MARS CAPITAL PARTNERS

Weekly Macro Review

w/c 27 July 2020

Key Themes

US headline consumer sentiment and sentiment around expected conditions have both fallen back to the lows reached at the start of pandemic.

> The Expectations Index fell back to 65.9 in July, tied with the six-year low recorded in May, providing no indication that consumers expect the recession to end anytime soon.

There was even some unusually downbeat commentary from the Mortgage Bankers Association this week regarding mortgage applications:

> "Homebuyers stepped back slightly, and there was a larger drop in purchase application volume for FHA, VA, and USDA loans. This trend, along with the fact that average loan sizes are increasing, indicate that prospective first-time buyers **are being impacted more by the rising economic stress caused by the resurgence in COVID-19 cases, as well as the uncertainty on how the next round of government support will take shape**."

Sentiment indicators are likely to worsen as additional benefits expire and if housing forbearance programs are not extended.

So far there has been no resolution regarding the extension for the expiring CARES Act benefits. The funding bill continues to be debated among Republicans. Some Republicans suggest enough stimulus has already been delivered and the Whitehouse wants to boost the economy prior to the election. The Democrats have an alternative set of priorities. There will likely be some resolution/compromise, but the Federal benefits have now started to expire.

The Federal Pandemic Unemployment Assistance program currently has over twelve million people on continuing claims. There are over 30 million people claiming ongoing unemployment insurance (at wk ending 11 Jul) across both state and federal programs.

The high frequency employment data (the regular state-based programs) is providing some mixed signals – the more recent data indicates that the small improvement in initial claims appears to be stalling and continuing claims also increased.

Regional manufacturing reports for July indicate at least a low level of momentum in production and shipments growth. Employment growth remains low, but there was improvement in hours worked. The advance durable goods report for Jun also indicated stronger growth for the month – except for non-defense airline orders. There appears now to be some greater momentum behind motor vehicle production and orders.

The decline in personal income in Jun was mostly due to the one-off CARES Act payments going through in the prior two months. In Jun there was an increase in wages and salaries, but levels remain well below a year ago. Incomes were boosted by unemployment insurance. Expenditures increased in Jun. But the year on year comparison highlights the severe decline in expenditure on Services – usually a very stable component. Any impact on expenditure and income from the current outbreak in infections in the US will likely start to show up from Jul.

In Australia, one of the largest states, Victoria, will go into a more severe shutdown for an estimated six (6) weeks due to the increase in infections. This will be another hit to the Australian economy, impacting business output, expenditure and employment at the state and National levels. At this stage, there is no indication of any renewed fiscal support for the state.

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US FOMC Rates Decision

Europe - Eurozone CPI (Jul), Eurozone GDP Q2 - Prelim

Japan – Retail Trade (Jun), Industrial Production Prelim (Jun)

Australia – CPI Q2, Private Sector Credit (Jun)

Trade – Updated: US-China Trade Talks, Brexit

No Update: US-Japan Trade Talks, US-Europe Trade Talks, US S.301 Investigation into Digital Services Taxes, Section 232. Car and Truck Imports, US-UK Trade Talks

US Data

Initial Jobless Claims (25 Jul), Continuing Claims (18 Jul) and PUA,

There was a further increase in the advance initial claims for the latest week ending 25 Jul, but not on a seasonally adjusted basis. The continuing claims for the prior week ending 18 Jul increased on both a seasonally adjusted and NSA basis.

This is, so far, two consecutive weeks of increases in initial claims (SA) and the first week that continuing claims increased (both SA and NSA basis). At best, the improvement in unemployment claims may be stalling.

Despite the weekly shifts, the total number of people making initial claims is still over one million a week – this is extremely elevated.

Across total federal and state programs for the wk ending 11 Jul, there was a larger decline in the total number of people claiming benefits.

> The total number of people claiming benefits in all programs for the week ending July 11 was 30,202,498, **a decrease of 1,601,699 from the previous week**. There were 1,722,040 persons claiming benefits in all programs in the comparable week in 2019.

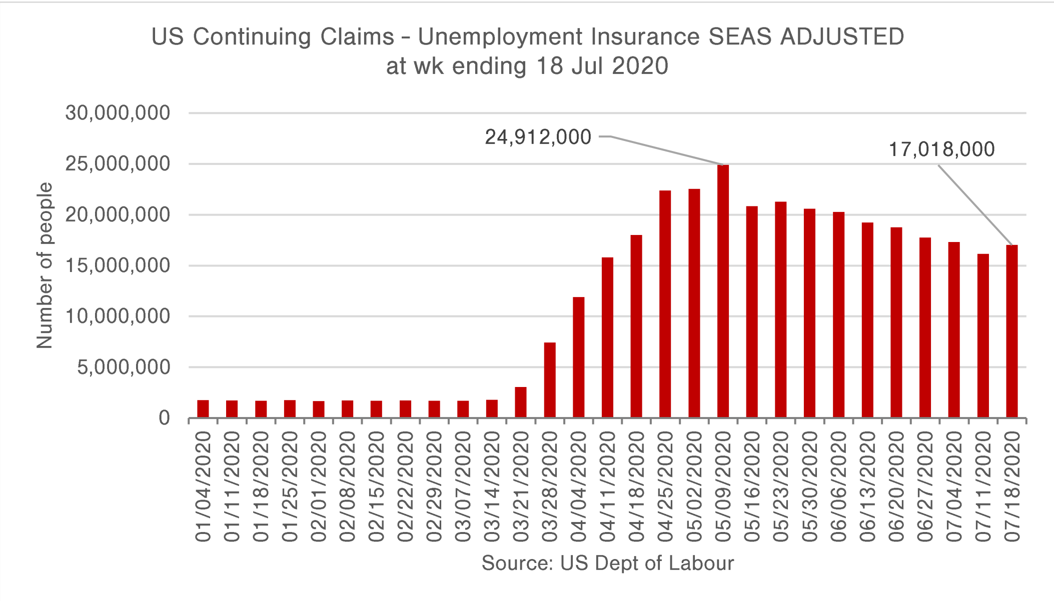
<u>STATE-BASED PROGRAMS</u>

<u>Advance Initial Unemployment Claims (SA) – wk ending 25 Jul 2020:</u> 1,434,000 people

This week is slightly higher than the 1,422,000 initial claims made in the week prior.

The NSA advance claims were lower at 1,205,871 claims for the week ending 25 Jul which was a fall of just under 200k claims made by people.

<u>Continuing Claims (SA) – wk ending 18 Jul 2020:</u> 17,018,000 people



The level of continuing claims unfortunately increased by 867k ongoing claims versus the week prior. The NSA level of continuing claims also increased in the week by +537k ongoing claims to 16,881,463 claims. The level of seasonal adjustment had forecast a decline of 323k ongoing claims.

FEDERAL PROGRAMS – PANDEMIC UNEMPLOYMENT ASSISTANCE (PUA)

Advance Initial PUA Claims (NSA) – wk ending 25 Jul 2020: 829,697 new claims made by people.

This was at least a fall of -106k new claims from the prior week.

The continuing PUA claims (NAS) decreased (compared to the week prior in the wk ending 11 Jul (latest data available); 12,413,322 continuing PUA claims.

The fall in the level of PUA continuing claims was more substantial at -766k less claims.

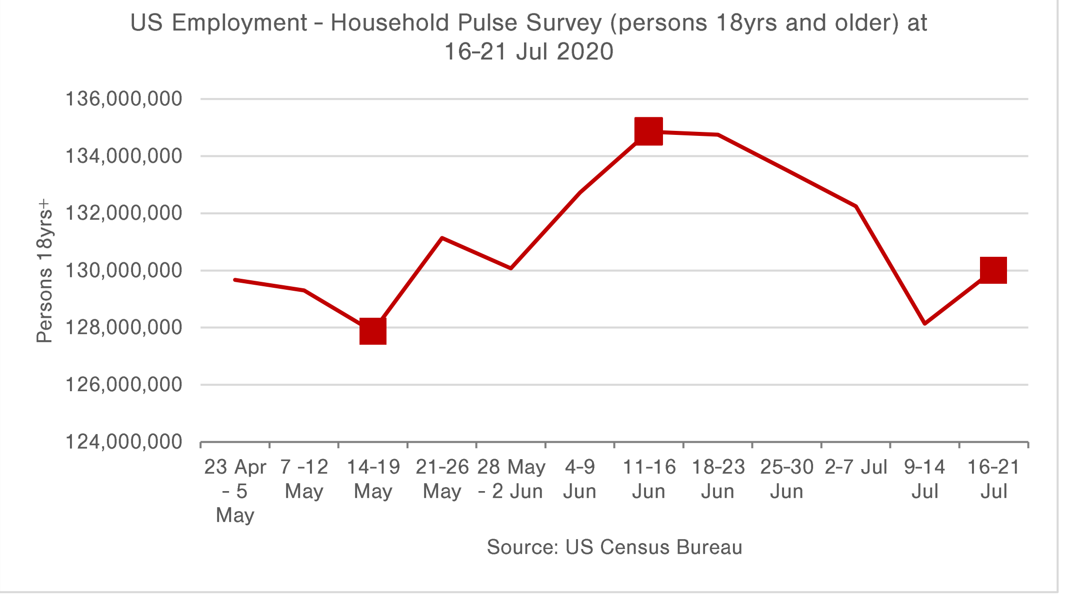
The Pandemic Emergency Unemployment Claims (PEUC) increased further in the wk ending 11 July from 940k to 1,055,098 claims.

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

Household Pulse Survey (Employment) 16-21 Jul

This is week twelve (12) of the household pulse survey. Employment levels increased this week by +1,860,000 people versus the week prior.

Given the declines in the prior weeks, the employment level is still approx. 4.8m lower than at (approx.) the last BLS reference week. The red squares reflect the last half of the equivalent BLS reference week (the weeks do not match up):



The increase in the latest week of +1,860,044 employed people was led by:

Government: +1,162,688 higher employment. This week increase basically offset the decline of -1,190,190 in the week prior.

Private Company: +612k higher employment. This only partially offset the -2m decline in the week prior.

Family Business: +811k high employment. This is the largest increase of the 12-week series.

Non-Profit and Self-Employed both declined further this week.

https://www.census.gov/data/tables/2020/demo/hhp/hhp12.html

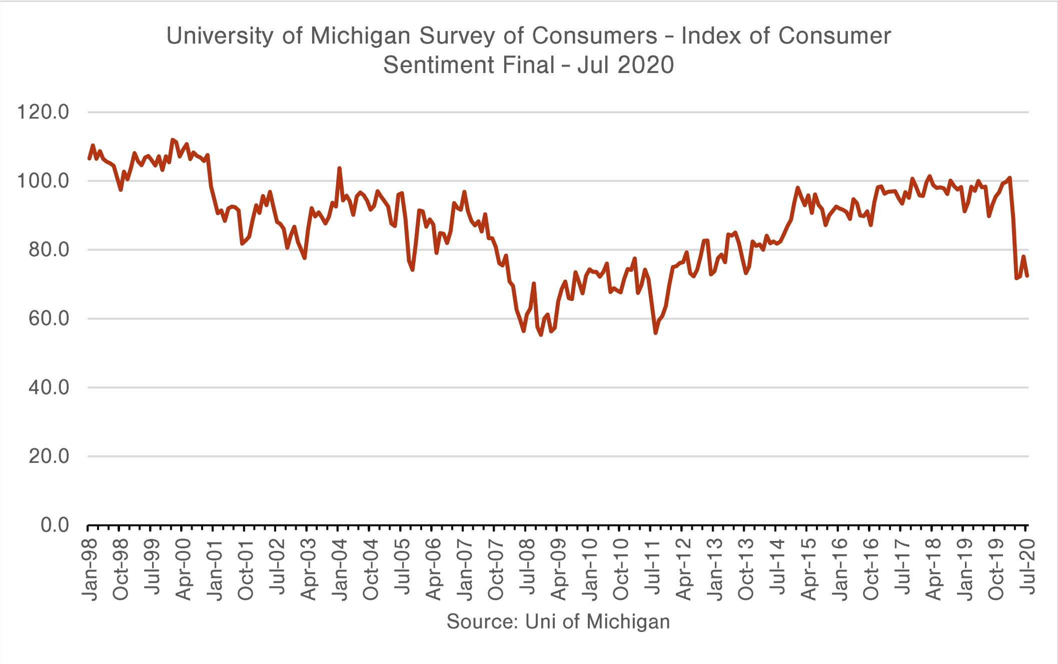
University of Michigan Consumer Sentiment – Final (Jul)

There was a further deterioration in consumer sentiment readings in the second half of Jul. Headline sentiment and sentiment around expected conditions are now back on par with the low point associated with this pandemic in Apr/May.

> The Expectations Index fell back to 65.9 in July, tied with the six-year low recorded in May, providing no indication that consumers expect the recession to end anytime soon.

Headline Index of Consumer Sentiment: Jul 72.5 (revised lower from 73.2) versus Jun 78.1

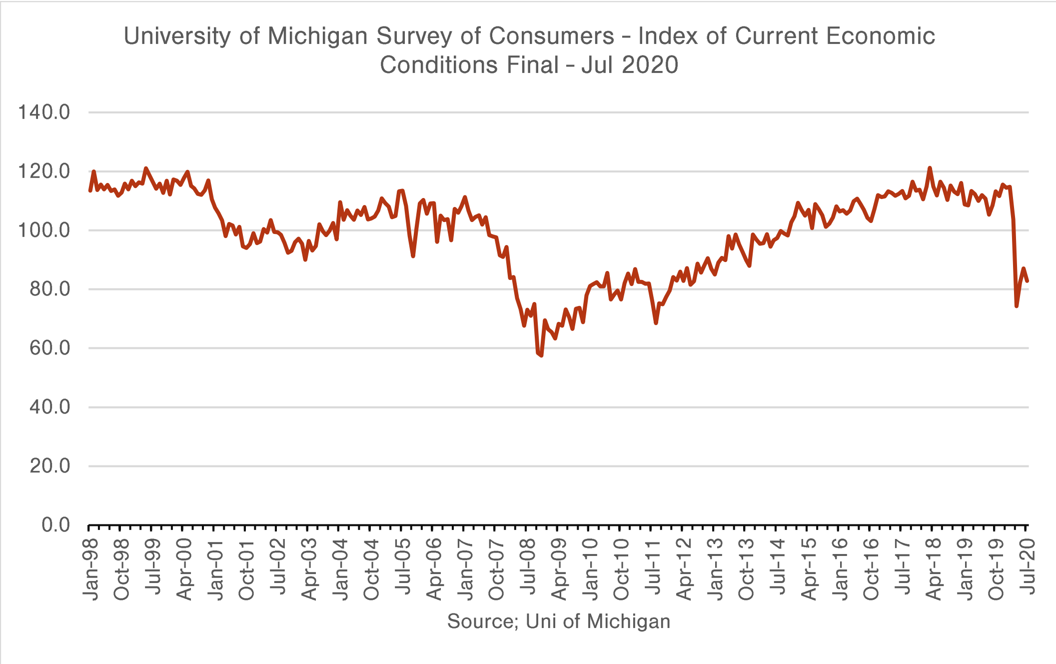
The low point of the index related to the pandemic was 71.8 back in Apr. The current reading is only marginally above this level:



Index of Current Economic Conditions: Jul 82.8 (revised lower from 94.2) versus Jun 87.1

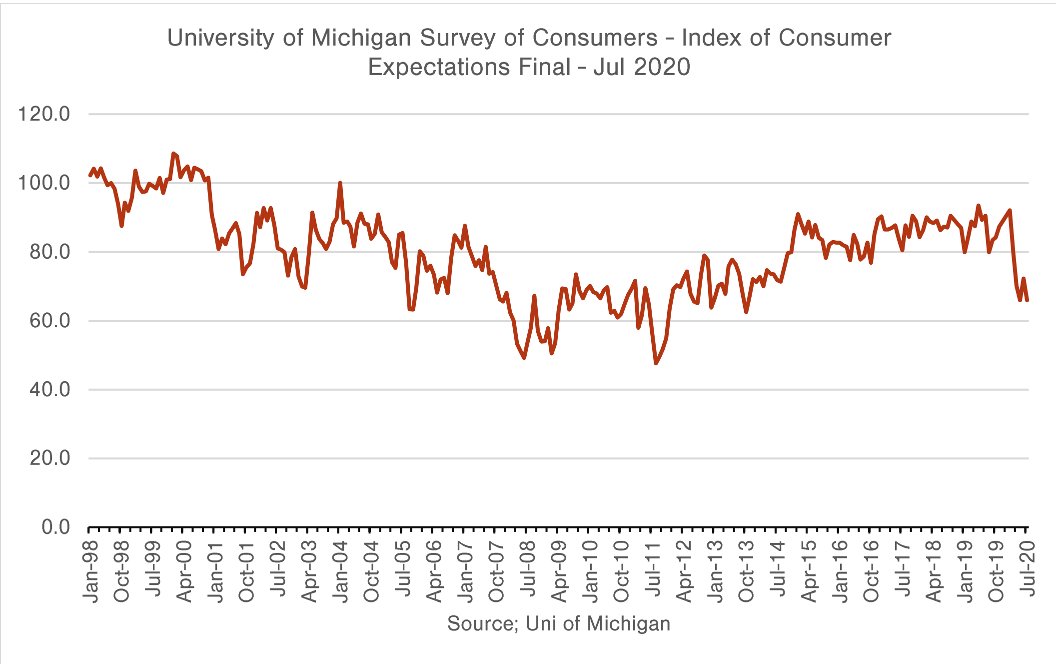
The low point of the index related to the pandemic was 74.3.

While the Jul reading is still above this level by a bigger margin (then headline sentiment), there is a risk that this deteriorates further as additional benefits expire before a new support bill is approved.



<u>Index of Expected Economic Conditions</u>: Jul 65.9 (revised lower from 66.2) versus Jun 72.3

Consumer expectations of future conditions have fallen to be on par with the low reached during first stage of the pandemic, which was also 65.9 in May.



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

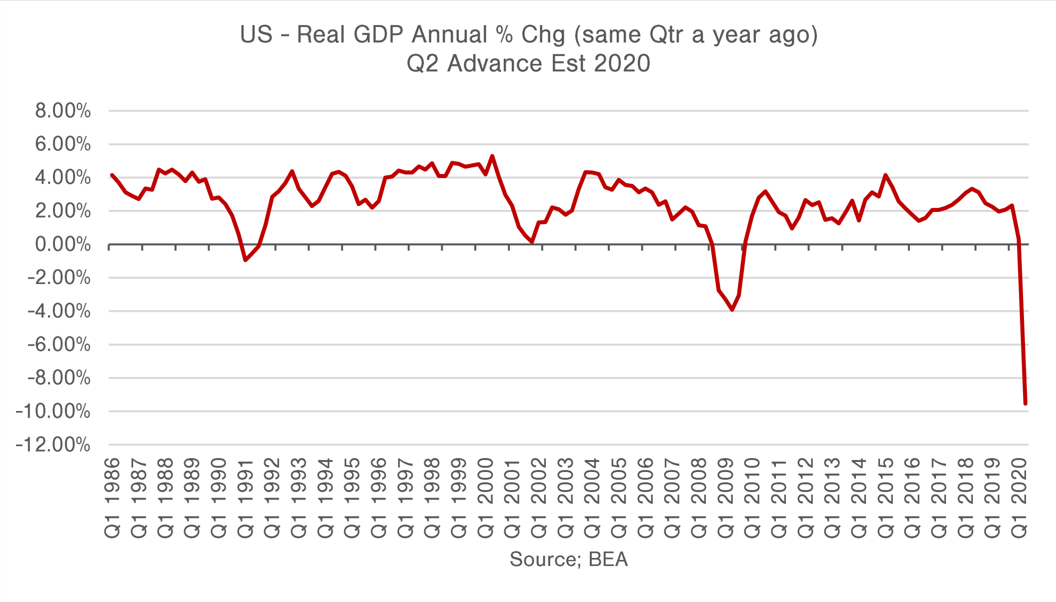
GDP Q2 – Advance Estimate

As expected, the decline in US GDP was severe in Q2. Most areas contributed to the decline this month except Government expenditure. Net exports also made a positive contribution, but underlying that, both exports and imports recorded severe declines. The decline in personal consumption expenditure made the largest contribution to the overall decline – led mostly by a fall in expenditure on Services.

<u>US Real GDP – Quarter change</u>: Advance Est Q2 -9.5% versus Final Q1 -1.3%

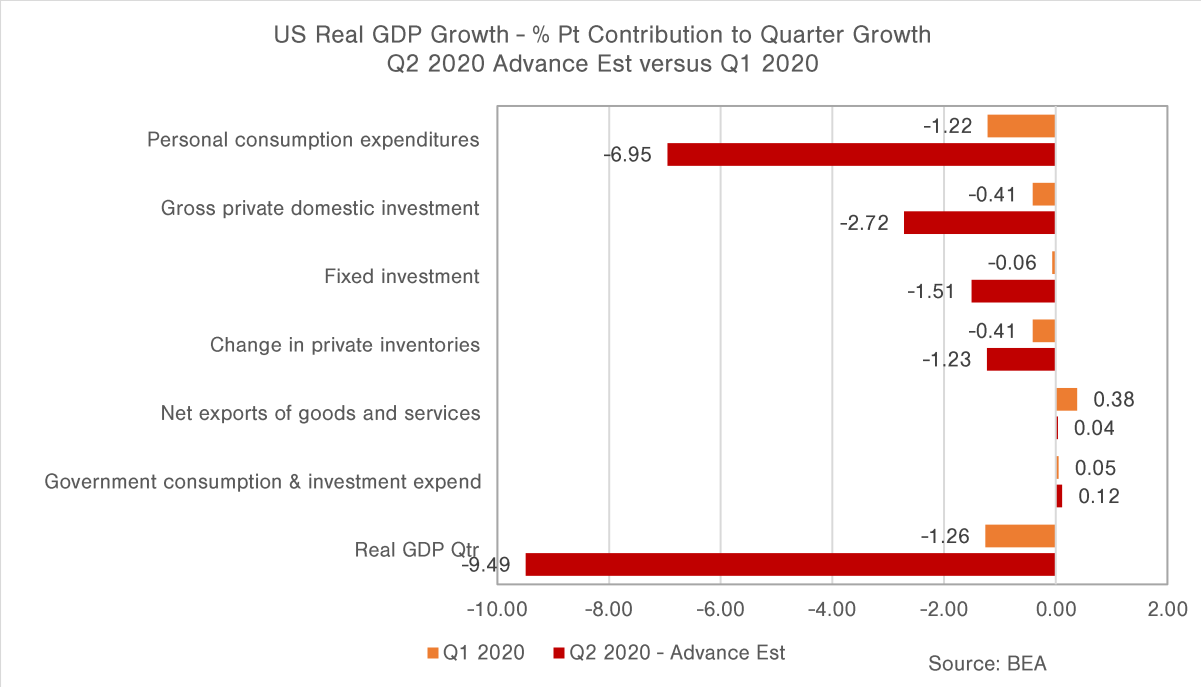
The change in real GDP shifted to a sharp decline on an annual basis in Q2 (not SAAR basis):

<u>US Real GDP – Annual change (same qtr a year ago):</u> Advance Est Q2 -9.5% versus Final Q1 +0.3%



The SAAR basis decline was -32.9% in Q2.

Performance by Expenditure Component



Most areas of expenditure contributed to the decline in real GDP for the quarter:

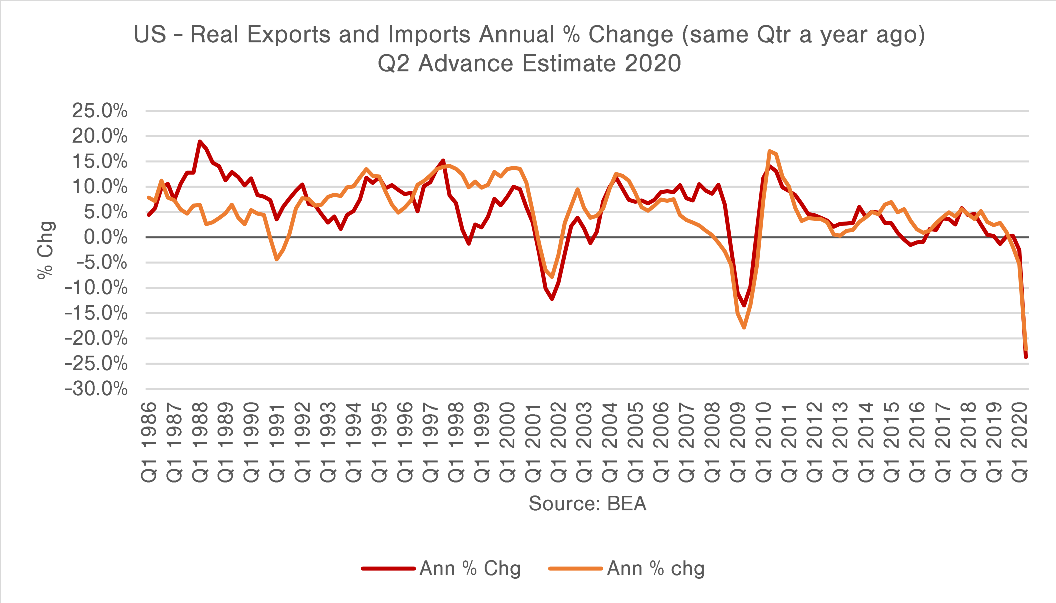
Personal consumption expenditure made the largest contribution to the headline decline, detracting approx. 7% pts from the headline growth. The biggest part of that decline was the 13.3% decline in expenditure on services, while the decline in goods expenditure was smaller at -2.9% for the quarter. The decline in durable goods expenditure was even smaller at only -0.4%.

Fixed Investment expenditure detracted -1.5% pts from headline growth and expenditure declined by 8.5% in the quarter. Declines were recorded across both residential (-11.5%) and non-residential (-7.6%) investment expenditure.

The change in inventories also detracted -1.2% pts from headline growth.

Net Exports made a slightly positive contribution to growth because the negative value of net exports became less negative in Q2 compared to the result in Q1. But underlying that, exports declined by -22.6% in Q2 and imports declined by -17.4%.

The annual decline in US exports and imports has accelerated in Q2:



Government expenditure and investment made a small positive contribution to headline growth in the quarter, adding +0.12% pts. A +4.1% rise in federal expenditure more than offset the -1.4% decline in state local government expenditure and investment.

https://www.bea.gov/data/gdp/gross-domestic-product

Advance Durable Goods Factory Orders (Jun)

There was more substantial improvement in durable goods orders and, shipments especially, this month. This was in line with the Jun industrial production data and the improved manufacturing PMI for Jun.

Excluding transportation, there was no change in unfilled orders, but inventories declined.

Key highlights; 1) the continued increase in motor vehicle orders and shipments, 2) the general acceleration in the growth of orders and shipments for non-transportation industries (except computers and electronic products), and 3) there was another substantial decline in the value of new orders for non-defense aircraft in Jun (not the change, the actual value). This reduced the overall growth in orders for the month.

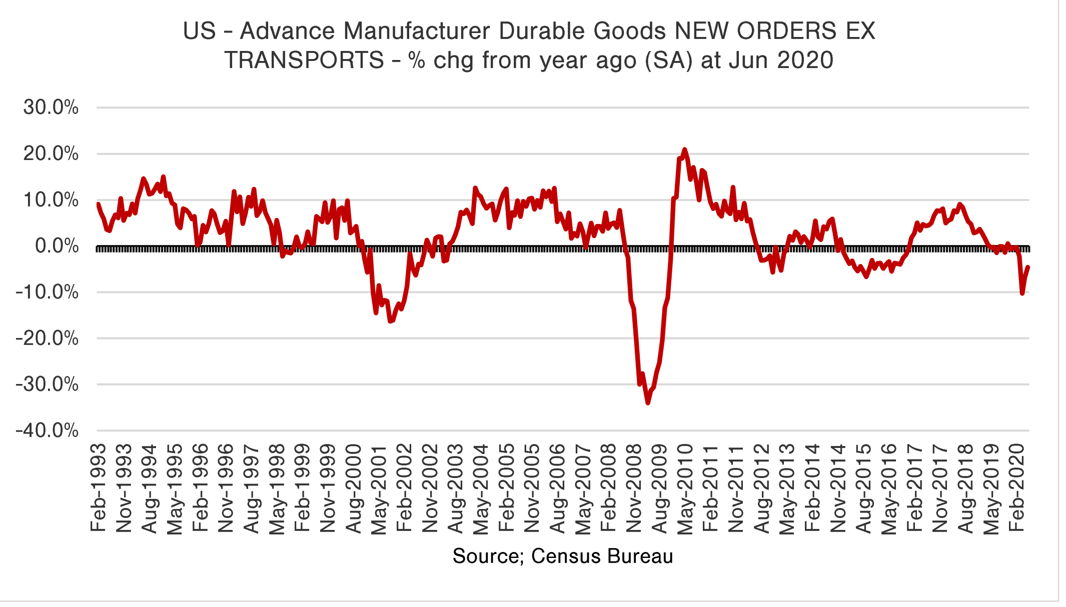
Durable Goods New Orders ($ val) – month change; Jun +7.3% (+$14bn) versus May +15.1% (+$25bn)

Most of the improvement in orders this month was due the growth in transportation equipment of +20% (+$9.2bn) in Jun. The big improvement was for motor vehicle orders +85% versus May (+$24.4bn). New orders for motor vehicles in Jun are now only 13.7% below the same month a year ago.

This was unfortunately offset by -$10bn in new orders for non-defense aircraft for Jun. This is not the pace of change; it is the actual value of orders for Jun (likely cancelled orders). The decline from the month prior was -$13.2bn in the value of orders. Orders for non-defense aircraft are 250% below the same month a year ago.

Other categories such as primary metals, fabricated metals products, and machinery all continued to record growth, albeit at a slightly slower pace.

On an annual basis, total durable goods orders are still -12.7% below the same month a year ago. This decline 'improves' excluding transportation equipment to -4.6% below the same month a year ago.



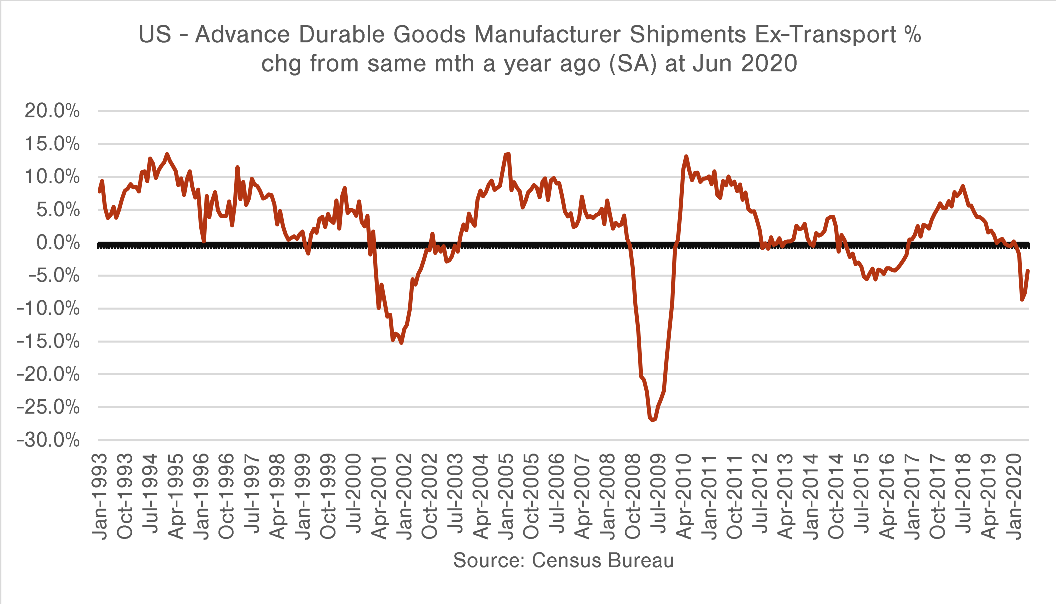
Durable Goods Shipments ($ val) – month change; Jun +14.9% (+$29.4bn) versus May +4.2%

The single largest contributor to the increase in shipments was motor vehicles +83% or +$23.6bn versus the month prior. Nondefense aircraft shipments increased by 18% versus May but are down 63% versus the same month a year ago.

Shipments growth increased across most categories at a faster pace this month - but the value of shipments remains below the same month a year ago across these categories.

The exceptions were computer and electronic products (-0.8% in the month) and defense aircraft (a decline of -0.7% in the month). Shipments of computer and electronic products is above the same month a year ago.

On an annual basis, durable goods shipments are now -9.5% below the same month a year ago. Excluding transports, shipments are only -4.3% below a year ago:

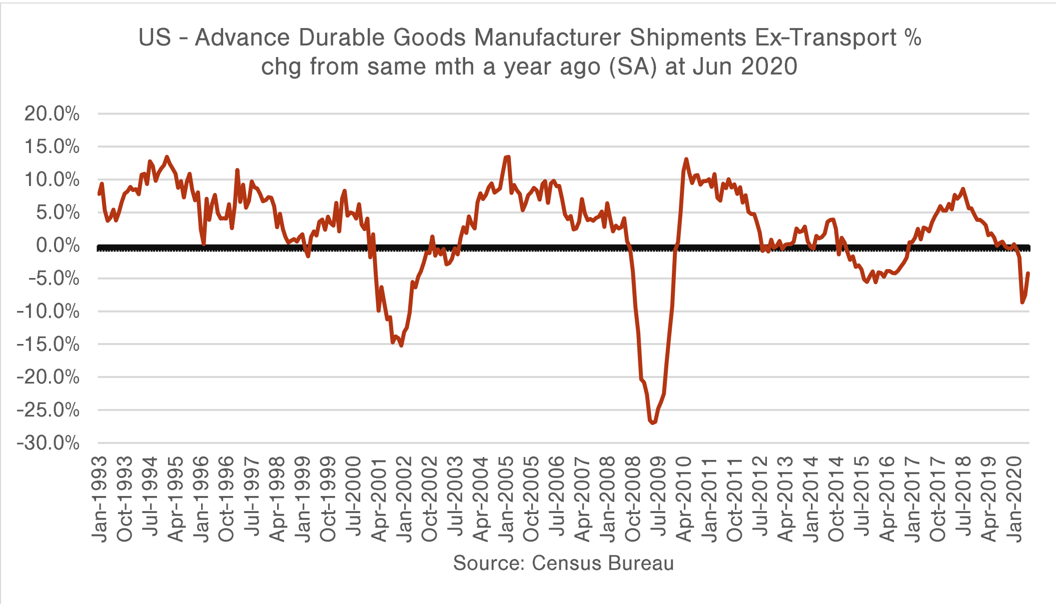


<u>Durable Goods Unfilled Orders ($ val) – month change</u>: Jun -1.4% (-$15bn) versus May 0%

The large decline in unfilled orders this month was the result of the likely cancellation of non-defense aircraft orders (-$14.5bn).

Motor vehicle unfilled orders increased by +3.8% in Jun (+$0.8bn). This was a relatively large improvement. On an annual basis, the decline in unfilled orders went from -52% in May to -15% in Jun. The supply chain appears to be slowly regaining some momentum.

Excluding transportation there was no change in unfilled orders this month; +0% in Jun. This indicates that growth in new orders still needs to increase further to start to see backlogs increase. This was also reflected in the capacity utilization figures, which remained lower in the Jun industrial production report.

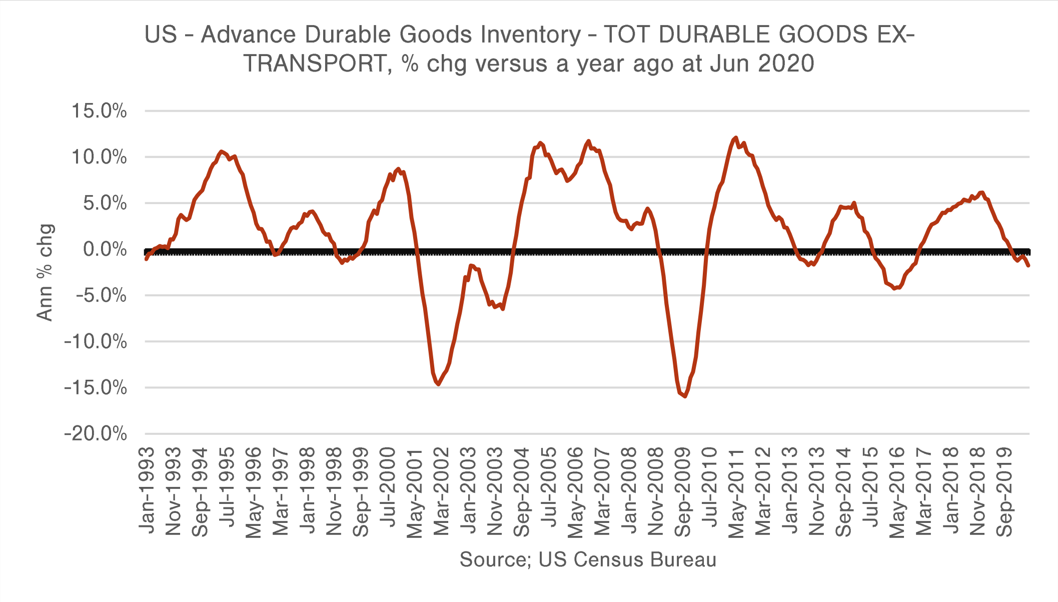


Durable Goods Inventory ($ val) – month change: Jun +0.1% (+$0.4bn) versus May 0%

The rise in inventories was led entirely by non-defense aircraft of +2.4% (+$1.8bn). The level of inventory is now +20% above a year ago. Orders and shipments for aircraft were already under pressure prior to pandemic and the pandemic impact on travel has left some airlines with excess capacity.

Most other categories recorded declines in inventory especially primary metals, fabricated metal products and machinery. This suggests firms were running down inventory to meet the increase in orders across these categories.

On an annual basis, the value of inventory of durable goods excl transport equipment declined by -1.8% versus the same month a year ago.



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

Dallas Fed Manufacturing Survey (Jul)

The index of general business activity in the region remained in slight contraction – meaning that the number of firms still reporting declines in general activity slightly outnumbered those reporting increases. The outlook uncertainty increased this month.

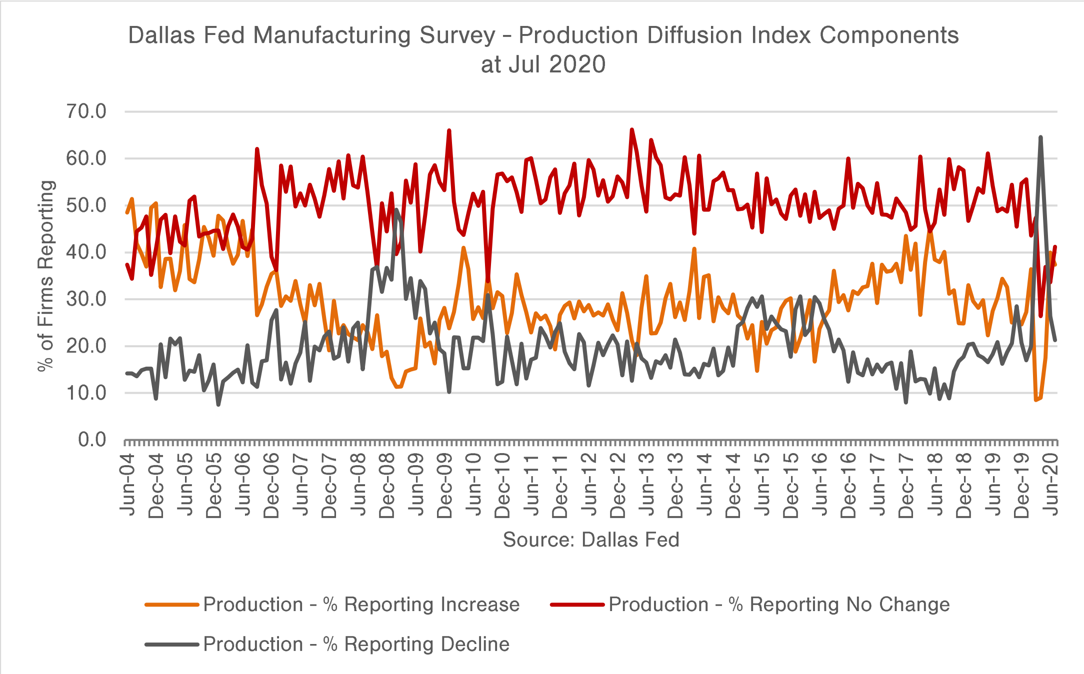
At the same time, the main index components of demand improved in Jul. But the underlying changes in firms performance in these indexes suggests that more firms were in a ‘no change’ holding pattern across these key measures. This is especially true for production, new orders, and the growth rate of new orders. There were more positive changes in shipments, and hours worked.

Headline Production Index; Jul 16.1 versus Jun 13.6

The headline production index increased slightly this month. But the underlying shift in firms production performance was mixed.

The proportion of firms reporting higher production than last month was lower (37% in Jul versus 40% in Jun). The grey line in the chart below is the proportion of firms reporting lower production in the month. This group is getting smaller after peaking in Apr at 64% of firms, but at 21.6% the proportion of firms reporting lower production is still elevated. Note that this group has become larger since mid-2018.

The biggest change this month was that more firms reported no change in production, and this increased from 33.6% of firms in Jun to 41.2% of firms in Jul.



As an indicator of future output, new orders signals are mixed.

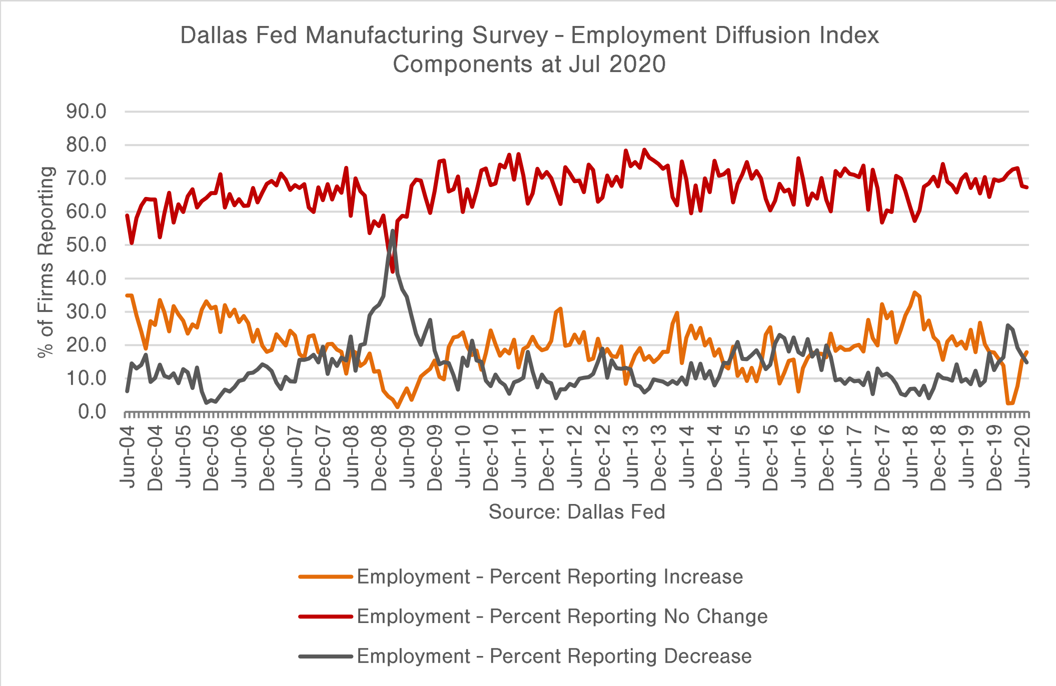
The new orders index also increased from 2.9 in Jun to 6.9 in Jul (still only a moderate pace of growth). But the underlying proportion of firms reporting higher new orders also declined from 32.4% to 30.6% (granted not a huge fall). The index increased because less firms reported lower new orders (29.5% in Jun down to 23.7% in Jul). Most firms reported ‘no change’ in new orders.

The growth rate in new orders shifted from net decline in Jun to a small increase in Jul. But again, most firms shifted into ‘no change’ from the month prior. Less firms reported a higher growth rate in new orders 24.8% in Jul versus 27% in Jun). But there was also a larger reduction in the proportion of firms reporting a lower/declining rate of growth in new orders, down from 33% in Jun to 23.5% in Jul (which is still elevated). There was a much larger increase in the firms reporting ‘no change’ in the growth rate of new orders increasing from 39.8% in Jun to 51.7% in Jul.

Shipments were more positive. The index increased from 3.1 in Jun to 17.3 in Jul. There was a slight increase in the firms reporting higher shipments, but the big change was a much lower proportion of firms reporting lower shipments (from 30.4% of firms in Jun to 18.4% in Jul). But still, 46% of firms reported no change in shipments from the month prior.

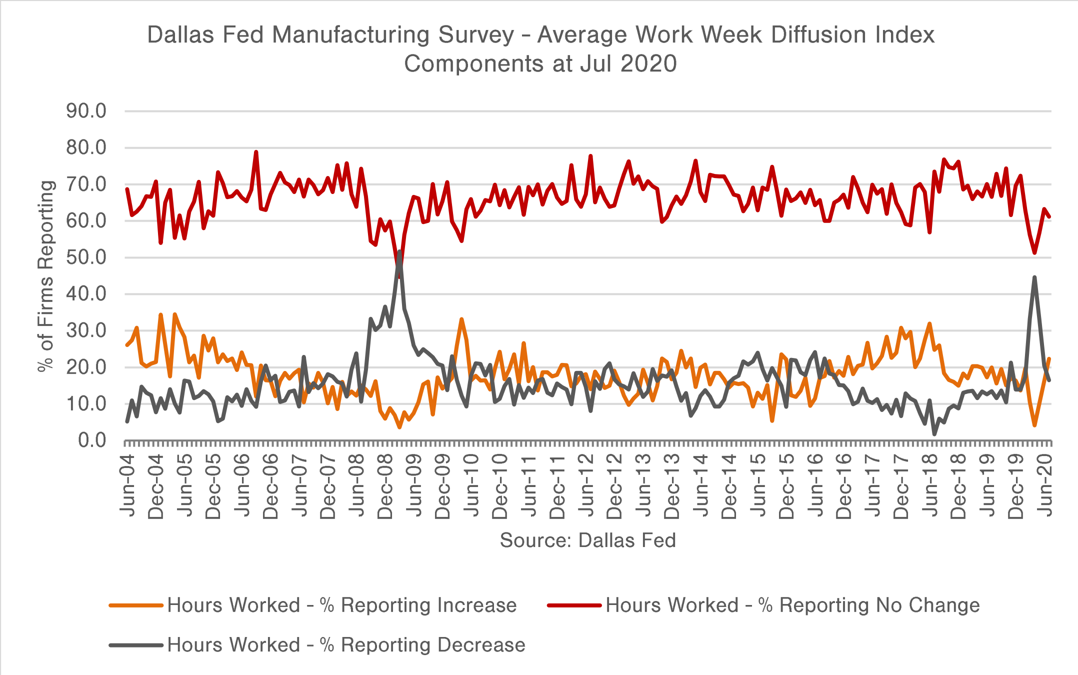
Both employment and hours worked indexes increased from net contraction to net expansion this month.

The employment index increased from -1.5 in Jun to 3.1 in Jul. As previously noted, the underlying trend has been little changed during this pandemic. Most firms made no change to employment levels throughout this pandemic (67.3 of firms in Jul). This was a better result than that of the GFC (see redline below):



The proportion of firms still reporting declines remains elevated at 14.8%, down only slightly from 16.9% in Jun. The number of firms reporting increases in employment increased slightly to 17.9% in Jul.

Hours worked is where most firms have focused for now. The index increased from -4.3 in Jun to 5.8 in Jul. But again, over 60% of firms reported no change in hours worked in Jul (compared to Jun). More firms reported higher hours (now up to 22% of firms) and less firms reported lower hours (now down to 16% of firms).



The index of outlook uncertainty increased notably this month from 9.1 in Jun to 20.9 in Jul. The increase in the index was the result of a larger decline in the number of firms reporting lower uncertainty (from 24.5% in Jun to 13.6% of firms in Jul). There was a small increase in the number of firms reporting higher uncertainty, now up to 34.5% of firms. Just over 50% of firms reported no change in uncertainty.

https://www.dallasfed.org/research/surveys/tmos/2020/2007.aspx

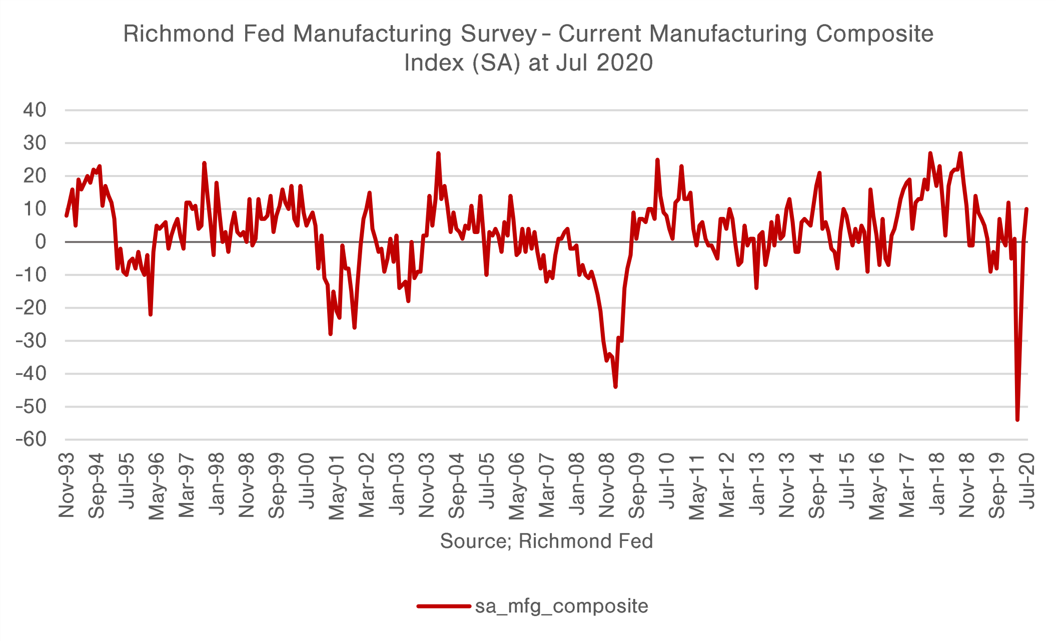
Richmond Fed Manufacturing Survey (Jul)

The composite index indicates that manufacturing activity in the region improved in Jul. The strongest component was the acceleration in shipments, but the volume of new orders also continued to increase at a slightly faster, albeit still only moderate, pace. Order backlogs increased for the first time in five months – a continued trend here could enable firms to either increase hours or employment.

Overall employment levels continued to contract in Jul – indicating that the number of firms reducing employment is still likely outnumbering the number of firms increasing employment. Instead, firms continued to increase the average workweek.

Headline Manufacturing Index: Jul 10 versus Jun 0

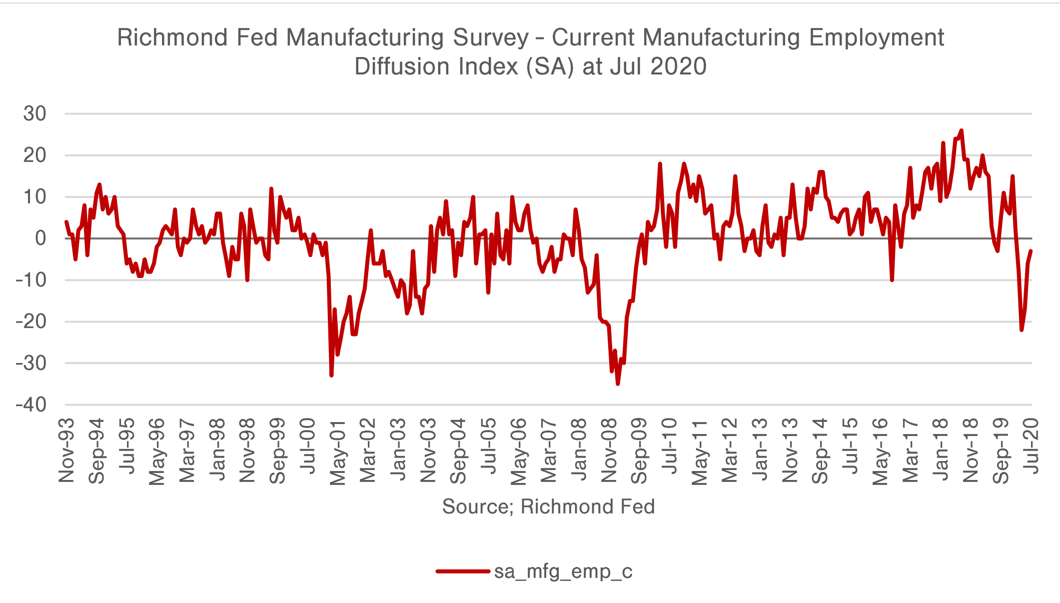
The increase indicates that a larger number of firms, on net, reported improved/higher manufacturing conditions than firms that reported lower/declining conditions overall.



This month, the shipments index increased notably from -4 in Jun to 23 in Jul. Finished goods inventories increased at a constant pace and capacity utilization increased at a faster pace, so its likely that overall production activity improved.

The volume of new orders index increased at a slightly faster pace from 7 in Jun to 9 in Jul. This index level reflects still relatively muted growth – indicating that more firms are reporting higher new orders than lower new orders, but by only a small margin. But it is an improvement, nonetheless.

Employment continued to contract on net – meaning that more firms were continuing to reduce employment than the numbers of firms increasing employment.



But instead, firms continued to increase hours worked, the index increased from 1 in Jun to 8 in Jul. The improvement in hours worked, like some other measures, has been slow. There has been no ‘snap back’ in demand, otherwise these indexes would likely be much higher.

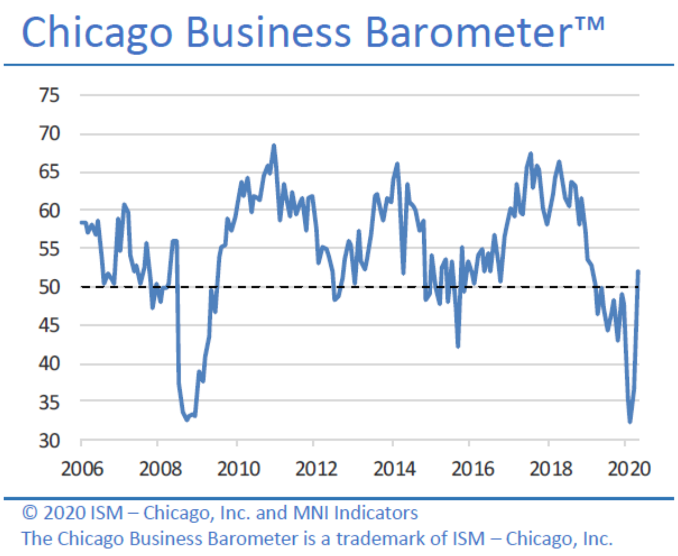
https://www.richmondfed.org/research/regional_economy/surveys_of_business_conditions/manufacturing/

Chicago PMI (Jul)

There was a larger improvement in the Chicago region PMI in Jul. The headline index shifted from a moderate pace of contraction to a slight expansion. This was the first time in twelve months that the index reading was above 50.

The caution with this “snap-back” result is that it needs to be taken in context of prior months decline. The prior month reading for the PMI at 36 indicates that most firms were reporting worsening conditions. As firms start to reopen, more firms will report ‘higher’ levels of activity just by virtue of reopening. In this case, you would then wonder why the headline PMI is not higher.

Headline Chicago PMI: Jul 51.9 versus Jun 36.6



New orders increased in Jul, but there is no note that the index is back into expansion.

> While some companies noted recovering orders, others reported continued difficulties due to the Covid-19 effects.

Production levels increased – which did put the index back into expansion. But order backlogs, while improving somewhat, remained in contraction. This indicates that despite whatever improvement in orders and production, firms are still able to work through backlogs of work i.e. there is little pressure on capacity yet.

The report notes that employment increased, but again, there is no mention of whether this index has shifted into expansion. In Jun, the employment index fell and remained below 50 with the quarterly reading the lowest since the GFC.

> Even though Employment ticked up 26.0%, there was anecdotal evidence that firms had to lay off staff as a result of the current health crisis. However, others mentioned difficulties in finding new staff.

https://s3.amazonaws.com/images.chaptermanager.com/chapters/b742ccc3-ff70-8eca-4cf5-ab93a6c8ab97/files/mni-chicago-press-release-2020-07.pdf

Personal Income and Consumption Expenditure (Jun)

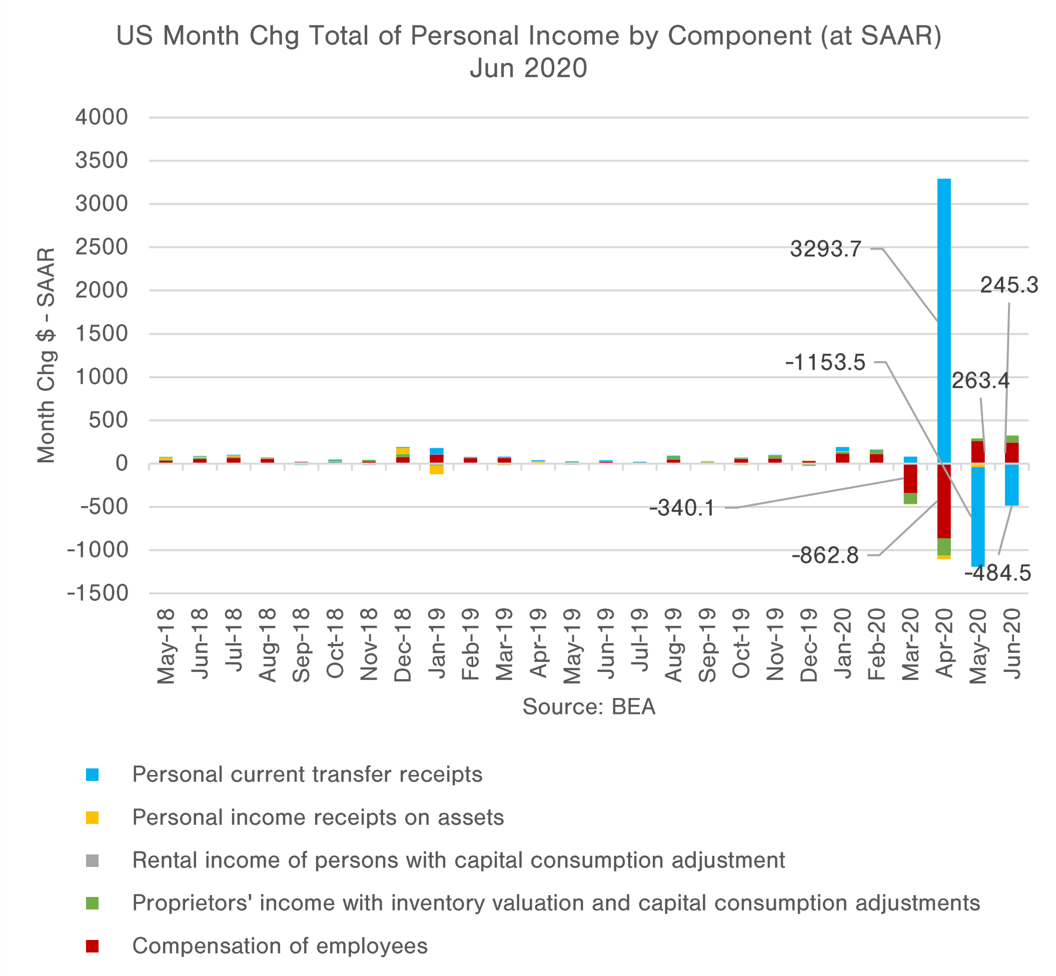
Personal incomes declined slightly in the month – this was mostly due to the last of the one-off CARES Act payments going through ('other' govt payments are almost back down to pre pandemic levels). Both wages and salaries and unemployment insurance payments increased in the month. Overall disposable personal income is +9% ahead of a year ago (wages and salaries are -2.4% below a year ago).

Expenditures increased in the month – led by both goods and services. But overall expenditure is still 5% below a year ago, mostly due to weaker expenditure on services.

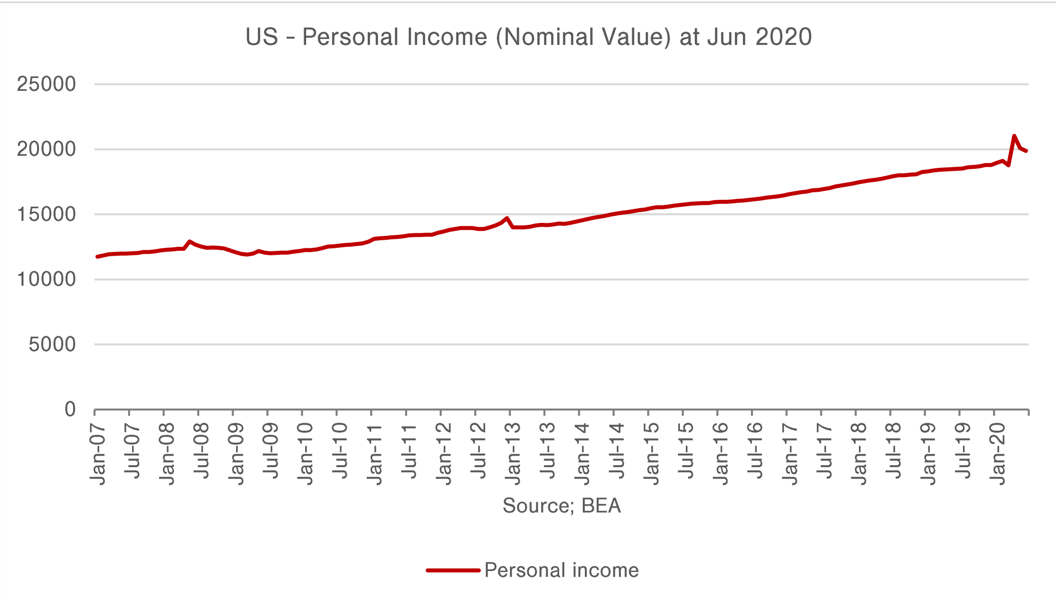
But in the month, the decline in personal disposable income and increase in outlays resulted in a lower saving rate compared to the month prior. Compared to a year ago, the saving rate is still extremely elevated.

PERSONAL INCOME

While total personal income declined in Jun compared to May, the level of personal incomes in Jun remain +7.4% ahead of a year ago – this is due mostly to the significant increase in government transfer payments since Apr.



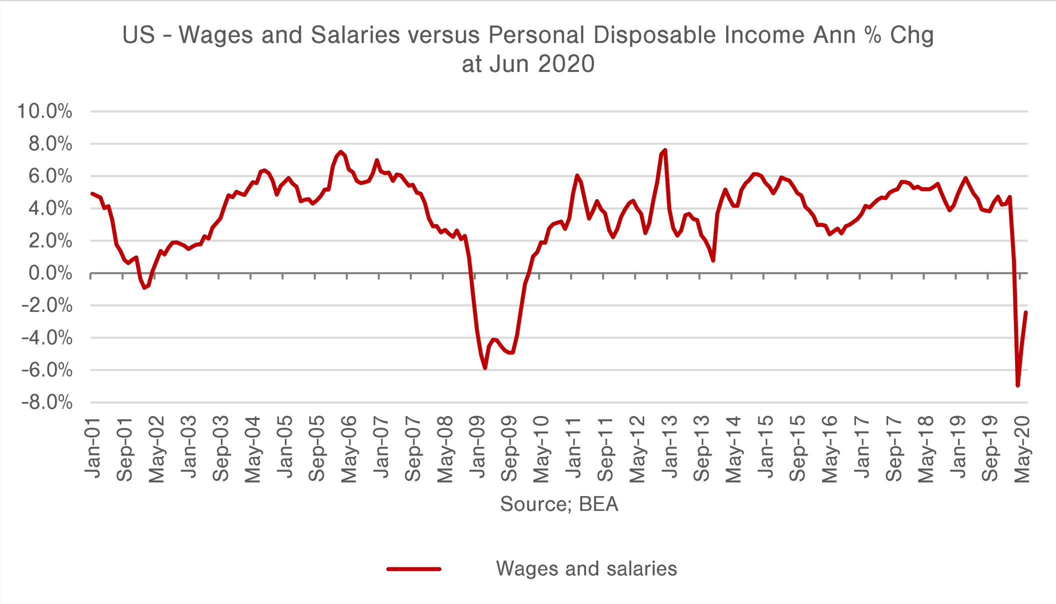
The decline in wages and salaries has been more than offset by increases in Government transfer payments - total personal income levels are above the pre-pandemic level:



<u>Total Personal Income – month change</u>: Jun -1.1% versus May -4.4%

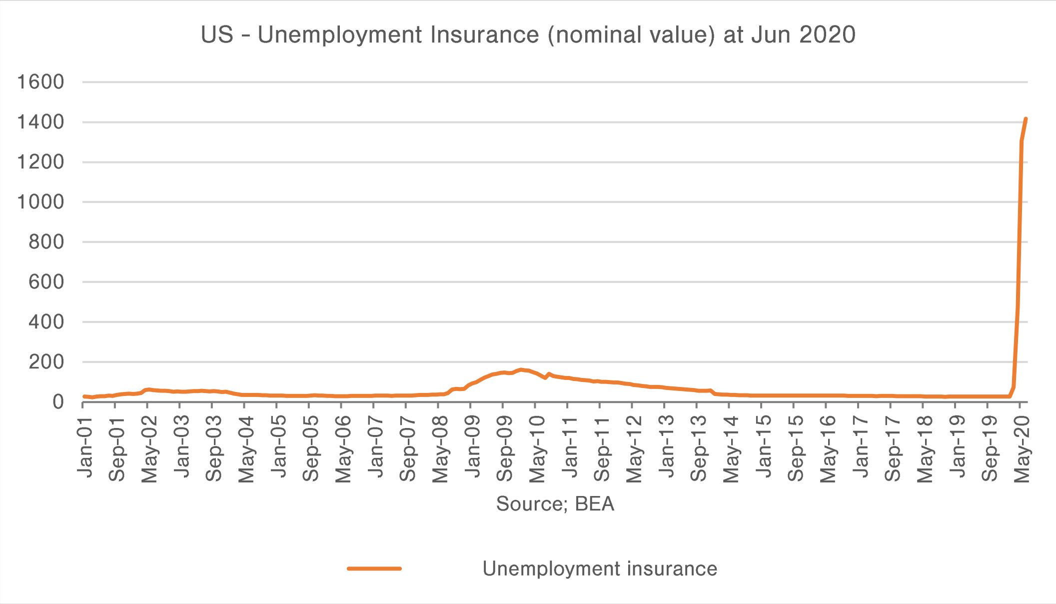
The largest component of personal incomes is wages and salaries.

In Jun, wages and salaries increased by 2.2% versus May. But wages and salaries remain well below where they were a year ago. The annual decline is now -2.4%. While this might not sound like much, consider that wages and salaries were growing at an annual pace of between 4% and 6% for the last few years prior to the pandemic:



The other significant contributor to personal income growth has been government social benefits to persons. This includes unemployment insurance.

Unemployment insurance continued to increase in Jun by +8% and is +5015% (not a typo) ahead of the same time a year ago.



“Other personal transfer receipts” was the line item for the one-time CARES Act payments. The decline in the month reflects the last of these payments going out to recipients.

Personal disposable income declined at a slower pace of -1.4% this month and remains +9% ahead of the same month a year ago.

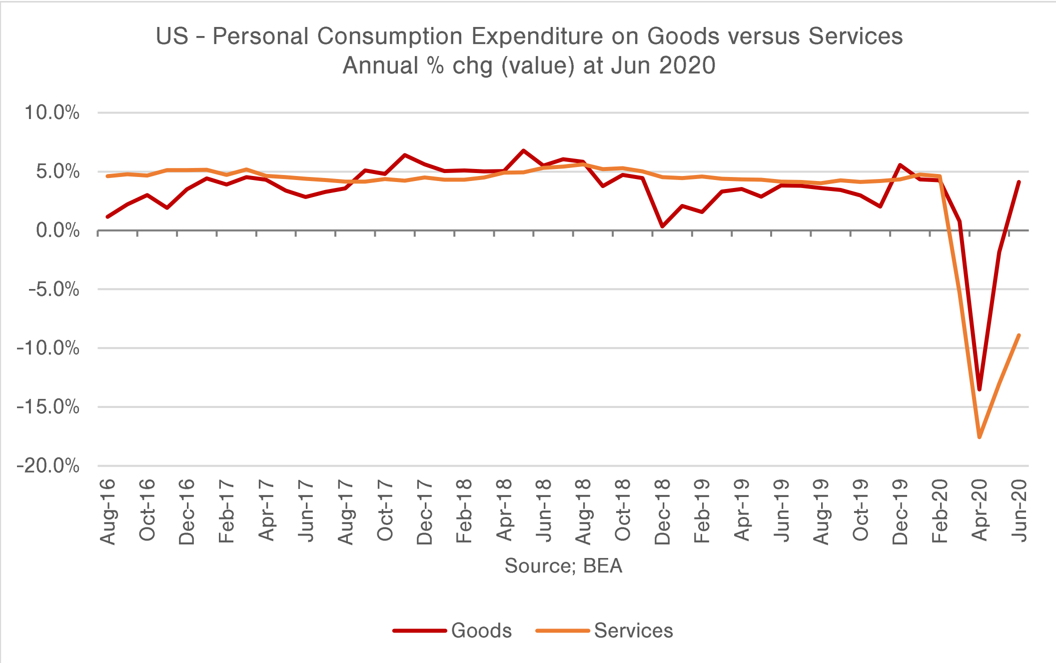
PERSONAL CONSUMPTION EXPENDITURE

There was a lift in outlays for the month, but overall expenditures are still 5% below the same month a year ago.

Personal Consumption Expenditure – month change: Jun +5.6% versus May +8.4%

Growth in the month was led by both goods and services expenditures.

But on an annual basis, total expenditures are still 5% below the same month a year ago (-6% in real terms). This has been the result of weaker spending on services – especially those areas most affected by social distancing requirements. Services is still to recover to last years' levels, let alone return to the consistent 5% annual growth level:

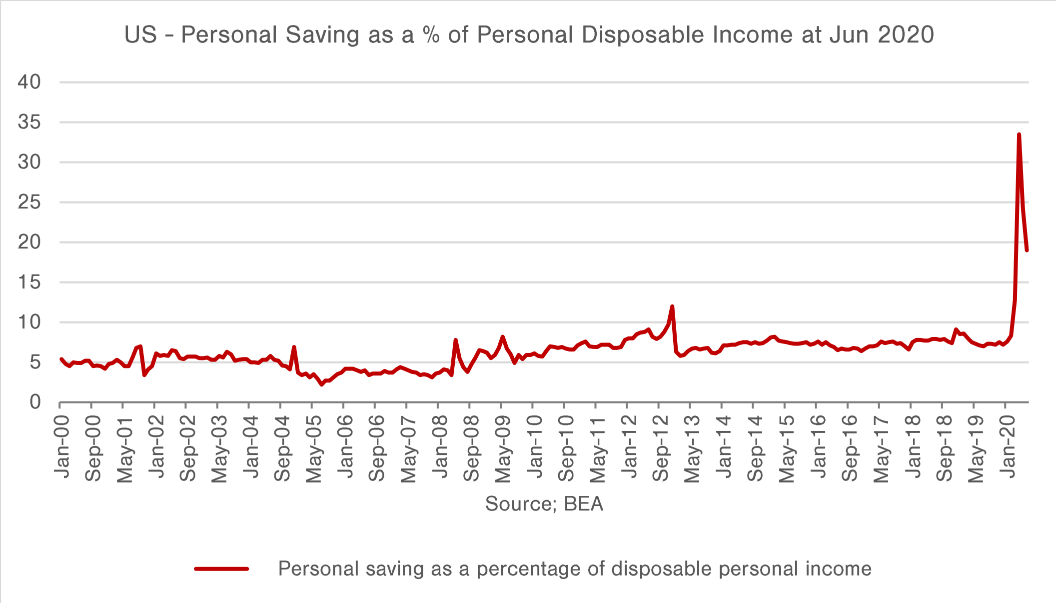


PERSONAL SAVING

This month there was a decline in personal income and an increase in outlays. This resulted in a lower level of personal saving.

Personal saving as a % of disposable personal income was lower at 19%, down from 24.2% in May.

But it is the year ago comparison that highlights the much higher level of saving. In Jun 2019, personal saving as a % of disposable income was 7.1%.



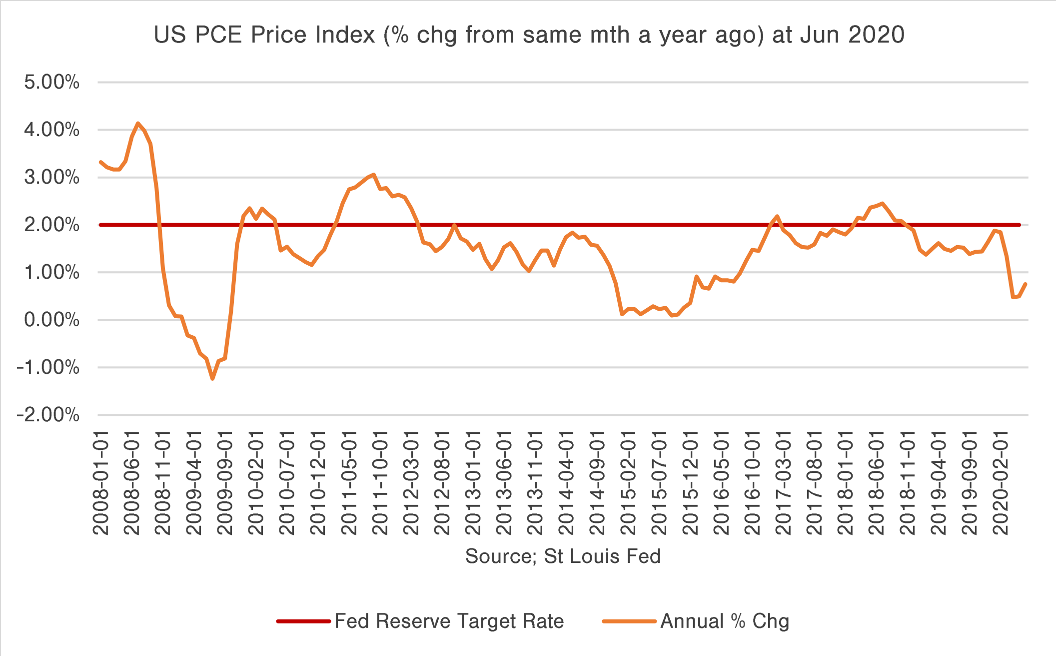
https://www.bea.gov/news/2020/personal-income-and-outlays-june-2020-and-annual-update

Personal Consumption Expenditure Price Index (Jun)

There was a small acceleration in the annual pace of headline PCE prices this month. This was led by a smaller decline in energy prices and an acceleration in annual growth of food prices. Services prices increased at a constant pace.

Of note is the continuing monthly growth in food for off-premise prices (albeit that monthly pace slowed this month) and the increase in energy prices – both increases impacting households this month.

PCE Price Index – annual change: Jun +0.75% versus May +0.5%



The small acceleration in the growth of the headline annual PCE price index was mostly the result of food and energy prices.

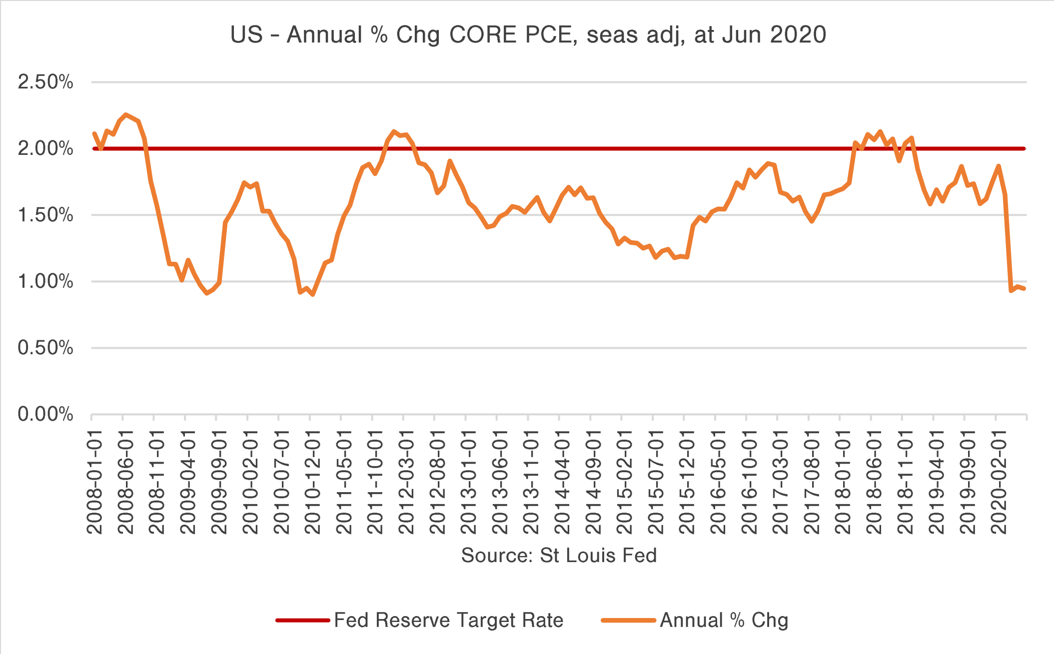
Food for off-premise consumption accelerated from +5.1% in May to +5.7% in Jun. This is well above the pre-pandemic level. Food prices increased notably in Apr and May and prices have continued to increase in Jun, albeit at a slower monthly pace.

Energy prices were still below a year ago in Jun, but by a lesser degree than in May. While prices were -23% below the same month a year ago in Jun, this was slower than the May decline of 32.6%. In the month of Jun (versus May), energy prices increased by 11%.

Excluding both food and energy prices, core PCE prices increased at the same annual pace in Jun as in May.

Note that the monthly increase in the PCE price index of +0.37% in Jun was the fastest for several years.

Core PCE Prices Index – annual change: Jun +0.95% versus May +0.96%



This reflects the constant pace of growth in services prices. Services prices overall increased by +1.8% in Jun versus +1.8% in May.

This pace of growth in services prices is still lower than the +2.4% - 2.5% consistent annual growth recorded prior to the pandemic.

https://apps.bea.gov/iTable/index_nipa.cfm

Mortgage Applications wk ending 24 Jul

Overall mortgage applications decreased slightly this week – with both refinance and purchase activity declining.

Market Composite Index (mortgage loan application vol) – wk ending 24 Jul 2020: -0.8% versus the week prior.

Refi's declined by -0.4% versus the week prior but were still +121% above the same week a year ago.

Purchase Index (a measure of completed loans and future home sales) declined by -2% versus the week prior.

> "Homebuyers stepped back slightly, and there was a larger drop in purchase application volume for FHA, VA, and USDA loans. This trend, along with the fact that average loan sizes are increasing, indicate that prospective first-time buyers are being impacted more by the rising economic stress caused by the resurgence in COVID-19 cases, as well as the uncertainty on how the next round of government support will take shape."

https://www.mba.org/2020-press-releases/july/mortgage-applications-decrease-in-latest-mba-weekly-survey-x271265

US FOMC Rates Decision – 29 Jul 2020

There were no changes made to monetary policy settings. Several programs were extended - the temporary US dollar swap lines, the repo agreement facility for foreign and international monetary authorities, and the Federal Reserve lending facilities.

The FFR target range remains at between 0% - 0.25%.

Developments

While economic activity and employment have improved somewhat, both remain well below the pre-pandemic levels.

> The recovery in household spending also likely owes to federal stimulus payments and expanded unemployment benefits, which provided substantial and timely support to household incomes. In contrast, indicators of business fixed investment have yet to show a recovery.

The path of recovery will depend on the course of the virus.

> The ongoing public health crisis will weigh heavily on economic activity, employment, and inflation in the near term, and poses considerable risks to the economic outlook over the medium term.

In his press conference, Chairman Powell noted the work of the Fed and used the opportunity to nudge the Federal government for its role in fiscal support:

> The path forward will also depend on policy actions taken at all levels of government to provide relief and to support the recovery for as long as needed.

Current Settings

The FOMC will maintain current levels of accommodation – enabling the flow of credit to households and business:

> "….over coming months the Federal Reserve will increase its holdings of Treasury securities and agency residential and commercial mortgage-backed securities at least at the current pace to sustain smooth market functioning, thereby fostering effective transmission of monetary policy to broader financial conditions."

Given the high level of uncertainty in the outlook, the FOMC will maintain the current level of accommodation and adjust and provide additional accommodation if required.

> The Committee will continue to monitor the implications of incoming information for the economic outlook, including information related to public health, as well as global developments and muted inflation pressures, and will use its tools and act as appropriate to support the economy.

Forward Guidance

From the statement, its clear that the FOMC is not considering any changing/tightening of policy. Some of the uncertainty around the pandemic would also likely need to be removed before the Fed would be confident that the economy was on the road to recovery. We are not close to that situation yet.

> The Committee expects to maintain this target range until it is confident that the economy has weathered recent events and is on track to achieve its maximum employment and price stability goals.

https://www.federalreserve.gov/newsevents/pressreleases/monetary20200729a.htm

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

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Europe

Eurozone CPI – Prelim (Jul)

There was a small acceleration in the headline CPI growth in Jul as more restrictions across member countries continued to be lifted. Annual growth overall remains muted due to the impact of lower energy prices.

Euro Area All Items CPI – annual change; Jul +0.4% versus Jun +0.3%

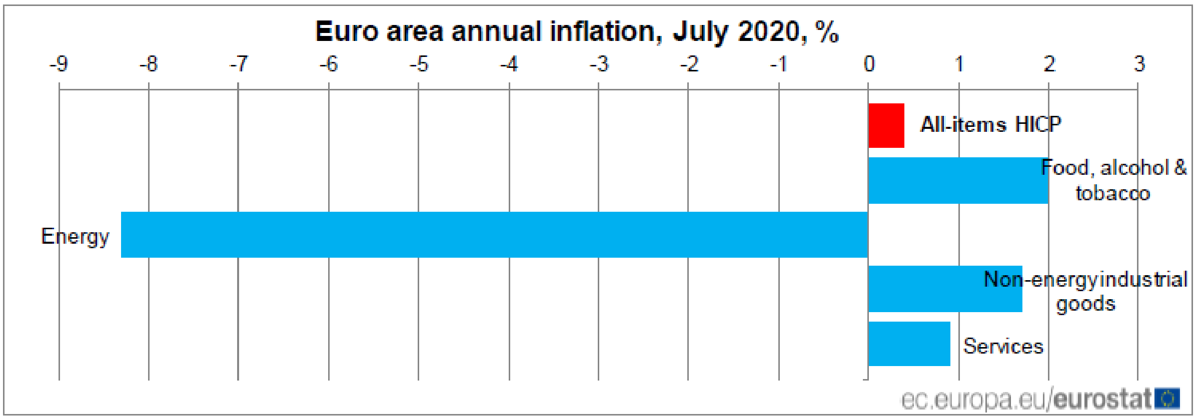
A year ago, the headline CPI growth was +1%.

The largest impact was energy prices. On an annual basis, energy prices declined by -8.3% in Jul – a slower pace of decline in Jun. In the month of Jul, energy prices increased by +0.6%.

The impact of lower energy prices is large: all items CPI ex energy is growing at a much higher rate of +1.4% and this is above the year ago annual rate of +1.1%.

The growth in food, alcohol, and tobacco prices eased this month from +3.2% in Jun to +2% in Jul. Notably, the growth in prices for unprocessed food eased and declined by -2.9% in the month of Jul.

Services price growth – the largest weight item in the index, eased somewhat in Jul to +0.9% after consistent annual growth of +1.2%.



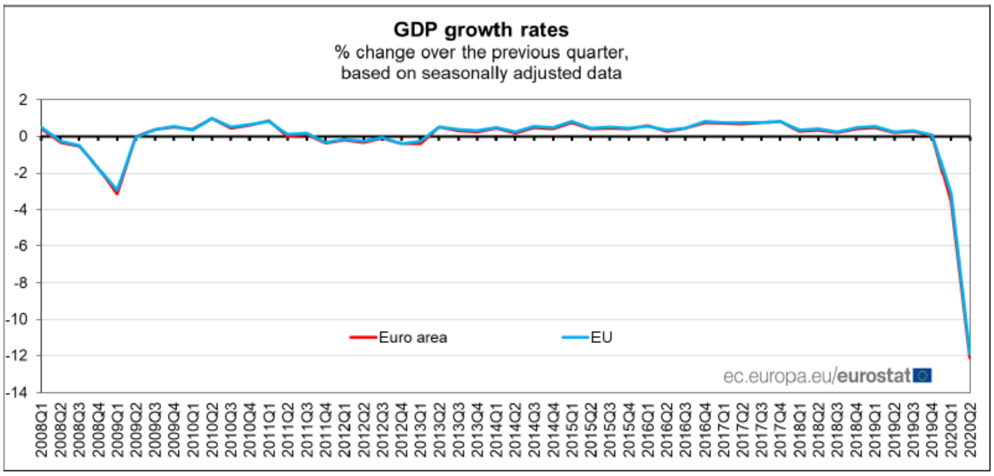
https://ec.europa.eu/eurostat/documents/2995521/11156763/2-31072020-AP-EN.pdf/c033a89c-da21-8888-d9a1-3bc1d0ce1a6f

Eurozone GDP Q2 – Prelim

Output across the Eurozone declined severely in Q2 after also declining in Q1. The second quarter encompassed the peak lock-down (Apr) as many member states were in the process of containing Covid-19 infections.

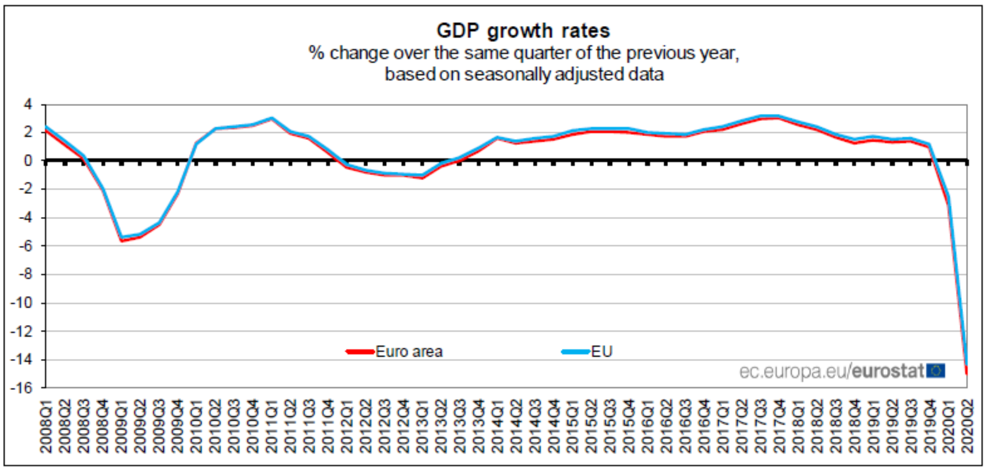
Eurozone Headline Real GDP – quarter % chg: Q2 -11.9% versus Q1 -3.2%

Declines were severe across several of the larger economies: Spain (-18.5%), France (-13.5%), Italy (-12.4%), and Portugal (-14.1%). The decline in German GDP was -10.1%.



On an annual basis, GDP also decline severely:

Eurozone Headline Real GDP – annual % chg: Q2 -14.4% versus Q1 -2.5%



https://ec.europa.eu/eurostat/documents/2995521/11156775/2-31072020-BP-EN.pdf/cbe7522c-ebfa-ef08-be60-b1c9d1bd385b

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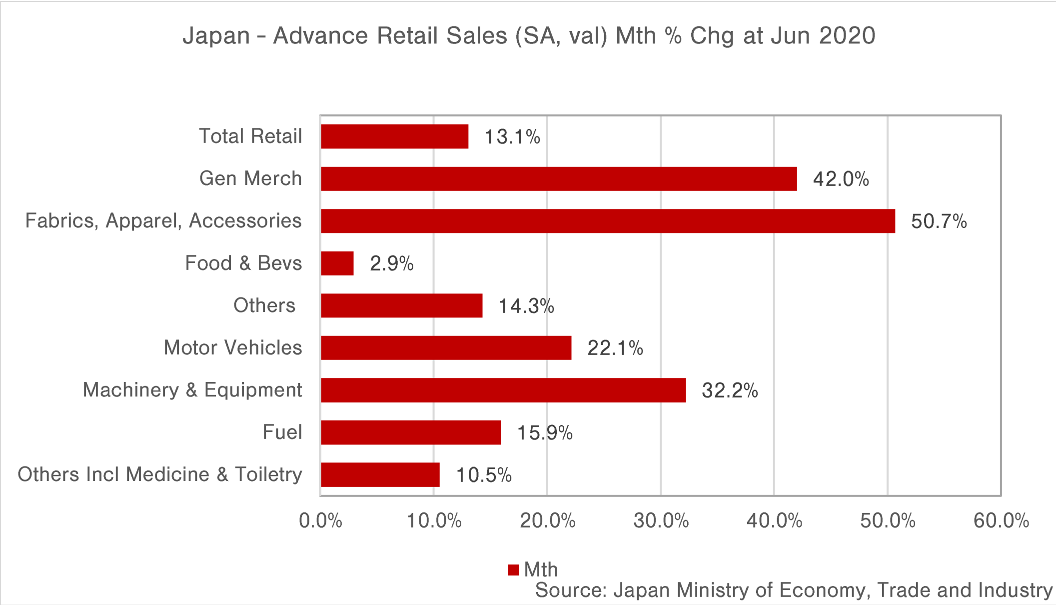
Japan

Retail Trade (Jun)

There was a stronger recovery in retail sales in Jun with all retail segments contributing to growth this month.

<u>National Retail Sales (SA, Val) – month change:</u> Jun +13.1% versus May +2%



While there was stronger growth in the month across all categories, sales are still below a year ago across some of the larger segments.

Motor vehicle sales were +22% in Jun but are still 18% below a year ago.

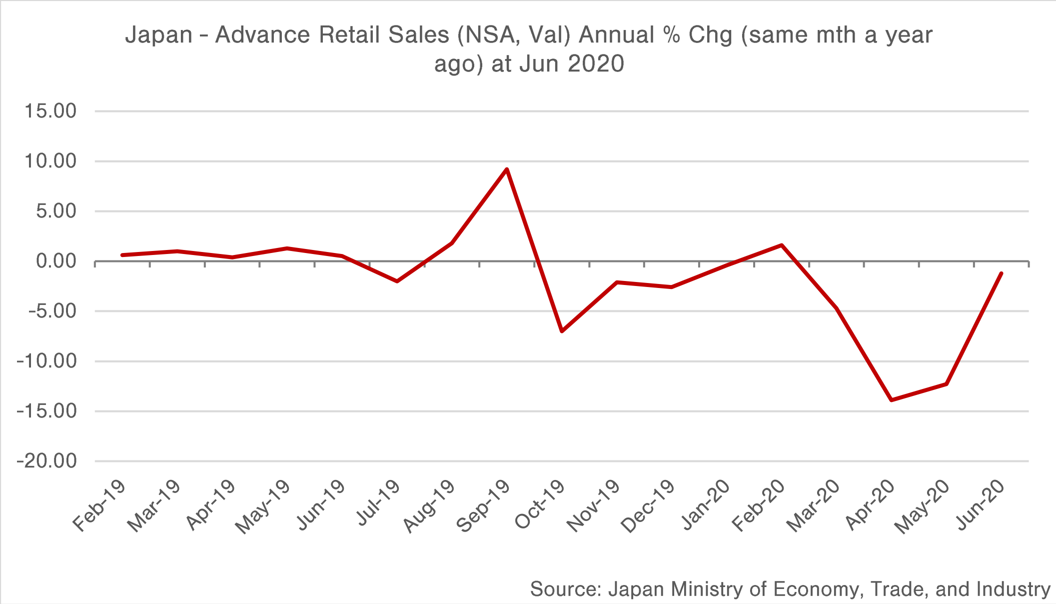
General Merchandise sales increased by +42% in Jun but is still -10% below a year ago.

Fabric and apparel sales were +50% in Jun but are still 4% below a year ago.

Segments such as Food & Bev sales grew at a 'slower' pace of +2.9% in Jun but are +4% ahead of a year ago.

Machinery & equipment sales remain strong at +32% in Jun and are +20% ahead of a year ago.

On an annual basis, total retail sales are now 'only' 1.2% below the same month a year ago. There has only been one month since Oct 2019, when retail sales were ahead of the same month a year ago (Feb 2020).



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

Industrial Production Prelim (Jun)

There was a small increase in production and a larger increase in shipments this month. This is broadly consistent with the Jun PMI indicating that slightly more firms were reporting higher output.

Inventory of finished goods continued to decline in the month. The inventory ratio of finished goods also declined but remains extremely elevated at a total level.

The forecasts are for much stronger growth in production for Jul. The Jun survey forecast a +9.2% increase in Jul, and the Jul survey has upgraded that forecast to +11.3%.

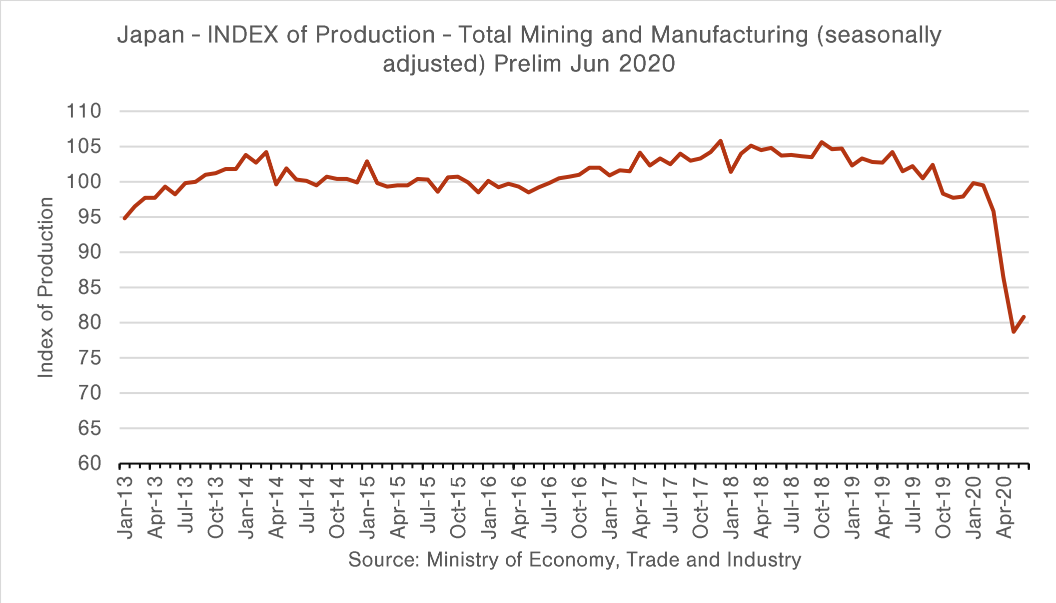
> Industries that mainly contributed to the increased in July: 1.Transport equipment, 2.Electrical machinery and Information and communication electronics equipment, 3.Chemicals, in that order.

This month there was further growth in the production and shipments of motor vehicles, while inventory declined. Improving domestic demand will help (see above).

The production and shipments of iron, steel, and non-ferrous metals continued to decline, and the inventory ratio of finished goods reached a new extreme high.

<u>PRODUCTION TOTAL MINING AND MANUFACTURING (SA) – MONTH CHANGE</u>: Jun +2.7% versus May -8.9%

The lift in Jun of +2.7% is quite low, especially given the context of the decline:



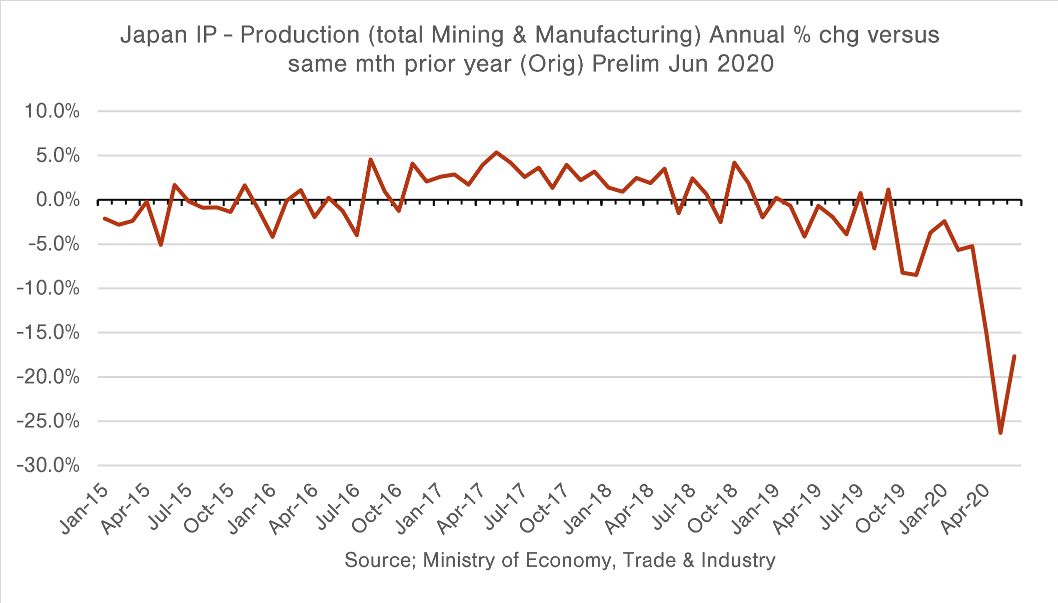
Production increased across most categories, but was led higher by a 23.7% increase in transport equipment for the month. Production of motor vehicles increased for the first time in four (4) months by +29%. The production level for motor vehicles is still -41% below the same month a year ago.

The production of production machinery was also higher this month by +10.2% - and production was higher across most production machinery subsegments.

Of note was that production continued to decline for iron, steel, and nonferrous metals by - 1.2% versus the -14% decline in May.

Low production growth was recorded across the other larger industries: fabricated metals (+0.3%), general-purpose and business machinery (+0.4%), and electronic parts and devices (+0.3%).

On an annual basis (NSA), production levels were -17.7% below the same month a year ago versus -26.3% in May:



<u>SHIPMENTS MINING AND MANUFACTURING – MONTH CHANGE</u>: Jun +5.2% versus May -8.9%

There was a larger rebound in shipments this month (compared to production growth).

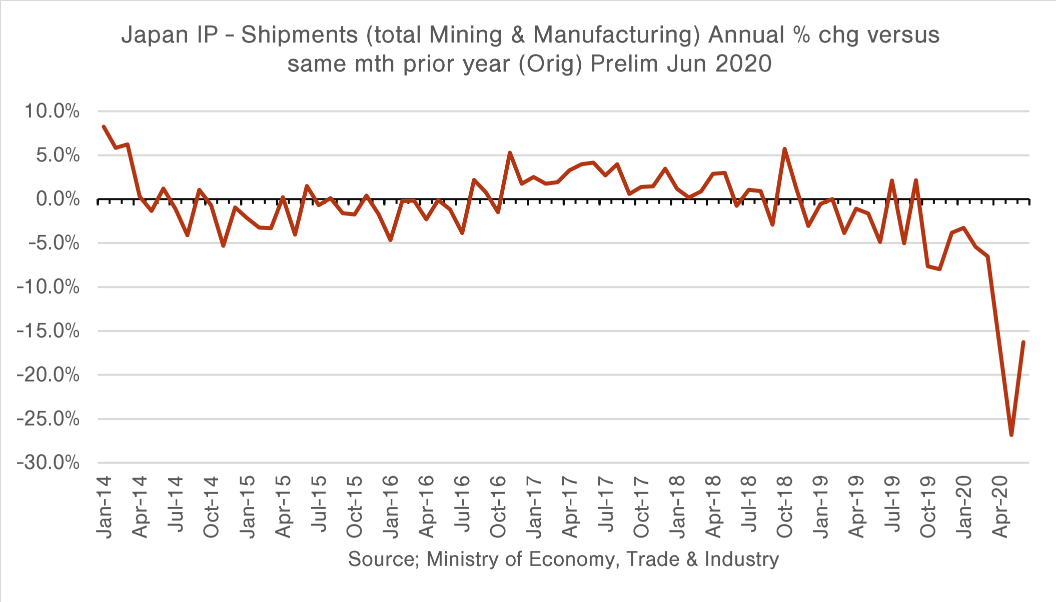
This was led by transport equipment +31.4% growth in shipments for the month. Motor vehicle shipments increased by 22.5% in the month.

Shipments of production machinery were also stronger at +11.2% in Jun versus -12.3% in May.

Further declines in shipments were recorded across iron, steel, and non-ferrous metals (-2.5% in Jun versus -16.1% in May) and electronic parts shipments declined by -3.3% in Jun versus -3.9% in May.

Other industries recorded moderate growth in shipments for the month: fabricated metals (+2.4%) and general purpose and business machinery (+4.2%).

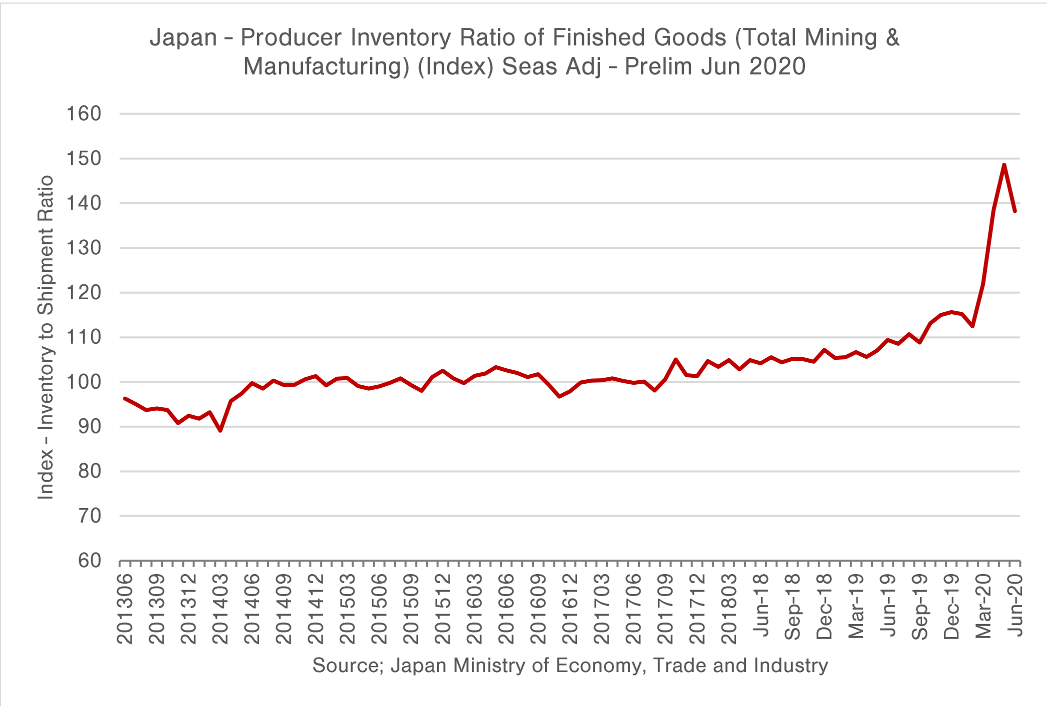
On an annual basis, shipments were -16.3% below the same month a year ago, which was an improvement from the trough in May of -26.8%.



<u>INVENTORY MINING AND MANUFACTURING – MONTH CHANGE</u>; Jun -2.4% versus May -2.6%

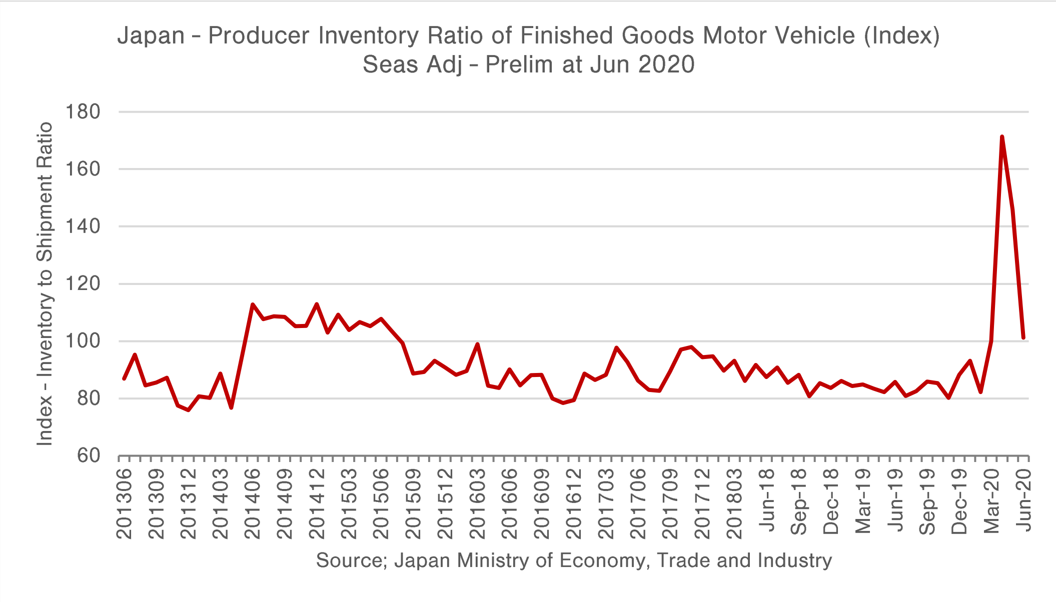
Producers inventory of finished goods continued to decline in Jun. The inventory of finished goods declined across all industries this month. But it is the inventory ratio that is more insightful this month.

The inventory ratio of finished goods was slightly lower than the prior month as shipments started to grow again this month. But the overall level of the inventory ratio remains elevated:



Iron, steel, and non-ferrous metals is the largest weight of the inventory index and inventory declined by -1.7% in Jun. Inventory is now 32% below the same month a year ago. But the inventory ratio of iron, steel, and non-ferrous metals reached a new high this month – reflecting the weaker/declining shipments.

Inventory of transport equipment declined by -14% in Jun after a -30% decline in May. The inventory of finished goods of motor vehicles declined further by -13% after a -31% in May. The inventory ratio of finished goods recorded another sharp decline and is now much lower – due to the increase in shipments. With inventory ratios slowly returning to more moderate levels, it will likely continue to support further production growth (see Jul forecast).



The decline in inventory was smaller across several industries: general purpose and business machinery (-0.7%) and electrical machinery (-0.8%). The inventory ratio for both remains elevated but eased in the latest month.

On an annual basis, inventory of finished goods is -17.7% below the same month a year ago.

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

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Australia

CPI Q2

The headline consumer price index declined in Q2 – the largest quarterly % decline in the series history going back to the Dec quarter 1948. Prices also shifted to decline on an annual basis.

The main drivers of the sharp fall in prices in Q2 were related to 1) the provision of free childcare, 2) a fall in education prices related to free before and after school care (in NSW, VIC and QLD), and 3) the fall in the value of automotive fuel.

This quarter, the nature of the price declines shows just how much of a boost there was to household income during the community shutdown (government funded). Most of the measures supporting households during the initial Covid shutdowns will be reversed.

All Items CPI – quarter change: Q2 2020 -1.89% versus Q1 2020 +0.34%

The decline of -1.89% in the Jun quarter is the largest in the series going back to the Dec quarter in 1948. While most categories contributed to the decline in prices this quarter, the largest contributors were:

Household Services: the childcare component detracted -1.32% pts from the headline qtr decline.

Transport: motor fuel detracted -0.79%pts from the headline qtr CPI change.

To a lesser degree, housing also contributed to the record fall this month. Utilities prices declined – via the provision of rebates in some capital cities. Rents fell by -1.3% contributing -0.1% pts to the headline decline. This was the first quarterly fall in rents since 1927.

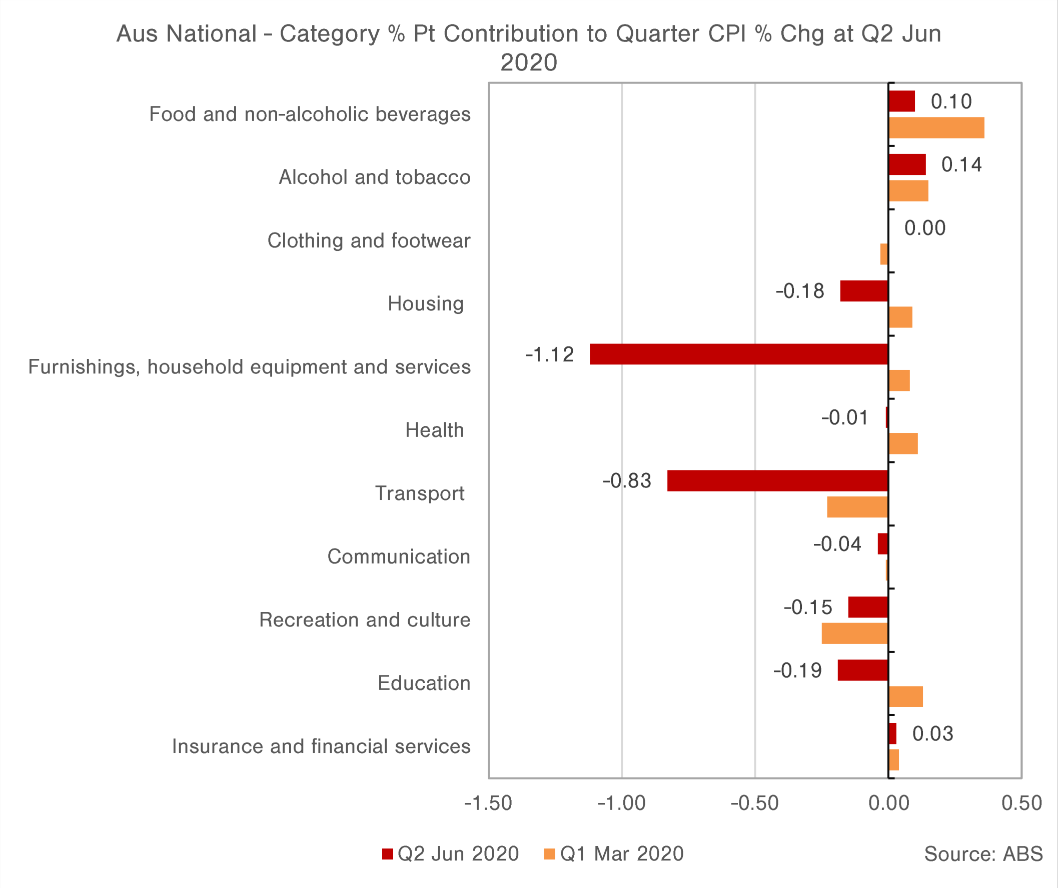
> Weak rental market conditions as a result of COVID-19 lockdown restrictions and rising vacancy rates saw rents fall in most capital cities in the June quarter.

Education prices also contributed to the headline decline with the provision of free before and after school care and free preschool for the second term.

Only food and alcohol prices increased this quarter. Food price growth slowed but remained positive.

> High demand saw a reduction in specials and genuine price increases on a range of long-life products such as canned tuna and canned meat, rice and pasta.

> Improved weather conditions saw a range of fresh produce return to typical seasonal prices, while mince meat saw temporary discounts.



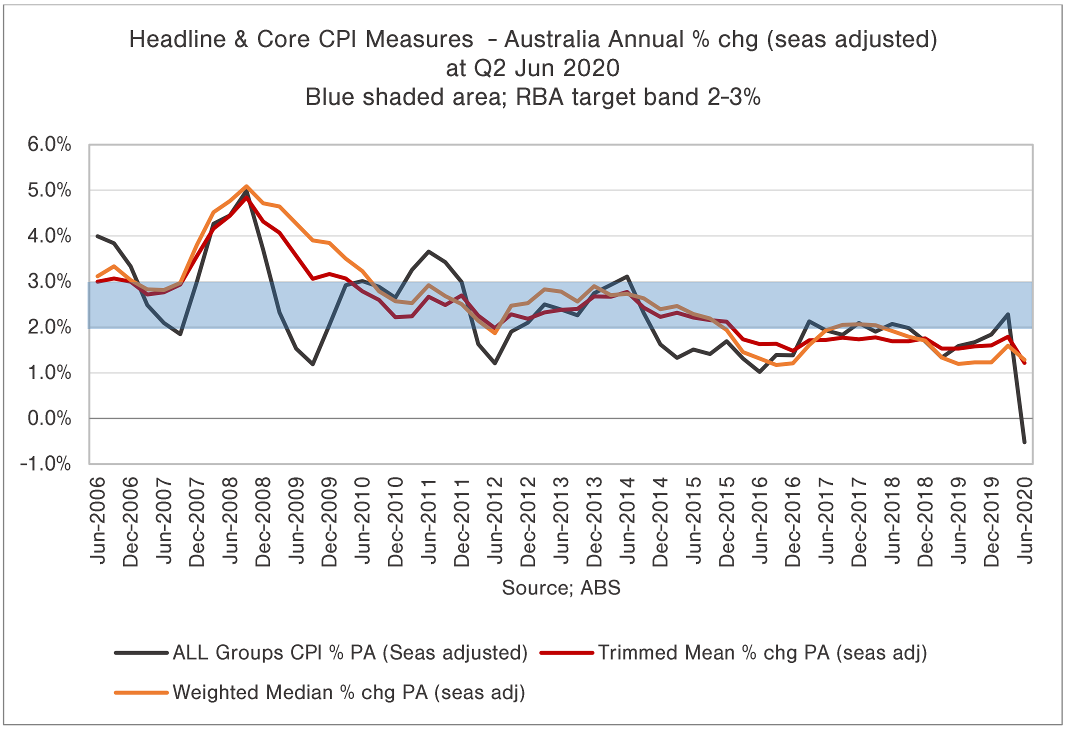
<u>All-Items CPI – annual change</u>: Q2 -0.35% versus Q1 +2.19%

Measures of annual growth in core CPI did not decline, but growth did slow (core CPI was slightly negative quarter on quarter).

Trimmed mean CPI – annual change: +1.2% in Q2 versus +1.8% in Q1

Weighted median CPI – annual change: +1.3% in Q2 versus +1.6% in Q1

All measures are well outside of the RBA 2-3% target band.



https://www.abs.gov.au/AUSSTATS/abs@.nsf/Latestproducts/6401.0Main%20Features1June%202020?opendocument&tabname=Summary&prodno=6401.0&issue=June%202020&num=&view=

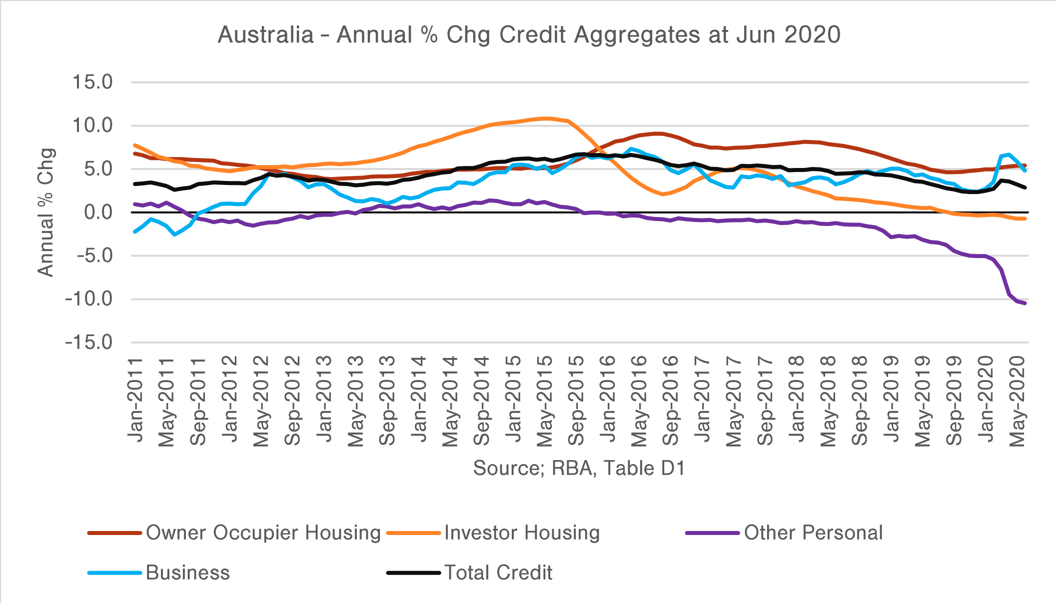
Private Sector Credit (Jun)

The growth in total outstanding private sector credit slowed further in Jun. This was led by a further slowdown in the growth of business credit, investor, and other personal credit. Outstanding credit for owner occupiers continued to grow at constant annual pace.

Firms are facing highly uncertain times related to the virus and future outbreaks. High credit growth in Mar for business credit (+3% in the month) was likely to help firms bridge the gap of the broader community lock-down – for a limited time. Firms may be now less willing to take on more credit given heightened uncertainty about the ability to control infections without severe lockdowns – i.e. the current outbreak in infections throughout Victoria (one of the two most populous states).

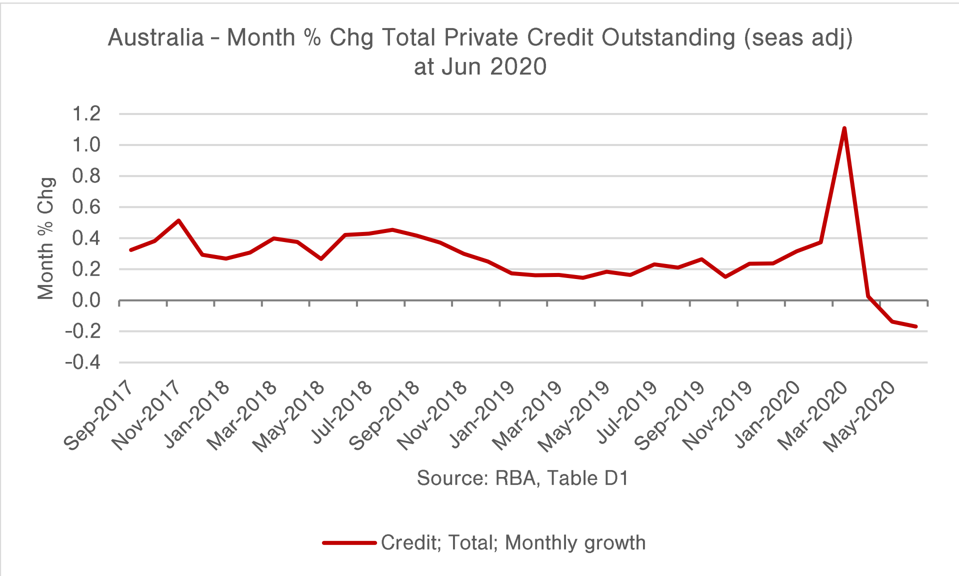
The next question is whether household credit will be affected? Owner occupier lending remains strong. But households have already been reducing personal credit and now at an accelerated pace. Lending for investment properties was already weaker prior to the pandemic. Mortgage lending overall will likely remain unclear until after mortgage payment forbearance programs expire.

<u>Outstanding Private Credit – annual change</u>; Jun +2.9% versus May +3.2%



The recent increase in private credit was led by business (likely) drawing down on lending facilities to bridge the period of community lockdowns back in Mar/Apr (in Mar business credit outstanding increased by 3% in a month).

This is visible on a month by month chart – and overall credit growth has declined since then. In Jun versus May, outstanding credit declined by -0.2%.



The main driver of the decline in the month has been a decline in the value of outstanding business credit, which fell by -0.8% in Jun and has declined now for the last two months. The outlook for many firms is still highly uncertain, especially given the renewed outbreak in infections in Vic and given that many restrictions on trade remain in place (esp for hospitality) across all states.

Investor credit has also been declining on a monthly and annual basis.

Owner occupier mortgage credit outstanding continues to grow at around +5.4%. There was no change on a monthly basis in Jun.

The level of outstanding ‘other personal’ lending continues to decline at an accelerated pace.

https://www.rba.gov.au/statistics/frequency/fin-agg/2020/fin-agg-0620.html

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Trade

US-China Trade Talks

Relations between the US and China remain tense. Attempts to de-escalate the situation (US Defence Secretary Mark Esper suggesting a meeting by the end of the year after Chinese Foreign Minister Wang Yi called for a reopening of channels of dialogue).

> But Wang's conciliatory posture, rather rare in recent months, was met with **an increasingly impatient, hostile administration under embattled US President Donald Trump, who was eager to get tougher on China to revive his imperilled re-election bid**. https://www.scmp.com/news/china/diplomacy/article/3095498/china-us-relations-why-wang-yi-went-back-wolf-warrior-mode

Tensions have been rising over several issues:

> President Donald Trump's administration has clashed repeatedly with Beijing over trade and the coronavirus pandemic, as well as China's imposition of a controversial new security law in Hong Kong. https://www.bbc.com/news/world-asia-china-53522640

> In the weeks leading to the consulate closures on both sides, which Beijing lamented as "unprecedented escalation", Washington significantly piled pressure on Beijing, with muscle-flexing in the disputed South China Sea, sanctions on Hong Kong and Xinjiang and its warming ties with Taiwan. https://www.scmp.com/news/china/diplomacy/article/3095498/china-us-relations-why-wang-yi-went-back-wolf-warrior-mode

A recent speech by US Secretary of State, Mike Pompeo had added further to tensions - "Communist China and Free World's Future" https://www.state.gov/communist-china-and-the-free-worlds-future/

The Chinese foreign ministry denounced the speech:

> "Pompeo made a speech in which he made a malicious attack on the Chinese Communist Party," Mr Wang said, adding: "To this, China expresses strong indignation and resolute opposition." https://www.bbc.com/news/world-asia-china-53522640

It has been unofficially observed that there was a low chance of a phase two trade deal being completed between the US and China. That position has been made somewhat more official:

> President Trump damped expectations for a promised phase-two trade pact with China on Friday, saying the relationship between the countries has been too badly damaged by the coronavirus pandemic.

> The economic fallout from the pandemic also made it increasingly unlikely that China would meet its targets for expanded purchases of U.S. goods under the

phase-one deal, fueling further doubts about prospects for new talks. https://www.wsj.com/articles/trump-pessimistic-on-phase-two-china-trade-deal-11594400326

It was only recently that USTR Lighthizer acknowledged the second phase of the trade deal in testimony to the House Ways & Means Committee (Jun 2020). https://waysandmeans.house.gov/sites/democrats.waysandmeans.house.gov/files/documents/HWMCTestimonyon2020TradeAgenda-Final.pdf

As a part of the push to localise production, the US is considering further stimulus 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

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

BREXIT

A new timetable for talks has been announced, with the final deadline aiming for a round of talks in Brussels on 2 Oct. https://www.business-standard.com/article/international/britain-european-union-set-new-timetable-of-meetings-for-post-brexit-deal-120080100099_1.html

The latest round of negotiations last week yielded little, if any, progress:

The two sides completed their latest round of negotiations in London on Thursday without being able to agree on the basic outlines of a deal to reassure businesses about the future, which Boris Johnson had said in June should be possible. https://www.theguardian.com/politics/2020/jul/24/germany-calls-on-uk-show-more-realism-brexit-negotiations

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

The face to face negotiations have so far not appeared to make much progress. 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

The following trade items have recorded no change in status:

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

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