Economy

Focus US
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US: have all of the risks really disappeared?

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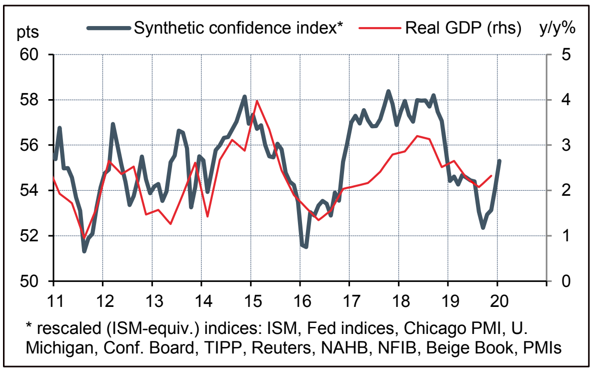
Last summer, the yield curve inverted, triggering panic about the outlook for the US economy. Having reverted to a normal position, the curve recently inverted once again… but optimism prevails. Why? First, because trade tensions have eased. Second, all the signs are there that the Fed is set to maintain an accommodative policy and may even loosen its policy if necessary (the latest reason is the uncertainty linked to the coronavirus epidemic). Third, the robust nature of household spending on consumer goods and real estate overshadows lacklustre business spending.

The week's focus

In January 2020, almost all economic confidence indices rose or remained on an uptrend. Our aggregate index gained 1.1pt to 55.3, compared with a symbolic threshold of 50, and stands at its highest level since December 2018. Its level is associated with a GDP growth rate of around 2.5% per year (chart lhs). At first glance, this signals a slight acceleration. In detail, confidence is above its post-crisis average in the construction sector and among consumers. It is close to normal in services. It remains weak in industry but is tending to pick up (table rhs). When the mood is positive almost everywhere, which side should we choose? A number of risks warrant monitoring.

- Boeing - The halt to production of the 737 MAX could have a significant impact on the growth figure in Q1, via inventory effects. How long the shock will last and its repercussions on subcontractors are not known at this stage. However, the aerospace industry accounts for only a small share of economic activity (2.7% of industrial production).
- Coronavirus – There is a good chance that the partial closure of the Chinese economy will reduce the demand addressed to US firms and possibly disrupt the production chain. Here again, exposure looks low: exports to China and imports of Chinese goods (excluding consumer goods) represent respectively 0.8% and 1.1% of GDP.
- Politics – Recent developments (see p.2) favour Donald Trump, which is good and bad for the economy (good: pro-market tone, bad: erratic economic policy dictated by very short-term considerations). That said, the campaign is only just getting underway and the candidate finally nominated by the Democrats could well cause concern on the markets.
- Fed – Based on its belief that the risk of overheating is low, the Fed plans to maintain extremely flexible monetary conditions. If there is a bias, it points towards an easing, not a tightening. But is this tenable if the economy starts to accelerate and might it not accentuate certain financial excesses?

US: synthetic confidence index



Sources: Thomson Reuters, Bloomberg, Oddo BHF Securities

US: confidence indexes by sector

		Jan.2020	Change		Average
		points	over 3 months	over 12 months	2012-to-date
Manufacturing	ISM	50.9	2.4	-4.6	53.8
	PMI	51.9	0.6	-3.0	53.7
	Others	53.9	1.7	-0.7	54.9
Services	ISM	55.5	1.1	-0.5	56.1
	PMI	53.4	2.8	-0.8	54.6
	Others	54.4	-0.4	2.2	55.9
Consumer		57.4	5.0	3.9	56.0
Construction		61.9	0.6	2.8	57.7
Beige book		54.3	0.8	-0.6	55.1

all indices are normalised on an ISM-equivalent basis (50 as threshold)

Economy

- According to the initial estimates of the Q4 2019 national accounts, real GDP grew by 2.1% q-o-q annualised in **Q4 2019**. In line with retail sales, household spending slowed to 1.8% after two dynamic quarters (3.1% in Q3 and 4.6% in Q2). Residential investment spending continued to firm up at +5.8%, contrary to what we have observed on business investment which was down for the third consecutive quarter. The employment cost index continued on its steady slope of the past two years (+2.7% y-o-y). The expansion phase therefore continues, with no apparent overheating.
- In **December**, construction spending almost stagnated (-0.2% m-o-m). The different segments prolonged the recent trends: acceleration in residential (+5.5% y-o-y), stagnation or even a slight decline in private non-residential (-0.1%) and a marked increase in public spending (+11.5%).
- In **January**, the ISM-manufacturing index showed a marked rebound (+3.1 points to 50.9), exiting the critical zone into which it fell this summer at the height of the tension on trade tariffs between the US and China. It is probably no coincidence that this rebound comes in the wake of an easing of tensions between the two countries.

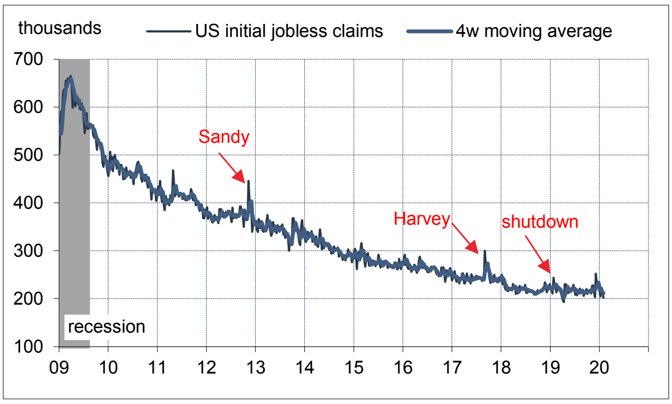
Monetary, fiscal and trade policy

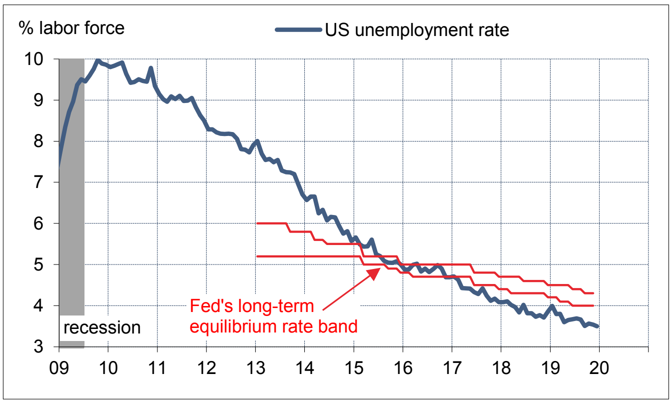
- Following the quarantine measures put in place by the Chinese government in an attempt to halt the spread of the coronavirus, China finds itself partly isolated from the rest of the global economy. Transport activity has been temporarily curtailed, Chinese business cannot resume normal activity (see our economy flash of 6 February: “Isolate China – the coronavirus makes Trump’s dream come true”). With regards to the partial trade deal signed with the US on **15 January**, China has committed to increase its purchase of American products. The goal, which already appeared out of reach under normal circumstances (around +$ 80bn in 2020), now appears to be even more so. To aid the resumption of activity, the Chinese finance ministry announced on **6 February** that trade tariffs were to be halved to 10% or 5% on $ 75bn of American goods.
- In **January**, the Fed’s survey of lending standards shows that the banking sector is cautious. For companies, lending conditions are stable while demand has ebbed slightly. For commercial mortgages, banks are proving restrictive on average, but less so than one year ago, and the dip in demand for loans is slowing, approaching a stabilisation phase. In the residential segment, lending standards are stable while demand, which has shown a sharp acceleration in recent months, is tending to become more moderate. The terms for consumer loans have tightened a little while demand is stable.
- The elections are nine months away, and the start of the election campaign is already unusual. Last week was not a good one for the Democrats. On **3 February**, total confusion reigned at the Iowa caucus, the first step in the process for selecting a candidate, due to a bug in the application for compiling the results. Three days later, the results are still disputed. Pete Buttitieg and Bernie Sanders are on top, neck-and-neck with 26% of the delegates, ahead of Elizabeth Warren (18%) and Joe Biden (16%). Mr Sanders is still favourite for the next primary in New Hampshire (**11 February**). Mr Biden needs to improve if he wants to maintain his image as national favourite. President Trump was acquitted in the impeachment trial on both charges - abuse of power (52 votes to 48) and obstruction of Congress (53 vs 47).

The week ahead

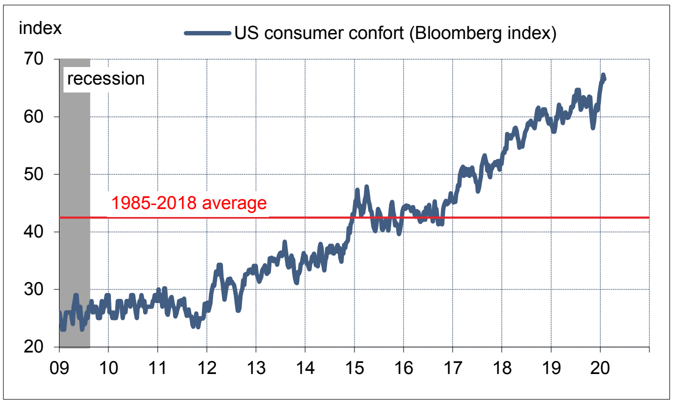
- Inflation in January’s CPI (published on **13 February**) will be boosted by a positive comparison base effect and could reach 2.5% y-o-y. The Fed is ordinarily more attentive to the core index which might slow from 2.3% to 2.2%. The CPI is a good half-point higher than the PCE which is favoured by the Fed. In any case, there are still no concerns on the inflation front.
- The latest activity figures in January are due out on **14 February** with retail sales and industrial production. The initial indications on consumption are encouraging with consumer confidence high and a slight rebound in car sales. Retail sales are expected at +0.3% m-o-m and industrial production at -0.3%. In this publication, we will be paying close attention to the initial estimate of the impact of the halt to 737MAX production.

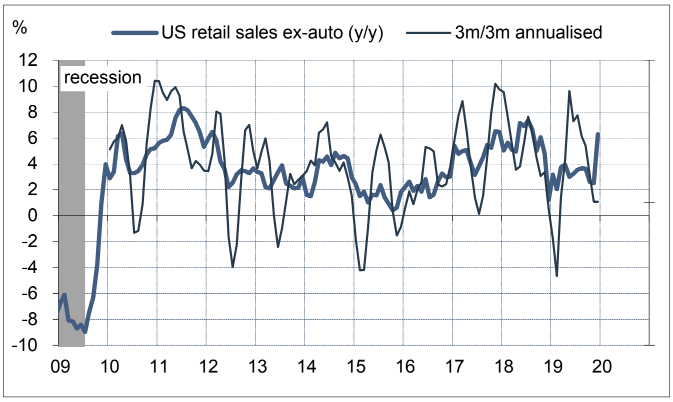
Appendix 1 - Labour market

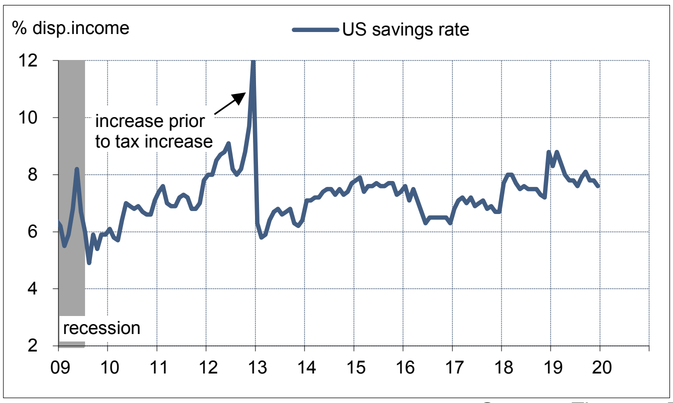


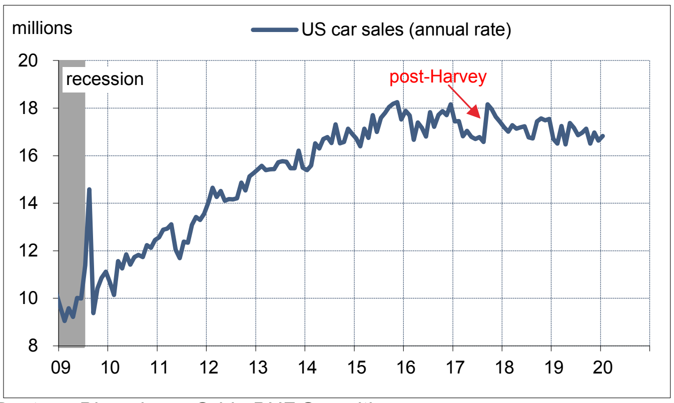


Appendix 2 - Consumer



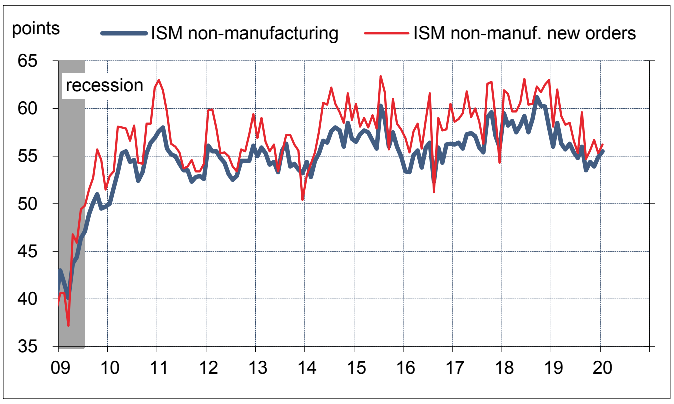


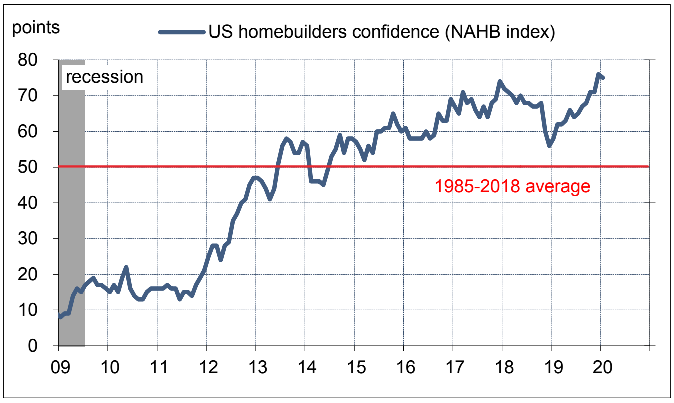


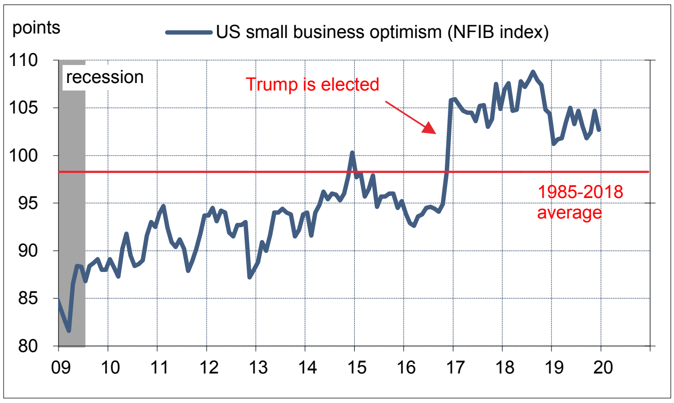


Sources: Thomson Reuters, Bloomberg, Oddo BHF Securities

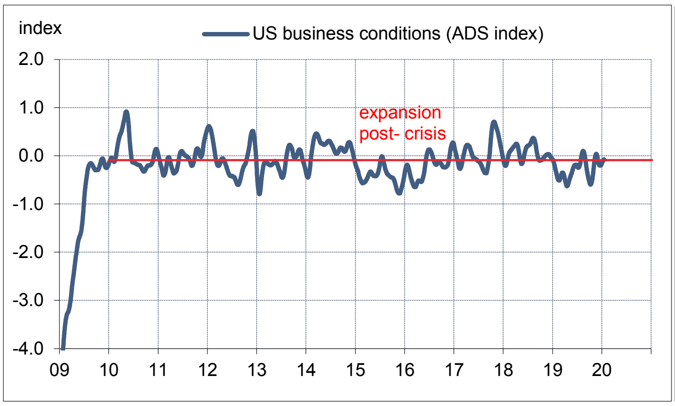
Appendix 3 - Business climate

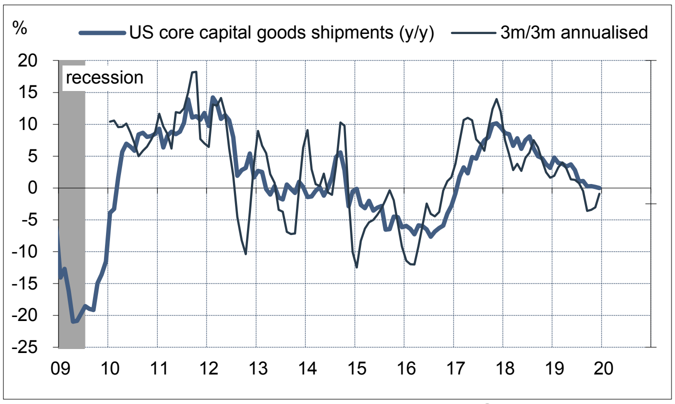


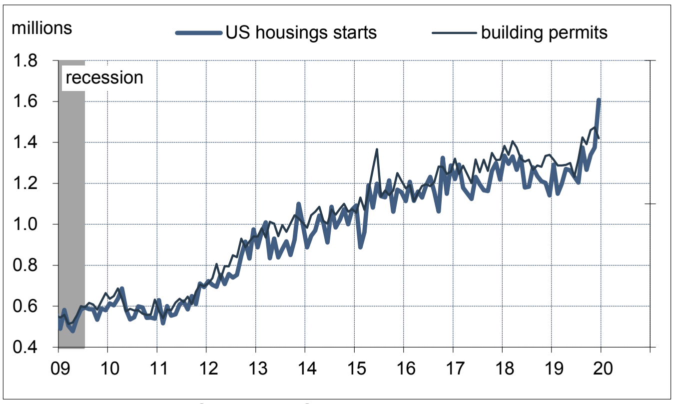




Appendix 4 - Conditions of economic activity

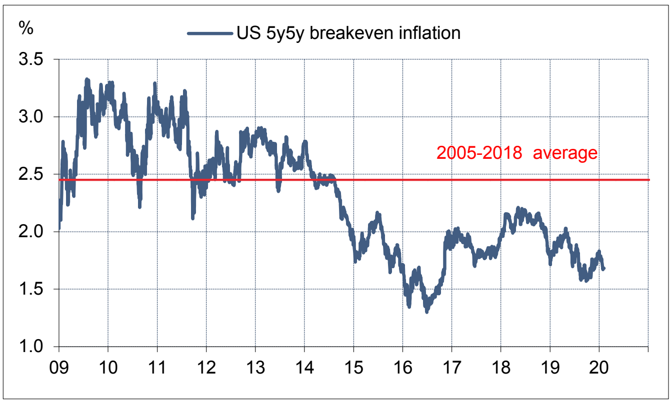


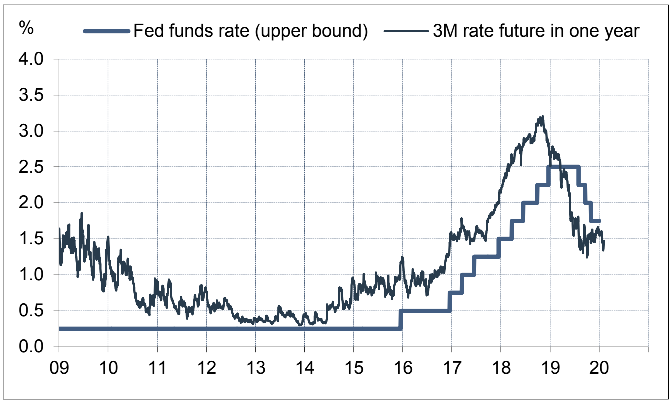


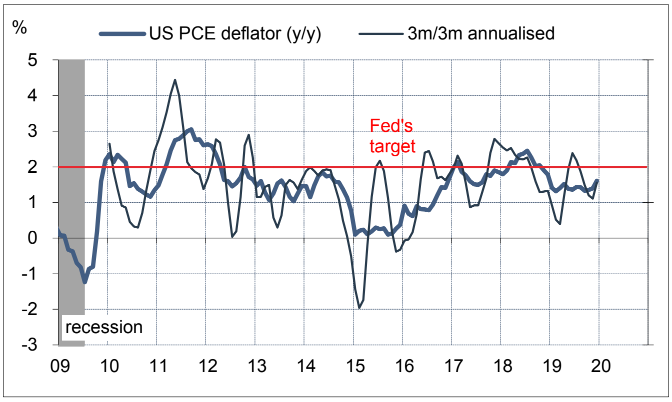


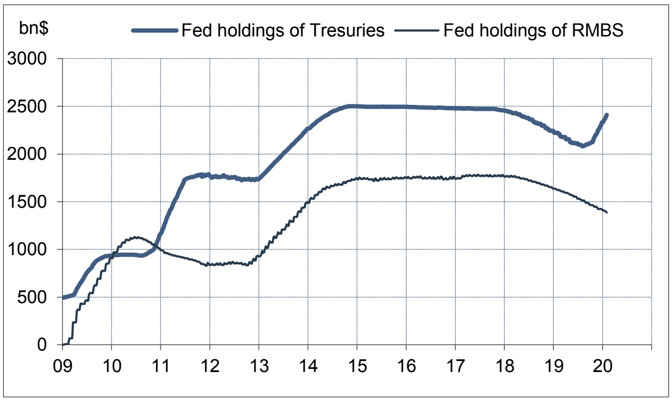
Sources: Thomson Reuters, Bloomberg, Oddo BHF Securities

Appendix 5 - Inflation and monetary policy

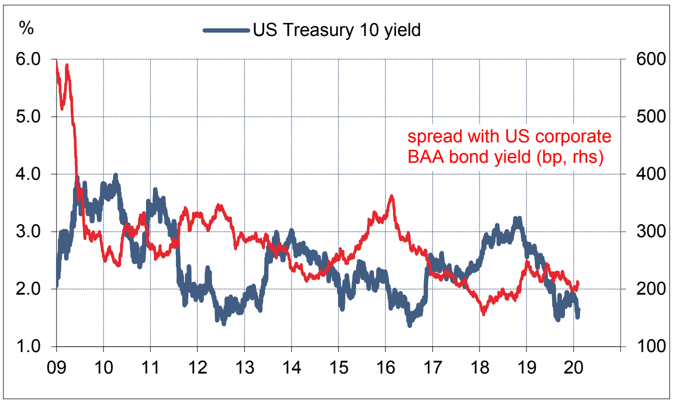


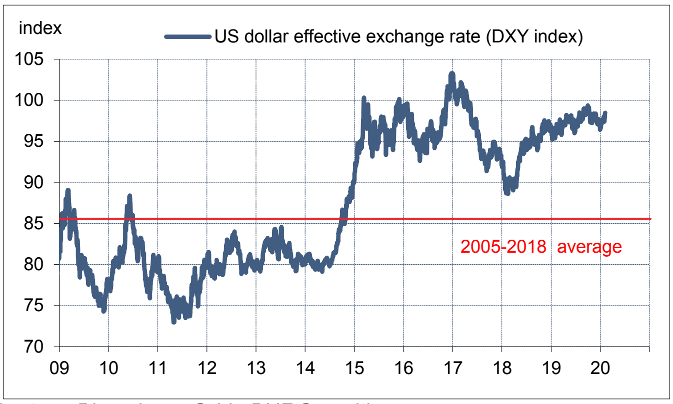






Appendix 6 - Financial markets





Sources: Thomson Reuters, Bloomberg, Oddo BHF Securities

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