MARS CAPITAL PARTNERS

Weekly Macro Review

w/c 28 September 2020

Key Themes

Data this week indicated some slowdown in the momentum of the US economic rebound.

There was a notably slower pace in the rebound of non-farm payrolls in Sep. In the last five months (May-Sep), there have been 11.417m jobs recovered in the US. A large deficit of -10.734m jobs remains – and this just accounts for the number of jobs lost during Mar and Apr.

The slower employment growth was mirrored by the employment report from the Household Survey. The decline in the unemployment rate was the result of a fall in participation. The number of permanent layoffs has continued to increase (but remains well down on the GFC). Employment growth slowed more substantially in Sep and most of the employment growth was part-time in nature. The employ to population ratio has increased from the Apr low of 51.3% to 56.6% in Sep (only slightly higher than in Aug). *The last time in history when the employment to population ratio was this low was back in Feb 1976.*

Initial claims were little changed in the latest week – still around the 1.4m level for both state and federal programs. But California has put its reporting on hold to clear the backlog of claims and application modifications – so data reflects last week data for California.

Income and disposable personal income declined in Aug. The decline was the result of a large fall from the expiration of the $600 additional payment on 31 Jul. Employee compensation growth was consistent compared to Jul but there was no acceleration in compensation growth. Expenditures increased at a slower pace. Given the decrease in disposable income, the level of savings fell by 23% compared to Jul. The saving rate is still almost double that of Jan levels.

Without extension of stimulus or benefits, further reductions in transfer payments will commence from late Dec as 39 weeks of PUA starts to expire. Another wave of reductions will likely start from Mar 2021 (26 weeks of state unemployment, 13 weeks of extended benefits, and 13 weeks of PEUC).

The annual PCE inflation rate increased at a faster pace in Aug. The core measure, excluding food and energy, indicates faster growth in underlying consumer prices of +1.8%. This acceleration will be important to watch, especially given the Fed average target of 2%.

Consumer sentiment firmed in the second half of Sep. This improvement was led mostly by higher income households. Levels remain well below those recorded at the start of the year.

There was some indication of slowing momentum in manufacturing growth. The headline ISM manufacturing PMI indicated that the pace of growth recorded in Aug was mostly maintained in Sep. Across key demand indicators, firms were reporting slower growth from the prior month. Of note was the slower pace of growth in new orders. The proportion of firms reporting higher/growth in new orders (compared to the prior month) has been falling and, in Sep, the number of firms reporting higher orders, was the lowest in the last four months. More firms also started reporting a decline in new orders. This will likely have implications for the pace of growth in production growth in the short-term. The production index also points to some levelling out of the growth momentum.

The US Markit PMI indicated a similar pace of growth in activity compared to the prior month – which remained moderate overall.

Outside of the US, the one highlight in the growth story was Germany. The increase in German manufacturing activity was a key driver of the overall improvement in the Eurozone manufacturing PMI.

The prelim annual Euro area CPI continued to decline in Sep by -0.3%. The month on month pace though remained positive at +0.1%. The main contributor to the annual decline was the continued fall in energy prices and price growth also slowed across services and non-energy industrial goods.

Retail sales in Japan rebounded in Aug but remain below a year ago. Manufacturing production continued to improve. The rebound in production remains uneven and led by a small group of industries. Most industries continued to record declines in finished goods inventories for the month of Aug.

Contents

US Data

Non-Farm Payrolls and Employment (Sep)

NON-FARM PAYROLLS (SEP)

Non-farm payrolls continued to increase this month, albeit at a notably slower pace.

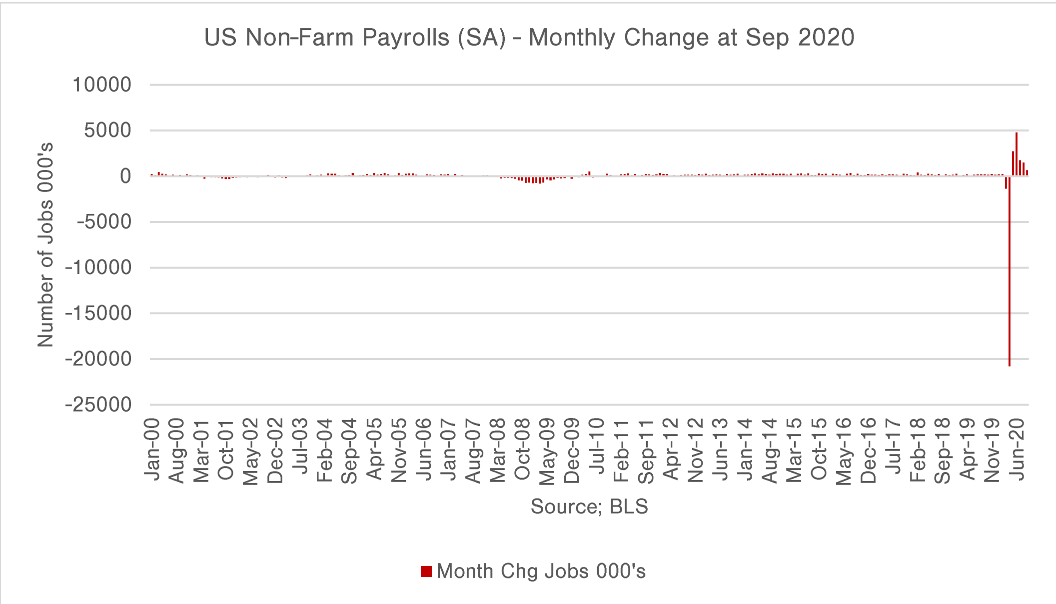
The increase in private sector jobs (mostly due to a continued rebound in service payrolls) was unfortunately partly offset by a fall in government payrolls (led by a decline in state and local education).

US Non-Farm Payrolls – month change: Sep +661k persons versus Aug 1.489m persons

The Aug figure was revised higher by +118k persons from the Aug release.

The overall increase in private sector non-farm payrolls was +887k persons this month. The total payrolls number was dragged lower by a reduction in government payrolls of -216k persons. Most of this was a reduction in state and local education payrolls.

In the private sector, most of the increase in payrolls was led by leisure and hospitality of +318k payroll jobs. Private services payrolls increased by +784k jobs whereas private goods-producing jobs increased by +93k.



The rebound in payrolls overall is slowing though. The decline in payrolls during Mar & Apr 2020 totalled 22.16m jobs. In the five months since then (May-Sep), there has been an increase of 11.417m jobs. A large deficit of -10.734m jobs remains – and this is just the deficit of the jobs lost during Mar and Apr.

HOUSEHOLD SURVEY – EMPLOYMENT

This month, employment growth slowed notably. Most of the growth that was recorded in Sep was part time employment (still better than the alternative of no employment). The much larger decline in total unemployed persons was the result of a further decrease in labour force participation. This resulted in a larger decrease in the unemployment rate for Sep.

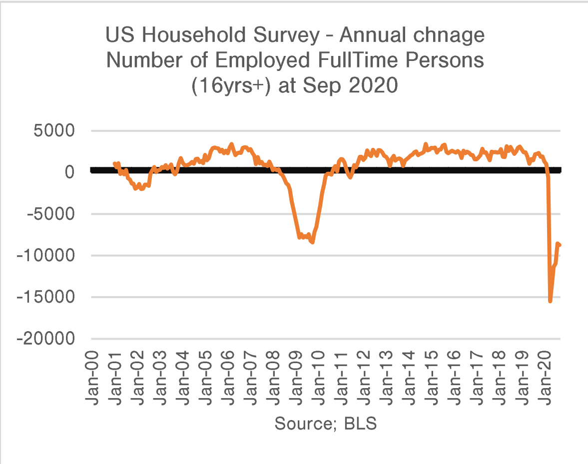
Total Employed Persons

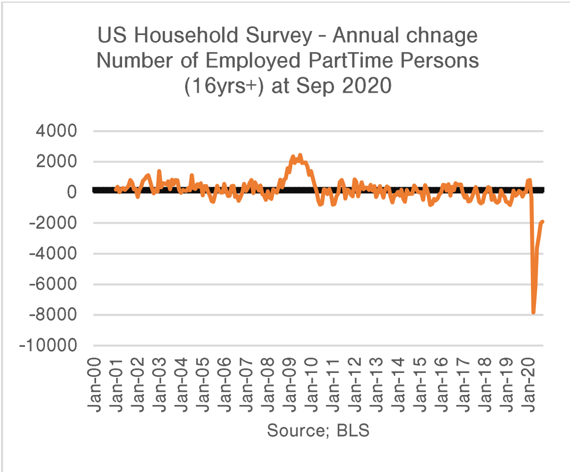
Total employed persons – month change: Sep +275k persons versus Aug +3.756m persons

The +275k growth in employment this month was made up of:

Full Time (FT) employed persons – month change: Sep +54k persons versus Aug +2.837m persons. The rebound in FT employment is extremely slow and is still -8.7m below the same month a year ago (from -15.5m at the worst level in Apr 2020).

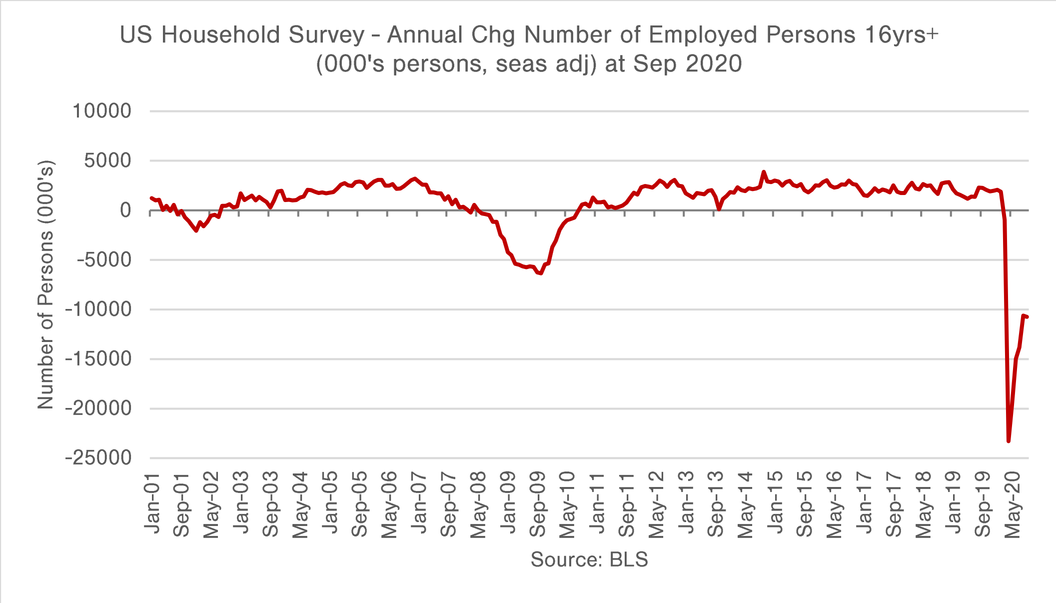
Part Time (PT) employed persons – month change: Sep +188k persons versus Aug +991k persons. The rebound in PT employment has been faster, with the Sep level -1.9m below the same month a year ago (-7.8m at the worst level in Apr).





One of the key differences between this recession and 2008/09 is that many FT jobs were replace by PT employment. This time, both forms of employment were impacted due to shutdowns.

On an annual basis, the total number of employed persons remains -10.7m below the same level from a year ago.

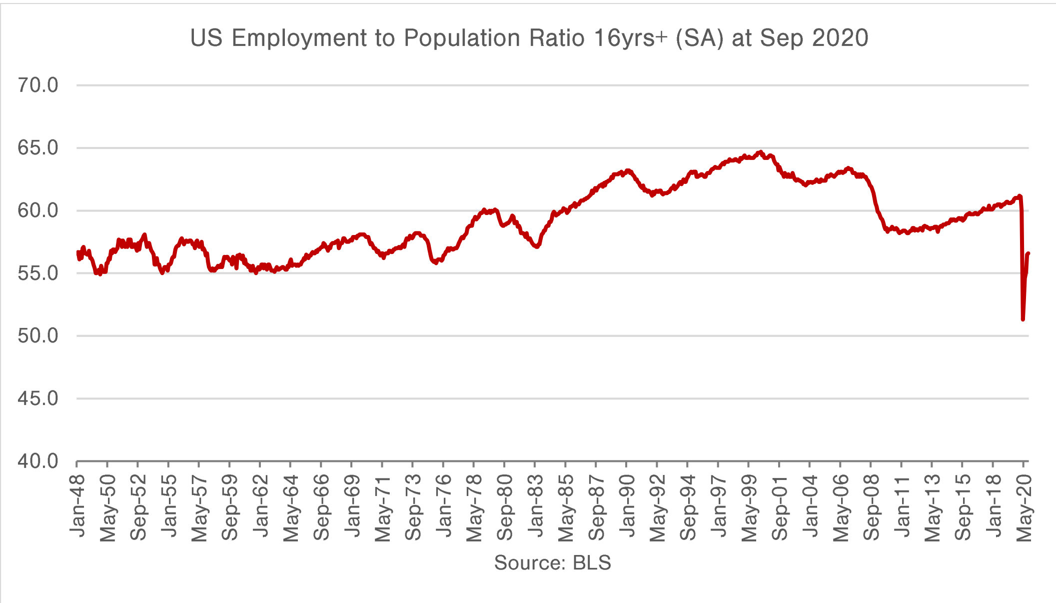


One of the more important measures of the employment level (to aid in comparison across time due to population growth) is the employment to population ratio.

Since the National lock down was lifted, the employment to population ratio has increased from a low of 51.3% in Apr to 56.6% in Sep. The Sep result increased slightly from 56.5% in Aug.

The last time in history when the employment to population ratio was this low was back in Feb 1976.

Note that employment levels as a % of population (for 16yrs+) never recovered the pre-2008/09 levels – or the pre-2000 levels either. The most recent peak was 61.2% in Jan 2020.

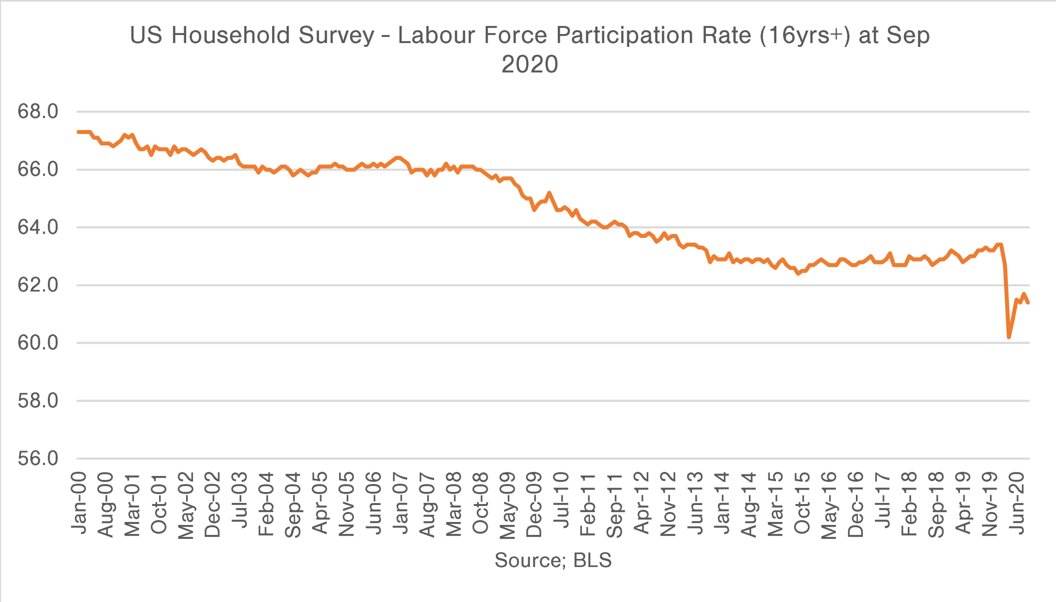


Labour Force

Labour Force – month change: Sep -695k persons versus Aug +968k persons

The decline in the labour force was the result of much slower growth in the estimate of what population adds to the labour force (+87k persons) and a decrease in participation which resulted in approx. 782k persons leaving the labour force.

The labour force participation rate fell from 61.7% in Aug to 61.4% in Sep.

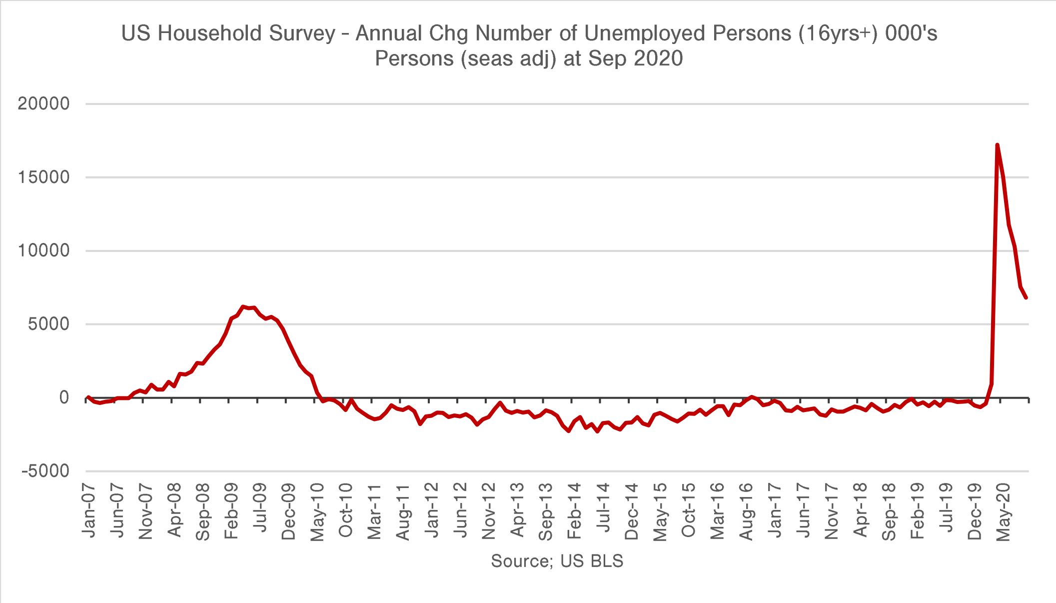


Total Unemployed Persons

With the decline in participation (and the labour force), total unemployment declined in the month.

Total unemployed persons – month change: Sep -970k persons versus Aug -2.8m persons

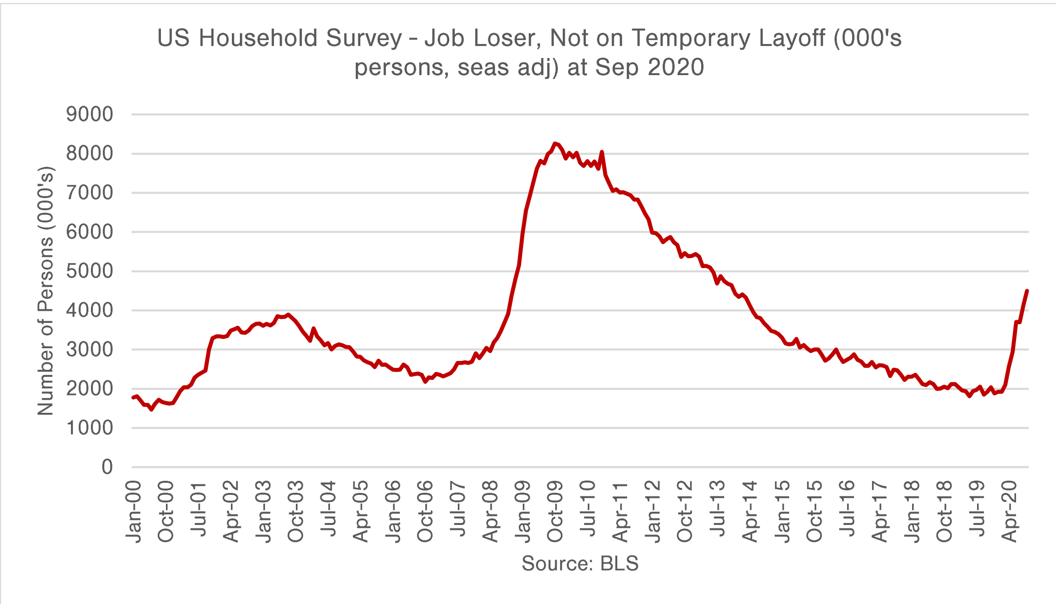
The total number of unemployed persons remains +6.8m above the same time a year ago. The Household Survey has total unemployed persons at 12.58m people in Sep 2020.



The unemployment rate declined from 8.4% in Aug to 7.8% in Sep.

The unique nature of this recession is that many workers were able to be placed on a temporary layoff. Some of these temporary layoffs are now turning into permanent layoffs.

Job losers on a temporary layoff slowed from 6.2m people in Aug to 4.6m in Sep. But those no longer on a temporary layoff increased from 4.1m in Aug to 4.4m people in Sep. The number of permanent losses has been increasing over the last four months – but is still well below the GFC peak.



Summary – Key Labour Market Indicators

000's people (16yrs+)	Annual chg - SEP 2020	Monthly Chg - SEP
The estimated change in the Labour Force due to pop growth (1)	787	87
How many jobs available for them? (employment growth) (2)	- 10,735	275
Difference (if negative, then employment growing faster than what pop adds to the labour force) (3)	11,522	-188
Change labour force participation - (if positive, people entering/returning to the labour force) (4)	- 4,695	-782
The remainder is the chg in total unemployed persons (declining if negative) (4) plus (3)	6,827	-970
Two views of annual growth in the labour force;		
Total employed persons plus total unemployed persons	- 3,908	-695
Est of what population adds to the labor force plus change in participation	- 3,908	-695
BLS reported change in the size of the labour force	- 3,908	-695

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

Initial Jobless Claims (wk ending 25 Sep), Continuing Unemployment Claims (wk ending 18 Sep), and PUA Claims

One of the key points this week is that the state of California has paused the processing of initial claims as of 19 Sep to help clear the backlogs of claims and to implement fraud technology measures. This will cause some impact on the National data – as California represents the single largest proportion of continuing claims (2.8m people as of wk ending 19 Sep). Once the pause is over, data will be revised to reflect the level of claims for the week in which they were filed.

> Currently, the EDD has **a backlog of nearly 600,000 Californians who have applied for UI more than 21 days ago and yet their claims have not been processed, and an estimated 1 million cases where individuals received payments but subsequently modified their claim** and thus are awaiting resolution. https://www.edd.ca.gov/About_EDD/pdf/news-20-49.pdf

Total advance initial claims (NSA) for both State and Federal programs in the wk ending 26 Sep was still just above +1.4m people. This was on par with the week prior.

State and Federal programs ongoing claims (NSA) as of wk ending 12 Sep were up by over 400k people to 26,529,810 people.

STATE PROGRAMS

Advance Initial Claims wk ending 26 Sep 2020 (SA): 837,000 people (week prior 873,000 claims)

The NSA initial claims were lower for the wk ending 26 Sep: 786,942 claims (versus 827,205 claims in the wk prior)

Continuing Claims wk ending 19 Sep 2020 (SA): 11,7676,000 claims (versus 12,747,000 in the wk prior)

FEDERAL PROGRAMS (Pandemic Unemployment Assistance – PUA)

PUA Initial Claims wk ending 26 Sep (NSA): 650,120 (up from 615,599 in the week prior).

PUA Continuing Claims wk ending 12 Sep (NSA): 11,828,338 claims (up from 11,510,888 claims in the week prior).

Pandemic Emergency Unemployment Compensation wk ending 12 Sep: 1,828,370 claims (up from 1,631,645 claims in the week prior).

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

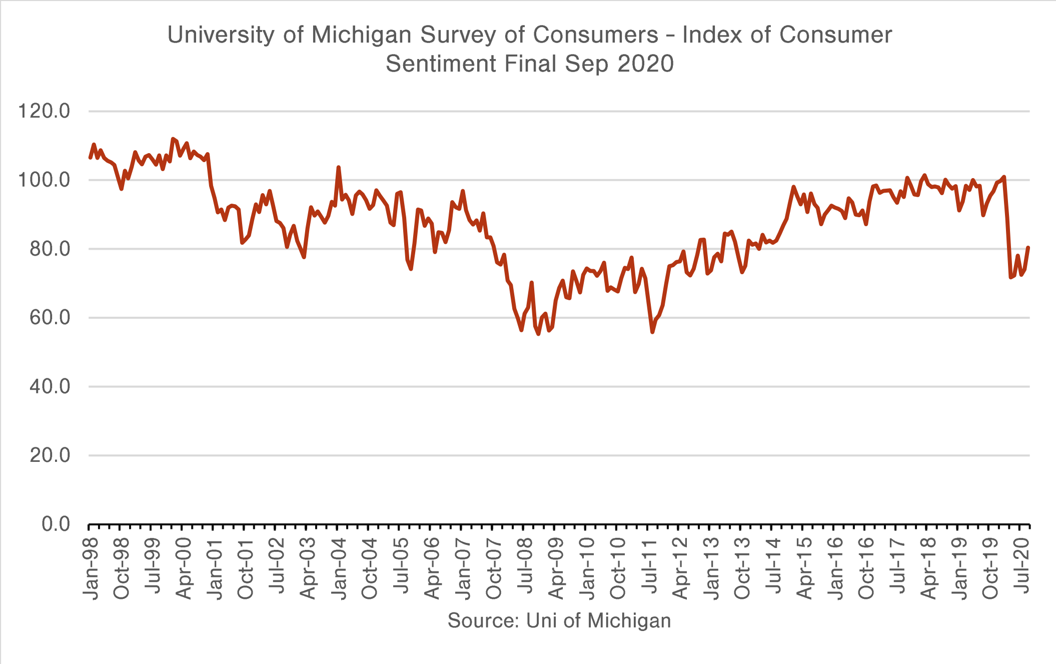
University of Michigan Consumer Sentiment Final (Sep)

Consumer sentiment continued to improve in the final half of Sep. All the main indexes recorded slightly higher readings in the second half of the month. The gains were led mostly by upper income households:

> The gains were mainly due to a more optimistic outlook for the national economy. While consumers have anticipated gains in the national economy ever since the April shutdown, **the September survey recorded a significant increase in the proportion that expected a reestablishment of good times** financially in the overall economy. The recent gains are encouraging even though they were **largely due to upper income households**. Indeed, the data indicate that lower income households face continued income and job losses compared with the modest gains expected by upper income households.

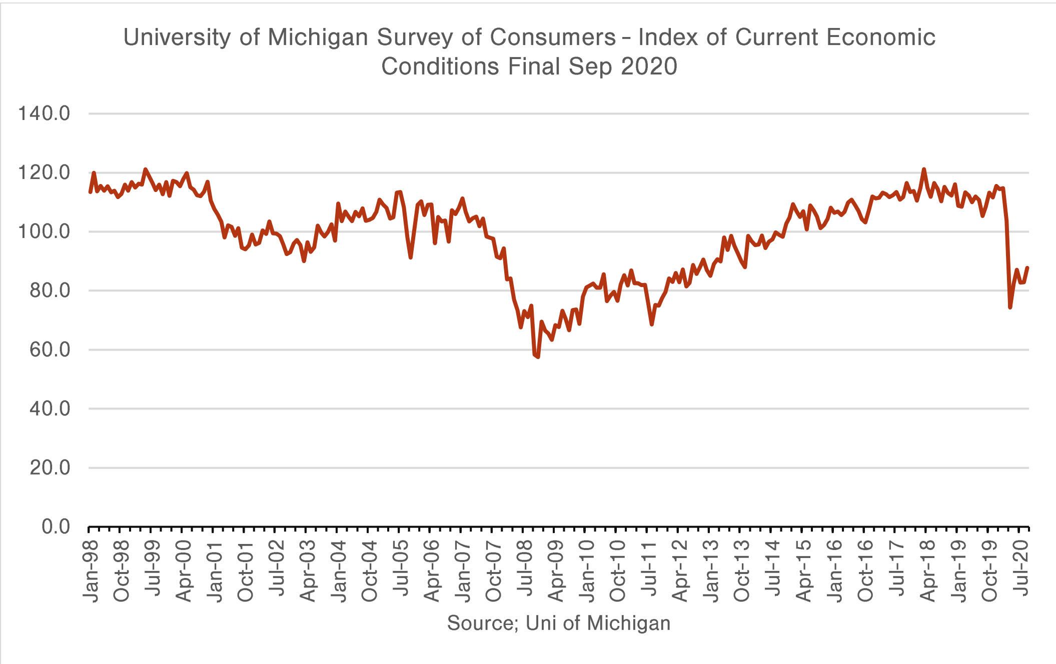
Index of Consumer Sentiment: Sep final 80.4 (78.9 in prelim) versus Aug 74.1

This was the highest reading of the last six months, but still below the peak of 101 in Feb 2020.



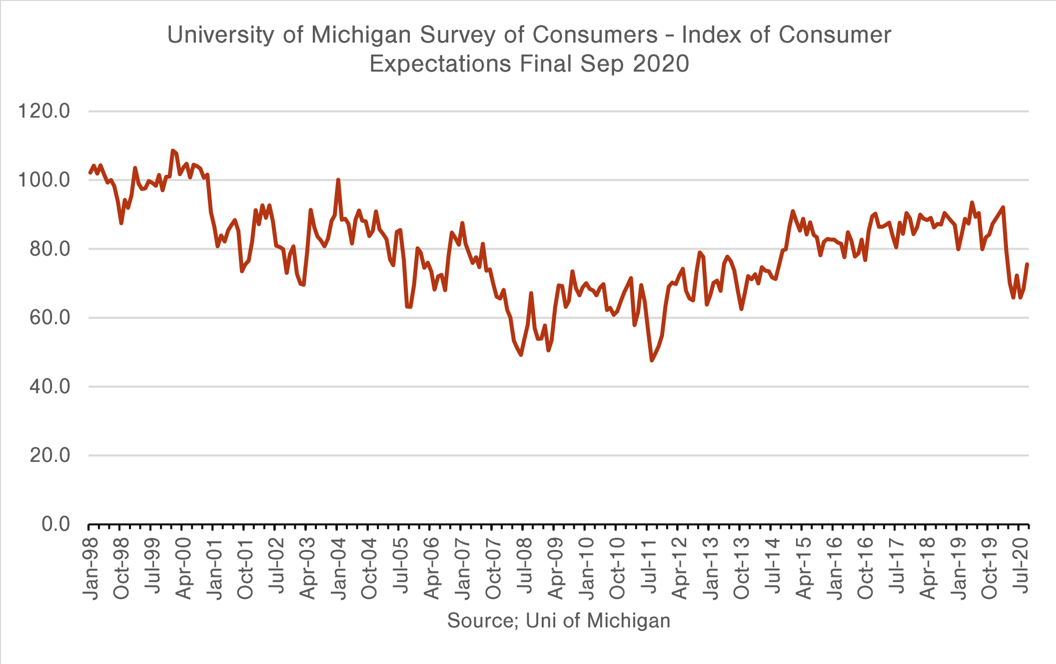
<u>Index of Current Economic Conditions</u>: Sep 87.8 (87.5 prelim) versus Aug 82.9

This remains well below the Dec 2019 level of 115.5 and the Mar 2018 peak of 121.2.



<u>Index of Consumer Expected Conditions</u>: Sep 75.6 (73.3 prelim) versus Aug 68.5

This is the highest reading since Mar 2020 but remains below the Feb level of 92.1.



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

GDP Q2 – Third/Final Estimate

GDP for the second quarter was confirmed at a SAAR of contraction of -31.4%. This is on the back of a -5% contraction at Q1 (SAAR basis also).

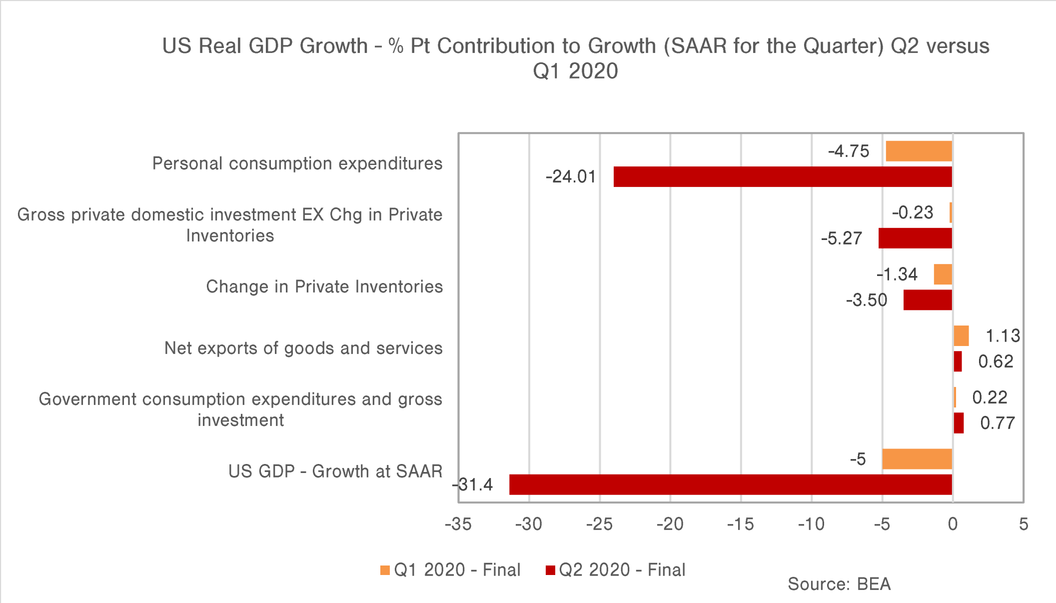
The quarter on quarter decline was -9% in Q2 2020 versus a -1.3% decline in Q1 2020.

In Q2, the severe decline in personal consumption expenditures was the largest contributor to the overall result.

Private domestic investment also contracted notably led by both non-residential structures and equipment, and residential investment expenditure.

Net exports appear to make a positive contribution to GDP in Q2. But this is a function of the net export calculation compared to the prior quarter. Both exports and imports declined at an accelerated pace in Q2. Exports declined by 18.8% in Q2 and imports declined by -12.8%.

This was offset by a positive contribution from an increase in government consumption and investment expenditure.



https://www.bea.gov/news/2020/gross-domestic-product-third-estimate-corporate-profits-revised-and-gdp-industry-annual

Personal Consumption and Income (Aug)

Total personal income declined in Aug. This was the result of a substantial reduction in transfer payments as the $600 supplemental payment expired from 31 July. This more than offset the increase in employee compensation. The annual growth in personal disposable income has now slowed down to be in line with pre-covid levels. But further reductions in pandemic-related support will likely see slower growth in disposable income.

Despite the fall in income, outlays continued to increase, but at a slower pace than in Jul.

The level of savings declined notably compared to the prior month due mostly to the removal of the supplemental $600 weekly unemployment payment, rather than due to accelerating expenditures.

Values quoted on SAAR basis.

<u>Personal Income</u>

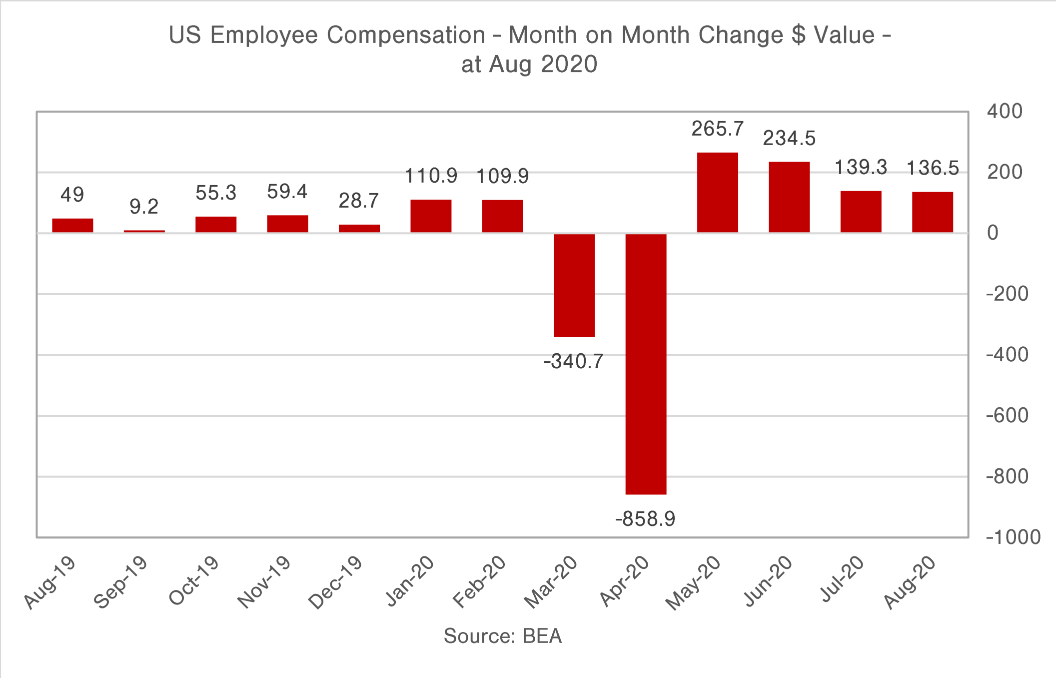
Total personal income declined this month by -2.7% (-$543bn), after increasing by +0.5% (+$91.9bn) in Jul.

An increase in employee compensation and income from capital in the month was not enough to offset the very large decline in transfer receipts in the month (due to the expiration of some benefits).

<u>Employee Compensation – month change</u>: Aug +1.2% (+$136bn) versus Jul +1.3% (+$139.3bn)

The pace of growth in employee compensation is very roughly in line with the increase (cumulative) in nonfarm payrolls during that time:

- Non-farm payrolls from May to Aug had recovered 10.6m jobs compared to the 22.1m jobs lost in Mar & Apr.
- The lost employee compensation from Mar and Apr was -$1.2tr and so far, compensation has increased by $776bn (cumulative from May to Aug).



Employee compensation is now -0.5% below the same month a year ago. But the pre-covid rate of growth in employee compensation averaged +4.7% throughout 2019.

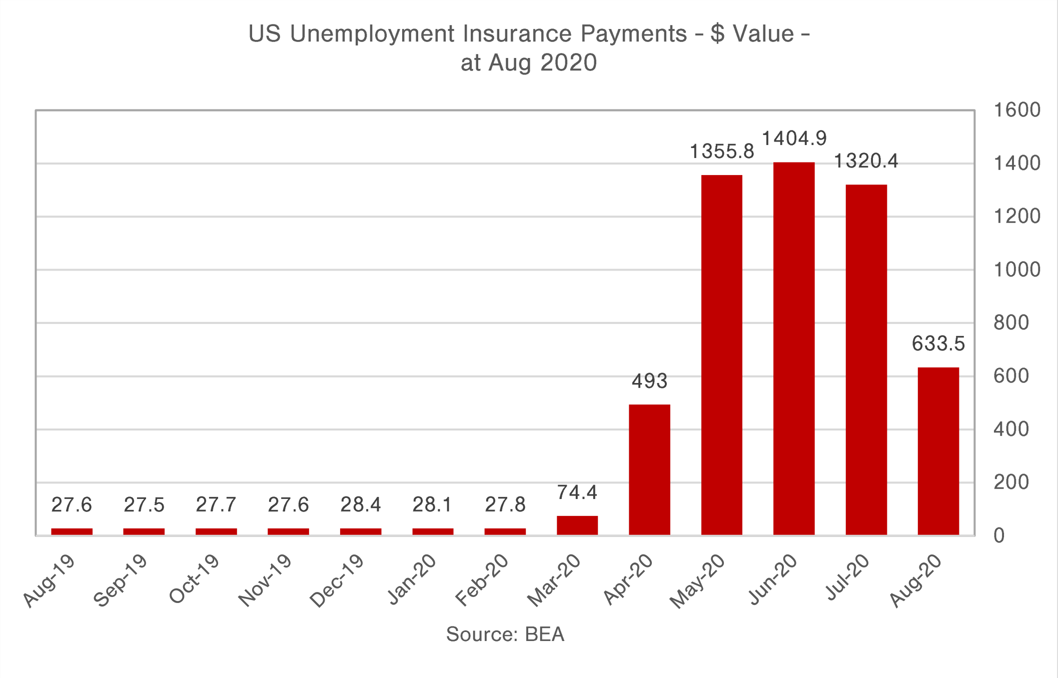
<u>Income from Capital – month change</u>: Aug +$58.7bn versus Jul +$29.4bn

This includes Proprietors' income with inventory valuation and capital consumption adjustments and Rental income of persons with capital consumption adjustment

<u>Personal Transfer Receipts – month change</u>: Aug -14.8% (-$725bn) versus Jul -1.3% (-$62.6bn)

This was a significant jump in the pace of decline in the month. This was led by a large fall in unemployment insurance payments in the month of -52% or -$686.9bn versus Jul.

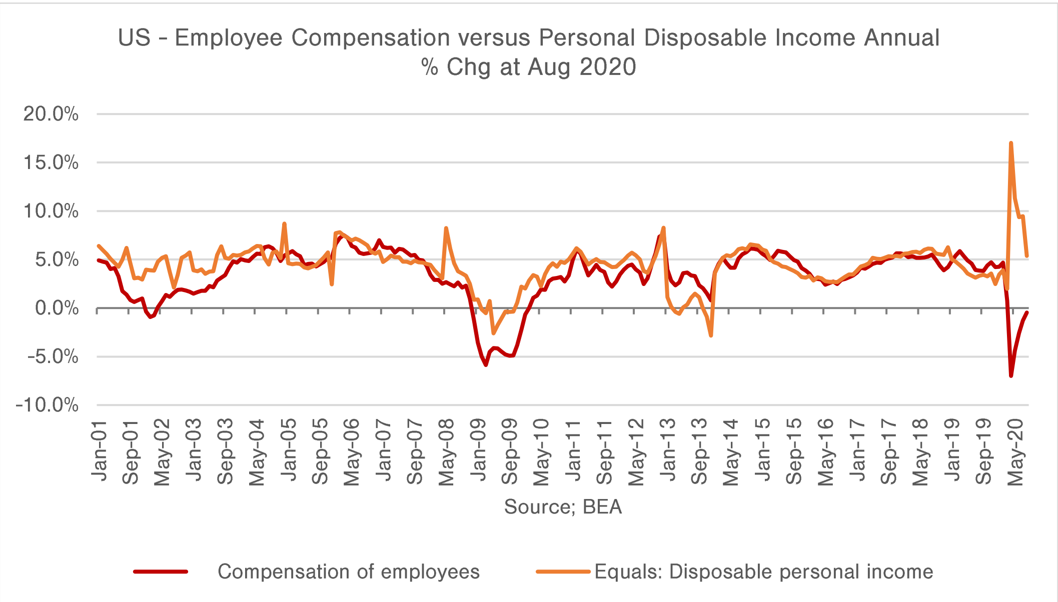
> In particular, the Federal Pandemic Unemployment Compensation program which provided a temporary weekly supplemental payment of $600 for those receiving unemployment benefits expired on July 31. https://www.bea.gov/news/2020/personal-income-and-outlays-august-2020



The other significant line item to record a decline within transfer payments is 'other'- this is the line item where one-off stimulus payments have been recorded. As expected, this continues to slow (most of the payments went through in Apr 2020).

After taxes, Disposable Personal Income declined by -3.2% in Aug (-$570bn) versus a +0.3% (+$62.3bn) increase in Jul.

On a year ago basis, employee compensation growth still lags considerably. But the stimulus and the unemployment insurance has ensured that overall disposable personal income growth has remained higher. In Aug, annual growth in disposable personal income was lower but was still approx. in line with historic levels (+5.4%).



As benefits start to expire over the next few months, the annual growth in disposable personal income will likely slow (unless employment growth starts to accelerate). In Aug, disposable personal income was +0.3% ahead of Jan (pre-Covid levels) and is only at this level because transfer payments in Aug are still +30% above the Jan level which is offsetting the shortfall in employee compensation which is still 2.6% below the Jan level in Aug.

Personal Consumption

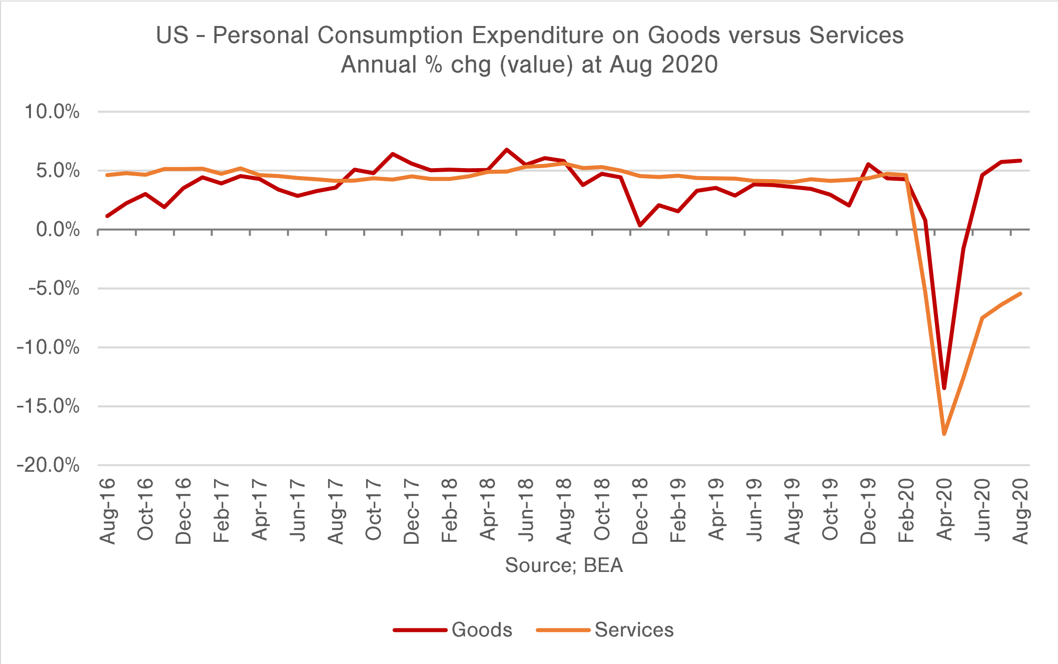
Personal consumption expenditure increased at a slower pace this month. This was led by slower growth across both goods and services expenditure.

Personal Outlays – month change: Aug +1% (+$141bn) versus Jul +1.5% (+$213bn)

Expenditure on goods slowed from +1.4% in Jul to +0.2% in Aug. Durable goods expenditure slowed and non-durable goods expenditure declined in Aug.

Expenditure on services slowed somewhat from +1.6% in Jul to +1.4% in Aug.

On an annual basis, goods expenditures are back up to +5.9% growth – very much in line with the pre-Covid pace of growth. Annual growth in services expenditures continues to lag notably at -5.4% below a year ago. Overall annual expenditures are -1.9% below the same month a year ago.



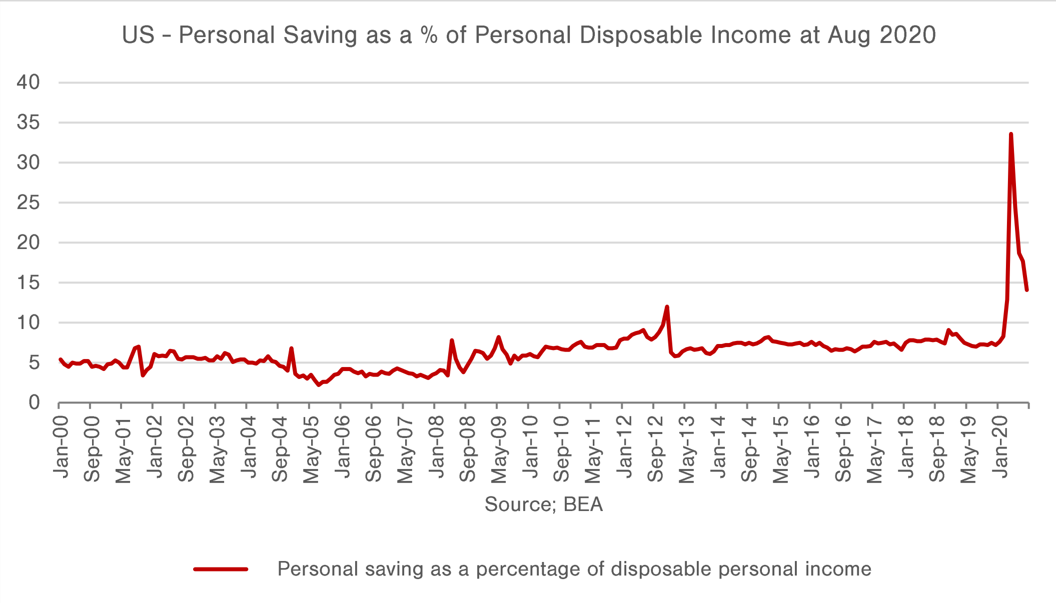
Personal Saving

This month personal saving declined as disposably income declined and personal outlays increased.

Personal Saving – month change: Aug -23% (-$723bn) versus Jul -5% (-$163bn)

The decline in saving was mostly a function of the large decline in supplemental unemployment insurance payments in the month (rather than as a function of accelerating expenditure).

Personal saving as a percentage of personal disposable income fell from 17.7% in Jul to 14.1% in Aug – and remains elevated:

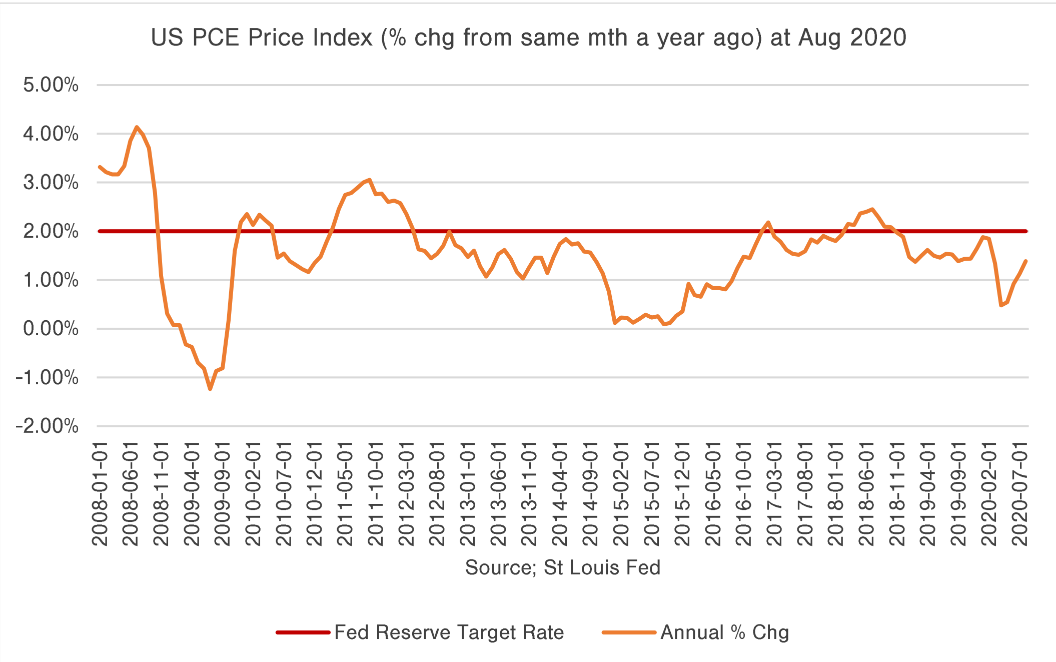


https://www.bea.gov/news/2020/personal-income-and-outlays-august-2020

PCE Price Index (Aug)

Headline consumer prices continued to increase in Aug. The key factors driving the increase were energy prices rebounding and a continued increase in both underlying goods and services prices. Excluding energy, the PCE price index increased at an annual pace of +1.8%.

Headline PCE Price Index – annual change: Aug 1.4% versus Jul +1.1%



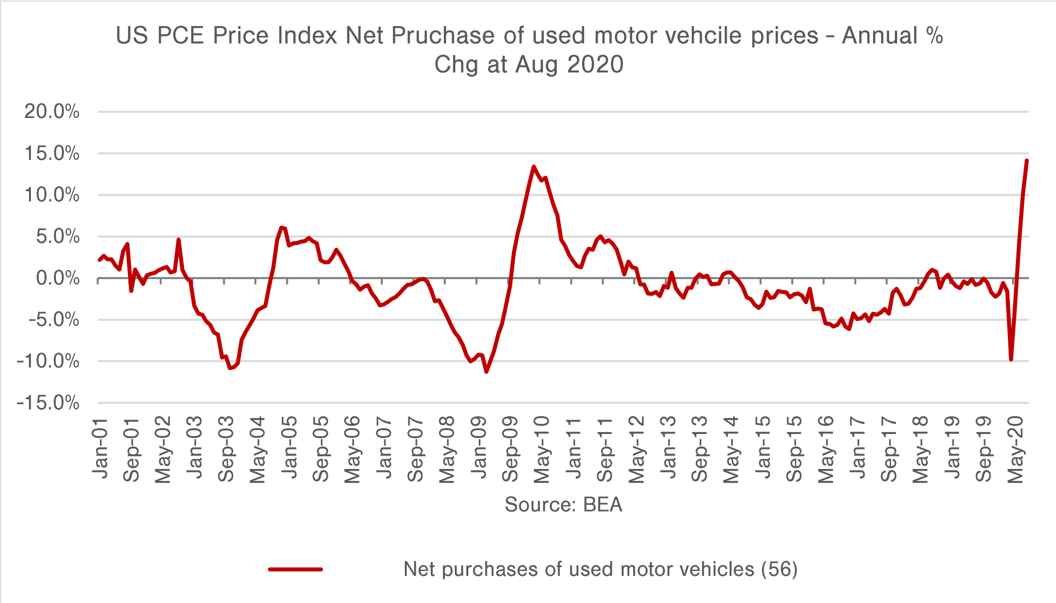
The annual growth in the PCE price index continued to increase at a faster pace in Aug. The underlying monthly change slowed slightly from +0.4% in Jul to +0.3% in Aug.

PCE Goods Prices – annual change: Aug +0.1% versus Jul -0.5%

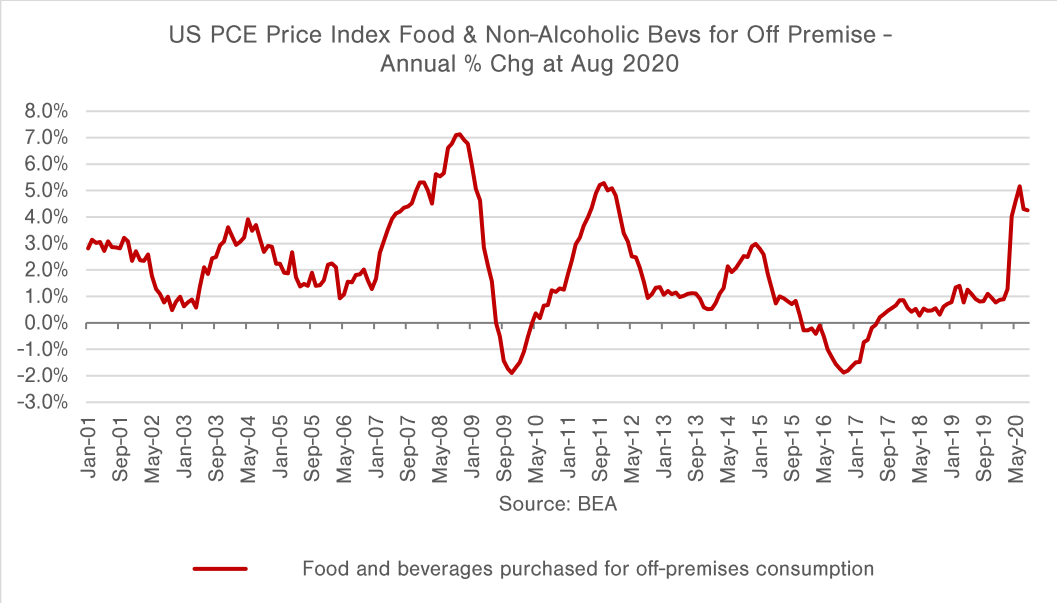
Goods prices continued to accelerate on an annual basis – both durable and non-durable goods prices contributed to the increase.

It is interesting to note the acceleration in the prices of motor vehicles. New vehicle prices declined in Mar and rebounded in Jul. But the bigger change is used car prices.

On an annual basis, prices for the Net purchase of used motor vehicle were up by +14.2% versus a year ago. Prices have increased notably on a monthly basis since May – likely the result of limited availability of new cars as well as demand for a relatively lower cost option.



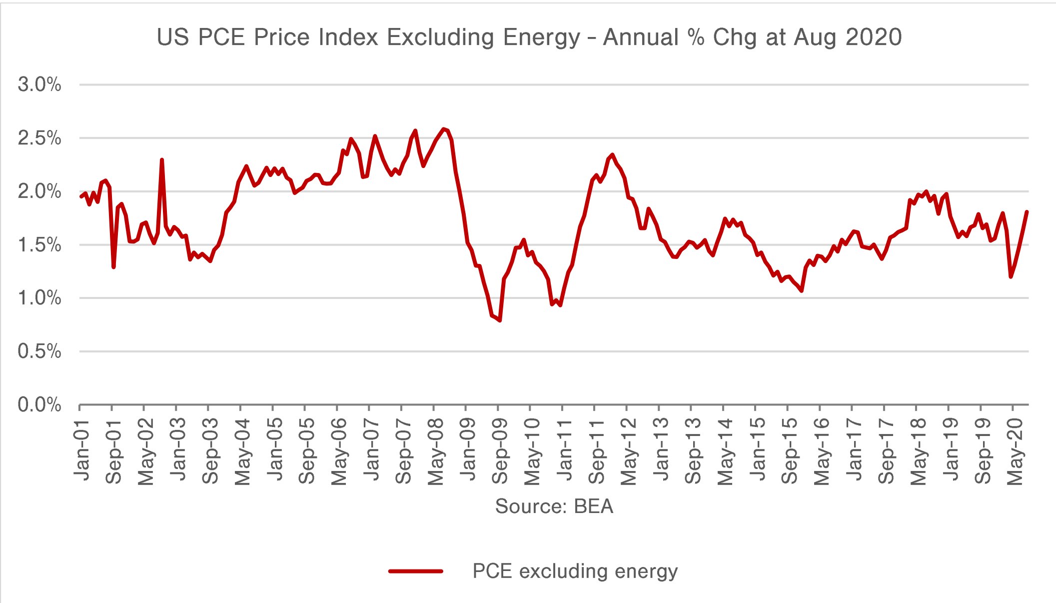
PCE Food prices for off-premise consumption have also increased notably, especially since Mar and Apr. In Aug, the annual growth remained elevated at +4.3% (same as in Jul). The Aug monthly change though was down slightly by -0.12% - hopefully reflecting some stabilization in the supply chain and availability.



One of the other larger contributors to the change in goods prices has been the offsetting decline and part rebound in energy prices.

Gasoline and other energy goods prices started to rebound from Apr – when prices declined on a monthly basis by -19%. In Aug, prices were up +1.9% on a monthly basis, but remain 16% below a year ago.

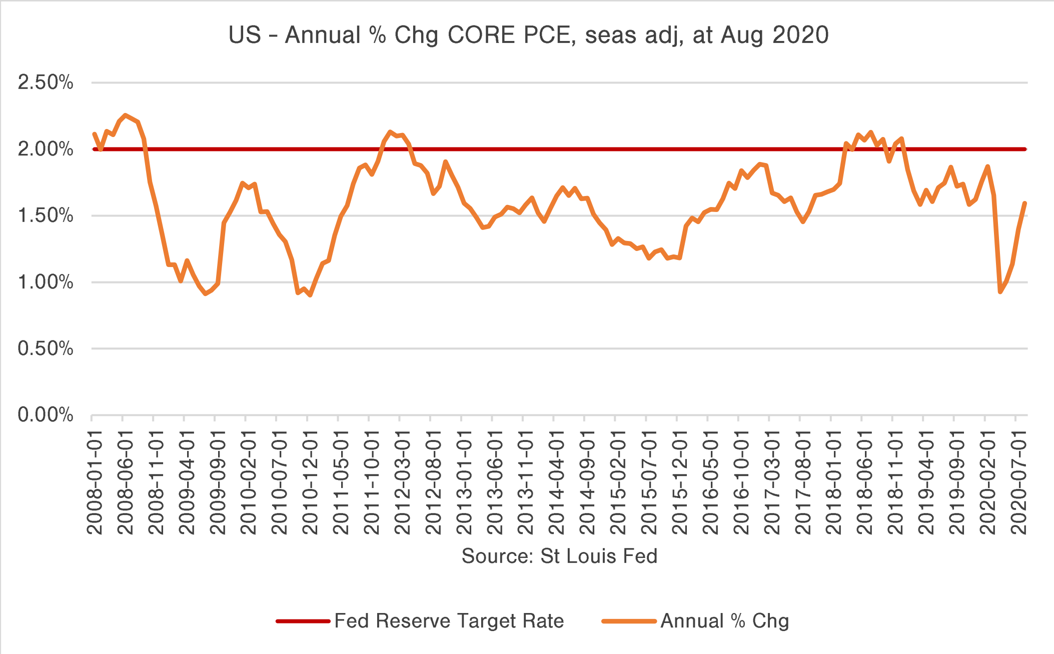
Excluding energy prices from the PCE price index indicates that underlying consumer price growth has rebounded and is growing at +1.8% versus the same month a year ago. The Fed target is to average 2% over time.



Services prices also continued to rebound in Aug and the monthly pace of growth is back to a more consistent level.

<u>**PCE Services Price Index – annual change**</u>: Aug +2% versus Jul +1.9%

The Core PCE price index, excluding food and energy is now back up to +1.6% in Aug on an annual basis.



Both underlying core goods and core services prices contributed to the further acceleration in Aug.

https://fred.stlouisfed.org/series/PCEPILFE#0

US ISM Manufacturing PMI (Sep)

The headline manufacturing PMI indicated that the pace of growth recorded in Aug was mostly maintained in Sep. Looking at the components that make up the indexes highlights a concerning trend – especially for the pace of growth in new orders. The proportion of firms reporting higher/growth in new orders (compared to the prior month) has been declining and in Sep, the number of firms reporting higher orders, was the lowest in the last four months. More firms started reporting a decline in new orders. This will likely have implications for the pace of growth in production growth in the short-term. The current production index also points to some levelling out of the growth momentum. The underlying components of the employment index were more positive in Sep but remained on net on contraction compared to the prior month.

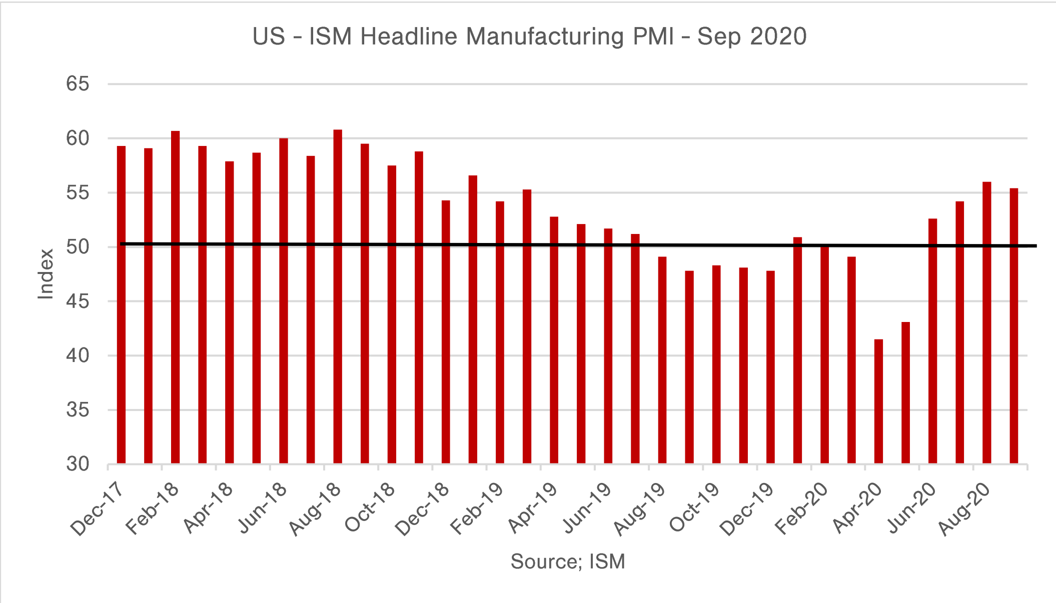
> "Among the six biggest manufacturing industries, Food, Beverage & Tobacco Products remains the best-performing sector, with Fabricated Metal Products and Chemical Products growing strongly. Computer & Electronic Products and Transportation Equipment expanded moderately. Petroleum & Coal Products remained a headwind to PMI® performance.

Headline ISM Manufacturing PMI: Sep 55.4 versus Aug 56

Fourteen of the eighteen manufacturing industries recorded a further monthly increase in activity in Sep. In order:

Paper Products; Wood Products; Food, Beverage & Tobacco Products; Furniture & Related Products; Electrical Equipment, Appliances & Components; Nonmetallic Mineral Products; Fabricated Metal Products; Chemical Products; Miscellaneous Manufacturing; Plastics & Rubber Products; Machinery; Textile Mills; Computer & Electronic Products; and Transportation Equipment.

The four industries reporting contraction in September are: Apparel, Leather & Allied Products; Printing & Related Support Activities; Petroleum & Coal Products; and Primary Metals.



The new orders index indicated that growth remained elevated, but the index fell from 67.6 in Aug to 60.2 in Sep. <u>There is a very important trend underlying this result.</u> The proportion of firms reporting higher/growth in new orders has been declining. The result in Sep of 35.2% of firms (reporting higher orders) is the lowest in the last four months. Even in Jun, the proportion of firms reporting growth in new orders was 37.3% of firms. This will likely have implications for the pace of growth in production growth in the short-term.

Also of note is the increase in the proportion of firms reporting lower or declining new orders – up from 12.9% in Aug to 18.9% in Sep. The proportion of firms reporting no change in new orders was slightly lower at 45.9% in Sep compared to 47.4% in Aug.

The new export orders index was little changed, up slightly from 53.3 in Aug to 54.3 in Sep. The underlying components were unchanged.

The production index was slightly lower in Sep but remains elevated at 61 (compared to 63.3 in Aug). The proportion of firms reporting higher production was lower in Sep than in Aug and was also the lowest level of the last four months at 34.3% of firms. Even back in Jun, the proportion of firms reporting higher production was larger at 39.2% of firms. There was only a slight increase in the proportion of firms reporting lower production (14.8% of firms in Sep).

Most firms, 50.9% of firms, reported no change in production. This is also the highest level of the last four months – and points to some levelling out of growth momentum.

The order backlogs index was little changed in Sep at 55.2 compared to 54.6 in Aug. Although the index increased slightly, there were less firms (26% in Sep versus 29% in Aug) reporting an increase in order backlogs. Most firms reported no change in order backlogs up from 51.3% of firms in Aug to 58.3% in Sep.

The employment index was slightly more positive. The index remained in contraction, but there was some improvement in the underlying components. The index increased from 46.4 in Aug to 49.6 in Sep. Slightly more firms increased employment (19.4% of firms up from 17.1% in Aug). Most firms continued to report no change in employment levels (58.9%). There was a slight decline in the proportion of firms reporting further decreases in employment which was 21.7% of firms in Sep compared to 23.6% of firms in Aug.

Other indicators: inventories continued to contract, but at a slower pace of contraction. This was led by more firms reporting higher inventories. Prices for raw materials increased at a faster pace.

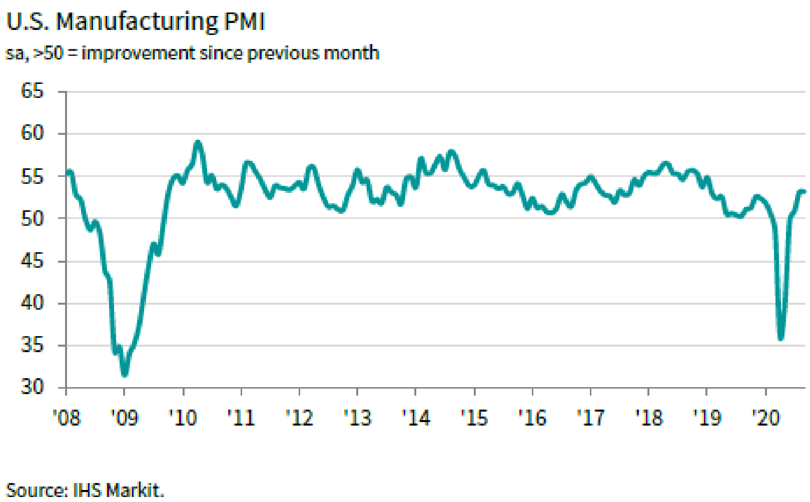
https://www.ismworld.org/supply-management-news-and-reports/reports/ism-report-on-business/pmi/september/

Markit Manufacturing PMI Final (Sep)

The PMI was revised slightly lower compared to the prelim release last week. The headline index indicated that activity expanded at a similar pace in Aug as in Sep.

Output increased at a slightly faster pace. New orders, and new export orders, also continued to increase, but at a slower pace compared to Aug. Order backlogs increased month on month for the second month in a row. Employment also increased, but at a more modest and slower pace compared to Aug.

Manufacturing PMI: Sep 53.2 (prelim 53.5) versus Aug 53.1



https://www.markiteconomics.com/Public/Home/PressRelease/dc4675fa98e94e5791259ac621e82c2c

Dallas Fed Manufacturing Index (Sep)

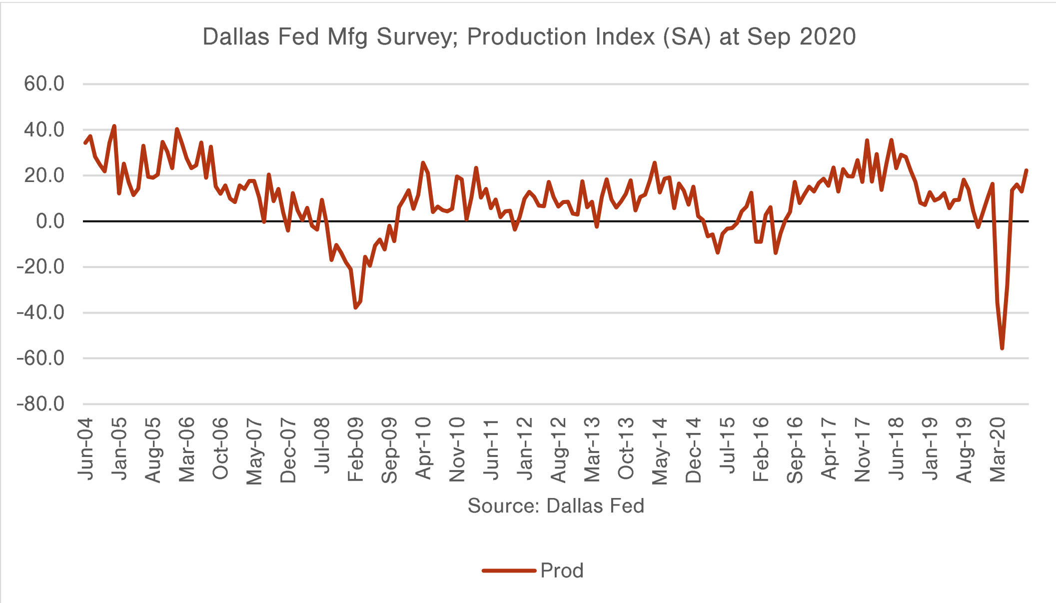
Manufacturing production increased at a faster pace this month. This was the overall strongest indicator of activity for the region in Sep. The new orders index indicated that growth was more stable this month. Shipment growth was also similar as in the month prior – and might indicate some easing in the pace of production growth in the short-term. Unfilled orders suggested that some capacity pressures eased. And this is also reflected in the slower growth in hours worked. Employment growth was more stable this month.

The index of the company outlook was still positive but just slightly lower than in the prior month. Almost 60% of firms reported no change in the outlook. Less firms reported an improvement and less firms reported a worsening in the outlook.

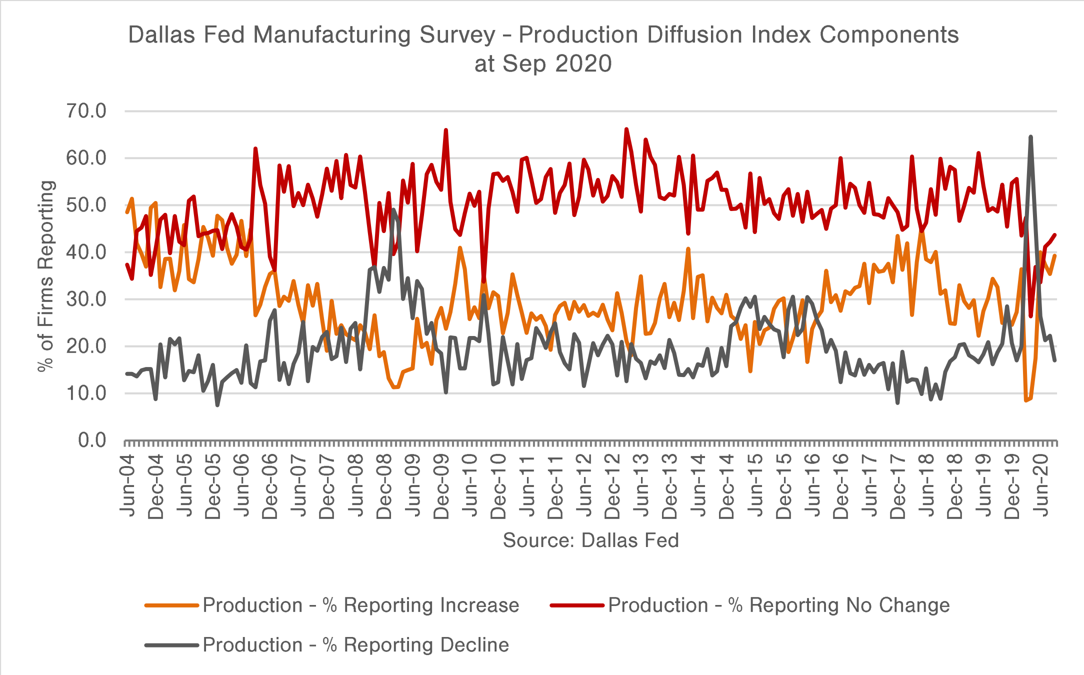
The important point, which is not clear from this report, is where production and activity levels sit compared to the pre-Covid shutdown period.

Manufacturing Production Index: Sep 22.3 versus Aug 13.1

The increase in the index this month was based on a positive underlying shift. More firms reported an increase in production, there was a smaller increase in firms reporting no change in production, and, importantly, there was a decline in the proportion of firms reporting a decrease in production levels (all compared to the prior month).



The diffusion index components indicate that the proportion of firms reporting increases in production is approaching the near term peak (currently 39.3% of firms versus the May 2018 peak of 45.5 – this is not the all-time peak though).



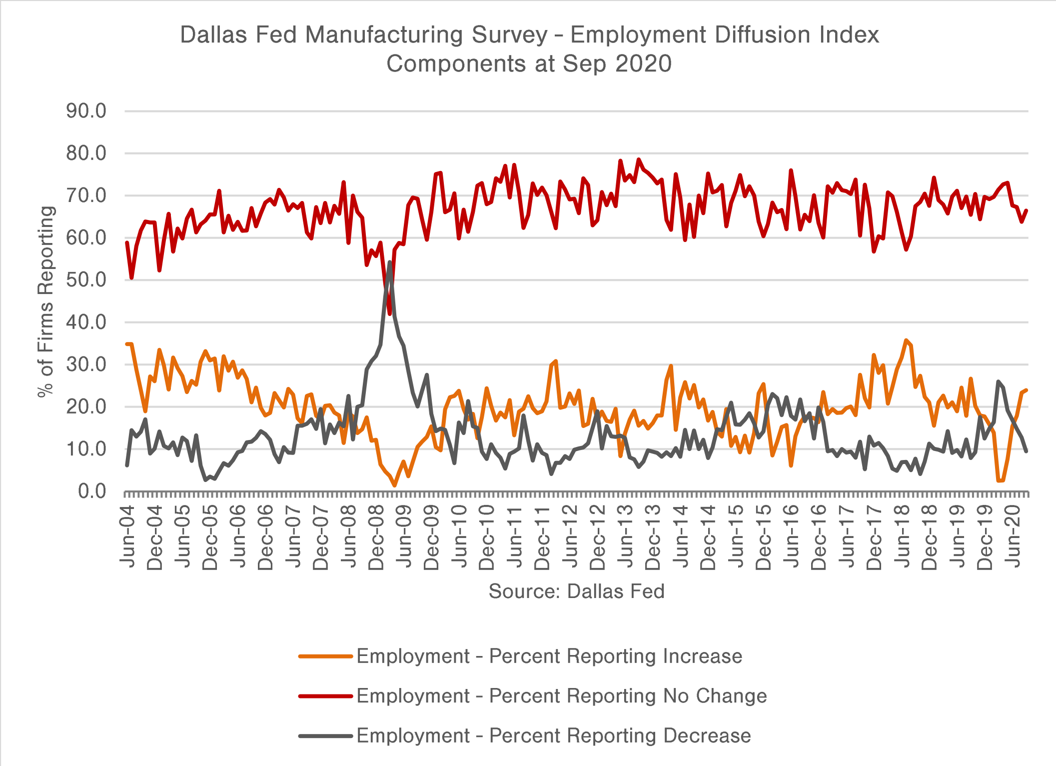
The proportion of firms reporting declines in production remains elevated but is at least back down to the pre-Covid level of 17% of firms. The proportion of firms recording no change to production levels remains lower than (the 2019) average at 43.7% of firms.

This month the growth in new orders accelerated with the index increasing from 9.8 in Aug to 14.7 in Sep. But the underlying composition was somewhat less positive. While there was a larger reduction in the proportion of firms reporting a monthly decline in new orders, there was also no change in the proportion of firms reporting an increase in new orders. The change in the index came from a larger increase in firms reporting no change in orders (which was 50.3% of firms in Sep versus 43.3% in Aug).

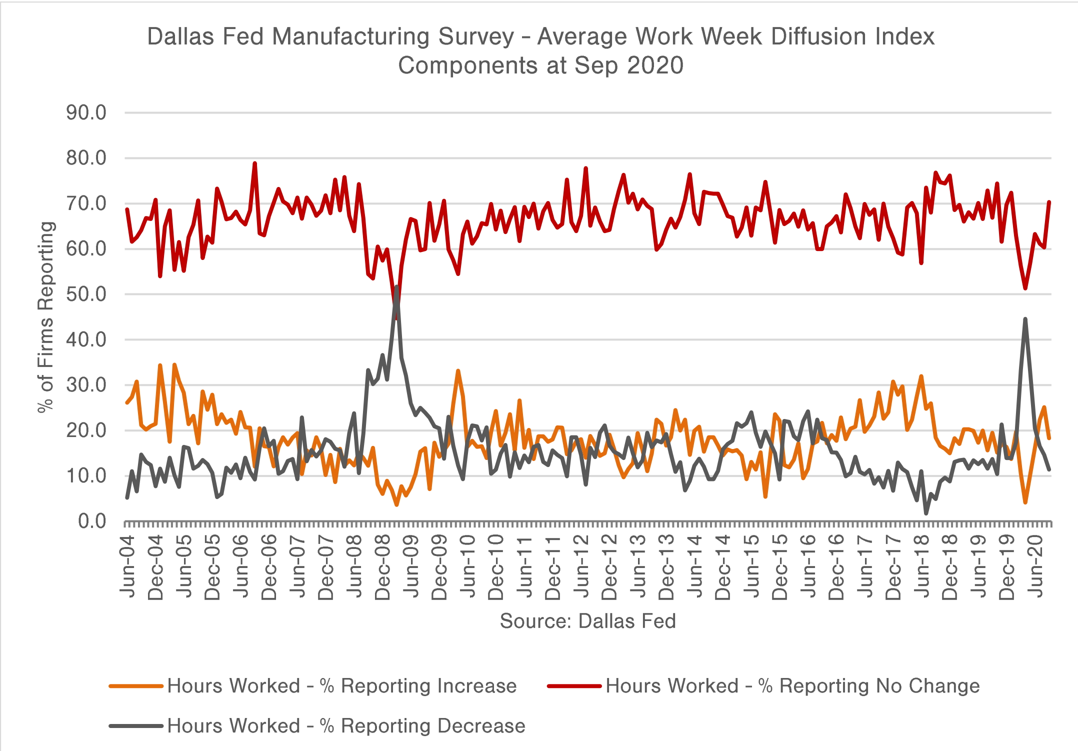
Shipment growth continued at a similar pace as in the prior month with the index slowing slightly from 23.3 in Aug to 21.5 in Sep. Less firms reported increases in shipments and less firms reported declines in shipments versus the month prior. There was an increase in firms reporting no change in shipments.

The growth in unfilled orders remained positive and expanded at only a slightly slower pace as the prior month. The index slowed from 7.8 in Aug to 6 in Sep. There was a similar less positive shift with less firms reporting growing backlogs (indicated easing capacity pressures), but there was also a decline in the proportion of firms reporting declining backlogs. There was instead a large increase in the proportion of firms reporting no change in backlogs.

The employment index increased from 10.6 in Aug to 14.5 in Sep. But diffusion index components indicate that there was only a slight increase in the proportion of firms reporting higher employment up from 23.4% in Aug to 24% in Sep. The change this month was positive in that there was a reduction in the proportion of firms reducing employment, but a corresponding increase in the proportion of firms reporting no change to employment – which was 66.5% of firms. The proportion of firms reporting unchanged employment has been mostly stable throughout the crisis. About a third of firms have either increased or decreased employment levels.

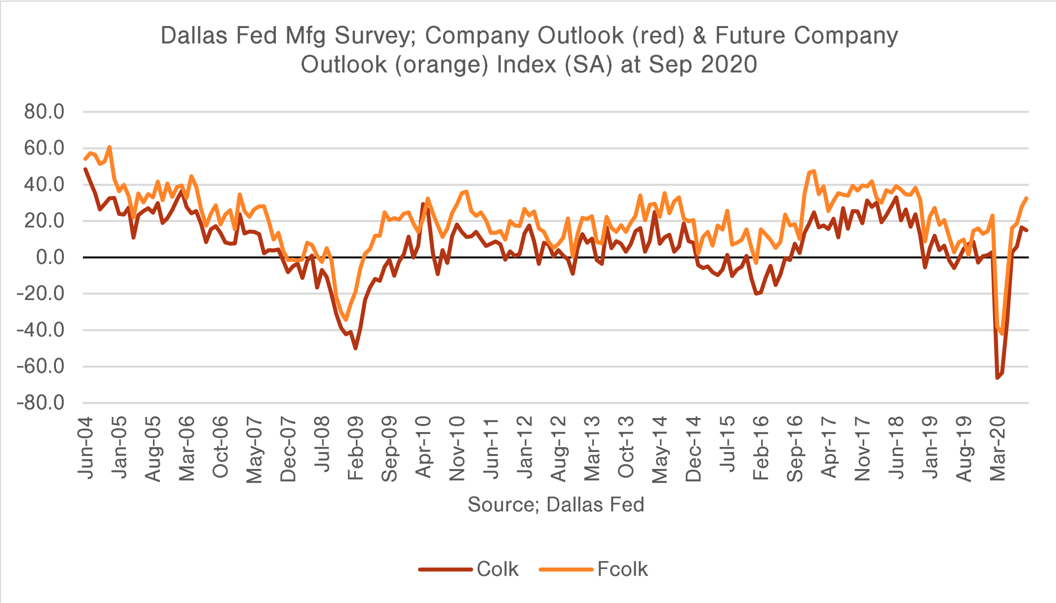


More firms instead changed the average workweek. This month there was a larger slowdown in the pace of the average workweek with the index slowing from 10.5 in Aug to 6.9 in Sep. There was a larger decline in the proportion of firms increasing hours (from 25% of firms in Aug to 18% in Sep). There was also a decrease in the proportion of firms reducing hours (from 14.6% of firms in Aug to 11.4% in Sep). Most firms instead maintained the current level of hours – 70.3% of firms in Sep versus 60.3% in Aug, which is now more in-line with the longer-term average:



The company outlook index eased slightly in Sep – more firms reported no change to the outlook. There was a decline in the proportion of firms reporting an improved outlook, but also a decline in the proportion of firms reporting a weaker outlook.

The future company outlook continued to improve – led by an increase in firms reporting no change.



https://www.dallasfed.org/research/surveys/tmos/2020/2009.aspx#tab-report

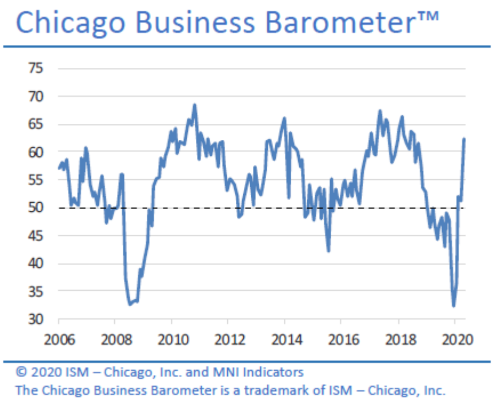
Chicago PMI (Sep)

Growth accelerated notably in Sep after virtually no change in Aug. Both production and new orders indexes indicated acceleration in the pace of growth this month. Order backlogs also increased at a faster pace indicating some pressure on current capacity.

Inventory also increased this month having declined month on month since May.

The employment index also improved, but firms continued to mention further layoffs in Sep.

Headline Chicago PMI: Sep 62.4 versus Aug 51.2



https://s3.amazonaws.com/images.chaptermanager.com/chapters/b742ccc3-ff70-8eca-4cf5-ab93a6c8ab97/files/mni-chicago-press-release-2020-09.pdf

MBA Mortgage Applications wk ending 25 Sep

There was a further decline in mortgage applications in the latest week. This was led mostly by a decline in refinance activity but also a decline in purchases.

Market Composite Index (mortgage loan application volume) wk ending 25 Sep: -4.8% versus the week prior.

The refi index declined by -7% from the prior week.

The purchase index declined by -2% from the week prior. Purchase applications remain +22% ahead of the same month a year ago.

> "Mortgage rates decreased last week, with the 30-year fixed rate mortgage declining 5 basis points to 3.05 percent - the lowest in MBA's survey. Despite the decline in rates, refinances fell over 6 percent, driven by a 9 percent drop in conventional refinance applications," said Joel Kan, MBA's Associate Vice President of Economic and Industry Forecasting. "There are indications that refinance rates are not decreasing to the same extent as rates for home purchase loans, and that could explain last week's decline in refinances. Many lenders are still operating at full capacity and working through operational challenges, ultimately limiting the number of applications they are able to accept."
>
> "Purchase applications also decreased last week, but activity was still at a strong year over-year growth rate of 22 percent. Even as pent-up demand from earlier in the year wanes, there continues to be action in the higher price tiers, with the average loan balance remaining close to an alltime survey high."

https://www.mba.org/2020-press-releases/september/mortgage-applications-decrease-in-latest-mba-weekly-survey-x272988

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Europe

Eurozone CPI Prelim (Sep)

The prelim annual CPI reading for the Euro area continued to decline in Sep by -0.3%. The month on month pace though remained positive at +0.1%.

The main contributor to the annual decline was the continued fall in energy prices.

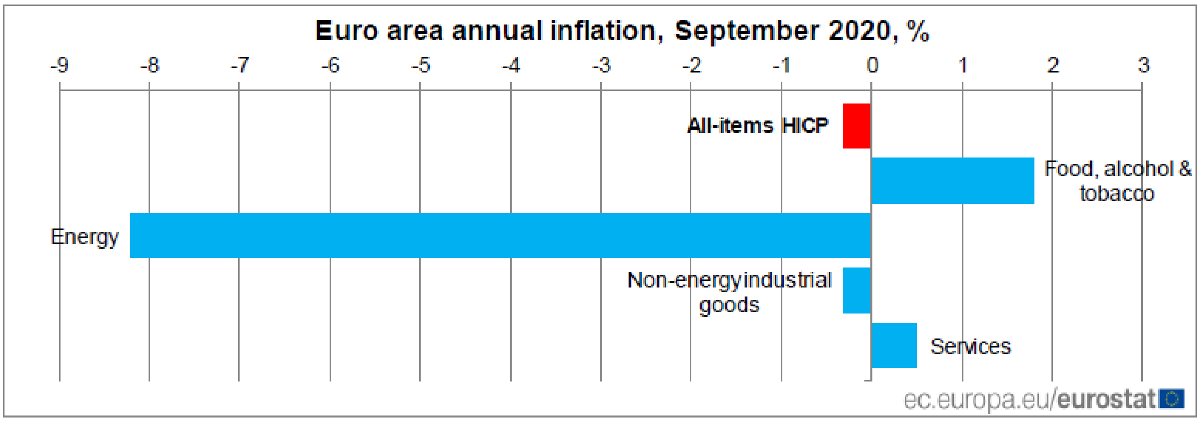
Euro area CPI – annual change: Sep prelim -0.3% versus Aug -0.2%

As of Sep, energy prices declined at a slightly faster annual pace of -8.2% (versus -7.8% in Aug).

Non-energy industrial goods also declined at a slightly faster pace of -0.3% in Sep versus -0.1% in Aug.

Growth in services prices also slowed on an annual basis. This is usually quite stable. The annual change in services prices slowed to +0.5% in Sep from +0.7% in Aug. In Sep 2019, services prices were increasing at an annual pace of +1.5%.

At the same time, food, alcohol and tobacco prices increased at a slightly faster pace of +1.8% in Sep (from +1.7% in Aug). Of note was the acceleration in growth of unprocessed food prices from 2.3% in Aug to +3.1% in Sep. The month on month prices declined slightly by -0.1% in Sep.



https://ec.europa.eu/eurostat/documents/2995521/10663654/2-02102020-AP-EN.pdf/96310899-d2db-1918-d6cb-c7a67f6163a3

Markit Eurozone Manufacturing PMI Final (Sep)

Manufacturing activity across the Eurozone increased at a faster pace in Sep.

Eurozone Manufacturing PMI: Sep 53.7 versus Aug 51.7

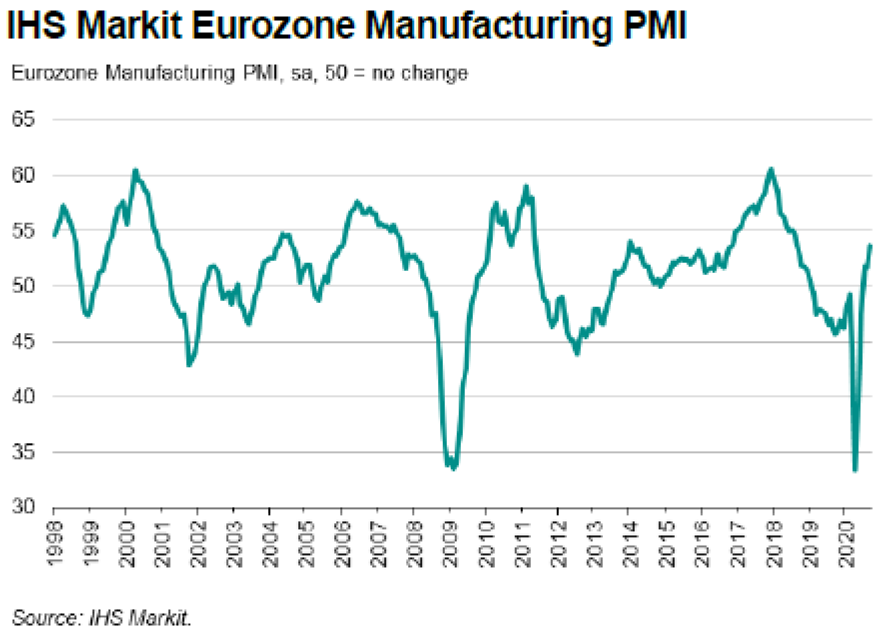
This is now the third month on month increase in the PMI after much substantial declines from Apr and May.

On a regional basis, improved manufacturing conditions in Germany was the main driver of faster growth in output, new orders, and new export orders.

> "The recovery would have been far more modest without Germany, however, where **output** has surged especially sharply to account for around half of the region's overall expansion in September. Germany's performance contrasted markedly with modest production growth in Spain, slowdowns in Italy and Austria, plus a particularly worrying return to contraction in Ireland. Excluding Germany, output growth would have weakened to the lowest since June.

A more modest month on month increase in the overall PMI was also recorded across Italy, Netherlands, Austria, and France. There was no change in conditions across Spain, Greece, and Ireland.

Across the broader Eurozone, and despite the overall month on month improvement, employment continued to decline, albeit at a slower pace.



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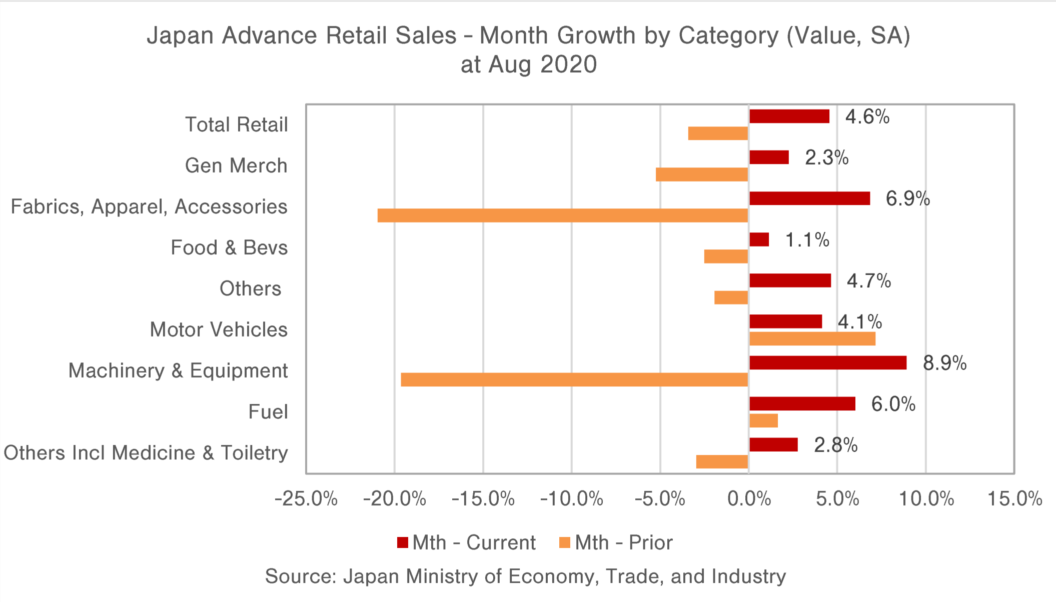
Japan

Advance Retail Sales (Aug)

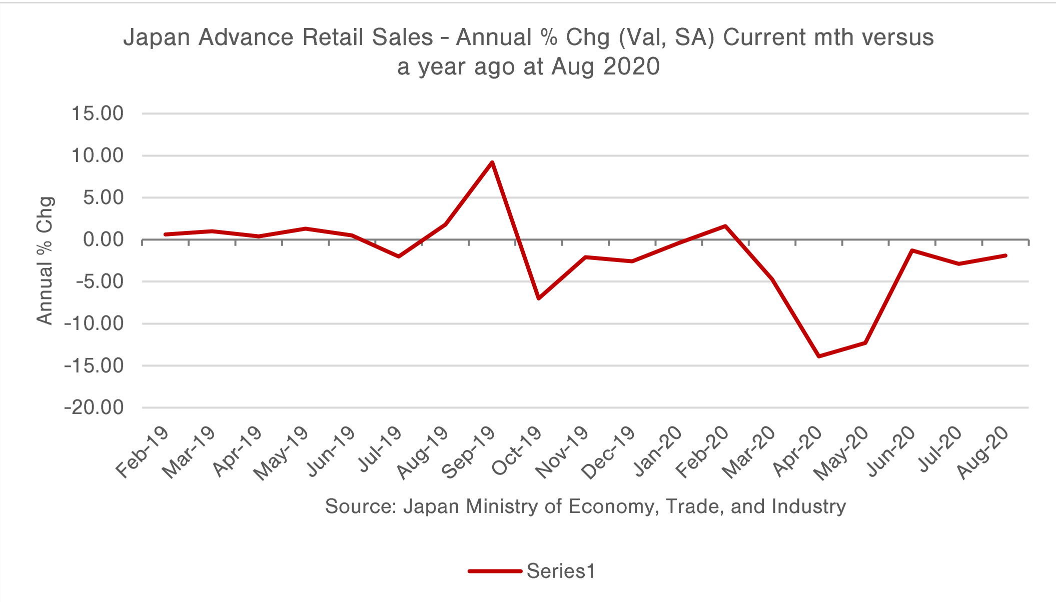
The value of retail sales increased across all sectors in Aug after declining in Jul. Despite the growth in the month, sales remain 2% below the same month a year ago.

Advance Retail Sales – month change (SA): Aug +4.6% versus Jul -3.4%

Growth in retail sales was recorded across all sectors in the latest month:



Advance Retail Sales – annual change (SA): Aug -2% versus Jul -3%



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

Industrial Production Prelim (Aug)

Industrial production and shipment growth in Aug slowed but remained positive compared to the month prior. Both production and shipments remain well below a year ago. Inventory continues to decline.

The forecast for Sep in Aug was for +1.9% growth and in Sep, this forecast has been upgraded to +5.9% growth in production.

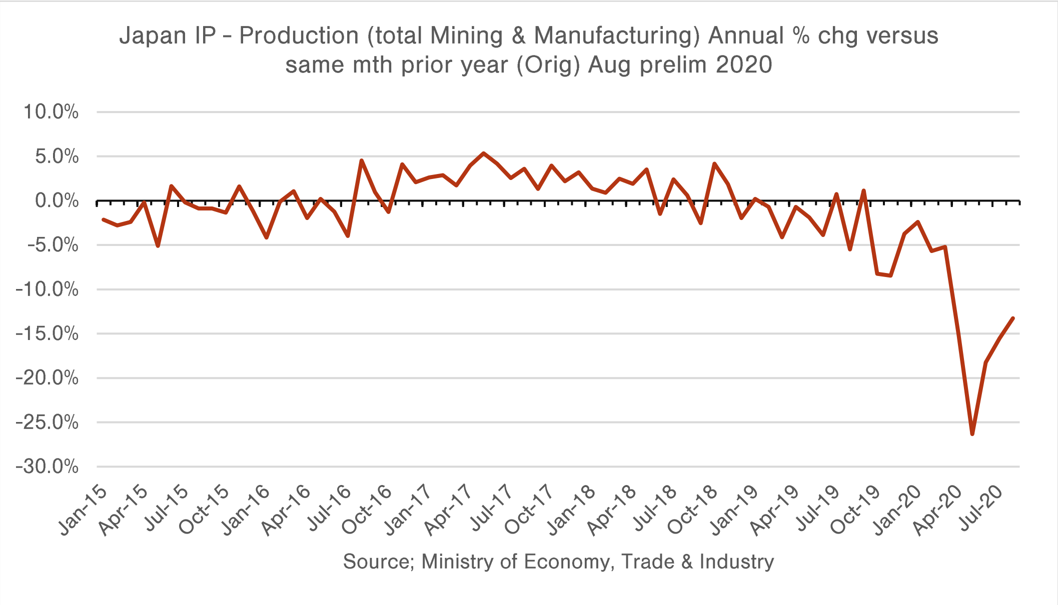
As of Sep, the forecast for production growth in Oct is +2.9%.

Japan Industrial Production – month change: Aug +1.7% versus Jul +8.7%

Production growth remained strong across: iron, steel, and non-ferrous metals, electronic parts and devices, transport equipment including motor vehicles.

Production still declined across electrical machinery and production machinery, including a 24% decline in semiconductor and flat panel display manufacturing equipment.

On an annual basis, production levels remain 13% below the same month a year ago.

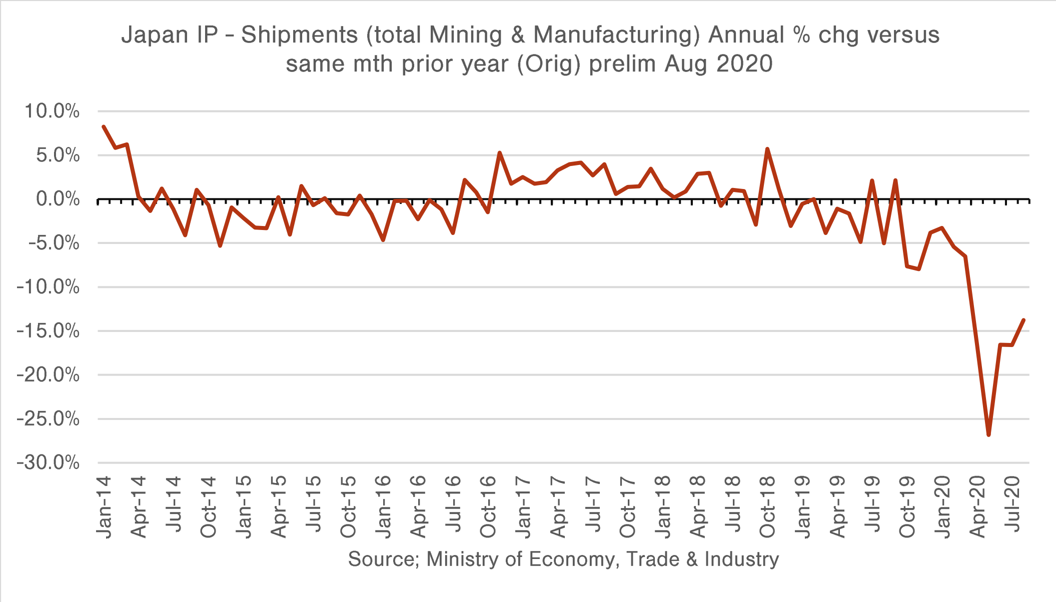


Shipments – month change: Aug +2.2% versus Jul +6.6%

Shipments remain strong across two categories this month; iron, steel, and non-ferrous metals, and transport equipment. Both have large weights in the shipment index.

Shipments declined in Aug (after increasing in Jul) across: fabricated metals, production machinery, electronic parts and devices, and electrical machinery.

On an annual basis, shipments remain 13.8% below the same month a year ago:



<u>Inventory of Finished Goods – month change</u>: Aug -1.4% versus Jul -1.5%

The inventory index continues to decline. This is being led by one industry in the index with the largest weight – iron, steel, and nonferrous metals (17% of the index) for which inventory declined by -5.2% in Aug after -2.5% in Jul. Shipments of iron & steel started to increase only in Jul and Aug and production levels have also just started to increase and are well down on a year ago.

Inventory only increased in the month across electronic parts and devices and transport equipment.

The overall index of producers finished goods inventory has been falling since Mar 2020 and the annual pace of decline in accelerating (-6% in Aug versus -4.8% in Jul).

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

Markit Manufacturing PMI Final (Sep)

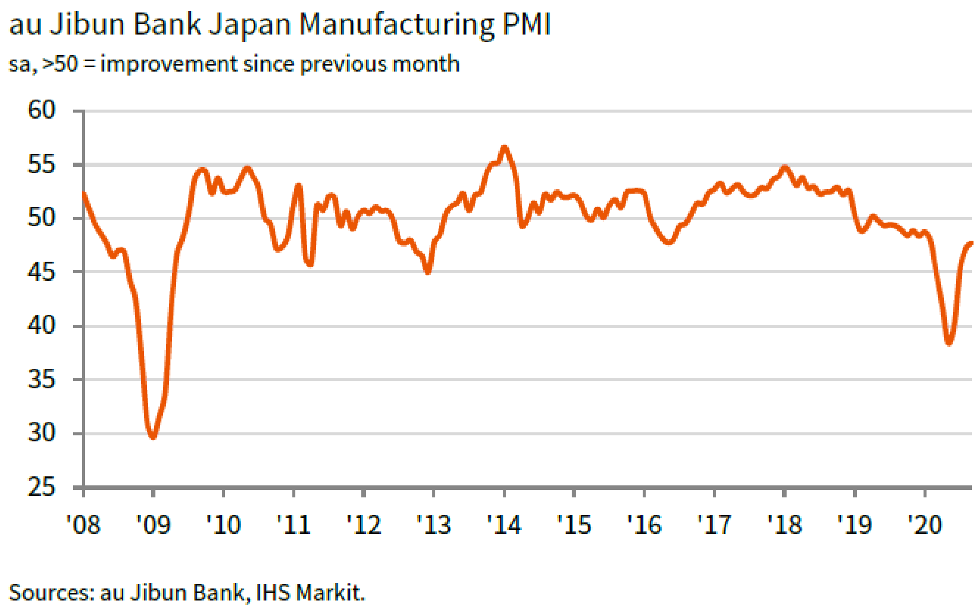
Manufacturing activity continued to contract in Sep and at a similar pace as in Aug. Across key measures of demand – both output and new orders continued to decline according the PMI, but both at a much slower pace. We can already see from the industrial production data that output has started to increase (monthly) on net since Jul. Levels remain well below a year ago.

Backlogs of work continued to decline at a 'sharp rate' indicating that spare capacity still exists.

Firms reported that employment was unchanged from the prior month.

> Manufacturers in Japan are increasingly confident that production volumes will expand during the next 12 months. More than twice as many survey respondents (37%) expect a rise in their output levels as those that anticipate a reduction (18%). The resulting index signalled the strongest business expectations since May 2018, which was mainly linked to hopes that the global economic impact of the pandemic will fade in the next 12 months.

Japan Manufacturing PMI: Sep 47.7 versus Aug 47.3



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Australia

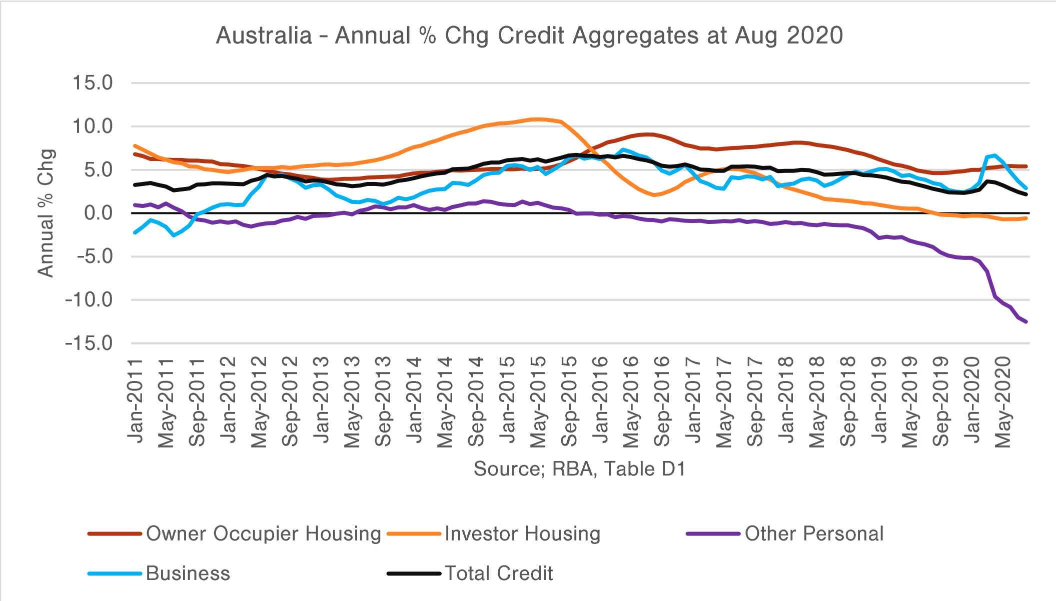
Private Sector Credit (Aug)

The annual pace of growth in outstanding private sector credit continued to slow in Aug. Outstanding private sector credit increased by +2.17% in Aug versus a year ago. The last time growth in credit was this low was in the period of Sep 2009 and Mar 2010.

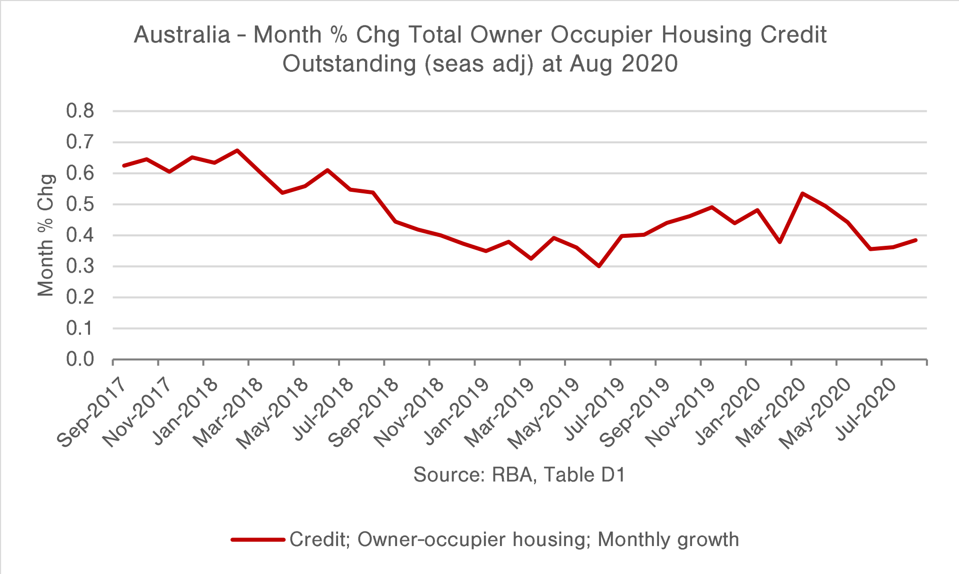
The only sector where growth in outstanding credit is at least constant is owner-occupier housing credit.

Private Sector Credit Outstanding – annual change: Aug +2.17% versus Jul 2.44%

On a monthly basis, outstanding credit was unchanged in Aug after declining in the prior three months. This comes after a substantial lift in the monthly growth rate in Mar of +1.1% - likely linked to many firms accessing lines of credit leading into the National shut-down.



Growth in outstanding owner-occupier housing credit remains the highest of all four sectors at +5.4% on an annual basis (more than twice that of overall outstanding credit growth). The annual pace of growth in outstanding owner occupier credit has been at this same level for the last four months. The monthly pace of growth is slightly higher than in Jul at +0.38% - but there has been little acceleration overall:



Outstanding credit for investor housing continued to decline on an annual basis by -0.6%.

Total outstanding business credit growth slowed from +3.7% in Jul to +2.9% in Aug – still above that of total outstanding credit. Outstanding credit has declined (month on month basis) for the last four months. This comes after a 3% increase in Mar – linked to firms accessing credit at the start of the Covid shut-downs.

Other personal credit outstanding continues to decline at an accelerated pace of -12.5% versus a year ago.

https://www.rba.gov.au/statistics/frequency/fin-agg/2020/fin-agg-0820.html

Markit Manufacturing PMI Final (Sep)

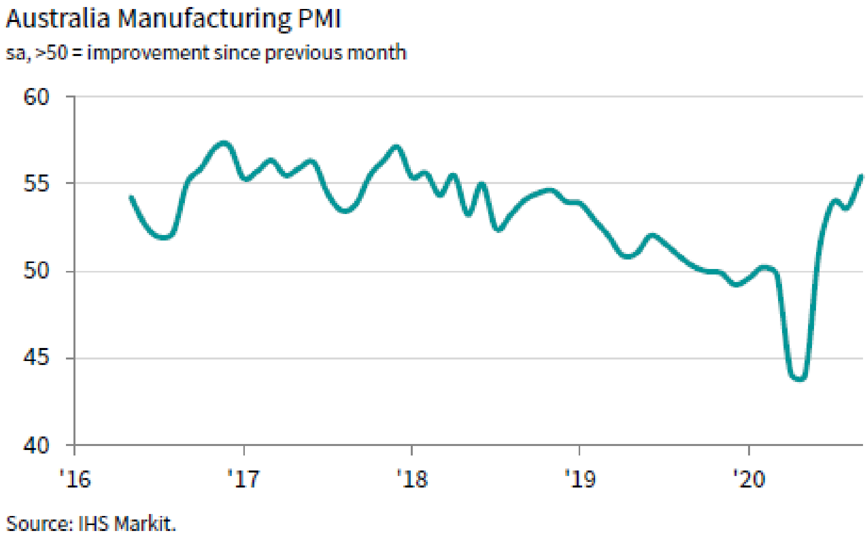
Manufacturing activity in Aus continued to expand at a faster pace in Sep. One point to note was the contribution from the worsening of delivery lead times to the headline PMI increase. Lengthening lead times is usually associated with stronger performance, but in this case, border closures (across most states) and trade restrictions (in Vic) contributed to the lengthening of lead times. The Markit PMI report did not include the output index this month but the prelim report had output expansion at a modest 53.6.

Overall, there was a continued month on month increase in output and new orders. New export orders increased. Government infrastructure and market confidence contributed to the improvement. The vast majority of Aus manufacturing is in the Food and Bev industry.

There was still a modest increase in the employment index this month.

The pace of Covid infections in Vic has slowed substantially because of the lockdowns and this has no doubt contributed to improved expectations about the future.

Aus Manufacturing PMI: Sep 55.4 versus Aug 53.6



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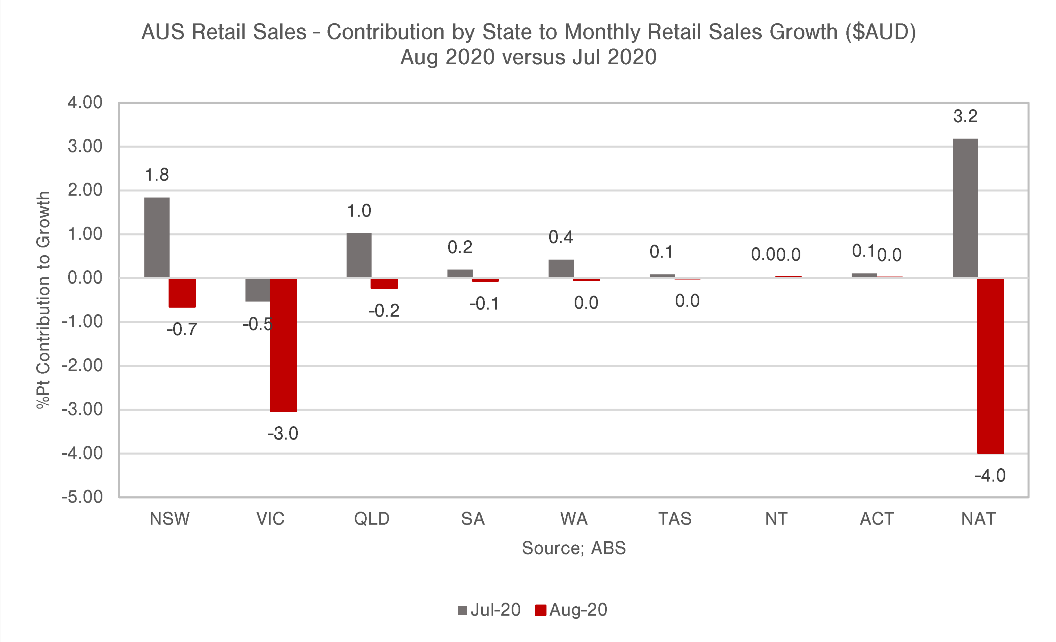
Aus Retail Sales (Aug)

Retail sales in Aug declined at a fast pace – led mostly by restrictions imposed in Victoria because of a Coronavirus outbreak in infections.

The decline in sales in Vic accounted for three quarters of the overall National decline. But sales also fell across most other states including NSW, QLD, SA, WA and Tas. Part of the reason for the weakness was border closures across these states.

Aus Retail Sales ($ value) – month change: Aug -4% versus Jul +3.2%

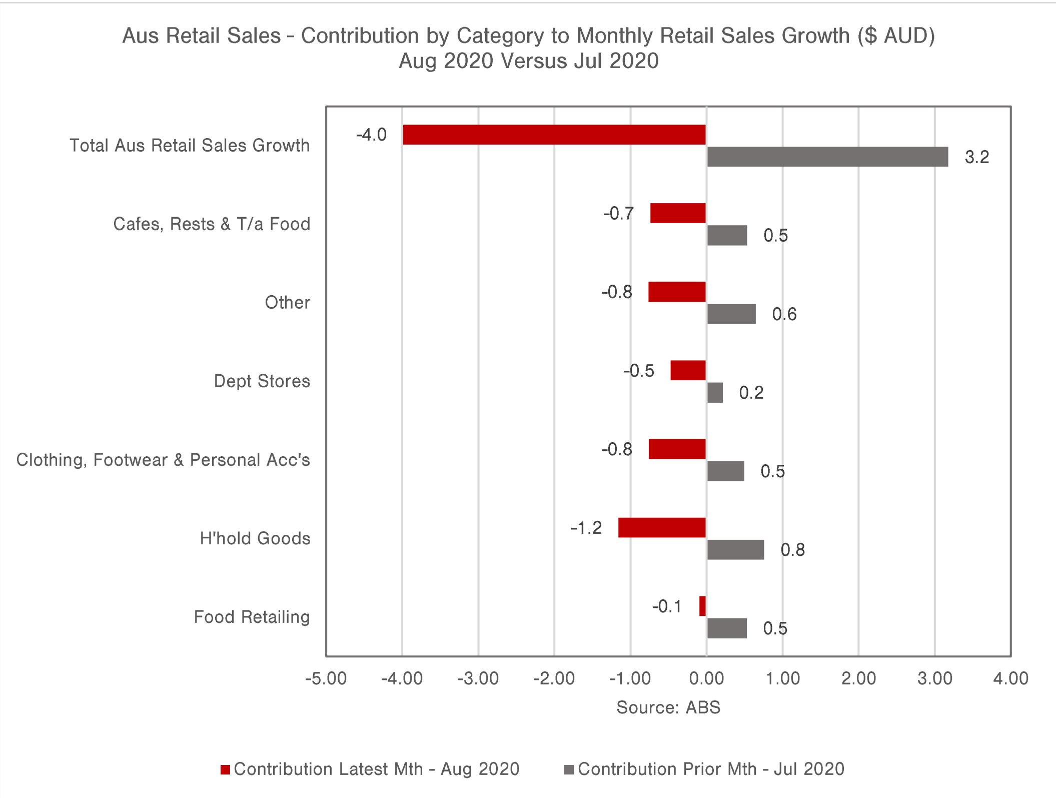
On a state basis, Victoria accounted for the bulk of the decline this month. But it was not the only state to contribute to the decline in retail sales. Sales declined across NSW, QLD, SA, WA and Tas.



The pace of decline across most states meant that sales declined across all retail categories this month.

The decline in household goods made the overall largest contribution to the decline this month, but the contribution to the decline from cafes, other, dept stores, and clothing stores was similar this month.

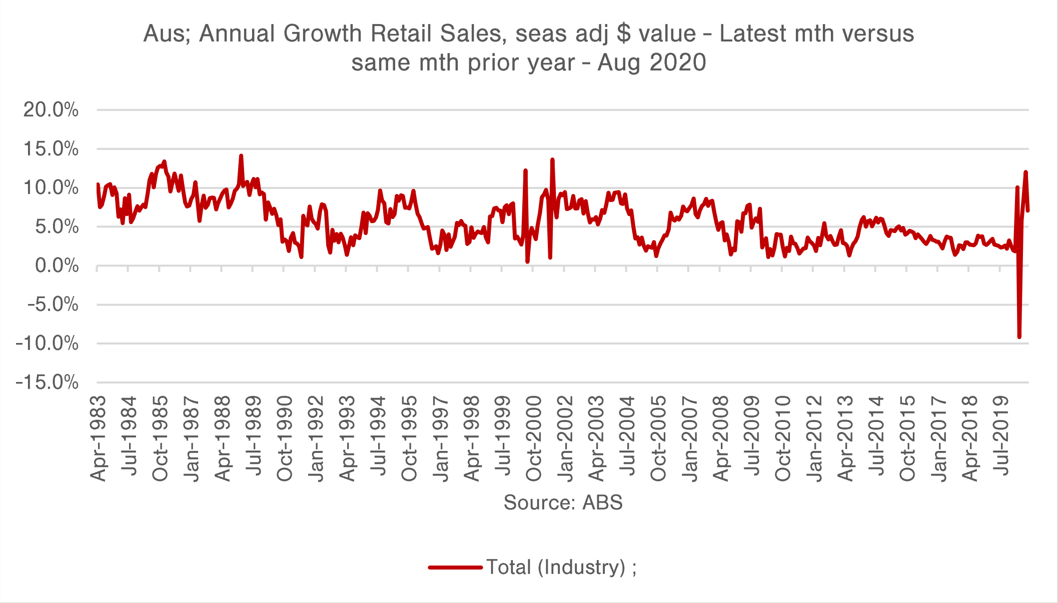
Retail sales in grocery stores declined only slightly by -0.2%.



<u>Aus Retail Sales ($ value) – annual change:</u> Aug +7.1% versus Jul +12%

Annual retail sales remain well above the same time a year ago and this has been led by only three categories. Grocery store sales are +14% versus a year ago – which might be somewhat different on a volume basis. Household goods sales are up +21% on a year ago. Sales across other retailing is also +8.4% ahead of a year ago.

Clothing, dept stores, and cafes/restaurant sales remain well down on a year ago.



https://www.abs.gov.au/statistics/industry/retail-and-wholesale-trade/retail-trade-australia/aug-2020#key-statistics

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Trade

US-China Trade Talks

There has been little change on the US-China trade front. The focus over the last week has been on the Presidential debate, stimulus discussions and, of course, the US President contracting Covid-19.

Relations between the US and China appear to remain tense. In a recent speech at the UN General Assembly, US President Trump demanded that the global community hold China responsible for unleashing “this plague onto the world”.

> With just weeks before the presidential election, Mr. Trump also used his speech to highlight what he sees as his foreign-policy achievements: isolating Iran, moving to withdraw forces from Afghanistan and orchestrating normalized ties between Israel and two Gulf Arab countries. But his attempt to shift the blame to China for the coronavirus pandemic — and away from what critics call his own inept response — was a dominant theme in the speech.
>
> “We have waged a fierce battle against the invisible enemy — the China virus,” Mr. Trump said. He spoke of American advances in lifesaving treatments, predicted success in finalizing and distributing vaccines and asserted: “We will end the pandemic, and we will enter a new era of unprecedented prosperity, cooperation and peace.” https://www.nytimes.com/2020/09/22/world/americas/UN-Trump-Xi-China-coronavirus.html

This was another speech by US President Trump likely targeted to his base (appearing tough on China), in the lead up to the election.

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

Talks will continue this week and next week on the post-Brexit trade deal between the UK and the EU.

> Boris Johnson and Ursula von der Leyen have approved a further month of Brexit negotiations after agreeing that enough progress has been made to justify a last push to reach a deal on trade and security.
>
> The fresh rounds were agreed after a phone call on Saturday afternoon between the British prime minister and European commission president. EU sources said the conversation was "not a game-changer" but not "unhelpful", with both sides showing resolve to find "landing zones" on the most difficult areas. https://www.theguardian.com/politics/2020/oct/03/johnson-and-von-der-leyen-extend-brexit-talks-by-a-month

The EU leaders will meet on 15-16 Oct and will assess progress of talks. The UK has also said that it "wants clarity" by 15 Oct as to "whether a deal is possible or not".

> The EU says that any deal must be sealed by the end of October, or in the first days of November at the latest, to leave enough time for ratification by the bloc before the end of the year. https://uk.reuters.com/article/uk-britain-eu-johnson/johnson-says-he-doesnt-want-no-deal-brexit-but-can-live-with-it-idUKKBN26P0B9?il=0

That next EC meeting was originally expected to be the final date allowing enough time for the EC to ratify any agreement. It is likely that a special meeting will be required before the Dec EC summit.

> When the next round of negotiations opens next week, the EU is hoping Frost will present a compromise proposal on the key issue of control of state aid to businesses. "There is better mood music but no substance yet from London to justify it," one diplomatic source said.
> https://www.theguardian.com/politics/2020/sep/25/brexit-brussels-punctures-optimism-that-deal-in-sight

The internal market bill (and the finance bill) has yet to be tabled in the UK parliament. The timetable for the bills will be an indicator of how talks are progressing between the two sides. The internal markets bill is the proposed UK Brexit legislation that would override the Brexit Withdrawal Agreement.

> The proposed legislation would override aspects of a landmark Brexit withdrawal agreement involving the treatment of the border between Northern Ireland, which is part of the United Kingdom, and Ireland, which will remain in the European Union.
> https://www.nytimes.com/2020/09/10/world/europe/brexit-boris-johnson-ireland.html

The latest minutes from the BoE underlines that current economic projections are based on an orderly Brexit with an established free-trade agreement between the UK and EU. The situation will be reviewed at the Nov BoE meeting – and it is possible that there will not be an agreement in place by then. This may trigger some further stimulus or emergency measures to be taken by the BoE.

A current list of all trade deals that the UK has so far negotiated is available at:

https://www.gov.uk/guidance/uk-trade-agreements-with-non-eu-countries-in-a-no-deal-brexit#trade-agreements-that-have-been-signed

The following trade items have recorded no change in status:

US-Europe Trade Talks

The USTR issued a modification to the products that are authorized by the WTO for additional duties due to the case regarding subsidies for large civil aircraft.

> USTR is removing from the tariff list certain products from Greece and the United Kingdom and adding an equivalent amount of trade from France and Germany. The changes are modest; the amount of products subject to countermeasures will remain unchanged at $7.5 billion and the tariff rates will remain unchanged at 15% for aircraft and 25% for all other products.
>
> "The EU and member states have not taken the actions necessary to come into compliance with WTO decisions," Ambassador Robert Lighthizer stated. "The United States, however, is committed to obtaining a long-term resolution to this dispute. Accordingly, the United States will begin a new process with the EU in an effort to reach an agreement that will remedy the conduct that harmed the U.S. aviation industry and workers and will ensure a level playing field for U.S. companies. " https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/august/ustr-modifies-75-billion-wto-award-implementation-relating-illegal-airbus-subsidies

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

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 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.

S.301 US 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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