

September 17th, 2019

A US cyclical uptick:

- 1) The Fed has a lot of interesting issues to chew over in the next day and a half. As it assesses the latest data flow, however, it will not miss the **signs of a cyclical uptick already underway** (Chart 1: **as per the 1998-99 mid-late-cycle adjustment narrative**). If you want to see signs of your adjustment working, you look to classic cyclical indicators (housing and manufacturing) for a response and this seems to be happening. The Fed can take the credit/blame for slowing housing and, now, helping lift it again. The **manufacturing output** story is obviously more complicated (in both cause and effect), but the **0.5%*m/m*, *sa*, gain in Aug** output (foreshadowed by the hours component of the labor report) **took the %3*m/3m*, *saar*, growth rate positive for the first time since February**. The manufacturing output gain came despite a 1%*m/m*, *sa*, drop in autos.
- 2) Another factor that will be discussed is the state of the money market and **the challenge that the NY Fed open market desk seems to be having in projecting reserve demands**. Over the past couple of days, overnight borrowing market rates have spiked due to an unforeseen combination of liquidity draining flows through Treasury operations (Chart 2; a combination of debt settlement and quarterly tax payments—which seem to have been stronger than anticipated?). The NY Fed did a repo operation to ease the stress this morning. **One obvious release valve would be for the FOMC to cut the rate paid on excess reserves once again in order to free up liquidity to flow from tightly-held bank reserves into the Fed funds market. The bigger picture message is that considerable uncertainty surrounds the operation of the USD money market, especially in a period of heightened uncertainty when segmentation of the market seems to go up.**

Chart 1
US cyclical indicators

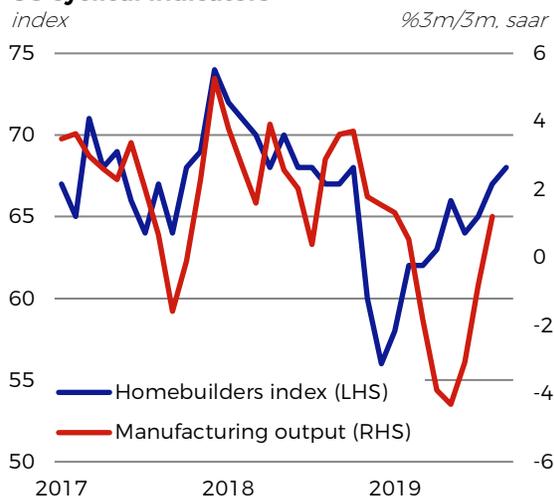
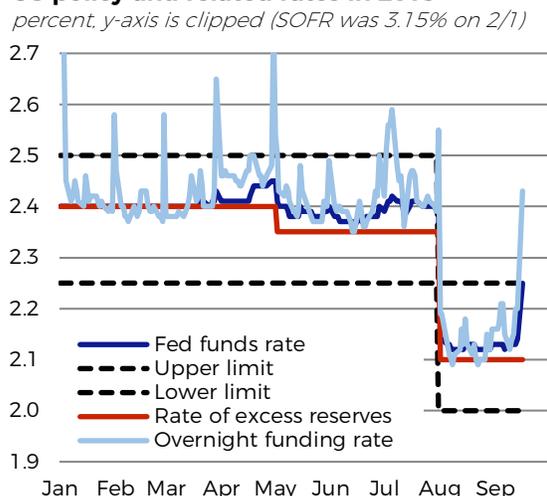


Chart 2
US policy and related rates in 2019



- 3) Asia update: as 2019 unfolds, China seems to be fading, as other EM Asia rebounds
 - a) My view is that **Chinese growth is in steady slowing mode, with the objective of policy being to cushion the slowing, rather than to perk growth back up to 7% or more** (Q4/Q4 growth in 2018 was 6.5%; in 2019, it will be 5.9%; in 2020, it will be 5¼%; by the mid-2020s, it will probably be down to 3%). By way of illustration, the latest housing

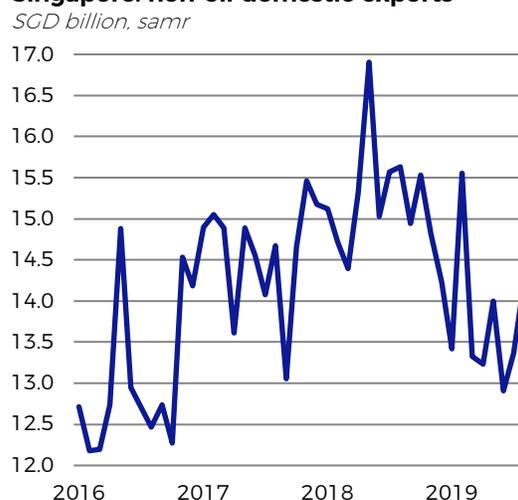
boom is showing signs of moderating, judging by the latest house price data (Chart 3). Overheating in housing (and mortgage lending) had been a concern earlier in the year.

- b) **Australian house price** deflation has moderated on timely monthly data, but the official house price **data for Q2 were still soft**, down an average of 0.7%q/q (nsa), and 7.4%oya (Chart 3). **The q/q decline was the smallest in a year** (this moderation does not look seasonal), so Q2 will likely end up being the housing price trough.
- c) **Singapore's core exports rebounded in Aug to their highest level since Feb** (Chart 4).

Chart 3
Urban house prices



Chart 4
Singapore: non-oil domestic exports



- 4) Central bank minutes. Three banks added more perspective to their on-hold decisions at their last meetings.
 - a) The [Riksbank](#): The MPC remains of the view that normalization is still the right policy, although major uncertainties in the outlook trimmed their view about what they need to do over the next couple of years. The minutes had a little more worry about downside risks than Governor Ingves had expressed after the meeting. **The rise in the unemployment rate (7.4%, sa, in Aug 2019, up a full point from Aug 18) is notable.** EURSEK is little changed since the Sep 4th meeting (it remains close to historic lows), even though the ECB eased and the Riksbank held to its tightening path.
 - b) The [RBA](#): The minutes of the Sep 3rd meeting underlined three slightly more bullish developments warranting an on-hold decision: (a) solid employment growth; (b) signs of a bottom in housing (see 3 b) above); and (c) likely Q2 growth of 2%q/q, saar (this indeed occurred).
 - c) **The Bank of Korea** (minutes of Aug 30th meeting not yet available in English): The headlines from the Korean release highlighted that the **bias remains for easing** (2 members of the 7-person board voted to ease). Fiscal policy is providing support and the economy bounced back in Q2. But **downside growth concerns remain, especially amid the trade dispute with Japan**, which will show up in Q3 data in coming weeks.

Important Information

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