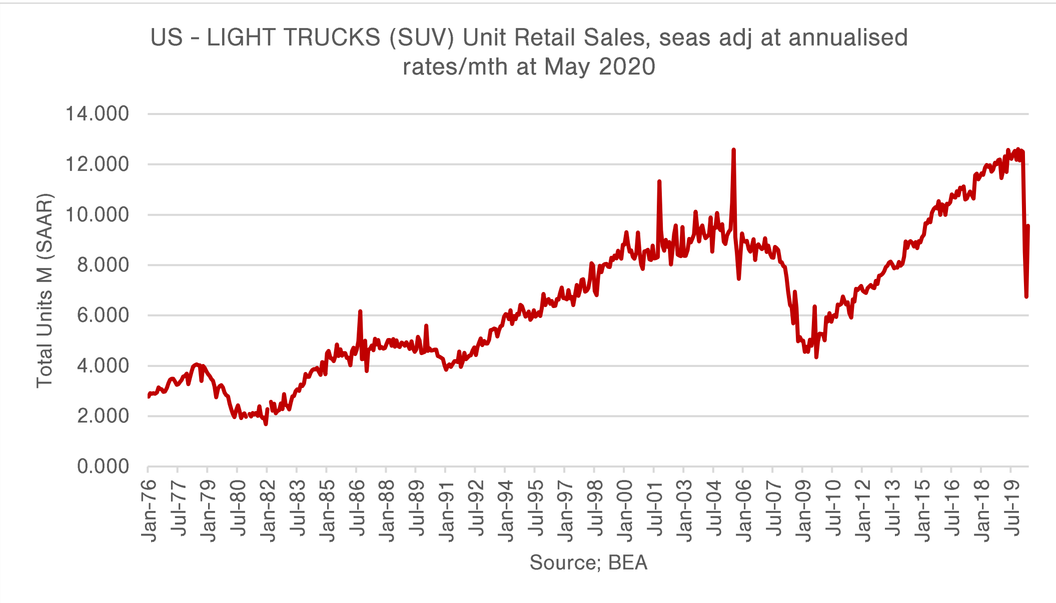
The pandemic restrictions have worsened the already weakening sales trend of Auto's. The rebound in the month was +34% in sales. But the level of sales is extremely low. Sales are still well below a year ago at -44% and significantly below the peak. The pre-Covid trend reflects more of a shift of consumer preference.




Light Trucks/SUV's Retail Sales (SAAR) – month; May 9.56m versus Apr 7.75m units

This is a stronger rebound for the month at +41% growth.

The peak in light truck sales was only back in Nov 2019 and the current pace of sales is 24% below this level.




https://www.bea.gov/data/consumer-spending/main

## Weekly Mortgage Applications wk ending 26 Jun

There was another weekly decrease in mortgage applications this week. Some of the commentary was more down-beat this week.

"Mortgage applications fell last week despite mortgage rates hitting another record low in MBA's survey. Investors are contemplating the risks of the recent resurgence of COVID-19 cases to the labor market and economy, and Treasury rates and mortgage rates are moving lower as a result,"

The market composite index (mortgage loan application volume) wk ending 26 Jun; -1.8% versus a week ago.

Refi's also fell 2% versus a week ago but are still +74% ahead of the same month a year ago. The refi share of mortgage activity fell to 61% in the latest week (from 61.3% in the week prior).

"Refinance applications also decreased but remained 74 percent higher than a year ago. The 30-year fixed rate has been below the 3.5 percent mark since late March. It is possible that many borrowers have already refinanced or are waiting for rates to go even lower."

The purchase index (a more leading indicator of finalised deals) declined by 1% in the latest week. The purchase index is now 15% higher than the same week a year ago.

https://www.mba.org/2020-press-releases/july/mortgage-applications-decrease-in-latest-mba-weekly-survey

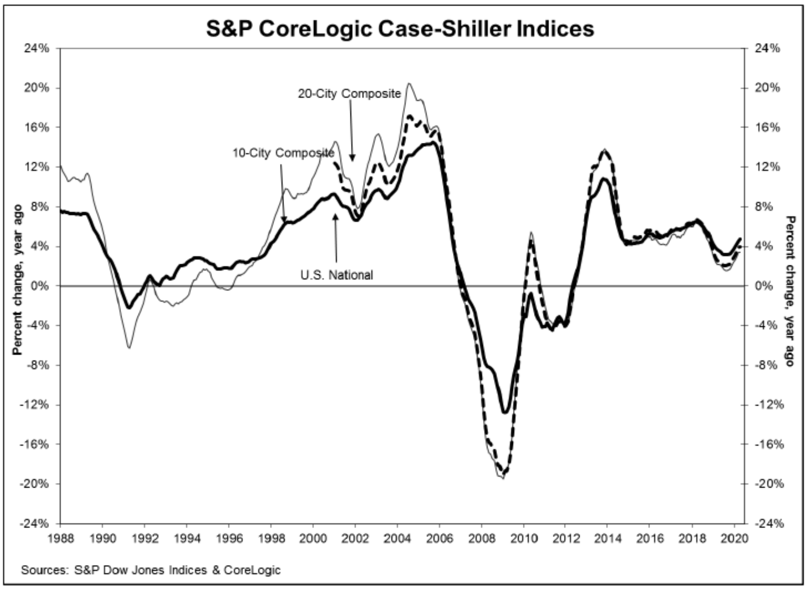
## Case/Shiller National House Price Index (Apr)

The national house price index recorded further acceleration in price growth in Apr.

National House Price Index (NSA) – annual change; Apr +4.7% versus Mar +4.6%

The 10-City Composite Index (NSA) – annual change; Apr +3.4% versus Mar +3.4%

The 20-City Composite Index (NSA) – annual change; Apr +4% versus Mar +3.9%




https://www.spglobal.com/spdji/en/index-announcements/article/annual-home-price-gains-remained-steady-in-april-according-to-sp-corelogic-case-shiller-index/

Return to top

# Europe

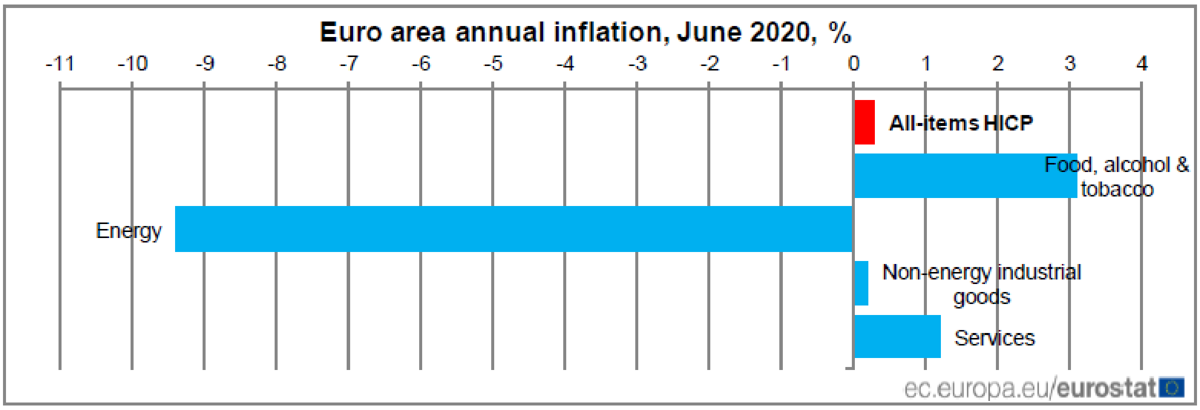
## Euro Area CPI Prelim (Jun)

The prelim reading showed a slight acceleration in the annual headline pace of CPI growth for Jun. The decline in energy prices is offsetting some higher growth in prices across other segments, especially food. The growth in CPI ex energy prices is growing at a much faster pace (albeit constant).

Headline Euro Area CPI – annual change; Jun +0.3% versus May +0.1%

The largest impact on the pace of CPI growth has been the decline in energy prices. In Jun, energy prices declined by -9.4% (compared to -11.9% annual pace in May).

The CPI ex energy prices is growing at faster pace of +1.3% in Jun (just down from +1.4% annual growth in May).




The annual growth in food prices is still high but has slowed slightly in Jun. Annual growth in food, alcohol, and tobacco +3.1% in Jun compared to +3.4% in May. A year ago, food, alcohol, and tobacco prices were growing at +1.6% (annual pace at Jun 2019).

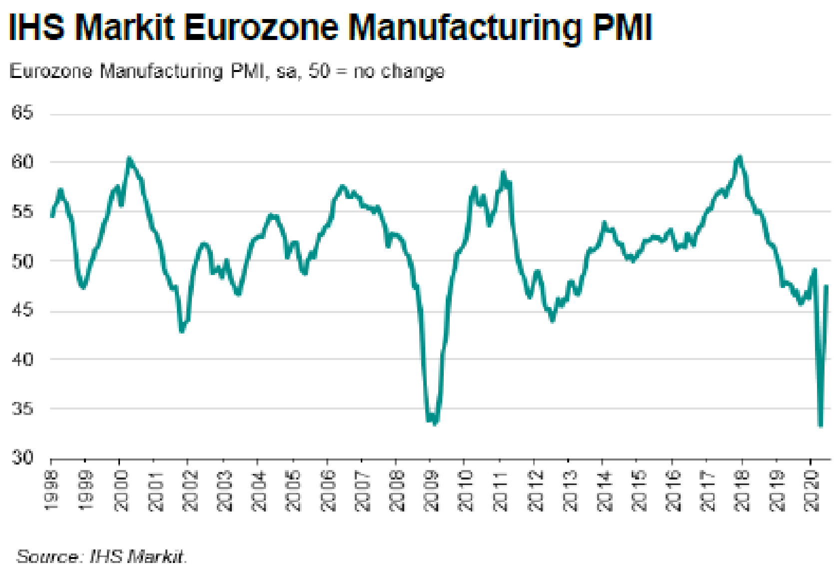
Growth in Services prices (the largest weight in the index), slowed slightly on an annual basis; Jun +1.2% compared to May +1.3%. Growth in services prices in Jun (monthly growth) was +0.7%.

https://ec.europa.eu/eurostat/documents/2995521/10294972/2-30062020-AP-EN.pdf/4d9c6e1d-b92c-431d-384a-2ab18f6eeaa6

## Eurozone Manufacturing PMI Final (Jun)

The headline PMI indicated a net contraction in activity, but at a slower pace than in the month prior. The detail underlying the headline PMI though, suggests that conditions are still challenging – especially across capital goods and intermediate goods producers. While much of the current weakness in manufacturing is linked back to the Covid shutdowns, many of the indicators have been weak for at least the last year.

Headline Manufacturing PMI; Jun 47.4 versus May 39.4




With the easing of severe lockdowns across key parts of the Eurozone, business activity has started to slowly return. But this should also been taken in context – while the shutdowns resulted in (virtually) a complete halt of activity, the manufacturing PMI has been in contraction, on net, for the last seventeen months across the broad Eurozone.

Both intermediate and investment goods continued to contract, but there was a return to growth amongst consumers goods producers.

Two countries recorded net growth/improving conditions in Jun – Ireland and France both recorded a headline PMI reading above 50. Germany continues to lag with a headline reading of 45.2 in Jun.

This month new orders and production continued to decline across the Eurozone. The declines were still the weakest of the last four months. But it means that the firms recording further declines in production and orders (in Jun) still outnumber those firms recording improvements.

New export orders also declined – this is the twenty first month of declines and the pace of decline remained notable.

Order backlogs also declined sharply in Jun – with the pace of decline 'severe'. This highlights the degree of spare capacity that still exists.

As a result, employment and working hours continued to decline.

Employment fell in June for a fourteenth successive month, and again at a noticeable pace. All nations recorded a drop in manufacturing employment, led by Germany, Italy and the Netherlands.

Purchasing activity continued to fall – contributing to overall weaker orders through the supply chain. Firms preferred to reduce existing stocks and reduce working capital.

Average lead-times for orders continued to increase.

Despite the somewhat downbeat data, firms became more optimistic about production in the next twelve months. Manufacturers hoped that continued easing of lockdowns would result in further growth in demand.

https://www.markiteconomics.com/Public/Home/PressRelease/8dba0049d5984917a8d216d8672b6872

## Eurozone Services PMI Final (Jun)

There was an improvement in the headline business services activity index. The index still showed that activity on net declined in Jun, but at a slower pace than the severe contractions in Apr and May. The number of firms reporting worsening conditions in Jun still outnumber the proportion of firms reporting improved/growing conditions in Jun.

> Companies continued to report weak underlying demand in June. Many remained risk averse, being reticent to commit to spending and hiring due to **persistent uncertainty as to the economic outlook**, and in particular the likely sustained weakness of demand for many goods and services due to **the need to retain many social distancing measures**.

Eurozone Services Business Activity Index; Jun 48.3 versus May 30.5

Despite the easing of some severe lock-down restrictions, output and new business continued to decline on net across the region. Order backlogs continued to decline. Firms still noted over-capacity issues and employment declined for the fourth month in a row. The pace of decline remained historically steep.

Despite firms noting slow traction across services firms, the outlook became optimistic.

> Finally, looking ahead to the coming year, service sector firms were at their most confident since February, with sentiment also returning to positive territory during the month.

https://www.markiteconomics.com/Public/Home/PressRelease/ad22c1110c7e481daad57928fd609231

Return to top

# Japan

## Retail Sales (May)

There was a small rebound in retail sales in May. Growth was stronger in the month across several categories. Overall retail sales are still 12% below the same month a year ago.

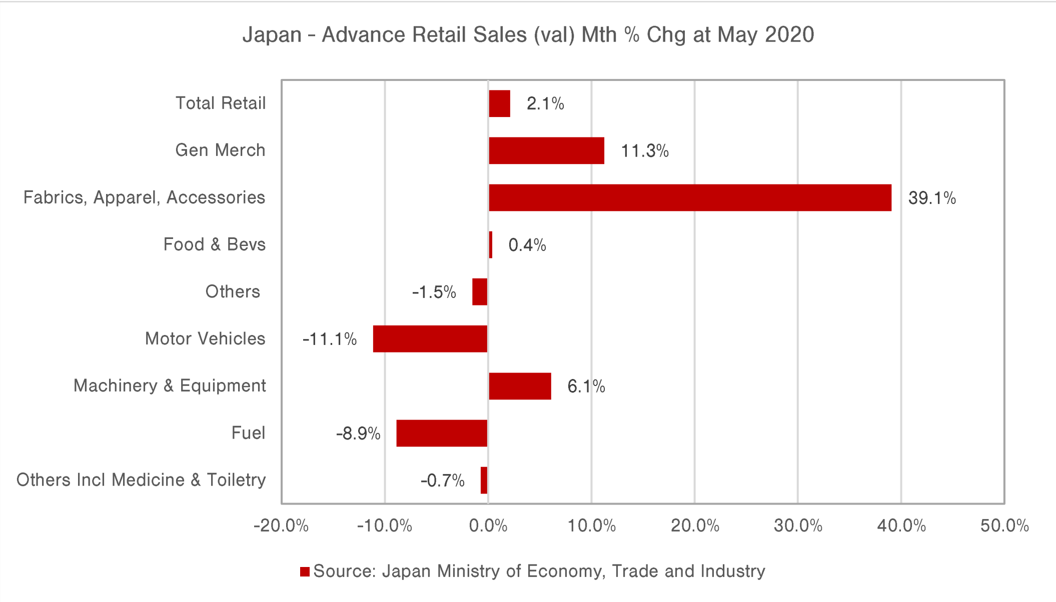
<u>Retail Sales (val) – month change</u>; May +2.1% versus Apr -9.9%

Sales growth was stronger most notably across fabrics, apparel, and accessories – but the level of sales was still 35% below the same month a year ago.

Sales were also stronger in the month across general merchandise and machinery and equipment. But sales in these categories is also still below a year ago (-36% and -9% respectively).

Retail sales of food and beverages was up slightly +0.4% in the month. This is the only category where the value of retail sales is ahead of the same month a year ago by +1.3%

Motor vehicle sales were down another 11% in sales this month and 34% below the same month a year ago.




On an annual basis, retail sales in May continued to decline at a similar pace as in Apr.

<u>Retail Sales (val) – annual change</u>; May -12.3% versus Apr -13.9%


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

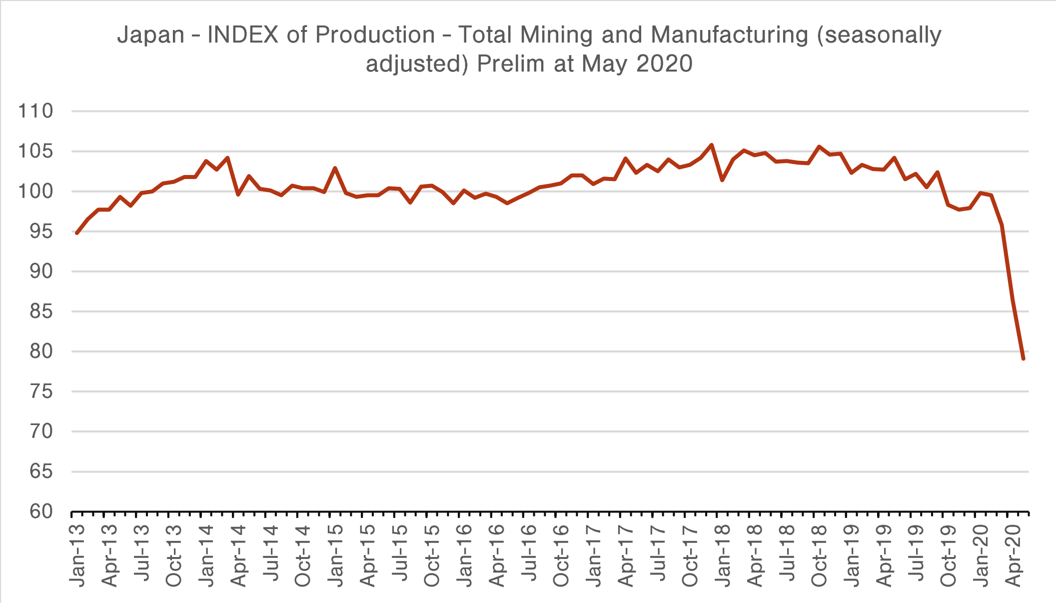
## Industrial Production Prelim (May)

Industrial production in May was much weaker – in line with the continued acceleration in the decline of manufacturing output from the PMI's of that month. The May trade result also hinted at the weaker production result for May. The prelim Jun PMI for manufacturing shows a further small acceleration in the pace of contraction. The METI website forecast is for growth in production and shipments in Jun and Jul.

One the largest contributors to the decline in the production (as well as exports) has been the decline in motor vehicles/passenger car production.

Production – month change; May -8.4% versus Apr -9.8%

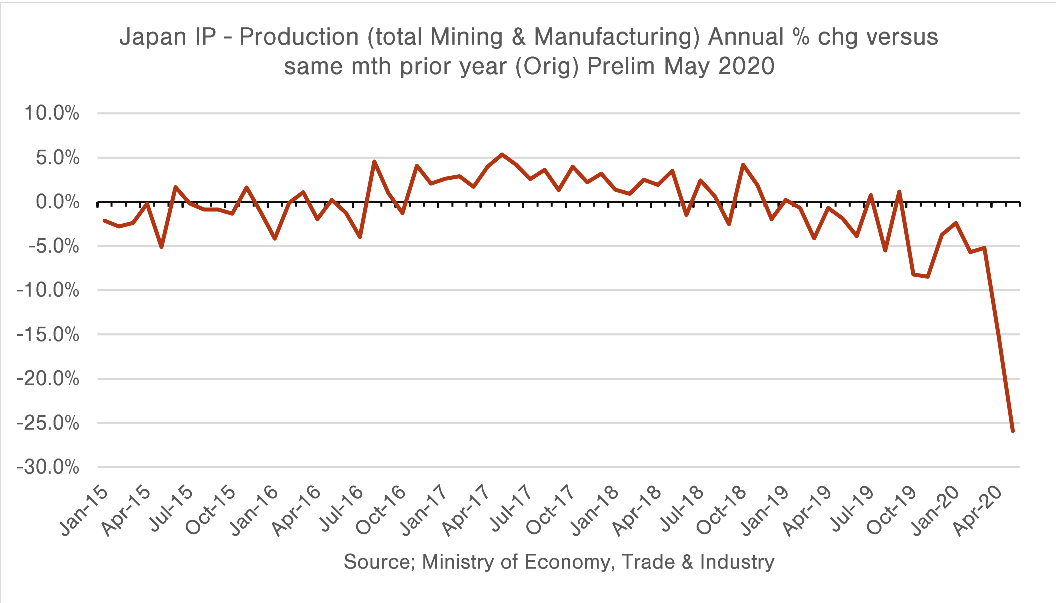
Production declined for the fourth month in a row (below is the index)




All major industrial groups contributed to the decline in production this month.

The largest weight in the index is transport equipment. Production of transport equipment declined by 19.4% in May (v -34.8% in Apr). There was a further 23% decline in the production of motor vehicles in May, after declining by 36.6% in Apr.

On an annual basis, industrial production in Japan fell to -26% below the same month a year ago;

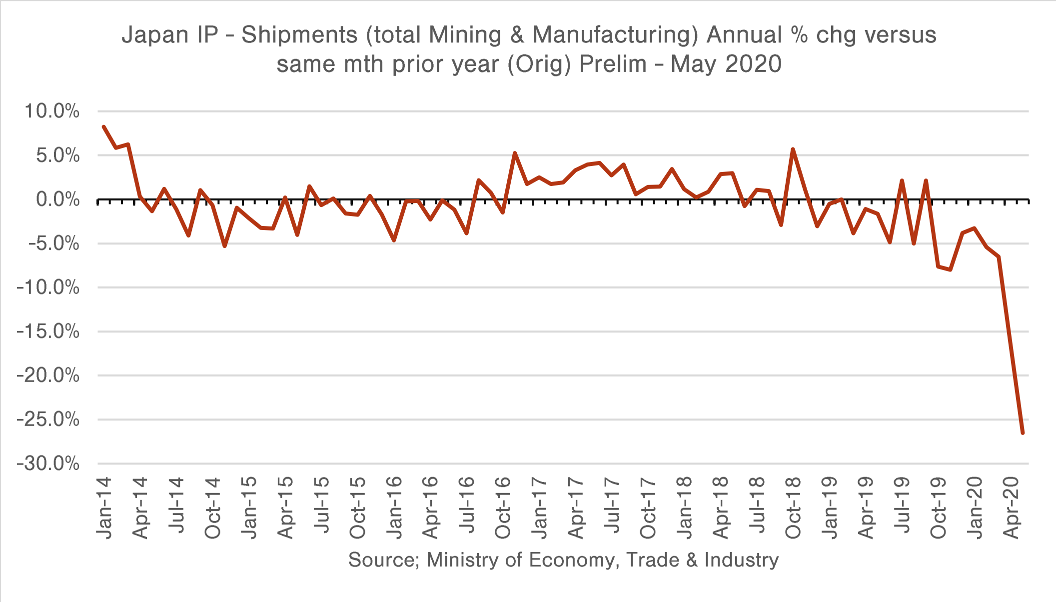



<u>Shipments – month change</u>; May -8.4% versus Apr -9.5%

Shipments all declined across all major industrial groups in May.

The largest weight of the shipments index is transport equipment. Transport equipment shipments were down another 17% in May versus the Apr decline of 32.6%. Within that, motor vehicle shipments were also down another 13% in May versus the 41% decline in Apr.

Shipments in May fell to -26.5% below the same month a year ago. The index of shipments has been declining on a year-ago basis since Oct 2019;

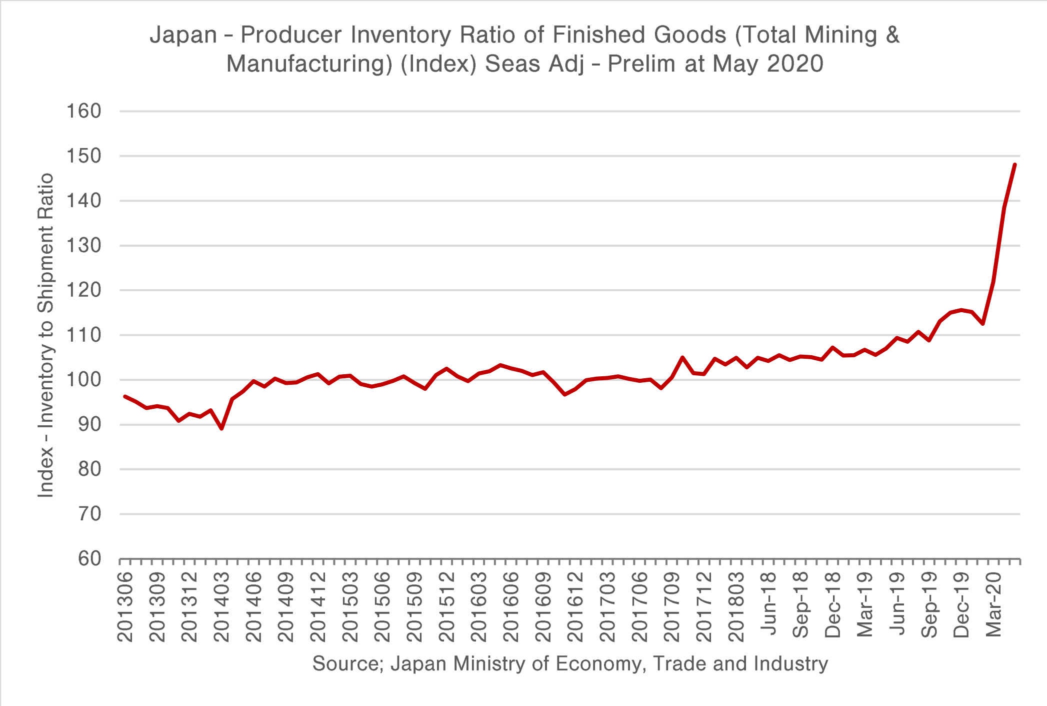



<u>Inventory – month change</u>; May -2.5% versus Apr -0.3%

The change in inventory was moderate across most industries, but the largest change was in transport equipment. The producer's inventory of finished goods for transport equipment declined by -30.8% in May after a +9.5% increase in Apr. Manufacturers are likely reducing these existing stocks.

The largest weight in the producer's inventory of finished goods is iron, steel, and non-ferrous metals. The value of inventory declined further in May by -2.7% versus -5.6% in Apr.

The producers inventory ratio of finished goods increased further and is still extremely elevated. This indicates that inventory levels remain too high given the weak level of shipments.



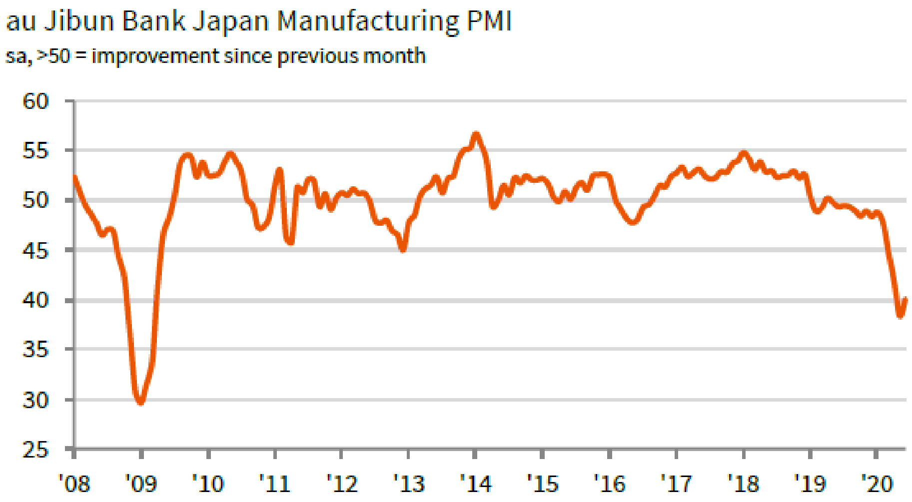

Given the large fall in the value of producer's inventory of transport equipment in May, the inventory ratio fell by 14% in May – compared to the +70% increase in Apr.

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

## Japan Manufacturing PMI Final (Jun)

There was a slight improvement in the final headline manufacturing PMI for Jun (compared to the prelim). Manufacturing activity still declined in Jun, but to a lesser degree than in May. This means that the number of firms reporting weaker conditions still outnumber those reporting improved conditions, but there was at least some improvement for a number of firms.

Headline Manufacturing PMI; Jun 40.1 versus May 38.4




Sources: au Jibun Bank, IHS Markit.

Production continued to decline in Jun, albeit at a slightly slower pace. Factories continue to operate at lower levels given weaker demand.

> Almost half of the survey panel (48%) recorded lower production, compared to 13% that expanded output in June.

New orders also continued to decline, but at a slightly slower pace. But the pace of decline remained 'steep'.

> According to anecdotal reasons, low consumption, continued business disruption due to the COVID-19 shock and weak market conditions contributed to the decrease in workloads.

Export orders continued to decline, slightly slower than in the month prior, but still at a 'steep' pace of decline. Export orders across consumer goods continued to improve, but orders across intermediate and capital goods producers continued to decline. Some firms noted increased order demand from China.

Order backlogs continued to decline at a similar pace as May – still at a multi-year low. This indicates that new orders growth likely remains too low.

Purchasing activity also declined further in Jun. See industrial production for May (above) – inventory to shipments is extremely elevated, so without further growth in new orders, firms are working through inventory levels rather than expanding production for the moment.

Employment levels declined at an accelerated pace.

Input and operating costs increased in Jun. Firms noted that stock shortages led to higher input prices. Firms reduced selling prices in Jun, likely adding further to margin pressures.

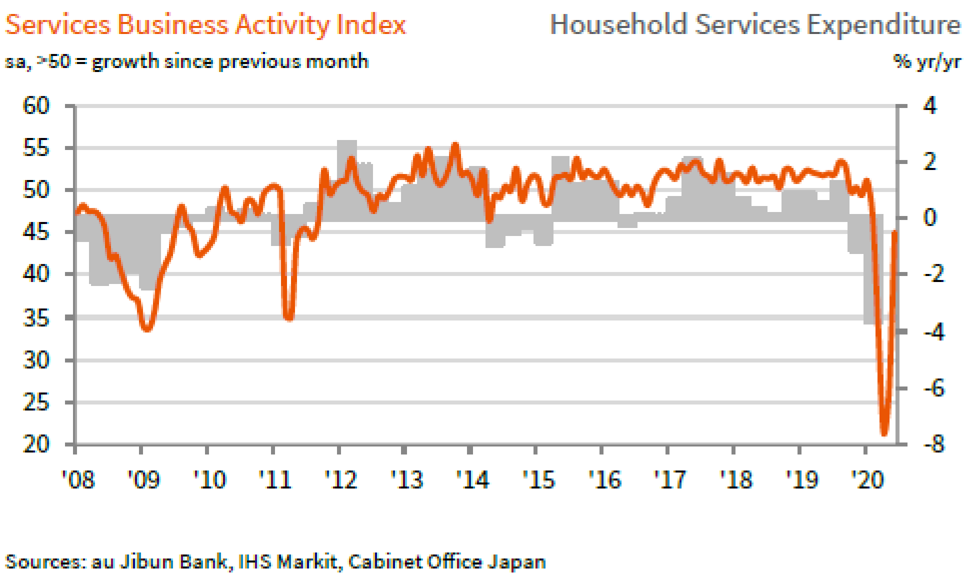
Despite the current situation, confidence shifted into positive territory for the first time since Feb. This was led by the expectation of a gradual recovery in the economy over the next 12-months.

https://www.markiteconomics.com/Public/Home/PressRelease/d30e160255d94ef79a900f96fb7d2536

## Japan Services PMI Final (Jun)

The services business activity index contracted again in Jun. Like the manufacturing sector, the pace of decline slowed. The number of service firms reporting weaker conditions still outnumber those reporting improving conditions, but to a lesser degree than in May. While there never strict lock-down measures implemented (more like guidelines), the lifting of the state of emergency resulted in service firms returning to some form of operation. Some sectors noted that a return to growth was limited by distancing rules.

Services Business Activity Index; Jun 45 versus May 26.5




Both output and orders continued to decline in Jun, albeit at a slower pace than in May. While there was the lifting of the state of emergency, most firms still recorded wither no change or a decline in output.

Outstanding business continued to decline, indicating the level of spare capacity that still exists. Most firms recorded no change in employment levels (88% of firms) but the index still showed a slight decline in employment.

> Looking ahead, businesses expect activity levels to remain constrained over the coming year by heightened economic uncertainty, a further shrinking in client numbers and below capacity operating rates. That said, the level of confidence improved to a four-month high as some firms were optimistic that the worst of the downturn had passed.

https://www.markiteconomics.com/Public/Home/PressRelease/c7f1d521ef2647e4bc36cc130227479a

Return to top

# Australia

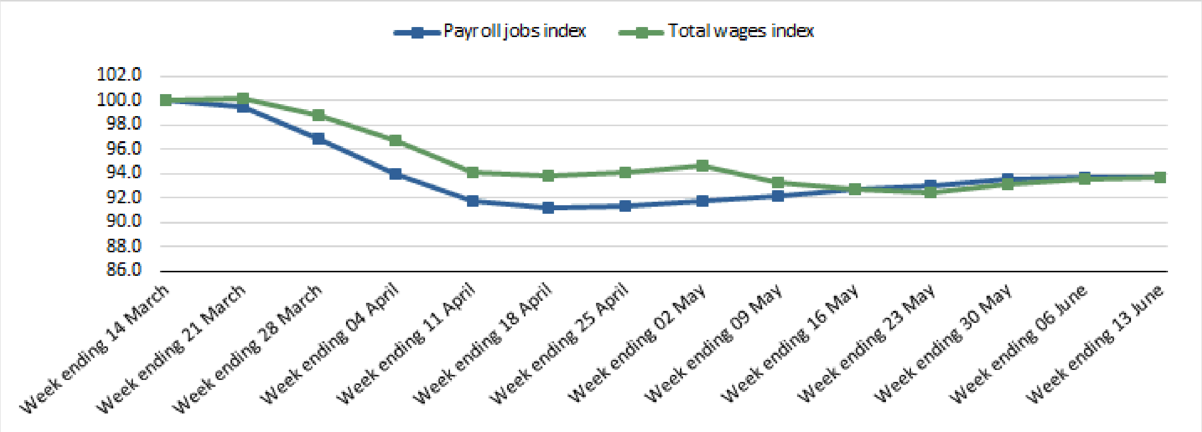
## ABS Weekly Payrolls wk ending 13 Jun

The weekly payroll numbers reflect mixed conditions. Despite the lifting of restrictions across most states, there was 0% change in payrolls between the wk ending 6 Jun and wk ending 13 Jun.

Latest week ending 13 Jun 2020; four states recorded lower payrolls than in the week prior – NSW, Vic, NT, and ACT. This was offset by growth in Qld, SA, and WA. There was no change in TAS.

Since the week prior to the start of shutdowns, wk ending 14 Mar, payroll jobs remain -6.4% below that level (as of wk ending 13 Jun. At the lowest point, payroll jobs were -8.8% below the wk ending 14 Mar.

*Chart; Changes in payroll jobs and total wages indexed to the week ending 14 March 2020*

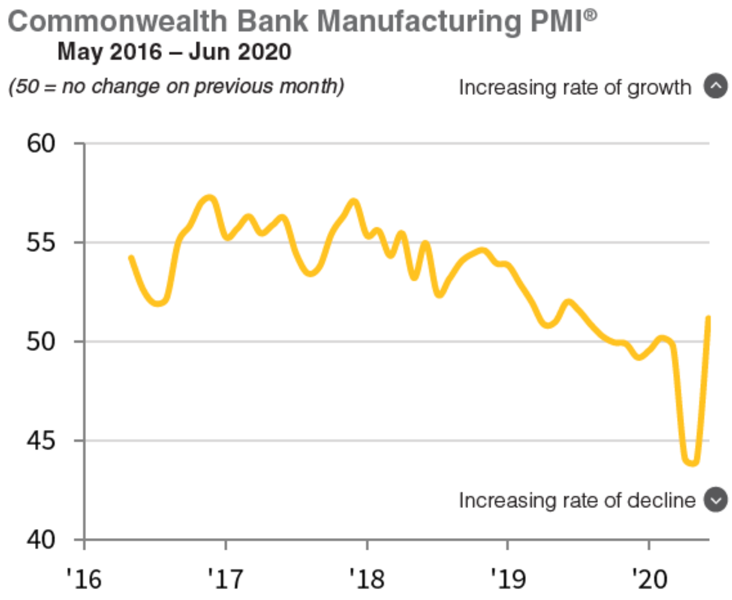



[https://www.abs.gov.au/ausstats/abs%40.nsf/mediareleasesbyCatalogue/400084FDCC1353C9CA2585500026370F?OpenDocument](https://www.abs.gov.au/ausstats/abs%40.nsf/mediareleasesbyCatalogue/400084FDCC1353C9CA2585500026370F?OpenDocument)

## CBA Manufacturing PMI Final (Jun)

The headline PMI showed that manufacturing activity expanded slightly in Jun after the decline of the last few months. Pandemic-related restrictions were eased throughout the states, enabling non-essential forms to reopen. Measures of demand such as output and new orders continued to decline in Jun, but at a slower pace. The remaining spare production capacity led to further reductions in employment. Firms started to report input supply shortages and 'limited freight capacity' – leading to a further lengthening in delivery delays.

Headline Manufacturing PMI; Jun 51.2 versus May 44




The pace of decline across output and new orders eased in Jun and was marginal compared to the more severe declines in Apr and May.

However, ongoing weakness in sales contributed to a rise in spare capacity which, in turn, dampened hiring. Employment declined for a seventh straight month amid reports of redundancies.

Firms continued to cut back on purchasing activity and opted to reduce inventories to meet production requirements.

Margins were again under pressure with input costs rising at a faster pace. Firms were only able to pass on part of the price increase.

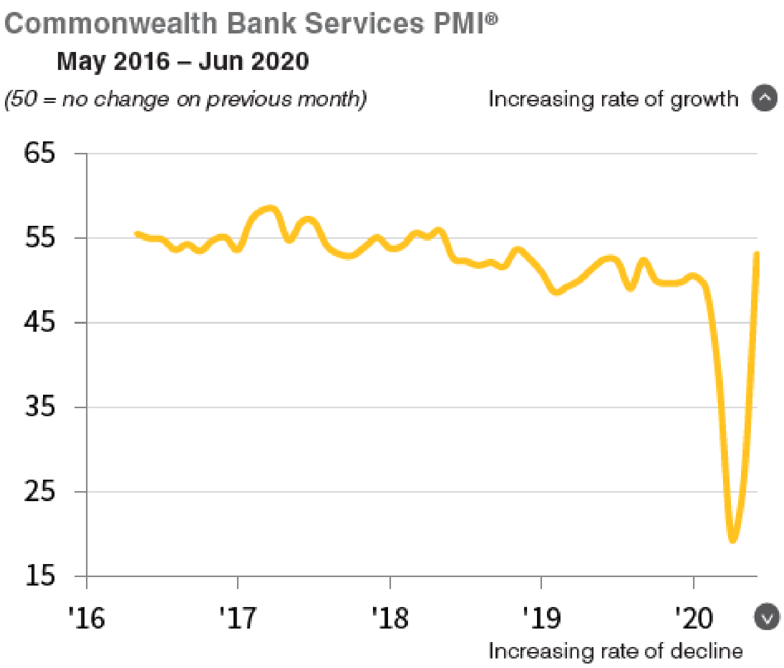
Finally, business sentiment improved further in June to a 16-month high. Confidence was underpinned by expectations of further easing of COVID-19 measures in the year ahead.

https://www.markiteconomics.com/Public/Home/PressRelease/2d424467f74c45b6a1a25c6de1a3abf4

## CBA Services PMI Final (Jun)

With the easing of many shut-down restrictions, services activity increased in Jun compared to May. This means that more firms recorded growth in output in Jun compared to May levels. But this does not provide insight as to how Jun activity levels compare to pre-shut-down. While the more severe restrictions have started to be lifted, capacity constraints are still in place across some service industries.

Headline Business Activity Index; Jun 53.1 Versus May 26.9




This is the first increase in output since Jan 2020 (so sales were slowing even before Covid restrictions).

New orders increased for the first time since Jan also, although growth was more marginal. External/export business continued to decline, but at a slower pace.

Backlogs of work increased. But firms, on net, continued to reduce employment. The pace of employment decline slowed from steeper levels of Apr and May.

Business expectations improved in Jun.

Optimism was built on expectations of a further easing of restrictions, **including for international travel**, in the months ahead.

[Note; Given the acceleration of infections in one of the largest Australian cities (Melbourne), it will be important to watch for changes to in the pace of easing of restrictions. The easing of any international travel quarantine restrictions is not likely to happen for a long time.]

https://www.markiteconomics.com/Public/Home/PressRelease/de695ae4dfc64fa98dc0481eab455d28

## Retail Sales (May)

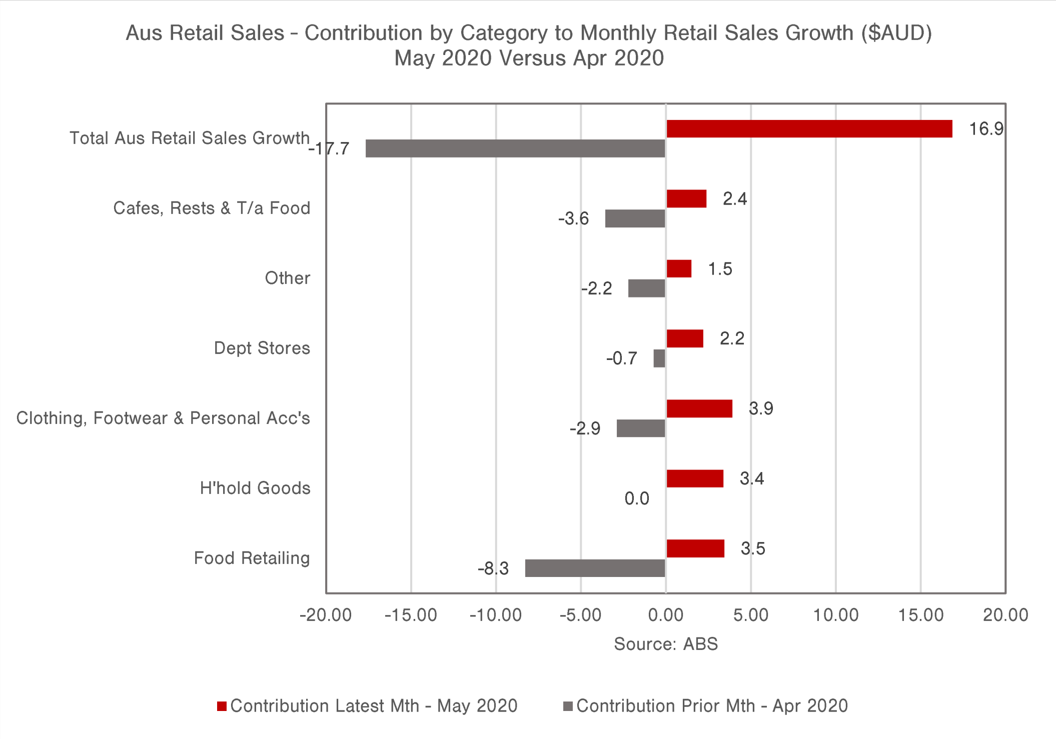
Retail sales rebounded in May versus the much lower levels of sales recorded in Apr (the peak of the shut-down in Australia). Some categories recorded stronger growth, but all categories recorded month on month growth in May. Grocery and household retailing are the two strongest performing categories on an annual basis. Sales of clothing and cafes/restaurants are still down 19 and 34% respectively, versus a year ago.

The stronger result across some categories is expected. Households are currently either; receiving withdrawals from Superannuation accounts (up to $10k before 30 June and the option for another $10k withdrawal after 1 Jul), more generous JobKeeper/Seeker payments, and many have mortgage payments on hold (and rent payments too).

Excluding grocery, retail sales in value terms, are flat to a year ago.

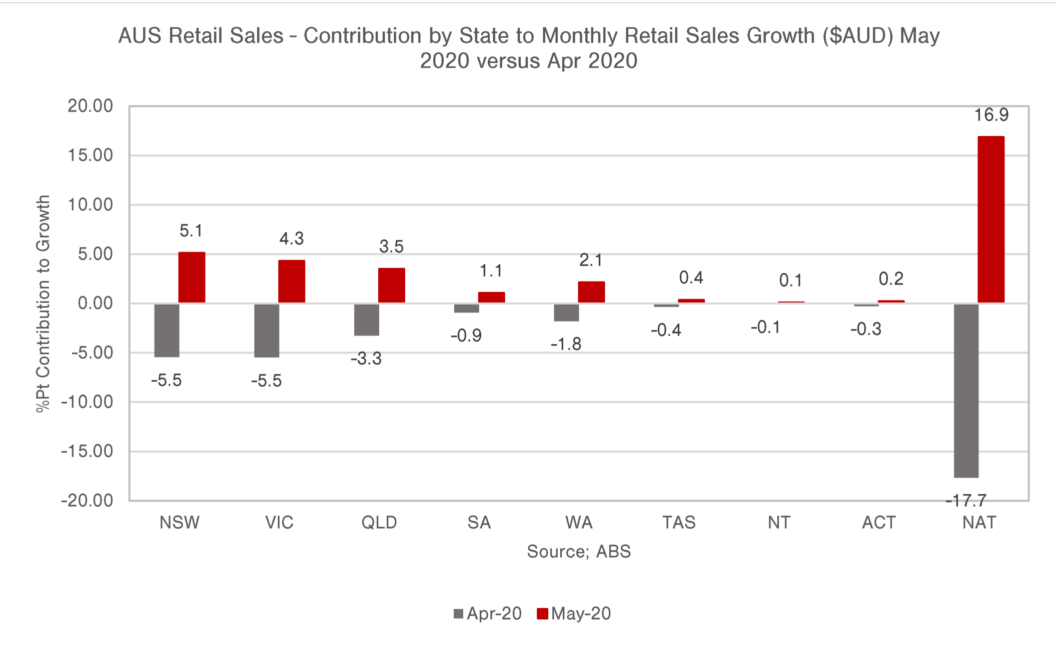
Retail Sales ($ val) – month change; May +16.9% versus Apr -17.7%

All categories returned to growth this month as severe shut-down restrictions started to be eased.



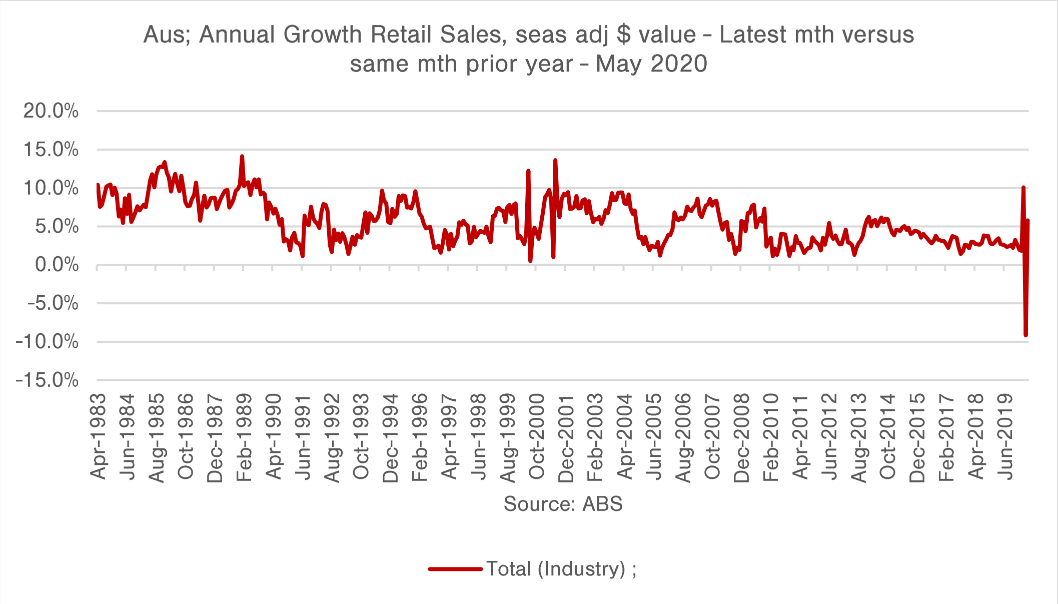

Retail Sales by State

Retail sales by state was also positive with sales returning to growth across all states in May.



On an annual basis though, growth is lagging across several key states – especially Vic. Annual growth in retail sales in Vic is only +0.9% compared to the National pace of +5.8%. Similarly, annual retail sales growth in NSW is also more moderate at +3.5%.

Retail Sales ($val) – annual change; May +5.8% versus Apr -9.2%




Excluding the impact of stronger grocery sales, the annual change in retail ex grocery is +0.8% in May.

https://www.abs.gov.au/ausstats/abs@.nsf/mf/8501.0

Return to top

## China

### NBS Manufacturing PMI (Jun)

There was a continued slight acceleration in growth across manufacturing in Jun. At an overall level, improvement in conditions are moderate at best. That said, production growth and new orders increased at a faster pace this month. There was also a notable improvement (weaker decline) in new export orders.

Order backlogs continue to decline at similar pace in Jun as in May and finished goods inventories continue to decline. Employment remained in contraction.

Headline Manufacturing PMI; Jun 50.9 versus May 50.6


### Non-Manufacturing PMI (Jun)

There was a further stronger acceleration in the headline non-manufacturing PMI in Jun. While most industries recorded growth in Jun compared to May, several were still below 50 –

> …the business activity index of leasing and business service industry, resident service industry, culture, sports and entertainment industry stayed below the threshold.

Four components were in positive territory this month. New orders growth was constant in Jun (52.7), the input price index was slightly higher (52.9), and the supplier delivery index was slightly lower (52.1). The business activities expectation index slowed slightly and is elevated at 60.3.

Note that all other PMI components are in contraction territory (five). Yet the headline non-manufacturing index accelerated to the equal highest growth in the last year.

Headline Non-Manufacturing PMI; Jun 54.4 versus May 53.6


http://www.stats.gov.cn/english/PressRelease/202007/t20200701_1771424.html

Return to top

# Trade

## US-China Trade Talks

As a part of the push to localise production, the US is considering a phase 4 of the stimulus package for manufacturing. This could have far wider effects than just an impact on Chinese manufacturing. Emphasis added.

> "Put simply, we need to create more manufacturing jobs," Navarro said. "Manufacturing jobs not only provide good wages but also create more jobs both up- and downstream through multiplier effects."
>
> Navarro said House Speaker Nancy Pelosi would like a $3 trillion dollar package, Senate Majority Leader Mitch McConnell would like a $1 trillion dollar package, but President Donald Trump would like a package of "at least $2 trillion dollars that is strategically focused around the President's two simple rules -- Buy American, Hire American -- **along with incentives for American companies to bring offshored jobs back home**."
>
> https://edition.cnn.com/2020/06/13/politics/navarro-white-house-coronavirus-stimulus/index.html

“Stage two” of trade negotiations were planned to follow on from last years’ agreement – but there has been no further progress. Phase two of the negotiation was recently acknowledged by USTR Lighthizer in testimony to the House Ways and Means Committee (emphasis added) (Jun 2020).

> The President directly confronted China’s abusive trade practices through substantial tariffs, resulting in the groundbreaking Phase One trade agreement signed on January 15 of this year. The agreement secured enforceable commitments from China to cease its abusive trade practices – including intellectual property theft, forced technology transfer, discriminatory regulations, and currency manipulation. It also committed China to significantly increase its purchases of U.S. goods and services by at least $200 billion over 2017 purchase levels.
>
> By establishing a strong dispute resolution system and maintaining tariffs on approximately $370 billion in goods from China, **the Administration has maintained the authority and leverage to enforce China’s compliance with the agreement while pursuing additional reforms under a future Phase Two agreement**.
>
> With China, “Phase Two” will focus on issues of overcapacity, subsidization, disciplines on China’s state-owned enterprises, and cyber theft.
>
> https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/HWMCTestimonyon2020TradeAgenda-Final.pdf

Reconfirming what a 'win' in the negotiations with China looks like – a statement of the key negotiating goals as outlined by the USTR from the initial USTR objectives (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

In recent testimony, USTR Lighthizer referred to the second phase trade deal negotiations with Japan.

> Last year, the United States also entered into two agreements with Japan that established preferred or zero-rate tariffs on more than 90 percent of U.S. food and agricultural products imported into Japan and enhanced the existing $40 billion in digital trade between our countries.
>
> In the case of Japan, the two countries intend to enter into further negotiations on customs duties, barriers to trade in services and investment, and other trade restrictions.
> https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/HWMCTestimonyon2020TradeAgenda-Final.pdf

Phase two of the deal negotiations were originally planned to commence around Apr/May this year. There is no indication of the timing for the start of phase two negotiations at this stage.

> After the deal enters into force, the countries have agreed to conclude consultations for further trade talks within four months. Then discussions between their lead negotiators, Foreign Minister Toshimitsu Motegi and U.S. Trade Representative Robert Lighthizer, will start again in earnest.
>
> The United States is seeking a full-fledged free trade agreement that covers areas including services and investment.
> https://www.japantimes.co.jp/news/2019/12/04/business/economy-business/upper-house-approves-united-states-japan-trade-deal/#.Xe3HTegzaUk

The issue for phase two talks is auto tariffs.

> Japan has said it has received U.S. assurance that it would scrap tariffs on Japanese cars and car parts, and that the only remaining issue was the timing. But Washington has not confirmed that.

https://www.reuters.com/article/us-usa-trade-japan/japan-lower-house-passes-u-s-trade-deal-auto-tariffs-still-in-question-idUSKBN1XT0IK

Details from the Congressional Research Service; https://crsreports.congress.gov/product/pdf/IF/IF11120#targetText=Japan's%20Diet%2C%20however%2C%20will%20have,effect%20on%20January%201%2C%202020.

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

USTR Lighthizer noted in recent testimony of the intention to continue to pursue negotiations with the EU. This still seems some way into the future – after US elections.

> The United States also seeks to rebalance our trade relationship with the European Union. For many years, U.S. businesses have been at a disadvantage in doing business in the EU. Both tariff and non-tariff barriers in the EU have led to increasing and unsustainable trade deficits with the EU – reaching $179 billion in 2019. With recent changes in EU leadership, the United States is hopeful for more progress **in the coming year**.
> https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/HWMCTestimonyon2020TradeAgenda-Final.pdf

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

Airline Subsidies

The US has officially notified the WTO that it has complied with the dispute raised by the EU on US subsidies to Boeing. The US has now enacted the Senate Bill that eliminates the preferential tax treatment for aerospace manufacturing.

> The removal of the subsidy fully implements the WTO's recommendation to the United States, bringing an end to this long-running dispute.
> https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/may/us-notifies-full-compliance-wto-aircraft-dispute

From 18 Oct, the US had implemented tariffs on some EU imports as a part of the WTO ruling on the Airbus case. This week, the USTR announced a further increase in the tariff rate in aircraft imported from the EU into the US from 10% to 15% - effected from 18 Mar 2020. https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/february/ustr-revises-75-billion-award-implementation-against-eu-airbus-case

Trade Deal Negotiations

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

The threat of auto tariffs also remains an issue, despite the US missing the S.232 deadline of 14 Nov. https://www.cnbc.com/2019/11/08/trump-wont-impose-tariffs-on-european-cars-eu-juncker-says.html

Digital Services

> France on Monday agreed to suspend a 3% digital tax on U.S. tech companies in exchange for Washington holding off on a threat to impose tariffs of up to 100% on a $2.4 billion list of French imports, a French diplomatic source said. **https://www.reuters.com/article/us-usa-trade-deals/after-china-trade-deal-europe-and-uk-next-on-trumps-to-do-list-idUSKBN1ZL2TJ**

The USTR S.301 investigation into the digital services tax approved by the French government has been completed and released its report on 2 Dec 2019;

> "USTR's decision today sends a clear signal that the United States will take action against digital tax regimes that discriminate or otherwise impose undue burdens on U.S. companies," Ambassador Robert Lighthizer said. **"Indeed, USTR is exploring whether to open Section 301 investigations into the digital services taxes of Austria, Italy, and Turkey**. The USTR is focused on countering the growing protectionism of EU member states, which unfairly targets U.S. companies, whether through digital services taxes or other efforts that target leading U.S. digital services companies." https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/december/conclusion-ustr%E2%80%99s-investigation

The proposed action includes up to 100% duties on certain French products imported into the US. The USTR is now inviting comments on the proposed action at a public hearing in Washington on 6-8 Jan 2020. https://www.federalregister.gov/documents/2019/12/06/2019-26325/notice-of-determination-and-request-for-comments-concerning-action-pursuant-to-section-301-frances

and

https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/january/public-hearing-proposed-action-frances-digital-services-tax-0

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

Back in May 2019, 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. A Reuters article during the week reported that President Trump may no longer be able to impose tariffs under this S.232 investigation because of the missed announcement deadline. Source: https://www.reuters.com/article/us-usa-trade-autos/trump-can-no-longer-impose-section-232-auto-tariffs-after-missing-deadline-experts-idUSKBN1XT0TK

> The 1962 act is clear about the time limits that a president has for invoking tariffs to protect U.S. national security.

The article outlines other recent cases where the increase in tariffs have been challenged due to missed deadlines (Turkey and the increase in steel tariffs in 2018).

The article outlines the “escape hatch” for President Trump;

> A clause in the 1962 law may offer an escape hatch for Trump. If an agreement is not reached within 180 days or proves ineffective, “the President shall take such other actions as the President deems necessary to adjust the imports of such article so that such imports will not threaten to impair the national security.” It adds that Trump would be required to publish these actions in the Federal Register, but does not specify a time frame.

For the moment, there have been no announcements made by the USTR or by the USTR on the Federal Register.

The threat of auto tariffs is likely to 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. There are other avenues for how these tariffs may be implemented.

## NEW – S.301 Investigation of Digital Services Taxes

The USTR has announced an investigation into various digital services taxes that have been implemented or have been considered for implementation, on US firms.

> "President Trump is concerned that many of our trading partners are adopting tax schemes designed to unfairly target our companies," said USTR Robert Lighthizer. "We are prepared to take all appropriate action to defend our businesses and workers against any such discrimination."

https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/june/ustr-initiates-section-301-investigations-digital-services-taxes

## US-UK Trade Talks

There has been no further update on trade negotiations between the UK and the US at this stage. Trade negotiations commenced w/c 4 May and were expected to run in parallel with the EU Brexit/trade negotiations.

A deal is not likely to be finalised until the completion of the UK-EU post-Brexit trade deal. https://www.washingtonpost.com/business/what-trump-johnson-want-from-us-uk-trade-deal/2020/06/10/e116d732-ab75-11ea-a43b-be9f6494a87d_story.html

https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/may/statement-ustr-robert-lighthizer-launch-us-uk-trade-negotiations

The actual details of the negotiations are largely unknown and causing concern in the UK;

> "The precise details of any UK-US Free Trade Agreement are a matter for formal negotiations, and we would not seek to pre-empt these discussions.
>
> "The Government is clear that when negotiating FTAs we will continue to protect our right to regulate in the public interest where we deem fit."
> https://www.express.co.uk/news/world/1288548/uk-government-brexit-trade-deal-chlorinated-chicken-farmers-us-trade-liz-truss

USTR Lighthizer also noted in his recent testimony of the US intention to continue to pursue a trade agreement with the UK;

> The Trump Administration has taken numerous steps to pave the way for negotiating a trade agreement with the UK, including a review of public comments, a public hearing, and extensive consultations with congressional and trade advisory committees. USTR published detailed negotiating objectives on February 28, 2019, and aims to reach an agreement with substantive results for U.S. consumers, businesses, farmers, ranchers, and workers as soon as possible.
> https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/HWMCTestimonyon2020TradeAgenda-Final.pdf

The USTR has 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

## BREXIT

Rounds of 'intensive' negotiations between the EU and UK commenced last week. These were the first face-to-face meetings since the beginning of the global pandemic. The talks will alternate between Brussels and London for five weeks through Jul and Aug.

> Without a new agreement, the two sides would see ties reduced to minimum standards set by the World Trade Organization, with high tariffs and serious disruptions to business.

https://www.japantimes.co.jp/news/2020/06/29/world/eu-uk-brexit/#.Xvlra5MzY_U

Negotiations last week, have so far not appeared to make much progress and this is raising concerns (again) for businesses over the potential disruption from a 'crash out' style exit.

> Analysts at Berenberg said they do not see a Brexit deal being reached by the end of the year, putting a 60% chance on negotiators switching focus to "limit the immediate economic and social disruptions" of a crash-out exit on 31 December.
>
> Michel Barnier, Europe's top Brexit negotiator, said on 30 June there was "no way member states or the European Parliament would accept" the UK's bid to smooth access to European markets for London's financial district after it leaves the EU. The UK's chief negotiator David Frost said on 2 July that there remained "significant differences" between the two sides "on a number of important issues". https://www.fnlondon.com/articles/fears-of-a-brexit-crash-out-return-to-haunt-the-city-20200706

Link to the EU draft is embedded in the release;
https://ec.europa.eu/commission/presscorner/detail/en/IP_20_447

The UK negotiating objectives;
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/868874/The_Future_Relationship_with_the_EU.pdf

Return to top