

Macro Weekly

Group Economics

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US, China firm, Europe feeble

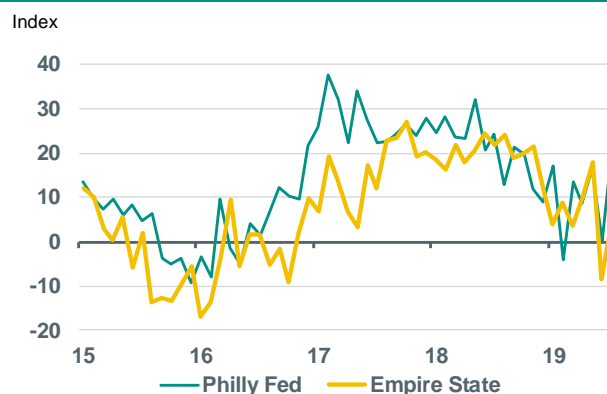
- **US data shows recession long way off**
- **China's policy stimulus effective**
- **Europe struggling**

Recent US economic data paints a picture of an economy that is unlikely to fall into recession any time soon. The current expansion is easily going to be the longest on record (records going back to the second half of the 19th century) as it is in the process this month of passing out the so far longest expansion without any sign of an imminent downturn. My colleague Bill Diviney recently published a note explaining why we don't think a recession is going to occur any time soon, despite many people pointing to the yield curve as a recession indicator. ([US Watch – Pathways to a recession](#))

Philly Fed index jumps

Whatever view one has, the data doesn't lie. It is clear that the global economy has weakened in the last 12 months or so and that the manufacturing sector has been the weakest link. It is also clear that things started to improve a little earlier this year until the unexpected re-escalation of the trade war led to a sharp downturn in various cyclical indicators. But most recently published US data gives rise to some optimism. Most positive was the much larger than expected rise of the Philly Fed index of business confidence in the Philadelphia Fed's district. This gauge jumped from 0.3 in June to 21.6 in July, the highest level in over a year and the biggest monthly jump since 2009. The equivalent index for New York state, the Empire State index, also improved in July, though less strongly: 4.3 in July versus -8.6 in June.

US: Philly Fed and Empire State (NY Fed)



Source: Bloomberg

Harder data was also firm. US retail sales rose 0.4% mom in June after a similar rise in May. Excluding autos and gasoline retail sales were up 0.7% mom after a rise of 0.5% in May. This is important as a recession in the US is all the more likely if the consumer stops spending. Recent data does not suggest that is happening or likely any time soon. Data on industrial production was reasonable. Overall industrial production was unchanged in June after rising 0.4% mom in May. But manufacturing output was up 0.4% mom after +0.2% in May.

The housing sector is sending mixed signals. The confidence index of home builders continues to be strong and inched up from 64 in June to 65 in July, but housing starts and building permits both fell in June. Given the drop in interest rates and, thus, mortgage rates, the response of the housing sector is somewhat underwhelming. A client who is involved in the property business in the US with a focus on Florida, recently told me 'the market is collapsing'. If that were true, that would be bad and really something important to watch. However, so far, I cannot see it in the data. Having said that, such alarmist stories by people from the ground make me vigilant.

Heading for 25bp Fed cut

The July FOMC meeting is approaching fast. Recent firm economic data could lead one to think that a rate cut is not necessary and that the Fed may refrain from cutting. Then there are people who consider a 50 bp cut a distinct possibility. We continue to think that the Fed will deliver a 25bp cut as it is a sort of insurance against possible damage caused by uncertainty over the trade talks with China. A 50bp cut would not seem justified by recent data, plus it might come across as a panic move: 'what bad stuff does the Fed know that we don't know?'

Is Chinese stimulus working?

China's economic data is hard to read at the best of times and policy intentions and the effectiveness of policy measures are also difficult to read. We do know that growth has eased and that policymakers have taken a range of measures to prop up growth. We also know that China is an open economy and while they are trying to rely less on trade and infrastructure investment, the Chinese economy is vulnerable to swings in world trade.

China: Retail sales

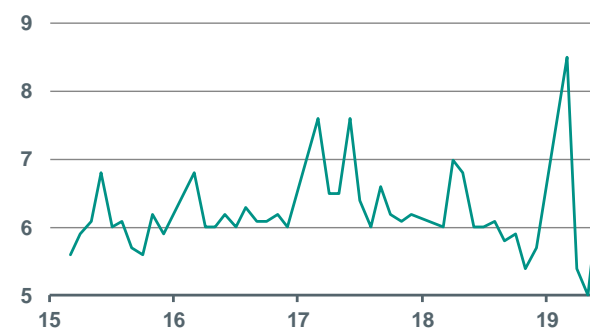
% yoy



Source: Bloomberg

China: Industrial production

% yoy



Source: Bloomberg

May data on industrial output and retail sales had been surprisingly weak. However, the June data was a lot better, suggesting that the stimulus measures are having a positive impact. Industrial production growth jumped from 5.0% yoy in May to 6.3% in June. Retail sales growth improved by a similar margin: up 9.8% yoy, versus 8.6% in May. Second quarter GDP growth slowed to 6.2% yoy, down from 6.4% in Q1. This was, however, in line with expectations. The qoq increase of 1.6% was actually slightly ahead of expectations.

Eurozone data unconvincing

While recent US and Chinese data was encouraging, data in the eurozone has been soft recently. Car registrations dropped 7.8% yoy in June, the weakest reading for the year. It must be said, however, that a powerful base effect is at play here and that effect is going to get much stronger in the two or three months ahead. Car sales were strengthening this time last year as buyers were trying to beat tighter emission rules. Car registration comparisons with a year earlier will be weak again in July and extremely weak in August, but will then improve spectacularly. Try to look at the underlying trend.

The German ZEW index, measuring the confidence in the German economy among analysts, was weak again in July. The expectations index deteriorated from -21.1 in June to -24.5 in July, close to the low for this cycle. The gradual improvement this series had shown since October last year has been completely reversed in just three months. The current conditions component fell from 7.8 in June to -1.1 in July, a multi-year low. While the ZEW index is not the most accurate gauge for the German business cycle, it is one of the earliest available indices and it shows what people are thinking. What the poor data is signalling is that the eurozone economy is hurting from the trade conflict and that Germany has a number of economic problems of itself. That is not new. What the data tells us is that Germany is, for the time being at least, unable to shake off these problems according to analysts.

Germany: ZEW index



Source: Bloomberg

Asia trade data weak, but not weaker

Looking at international trade data from Asia is like taking the pulse of the global economy. Data has weakened in recent months. The most recent data in Japan and Taiwan was soft again, but at least not weakening any further. Japanese exports were down 6.7% yoy in June, after falling 7.8% in May. Imports were down 5.2% yoy in June after -1.5% in May.

Taiwan's data actually improved a little in June: Exports were up 0.5% yoy having been down 4.8% in May, while imports were actually up 6.6% yoy after -5.9% yoy in May. Earlier published Korea trade data for June had been very weak.

Main economic/financial forecasts										
GDP growth (%)	2017	2018	2019e	2020e	3M interbank rate	11/07/2019	18/07/2019	+3M	2019e	2020e
United States	2.2	2.9	2.2	1.5	United States	2.30	2.30	2.20	1.90	1.80
Eurozone	2.6	1.9	0.7	0.9	Eurozone	-0.36	-0.37	-0.45	-0.45	-0.52
Japan	1.9	0.8	0.7	0.3	Japan	0.07	0.07	-0.10	-0.10	-0.10
United Kingdom	1.8	1.4	1.2	1.2	United Kingdom	0.77	0.77	0.80	0.80	0.80
China	6.9	6.6	6.2	5.8						
World	3.8	3.5	2.9	3.0						
Inflation (%)	2017	2018	2019e	2020e	10Y interest rate	11/07/2019	18/07/2019	+3M	2019e	2020e
United States	2.1	2.4	↑ 1.8	2.0	US Treasury	2.12	2.04	2.0	1.90	2.00
Eurozone	1.5	1.7	1.1	1.0	German Bund	-0.26	-0.31	-0.4	-0.50	-0.30
Japan	0.5	0.9	1.1	1.6	Euro sw ap rate	0.23	0.13	0.3	0.20	0.35
United Kingdom	2.7	2.5	1.4	1.8	Japanese gov. bonds	-0.14	-0.14	-0.1	-0.10	0.00
China	1.6	2.1	2.5	2.5	UK gilts	0.84	0.76	0.8	0.80	1.00
World	3.0	3.4	3.9	3.4						
Key policy rate	18/07/2019	+3M	2019e	2020e	Currencies	11/07/2019	18/07/2019	+3M	2019e	2020e
Federal Reserve	2.50	2.25	2.00	1.75	EUR/USD	1.13	1.12	1.12	1.12	1.20
European Central Bank	-0.40	-0.50	-0.50	-0.60	USD/JPY	108.5	107.3	104	100	95
Bank of Japan	-0.10	-0.10	-0.10	-0.10	GBP/USD	1.25	1.25	1.24	1.24	1.40
Bank of England	0.75	0.75	0.75	0.75	EUR/GBP	0.90	0.90	0.90	0.90	0.86
People's Bank of China	4.35	4.10	4.10	3.85	USD/CNY	6.87	6.88	6.90	6.90	6.70

Source: Thomson Reuters Datastream, ABN AMRO Group Economics.

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