High Frequency Economics®
Daily Data Analysis and Assessment of the Global Economy

Daily Notes on the **Global Economy**

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Two Tales Of Credit Woe

While the world watches equity markets decline—yesterday ended badly in North America and Europe, after a hard session in Asia—we macroeconomists at High Frequency Economics are watching the decline of bank lending in the United Kingdom and Japan. When bank lending grinds to a halt, it either means banks are not lending or borrowers are not borrowing. Either way, it is a sign of a banking system that is not doing what it is supposed to, specifically getting credit into the economy.

We hear a lot of talk about alternative sources of funding to bank credit in the twenty-first century: Crowd funding, direct access to capital markets, venture capitalists, non-bank lenders, foreign investment and such. But we have yet to see compelling empirical evidence that any or all of these sources of liquidity are important enough to substitute for the centuries-old model of banks as the primary financial intermediaries for individuals and small businesses, if not bigger ones, too.

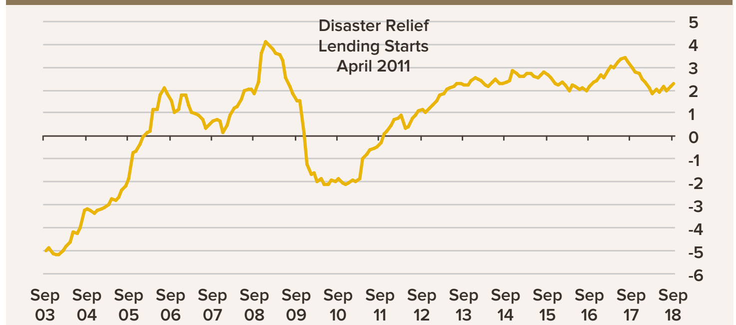
We are particularly interested in lending to households, because the health of the housing market depends on it. So does the health of many big-ticket industries, like autos and consumer durables. We are also interested in credit card lending, not just for financing consumer spending but because many small businesses depend on credit cards for working capital. If Joe the Plumber cannot charge his pipes on a credit card, financing the work until he is paid upon completion, he probably cannot do the job. As for SMEs, their health is critical to the future of the economy: Tomorrow's big businesses are today's small businesses. SMEs, not the biggest companies, create almost all the new jobs in any economy and are the source of much investment and innovation.

Call us old fashioned, but everything we ever learned about economics tells us that credit should grow roughly in proportion to the rate of growth of nominal GDP. When credit grows by less than that, it is constraining real activity as well as prices.

The bottom line of the Bank of England's latest *Credit Conditions Survey* is that credit growth is not likely to pick up any time soon. Were credit booming, that would be fine. However, bank lending in Britain has slowed from a 6% year-over-year rate of increase in August 2017 to a 0.7% yearly pace in August 2018. Bank credit conditions are broadly unchanged, so it is not like banks are trying to push loans out the door. Who can blame them? With Brexit just 24 weeks away, many businesses face great uncertainty, even existential threats. Consumers could lose their jobs. Businesses could fold altogether. *What bank wants to write a loan to a household or a business that may have only 23 weeks of income left to go? This is part of the cost of Brexit uncertainty.* In any case, 0.7% credit growth is insufficient to accommodate GDP growth of 2-1/2%—or even 1%—with 2% inflation. That kind of real GDP growth may be realized for brief periods, but it cannot be sustained.

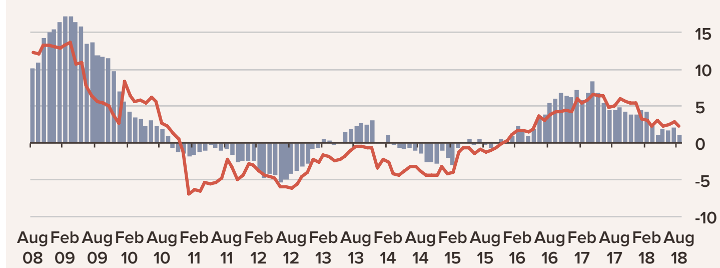
This is not the time or place to accuse the BoE of stealthily compelling banks to tighten up on lending. However, the Bank cannot be judged innocent of blame for causing this credit crunch in Britain.

Japan: Bank Lending, Percent Change Year Ago



United Kingdom: Growth Of Broad Money And Credit

Bars Are M4, Red Line Shows M4 Lending, Percent Change Year Ago



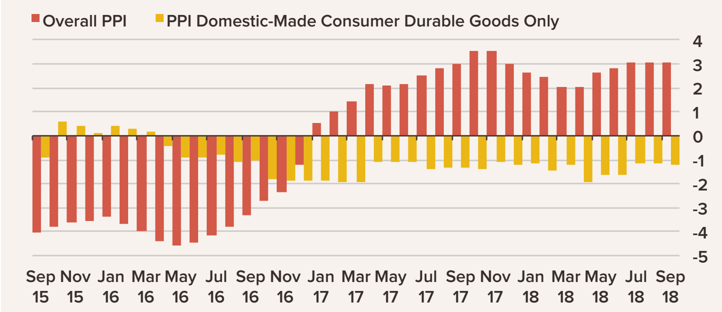
In Japan, bank lending is down to a 2.3% year-over-year pace, according to yesterday's report. It was up to 3-1/2% in the summer of 2017, and that was actually adequate to accommodate decent GDP growth at a time when prices were falling. However, 2.3% credit growth is insufficient when CPI is rising 1.3%. The bigger question is why is Japan's bank lending failing to grow faster than 2.3% per year given the trillions of yen of asset purchases the BoJ is undertaking: Every time the BoJ buys bonds from the open market, bank deposits and excess reserves go up. Why are these excess reserves not being loaned out?

Yields On 10-Year Government Bonds @ 22:00 GMT

	Coupon	Maturity	Yield (%)	Prev (%)	Chge (bps)	Δ vs U.S.	Prev Δ vs U.S.
United States	2.875%	8/28	3.144	3.191	-5		
Japan	0.100%	6/28	0.131	0.138	-1	-301	-305
Germany	0.250%	8/28	0.517	0.551	-3	-263	-264
United Kingdom	4.250%	12/27	1.536	1.591	-6	-161	-160
Italy	2.800%	12/28	3.561	3.503	+6	42	31
France	0.750%	11/28	0.879	0.899	-2	-227	-229
Canada	2.000%	6/28	2.496	2.550	-5	-65	-64
Australia	2.250%	5/28	2.724	2.748	-2	-42	-44
China	3.690%	5/28	3.595	3.620	-2	45	43

Note: All yields converted to a comparable semi-annual basis. Data collected 22:00 GMT daily, from market sources believed to be reliable by High Frequency Economics. These data are market indications only, not quotes.

Japan: Producer Price Index, Percent Change Year Ago



Our thinking is that there are not a lot of bankable propositions in Japan to lend to.

On the consumer side, there are fewer consumers in Japan each year as the population shrinks. Consumers borrow less at the late stages of their life cycles, with homes furnished and kids educated and out the door. Houses and autos are the big-ticket lending items for households. Japan actually needs fewer housing units each year as the population shrinks, and seniors buy new cars less often than younger households. Deceased consumers do not buy new cars at all.

On the business side, who needs to start a new business or invest in increasing capacity or output in Japan? The economy is shrinking with the population. Exports cannot pick up the slack, with heavy-hitting competitors in Asia stealing manufacturing businesses from Japan left and right. So even if banks in Japan want to lend more, they face a dearth of bankable propositions. These are all indications of a decaying economy.

The equity market news is bad. *However, the monetary data from Japan and Britain suggest that there is core weakness in the underlying economy. Whether depressed bank lending is the cause of this weakness or a symptom of it... well, does it matter?*

Euro Zone

There were no economic reports yesterday.

Today, EuroStat will release the industrial production report for August. *We expect a small 0.1% decline on the month, leaving the index 1.1% lower than a year ago and 4.9% lower than its peak in the spring of 2008.* Next week, the ECB will conduct its usual seven-day repo operation on Monday and Tuesday. Also Tuesday, EuroStat will release the international trade report for August. Wednesday, we will see revised CPI estimates for September, along with September data on vehicle registrations and August figures on construction output. Friday, current account estimates for August are due. Also next week, EU leaders will gather for a Summit on Wednesday, Thursday and Friday. The big event will be the Brexit deliberations on Thursday.

Italy

We did not see any economic releases yesterday.

No major releases are planned for today, either. Monday is the big day: Rome will present its budget to Brussels for review. Tuesday, we will see August data on industrial orders and international trade, as well as updated CPI estimates for September. Friday, we expect current account estimates for August.

Germany

There were no economic releases yesterday.

Revised CPI estimates for September are due today. The only release currently scheduled for next week is the ZEW survey for October, due Tuesday. However, before the week is through, we should see August data on import prices and WPI for September.

A Quick Look At Upcoming Events

	Friday	Monday
Japan	M2+CDs (9) **Tertiary Index (8)**	Industrial Production (8r)
Australia	Mortgage Approvals (8)	Nothing
Euro Zone	**Industrial Production (8)**	Call For Repo Tenders
Germany	CPI (9r)	Nothing
France	Nothing	Nothing
United Kingdom	Nothing **24 Weeks To Brexit**	Nothing **165 Days To Brexit**
Canada	Teranet HPI (9)	Loan Officer Survey (Q3)
United States	**Michigan Sentiment (10p)** Import Prices (9) Treasury Budget (9)	Empire State Survey (10) **Retail Sales (9)** Inventories (8)
Worldwide	**IMF Annual Meetings**	Nothing

Underscore=Already released *Italics*=Estimated release date
CCI/BCI/BSI=Consumer/Business Confidence HPI=House Price Index

Further Down The Road...

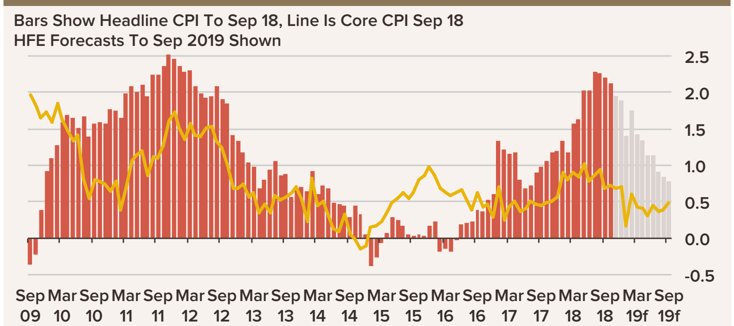
October 8 - 14	IMF Annual Meetings—Bali
October 15	Italy Budget Submitted To EU
October 18	EU Summit
October 24	Canada—BoC Governing Council Decision
October 25	Euro Zone—ECB Governing Council Decision
October 29	United Kingdom—Budget 2019-20
October 31	Japan—BoJ Board Decision
November 1	United Kingdom—MPC Decision
November 6	Australia—RBA Board Meeting
November 8	United States—FOMC Decision
November 30	G-20 Summit—Buenos Aires
March 29, 2019	**Brexit**

Japan

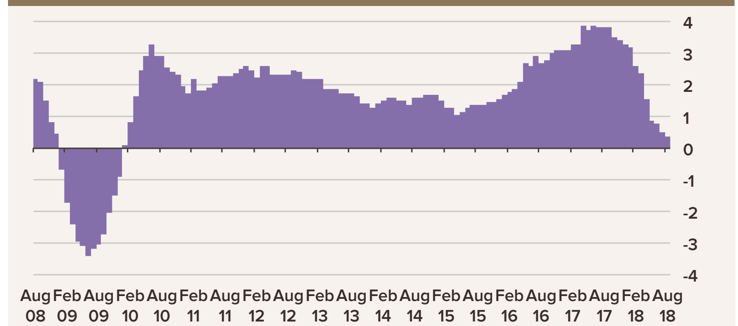
The BoJ reported yesterday that **bank lending** was up 2.3% over the 12 months ended September. That is better than the 2.2% year-over-year rise in August, but we cannot find anything else good to say about this result. *How can we hope for Japan's economy to "recover" to even 1% real GDP growth and 2% inflation when bank lending is only rising 2.3% year-over-year? Furthermore, how can we not be amazed and alarmed that banks are not finding bankable propositions to pump excess reserves out the door, even as the BoJ is stuffing its coffers with trillions of yen generated by its asset purchases each year? Sorry, but we see no good news in this report: Bank lending growth is inadequate to support desired economic activity by all reasonable standards, and it is not picking up, either.* We discuss bank lending in Japan in our essay above.

The **producer price index** for September was reported 3.0% higher than a year ago, as it was in July and August. The secret to understanding the PPI data is to strip away prices of stuff that does not affect CPI. So ignore raw materials, intermediate goods and capital goods: **Prices of domestically manufactured consumer goods at the factory gate** were up just 1.1% year-over-year in September after a 1.0% rise in the 12 months ended August. If you strip out non-durable goods prices—that would be mostly food—**prices of consumer durables** actually declined 1.2% in the 12 months ended September after a drop of 1.1% over the 12 months ended August. Now we are looking at the part of PPI the BoJ can affect with monetary conditions, and that directly feeds into CPI. *We see no sign of any threat to consumer price stability coming down the pipeline, at least not from domestic costs.*

France: Consumer Price Index, Percent Change Year Ago



Canada: New Housing Prices, Percent Change Year Ago



Today, look for September figures on the growth rate of the broad monetary aggregates from the BoJ. Also today, the tertiary sector index for August is due. *We estimate the tertiary index, a bellwether for GDP growth, rose just 0.1% in August.* Monday, METI will release revised estimates of industrial production for August. Then, the calendar is empty until Thursday, when we will see September data on international trade. Friday, BoJ Governor Kuroda will deliver a speech to a banking audience in Tokyo.

United Kingdom

The Bank of England's quarterly ***Credit Conditions Survey*** showed an increase demand for unsecured credit in the third quarter—specifically, for credit cards—but decreased supply. Lending supplied to small businesses was reported flat, with demand for loans from SMEs reported softer. Demand for mortgages was about unchanged, while demand for refinancing jumped. *We are watching the progressive slowdown in bank lending with some alarm.* Bank lending was last reported just 0.7% higher than a year ago in August. That figure was 6% one year earlier. *Dare we call a decline in the yearly rate of bank lending growth from 6% to 0.7% catastrophic? Then again, who can blame banks for not wanting to take on risk with an existential event like Brexit looming just half a year down the road?* ***Call us old fashioned, but why shouldn't we be concerned that a credit crunch is corseting all prospects for economic growth in Britain, regardless of the way the Brexit transition works out?*** We discuss all of this above.

Here is our daily countdown: **Only 168 days remain until Brexit.** *That is not a lot of time, eh? Hard Brexit remains the most likely outcome, in our opinion. It is the default result if no other arrangement can be negotiated. No plausible plan that leads to any other result is in sight.* **Join our global webinar next Thursday for an in-depth assessment of what a hard Brexit outcome means on both sides of the Channel.** Click here for more information or to register.

No economic releases are due today. Tuesday, NatStats will release the latest employment report, including claimant-based unemployment data for September and ILO-based data for August. We will also see August data on wages in this report. Wednesday will bring the CPI and PPI reports for September. Thursday, NatStats will publish the official report on retail sales volumes for September. Friday, we will get an update on the public sector balances for September. Also Friday, BoE Governor Carney will be addressing the Economic Club of New York.

France

INSEE yesterday confirmed its flash estimate that **headline CPI** was 2.2% higher than a year ago last month. **Underlying CPI**, reported for the first time in yesterday's release, slowed to a 0.7% year-over-year rate of increase in September from 0.9% in August. *Keep in mind that the yearly rate of increase of headline CPI will fall to the core rate when energy prices stop rising... as eventually they must.*

No economic releases are due today, and next week's calendar is completely empty.

Australia

We did not see any economic reports yesterday.

Today, we expect August data on mortgage approvals from ABS. *We estimate approvals fell 0.6% on the month for an 8.1% year-over-year drop. The trend in approvals has been slowing, to the delight of the RBA Board.* Tuesday, the RBA will publish the minutes of the Board meeting held earlier this month. Wednesday, the September employment report is due.

Canada

StatCan's **new house price index** was just 0.4% higher than a year ago in August after a 0.5% year-over-year increase in July. *That is not much.* New house prices were flat in Toronto on the month—seasonally adjusted, of course—and down 0.2% in Vancouver. Overall, new home prices are rising only slowly, and slowing. Of course, new homes are only a slice of the residential real estate market. Today, we will see a broader measure of housing prices from Teranet: Its index covers fewer geographic areas than StatCan, but it encompasses all residential transactions. Teranet's index is also more current.

Teranet's composite-11 house price index for September will be today's economic release. Monday, we will see the BoC's quarterly *Senior Loan Officer Survey*. Tuesday, we expect August data on international securities flows from StatCan. Wednesday, the survey of manufacturing for August is due. Thursday, StatCan will publish August data on unemployment insurance claims. Friday, we will see the retail sales report for August and the consumer price index for September.

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