High Frequency Economics®

Daily Data Analysis and Assessment of the Global Economy

HFE Webinar:
Calendar Changes, World's Economic Woes Increase?

Carl Weinberg & Rubeela Farooqi
High Frequency Economics

High Frequency Economics®

Daily Data Analysis and Assessment of the Global Economy

The World's Economic Woes Shift Into A New Year

Carl B. Weinberg
Chief Economist

www.hifreqecon.com/Jan2020

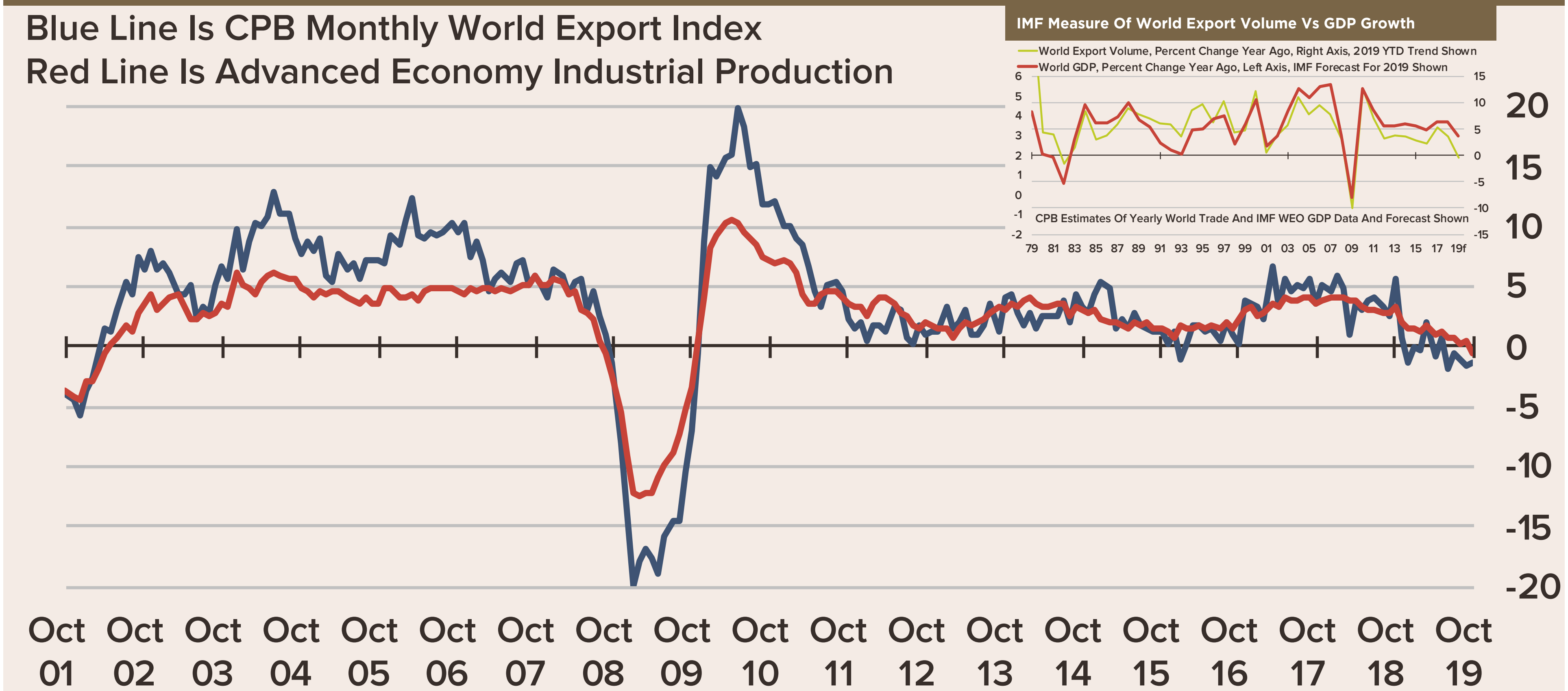
High Frequency Economics: Where We Stand

- The latest figures show **world trade** was contracting through October. Nothing comes from that!
- **Global interest rates** are still mostly negative, at least at the short end.
- **Euroland's industrial recession** cannot end until inventories fall back into line. There is no sign of that happening yet.
- **CPI-based inflation** will stay below target for a long time in advanced economies. The ECB will not be hiking rates or reducing the size of its balance sheet before 2020.
- The BoJ is stealthily **tapering JGB purchases** to prevent yields from falling too far below zero. The population is aging and shrinking: Demand will fall faster than supply, CPI will fall.
- **Brexit** is a supply shock that will cause stagflation. The areas most affected will be services, construction, agriculture, and of course the City. Immigration will be quashed—that is the problem.
- **China will report GDP growth of 6.3%** year-over-year for Q4. This will be a positive surprise for financial markets.
- **The risk of war between the United States and Iran went up last night** when Iran attacked U.S. bases. Oil prices may be rise, but they will not affect inflation metrics or growth much.

World Trade Volumes Are Declining Outright: Nothing Good Can Come From This

The latest figures from the Dutch Central Planning Bureau show world trade was contracting as of October. Everytime world trade has turned down in the postwar period, world GDP has turned down—slowed, if not contracted—in parallel. We have no plausible comprehensive explanation for the dip in global exports, so we cannot be sure if it will extend further or stop right here. Unless current trends reverse, we will see the fourth yearly dip in global exports since the data began in the 1970s!

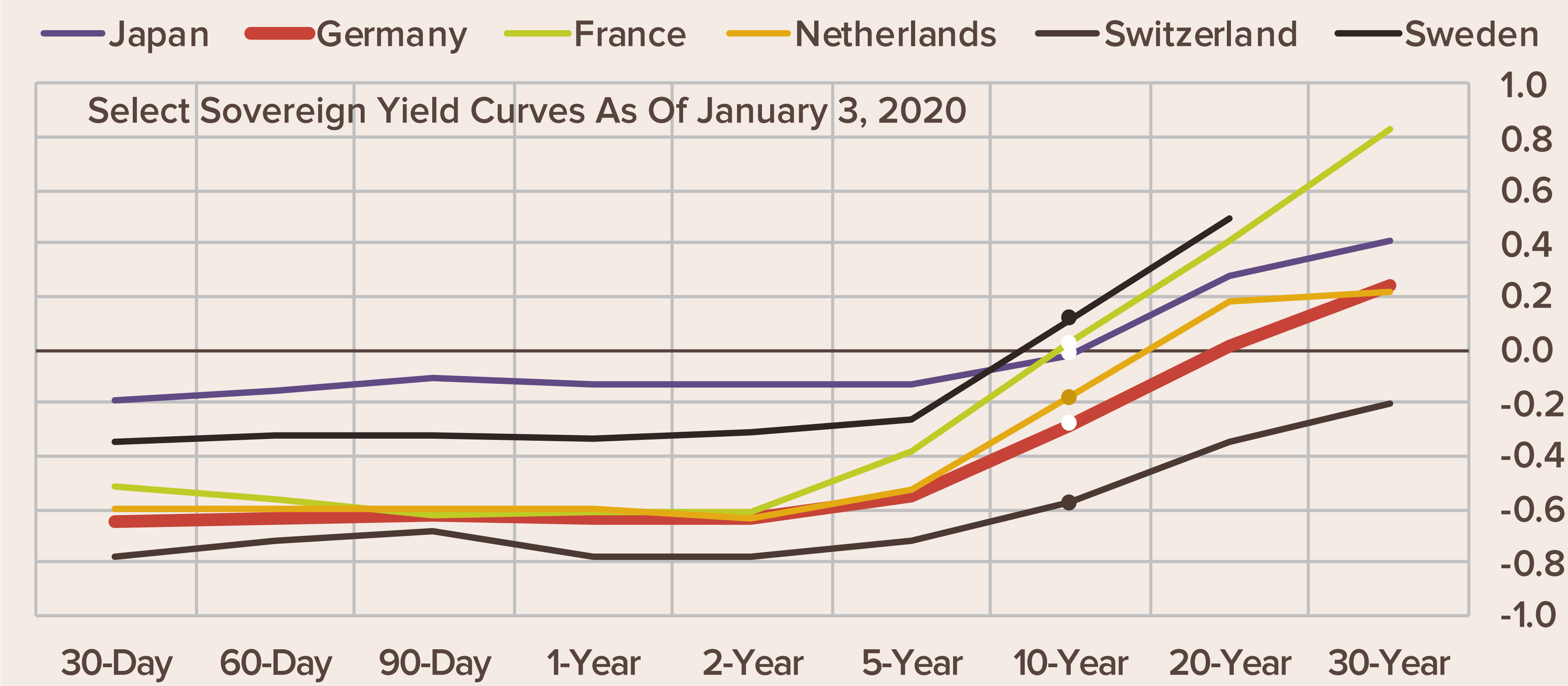
World Export Volume, Percent Change Year Ago



Bond Yields Are Still Negative In Many Markets: Nothing Good Can Come From This

Negative bond yields and interest rates mean that money has no value: You have to pay people to hold money without risk. Negative yields mean people are better off spending their savings, and that is a threat to price stability. Negative yields mean investors are driven out of bonds and cash into stocks, where a bubble may inflate. Negative yields put a cashflow crimp on financial intermediaries like pension funds and insurance schemes. Negative yields mean there are no profitable bank loans. Falling yields undermine the solvency of large pools of money. Negative short term sovereign yields are the benchmarks for pricing all credit in an economy. *Uh, oh!*

HFE's League Of Negative 10-Year Bond Yields



HFE's Oil Price Calculus

HFE estimates that about half of any percentage-point increase in crude oil prices gets passed through to consumer-facing energy products.

Petroleum based products are estimated to make up about 4% of the CPI basket of goods.

Therefore: $\%\Delta CPI = (\%\Delta CrudeOilPrice / 2) * .03$

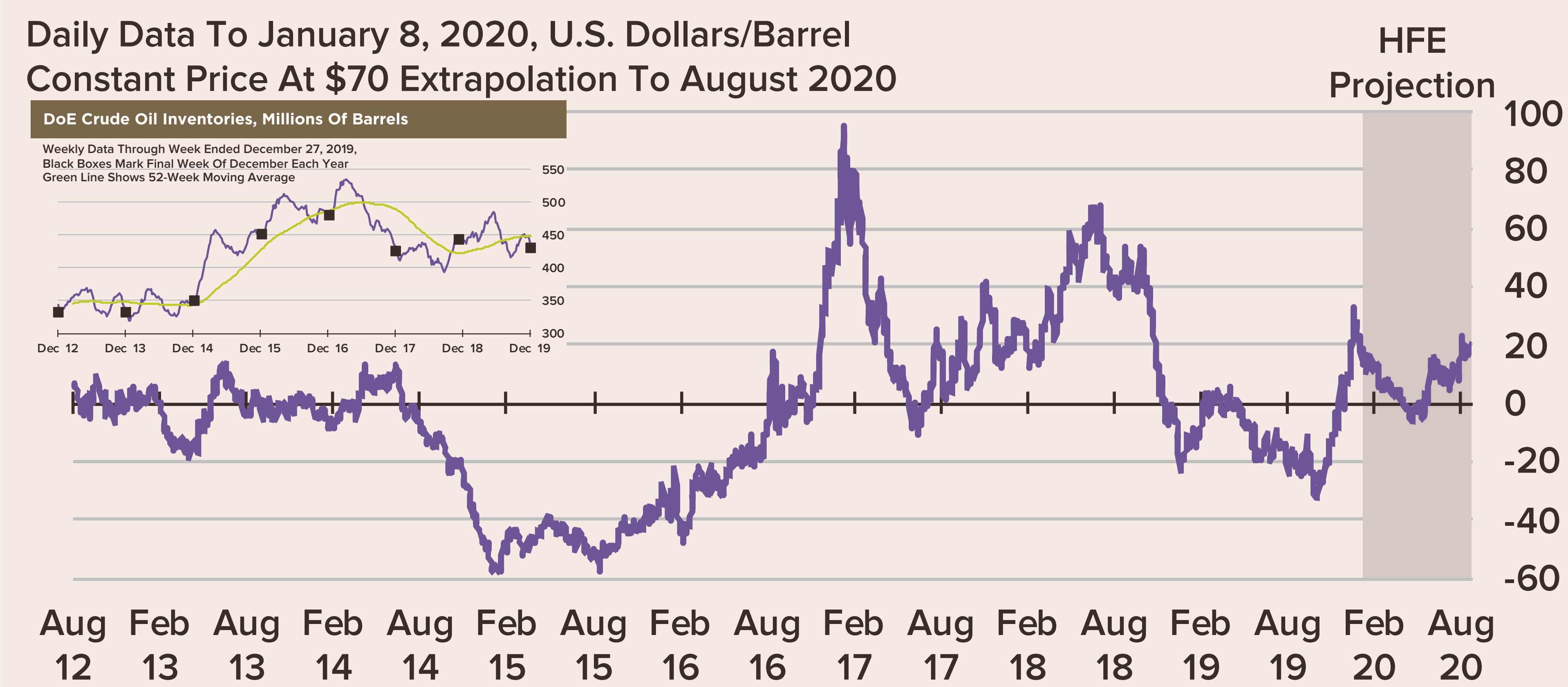
Or, a 20% rise in crude oil prices means energy prices in CPI will rise by 10%. That should push up the yearly rate of CPI increases by 0.3 percentage points. It will be a visible pickup, but not a catastrophic one by any means.

- If oil prices hold around $70 per barrel for the rest of this month, they will average just 15% higher than a year ago.
- When evaluating the impact of any oil price shock on an economy, remember that the global oil market is awash with stockpiles of unsold crude. The U.S. tight-oil revolution means Iran—and OPEC—is no longer the swing supplier of crude oil to advanced economies. OPEC produces only 30% of the global oil supply.
- The intensity of oil use within most advanced economy has dropped a lot since the 1970s.

Brent Prices At $70 Per Barrel Should Scare No One

Brent crude oil prices at $70 per barrel, if sustained, will leave them 15% higher than a year ago in January. The year-over-year increase in Brent prices—that is what matters to inflation metrics based on year-over-year changes in CPI—will drop to zero or slightly below by spring if $70 is maintained, and will print less than 20% by the end of the summer. The back-wardated futures curve for Brent crude points to a $6 drop in crude oil prices over the next six months. DoE data and IEA forecasts show inventories are ample and rising, assuming little output of crude from Iran in any case.

Brent Crude Oil Price Base Scenario, Percent Change Year Ago

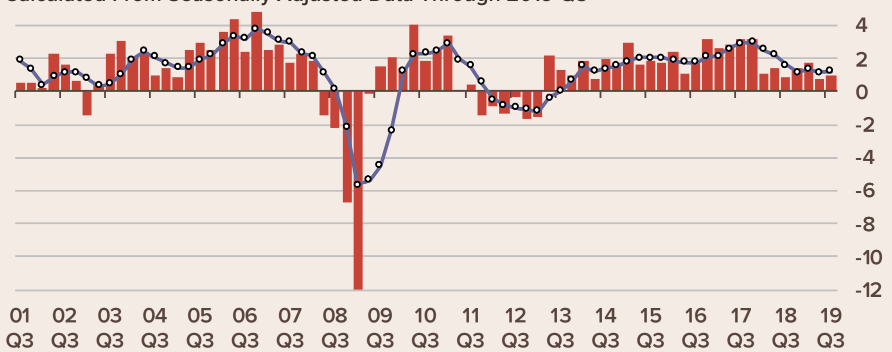


Euroland's Industrial Recession Will Only Get Worse

All indications signal an industrial recession in the Euro Zone. Monetary policy is tapped out. However, easy money does not force firms to liquidate the huge excess inventories of unsold goods they currently hold, financed today at negative interest rates. Easy money will not restore economic confidence or boost consumer spending. Easy money will not get banks lending again, because the capital adequacy hurdles banks face will not be dissipated by central bank policies. The near-term outlook for Euroland GDP is grim.

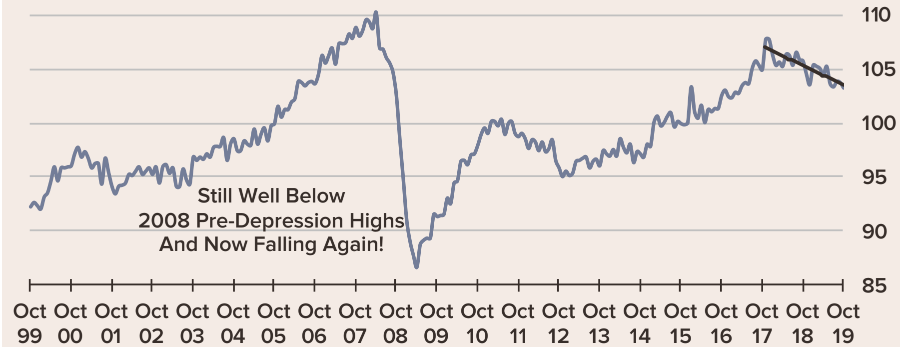
Euro Zone: GDP

Seasonally Adjusted Annual Rate (Bar) and Percent Change Year Ago (Line)
Calculated From Seasonally Adjusted Data Through 2019 Q3



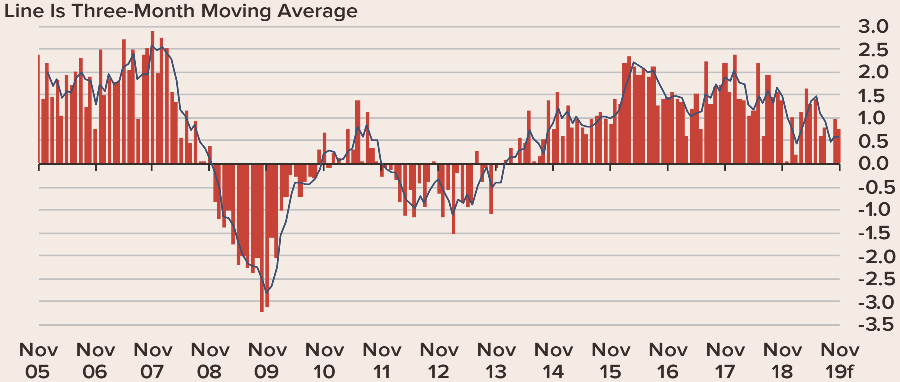
Euro Zone: Industrial Production Index

Seasonally Adjusted, 2015 = 100, Excludes Construction
Trend Since 17 Q4 Drawn



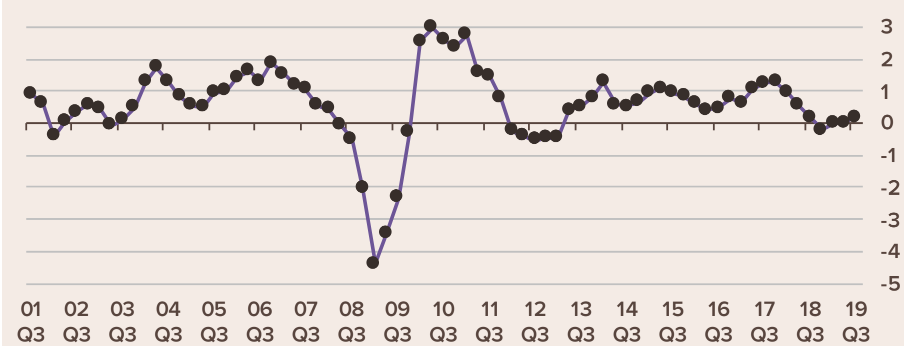
Euro Zone: Employment, Percent Change Year Ago

Line Is Three-Month Moving Average



Euro Zone: GDP Per Worker — Productivity — Growth

Percent Change Year Ago, EuroStat Data
Calculated By HFE From Seasonally Adjusted Data Through 2019 Q3

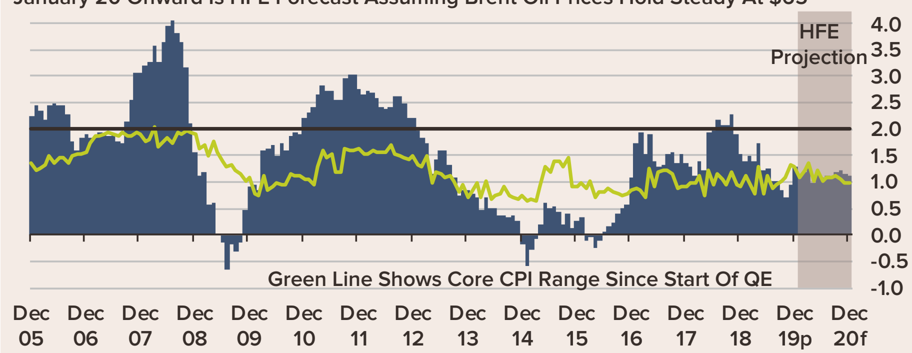


The ECB's Big Bazooka Is Out Of Ammo

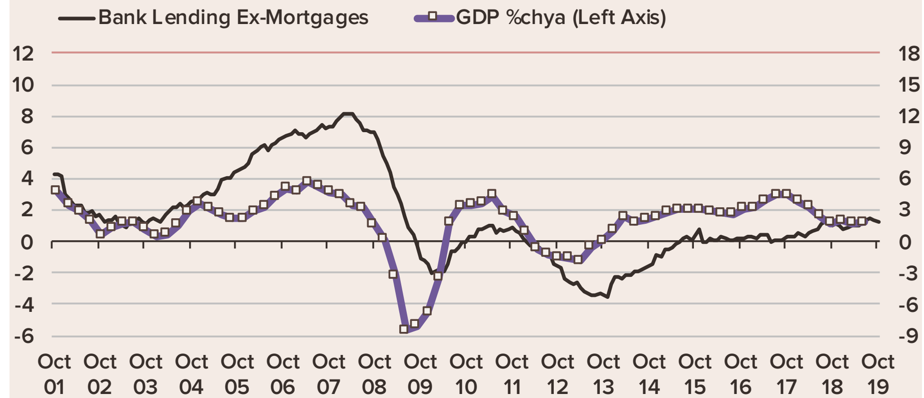
People are looking to the ECB for solutions that will mitigate the economic downturn. So far, we have heard nothing new from ECB President Lagarde. We don't think more QE or more-negative negative interest rates can get banks to lend more, or raise economic confidence, or get companies' inventories down without production cuts. In any case, more bond purchases are legally out of the question. Markets will be disappointed by milquetoastian tweaks to ECB policy, but the central bank is out of options.

Euro Zone: CPI, Percent Change Year Ago

Blue Bars Are CPI, Green Line Is Core CPI, Black Line Is ECB Inflation Target
January 20 Onward Is HFE Forecast Assuming Brent Oil Prices Hold Steady At $65

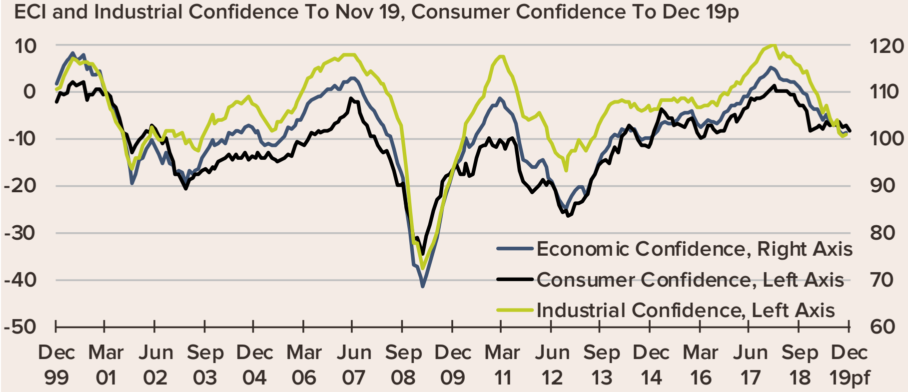


Euro Zone: Bank Lending Vs GDP, Percent Change Year Ago



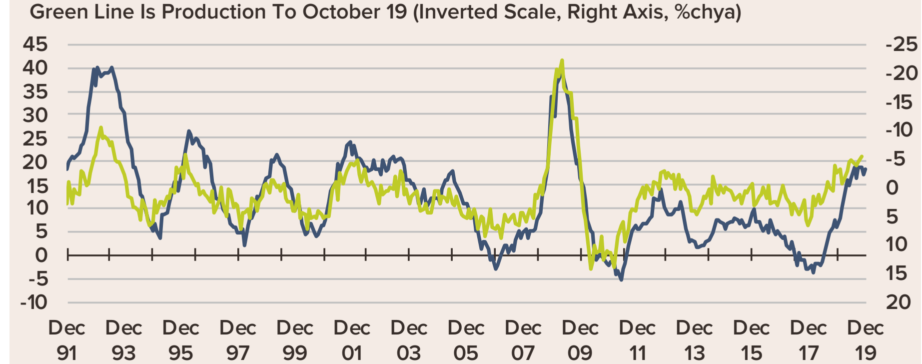
Euro Zone: Economic Confidence Indexes

ECI and Industrial Confidence To Nov 19, Consumer Confidence To Dec 19p



Germany: IFO Inventory Index

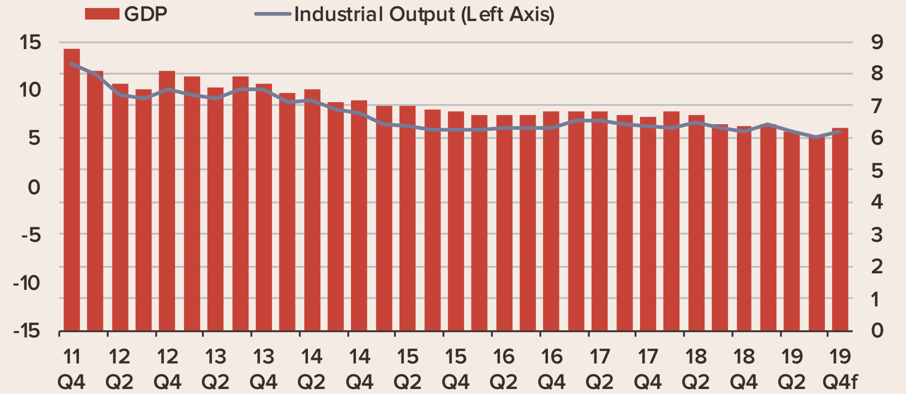
Blue Line Is IFO Inventory Index To December 19 (Left Axis)
Green Line Is Production To October 19 (Inverted Scale, Right Axis, %chya)



China's Trump Slump Will Not Last Forever...

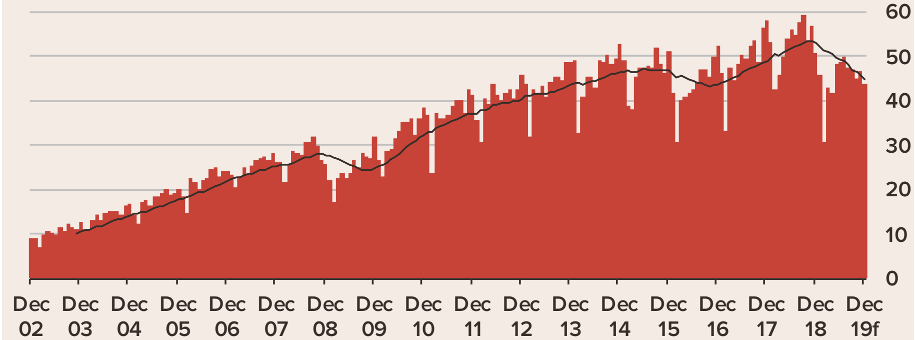
Monthly industrial production reports have been miserable, but not as miserable in Q4 as in Q3. Also, there is a basis effect from the year-ago drop in exports that will make year-over-year increases in production look bigger. So both industrial production and GDP should print faster year-over-year in the fourth quarter. This will be a positive surprise for the markets.

China: GDP Vs Industrial Output, Percent Change Year Ago



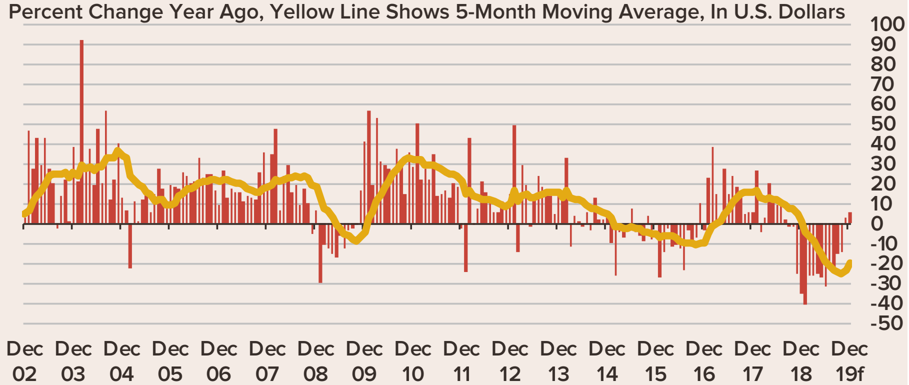
China: Gross Trade With The United States

Exports To Plus Imports From The United States
Billion Of U.S. Dollars, 12-Month Moving Average Shown



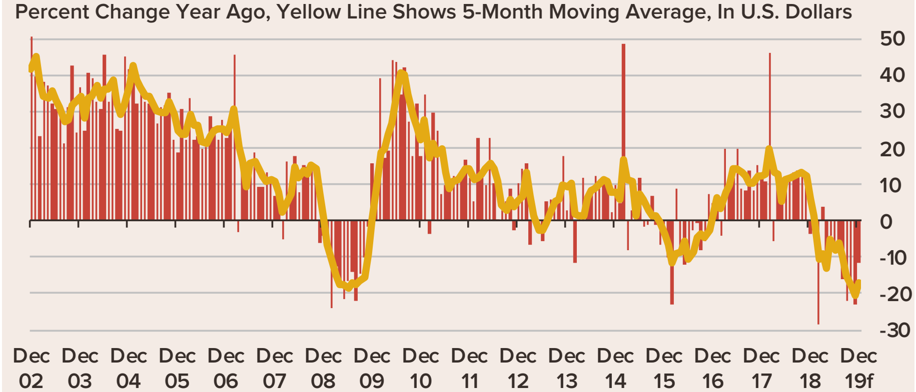
China: Monthly Imports From The United States

Percent Change Year Ago, Yellow Line Shows 5-Month Moving Average, In U.S. Dollars



China: Monthly Exports To The United States

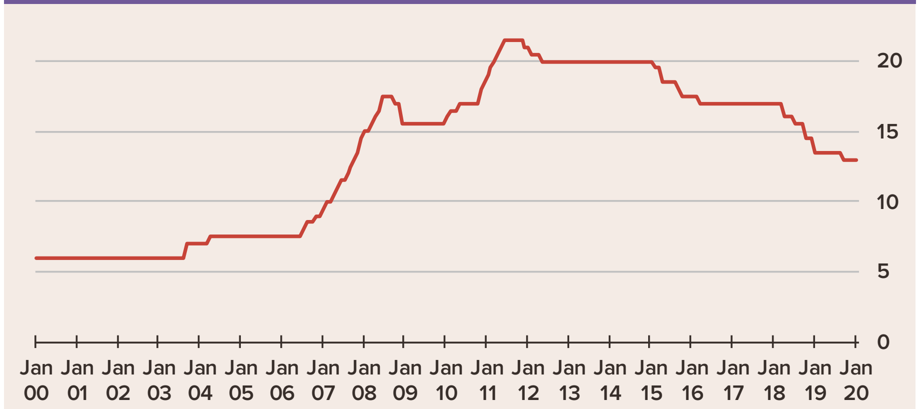
Percent Change Year Ago, Yellow Line Shows 5-Month Moving Average, In U.S. Dollars



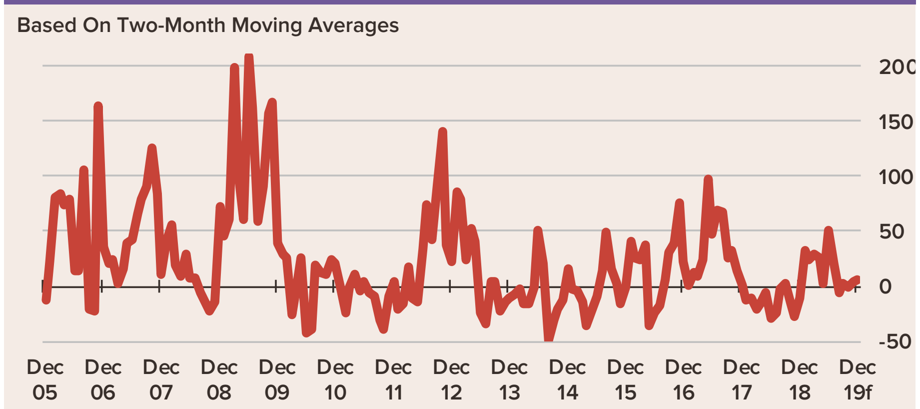
Monetary Policy To China's Rescue?

A good part of the recent cuts in the required reserve ratio will simply keep the year-over-year growth rate of monetary stimulus steady. Take the reserve requirement cut that just took effect last week. A one percentage point cut in the RRR in January 2019 added at least a percentage point to the growth rate of quasi-money, or domestic credit. Without a knock-on cut this year, the yearly growth rate of quasi-money would fall. We expect the PBOC to cut the RRR again in September to offset impact of the year ago cut on credit growth.

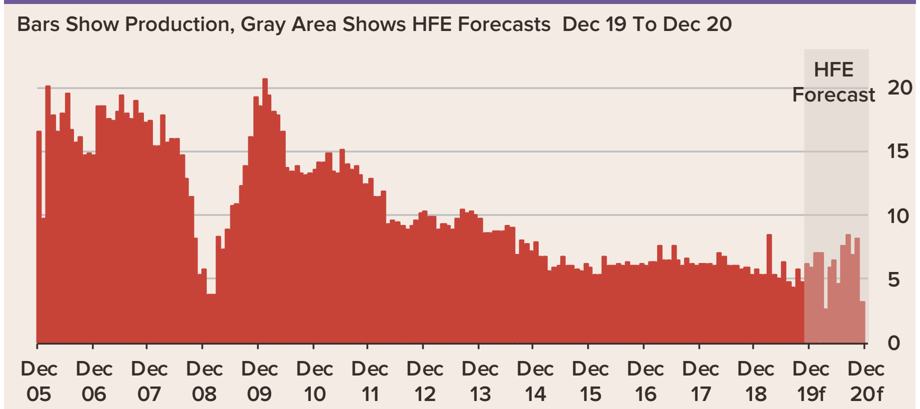
China: Required Reserve Ratio At Major Banks, Percent



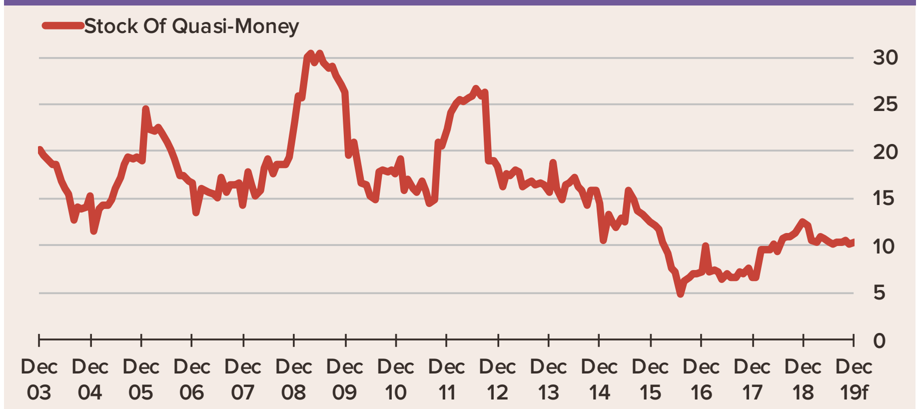
China: Aggregate Financing, Percent Change Year Ago



China: Industrial Production, Percent Change Year Ago



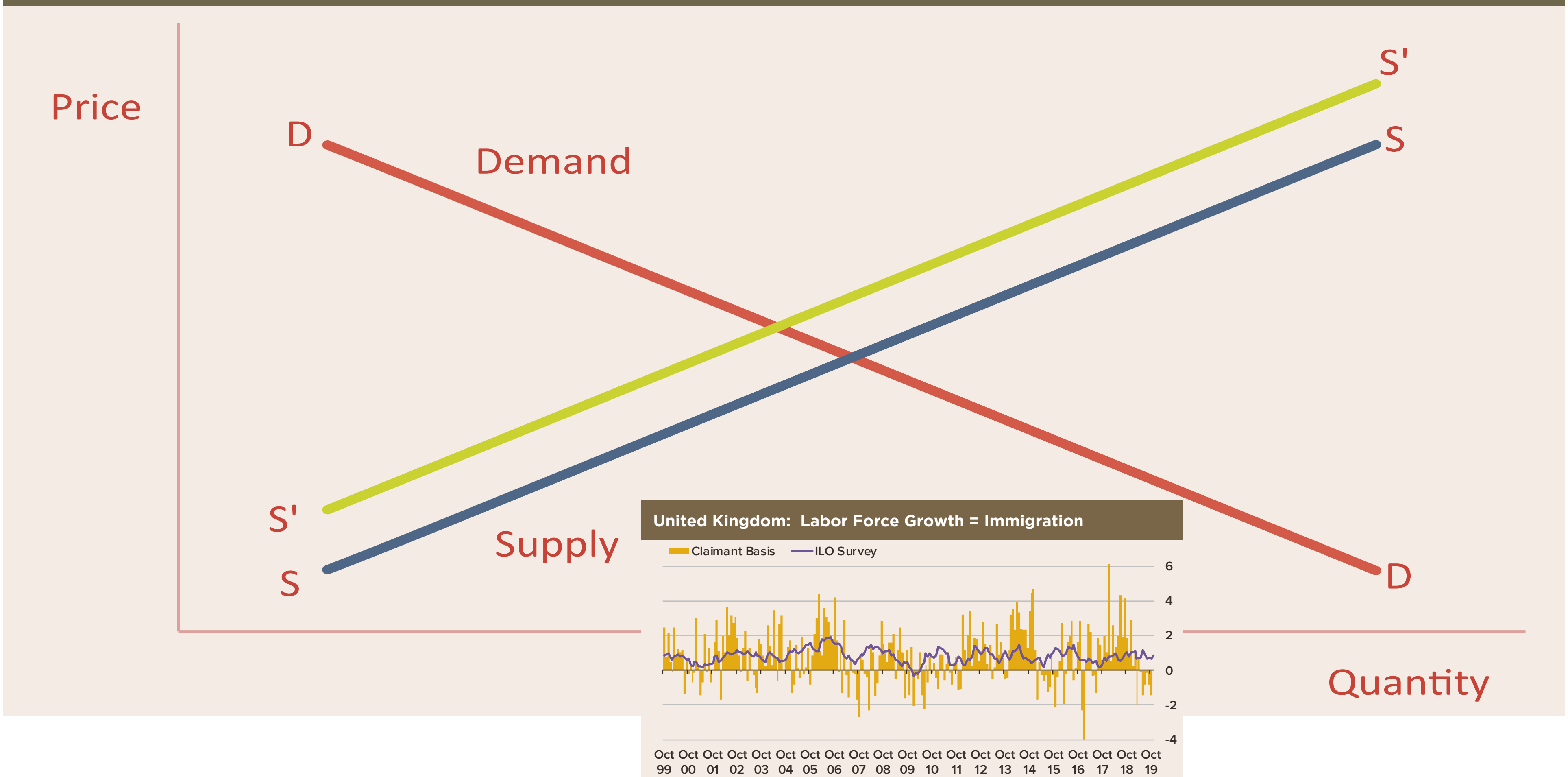
China: Growth Of Domestic Credit, Percent Change Year Ago



Brexit In A Single Chart

Pre-Brexit transition uncertainty crimps investment, shifting the demand curve to the left initially. This is the recession with below-target inflation metrics we are experiencing right now. After Brexit, the supply curve will shift to left, as immigrant workers lose jobs and return home in the face of hostile conditions for employment and living in Britain. A rise in prices plus a reduction in output is the outcome—a stagflation, to invoke the language of the 1970s. The best BoE policy in stagflation is to put interest rates as low as they can go to encourage investment to offset the shortfall of labor.

Supply And Demand Curves



High Frequency Economics®

Daily Data Analysis and Assessment of the Global Economy

Outlook 2020: Growth Momentum Fading?

Rubeela Farooqi
Chief U.S. Economist

www.hifreqecon.com/Jan2020

U.S. Economic Outlook: Key Highlights

- The US economy is set to grow at a more moderate pace in 2020, broadly in line with the longer-run estimate for growth in the Fed's latest Summary of Economic Projections.

- The consumer will continue to drive growth going forward. Residential investment is also set to make a positive contribution. Business confidence and investment may benefit from less uncertainty on trade.

- The labor market should remain strong, with the unemployment rate at a 50-year low and measures of underemployment improving.

- Inflation is likely to gradually rise towards the Fed's 2% target.

- Against a backdrop of moderate growth, a strong labor market and low inflation, the Fed is likely to stay on the sidelines in 2020, unless there is a material change in the outlook.

Modest Growth, Low Inflation And Fed On Hold

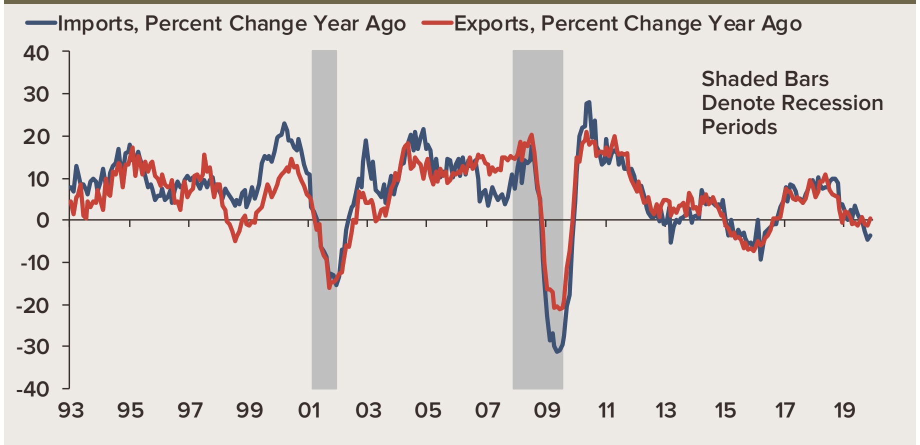
HFE's Economic & Financial Forecasts

%ch From Previous Period, Annual Rate, Except Where Noted; ***Forecasts In Bold***

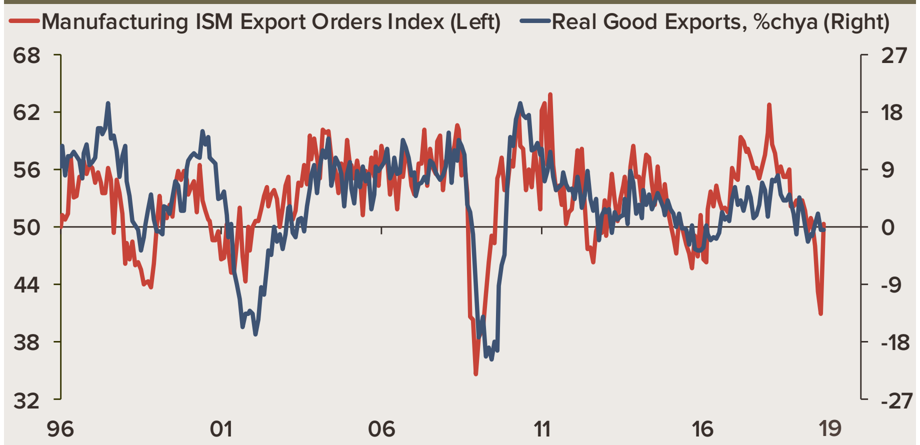
	2019				2020				Calendar Average			Q4/Q4		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2018	2019	2020	2018	2019	2020
Real GDP	3.1	2.0	2.1	**2.0**	**1.2**	**2.0**	**2.0**	**2.0**	2.9	2.3	**1.8**	2.5	**2.3**	**1.8**
Final Sales	2.6	3.0	2.1	**1.9**	**1.8**	**2.0**	**2.0**	**2.0**	2.8	2.2	**2.0**	2.2	**2.4**	**1.9**
Domestic Final Sales	1.8	3.6	2.2	**1.6**	**2.1**	**2.0**	**2.0**	**2.0**	3.0	2.3	**2.1**	2.6	**2.3**	**2.1**
Net Exports (pct pt contr)	0.7	-0.7	-0.1	**0.2**	**-0.4**	**-0.1**	**-0.1**	**-0.1**	-0.3	-0.2	**-0.2**	-0.4	**0.0**	**-0.2**
Inventories (pct pt contr)	0.5	-0.9	0.0	**0.1**	**-0.5**	**0.0**	**0.0**	**0.0**	0.1	0.2	**-0.2**	0.3	**-0.1**	**-0.1**
Consumption	1.1	4.6	3.1	**2.0**	**2.0**	**2.0**	**2.0**	**2.0**	3.0	2.6	**2.3**	2.6	**2.7**	**2.0**
Business Fixed Investment	4.4	-1.0	-2.3	**0.2**	**3.1**	**3.0**	**3.0**	**3.4**	6.4	2.2	**1.6**	5.9	**0.3**	**3.1**
Structures	4.0	-11.1	-9.9	**-3.9**	**1.5**	**2.0**	**2.0**	**2.5**	4.1	-4.1	**-1.6**	2.6	**-5.4**	**2.0**
Equipment	-0.1	0.8	-3.8	**-0.2**	**1.5**	**2.0**	**2.0**	**2.5**	6.8	1.5	**0.7**	5.0	**-0.8**	**2.0**
Intellectual Property	10.9	3.6	4.6	**3.3**	**6.0**	**5.0**	**5.0**	**5.0**	7.4	7.5	**4.8**	9.3	**5.6**	**5.2**
Residential Investment	-1.1	-2.9	4.6	**3.4**	**2.0**	**1.0**	**1.0**	**0.0**	-1.5	-1.7	**1.8**	-4.4	**1.0**	**1.0**
Exports	4.2	-5.7	0.9	**-1.0**	**-1.0**	**2.0**	**2.0**	**2.0**	3.0	-0.2	**0.1**	0.4	**-0.5**	**1.2**
Imports	-1.5	0.0	1.8	**-2.1**	**2.0**	**2.5**	**2.5**	**2.5**	4.4	1.4	**1.3**	3.2	**-0.5**	**2.4**
Government	2.9	4.8	1.7	**1.0**	**1.8**	**1.6**	**1.6**	**1.6**	1.7	2.2	**1.8**	1.5	**2.6**	**1.7**
Inventories (ch $B annual rate)	116	69	69	**73**	**48**	**50**	**52**	**54**	48	82	**51**	93	**73**	**54**
CPI	0.9	2.9	1.8	**2.0**	**2.3**	**2.4**	**2.5**	**2.5**	2.4	1.8	**2.3**	2.2	**1.9**	**2.4**
Core CPI	2.3	1.8	3.0	**2.1**	**2.5**	**2.4**	**2.5**	**2.5**	2.1	2.2	**2.4**	2.2	**2.3**	**2.4**
Core PCE Prices	1.1	1.9	2.1	**1.9**	**2.0**	**2.1**	**2.1**	**2.1**	1.9	1.7	**2.0**	1.9	**1.7**	**2.1**
Unemployment (%, level)	3.9	3.6	3.6	**3.5**	**3.5**	**3.5**	**3.5**	**3.5**	3.9	3.7	**3.5**	3.8	**3.5**	**3.5**
Federal Budget Balance ($B, FY)									-779	-984	**-1050**			
% Of GDP									-3.8	-4.6	**-4.8**			
												End Of Year		
Fed Funds Target (%, EOP)	2.38	2.38	1.88	1.63	**1.63**	**1.63**	**1.63**	**1.63**	1.8	2.1	**1.6**	2.38	1.63	**1.63**
10-Year Treasury (%, EOP)	2.4	2.0	1.7	1.9	**1.8**	**1.9**	**2.0**	**2.1**	2.8	2.1	**1.9**	2.7	1.7	**2.1**
30-Year Treasury (%, EOP)	2.8	2.5	2.1	2.4	**2.2**	**2.3**	**2.4**	**2.5**	3.0	2.5	**2.3**	3.0	2.3	**2.5**
S&P 500 (level, EOP)	2834	2942	2977	3220	**2863**	**2825**	**2788**	**2750**	2716	3231	**2825**	2507	2950	**2750**

Trade Flows And Manufacturing Weak

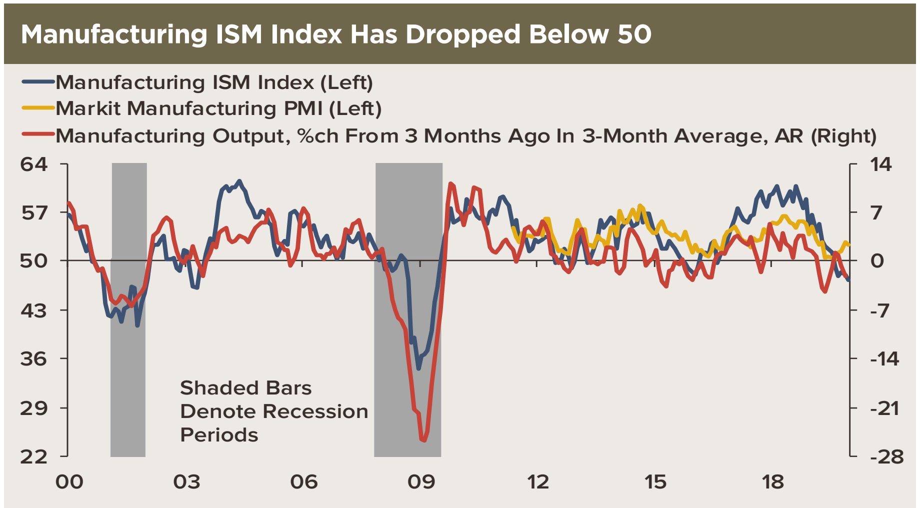
US Exports Have Weakened In Line With Global Trade Flows

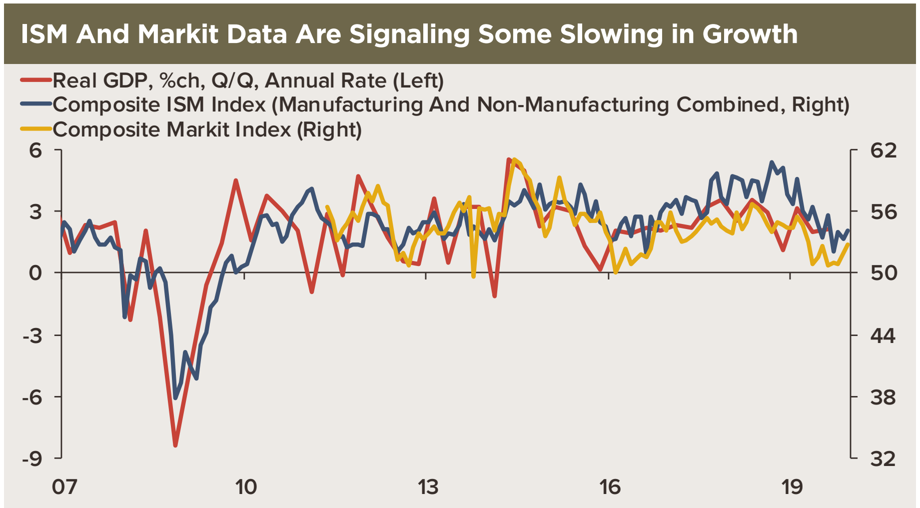


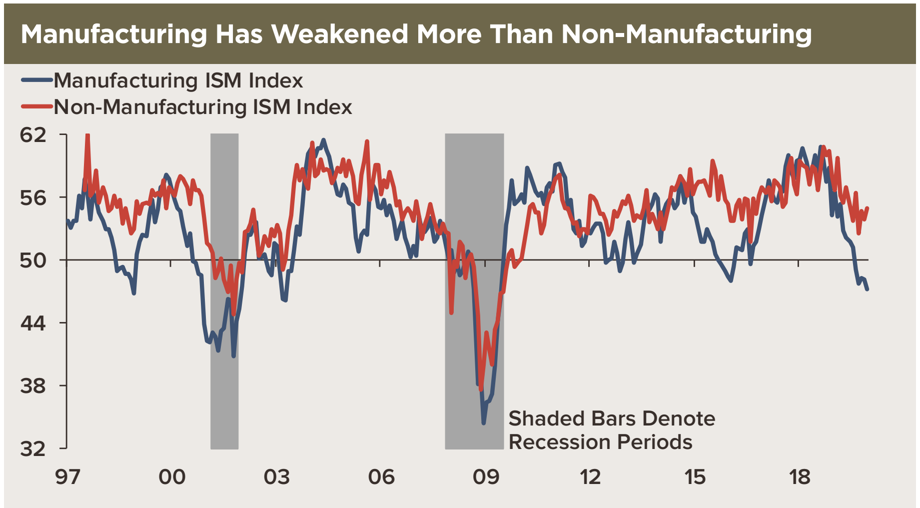
Manufacturing ISM Export Orders Index Remains Weak



Manufacturing Weak But No Spillover To Non-Manufacturing

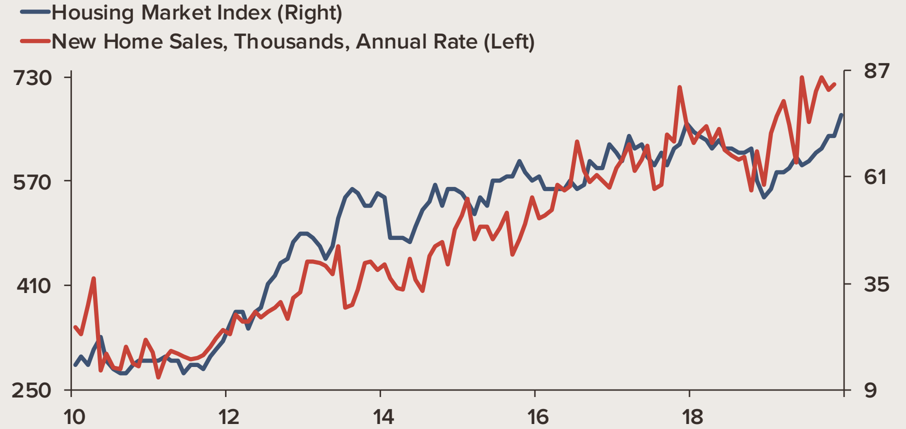




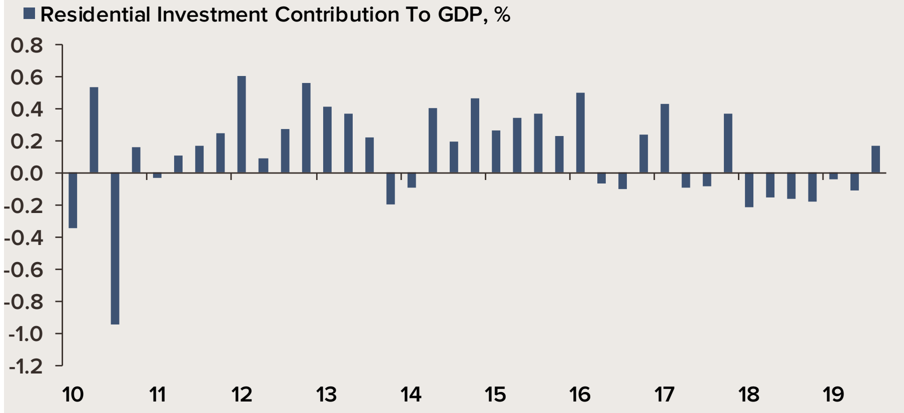


Residential Investment Positive

Housing Market Index Rose In 2019 After A Drop In 2018

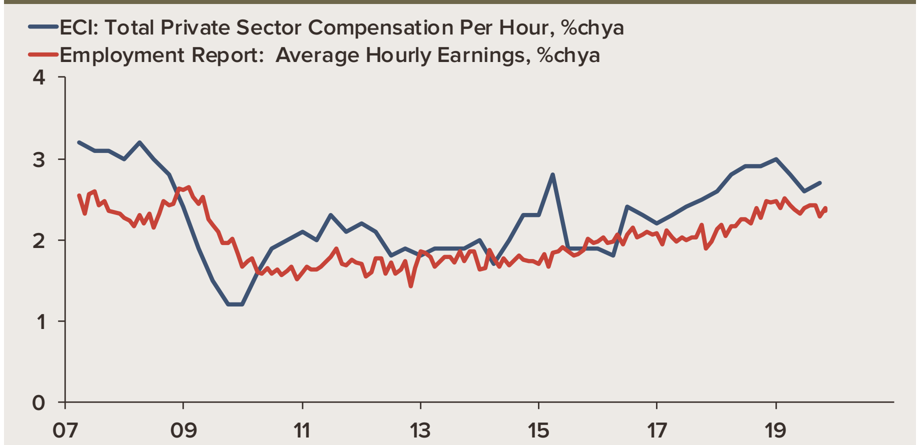


Residential Investment Is Likely To Be Positive In 2020

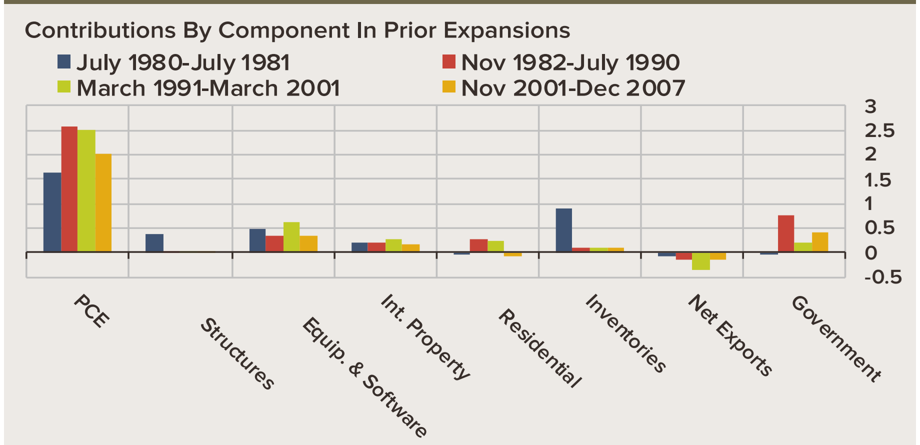


Tight Labor Market Putting Upward Pressure On Wages

Wages Have Been Accelerating

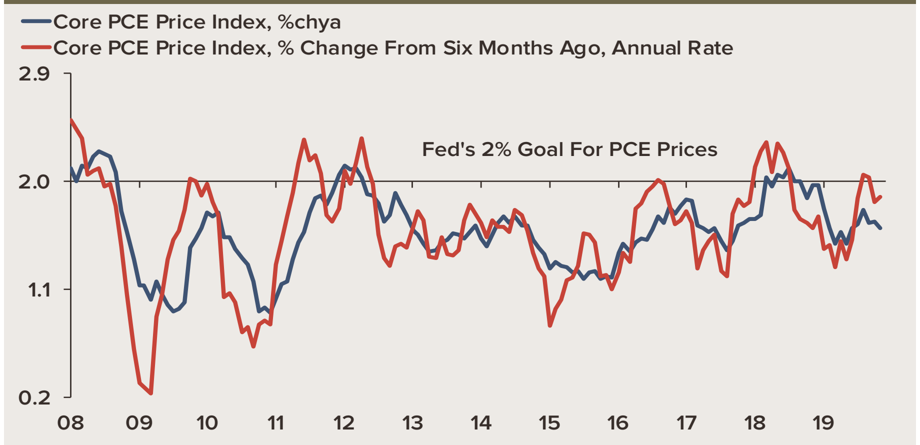


Consumer Spending Has Been Driving Force Behind Growth

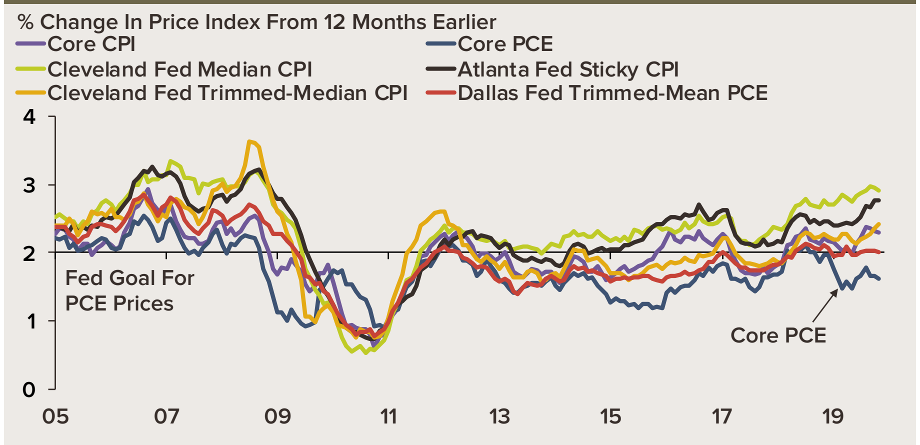


Trend In Core Inflation Remians Tame, Without Deceleration

Early-2019 Weakness In Core PCE Prices Is Being Reversed



Most Inflation Trend Measures Show Little Net Chnge In Past Year



Risks To The Outlook

- **A slowdown in consumer spending.**
- **Trade-related uncertainties.**
- **Weak residential and business investment.** The recovery in the housing market may not be as sustained and strong as needed, and business investment has yet to respond to fewer uncertainties surrounding trade.
- **Slowing global growth.**
- **Geo-political uncertainties.**

Fed Policy

- After a mid-cycle adjustment that resulted in a cumulative 75 basis points of easing, the Fed has indicated it is on hold.
- The most recent dot plot revealed that most policymakers expect no change in policy this year, with a few expecting policy to be tightened modestly.
- Despite the potential for tightening shown in the dot plot, we think the bias to policy remains downward.
- If economic conditions continue on their expected path, the Fed will stay on the sidelines. If there is a material change in the outlook, that will change. The question is, what constitutes a material change in the outlook?

High Frequency Economics®

Daily Data Analysis and Assessment of the Global Economy

HFE Webinar:
Calendar Changes, World's Economic Woes Increase?

Carl Weinberg & Rubeela Farooqi
High Frequency Economics