Key Developments[1] & Chart of the week

17 Sep 2021

US inflation eases back, China's output growth slows, Euro-area inflation stays contained.

	Outcome	Previous	Comment
US CPI (Aug, m-o-m)	+0.3%	+0.5%	Smallest increase since January
US retail sales (Aug, y-o-y)	+0.7%	-1.8%	Boosted by online purchases
China real retail sales (Aug, y-o-y)	+2.5%	+8.5%	Unambiguously weak
China industrial prod'n (Aug, y-o-	+6.7%	+7.8%	Ditto
Euro-area CPI (Aug, y-o-y)	3.0%	2.2%	High; but the core is below 2%
Euro-area labour cost (Q2, y-o-y)	-0.1%	1.3%	A different story from prices
UK CPI (Aug, m-o-m)	0.7%	0.5%	Increase in both headline and core
UK retail sales (Aug, m-o-m)	-0.9%	-2.8%	Down on the month, flat on the year

US inflation. More evidence for the 'case for transitory'

- 'Headline' CPI rose 0.3% in August, the 'core' by 0.1%, in both cases the smallest increase since January,[2] and bringing the annual rates down from 5.3% to 5.2% and 4.2% to 4.0%, respectively.
- Many of the factors that contributed to the earlier pickup in inflation have begun to reverse.[3]

US retail sales. Consumers pivot to buying online, while auto sales continue to fall

- A 5.3% jump in online retail sales more than accounted for a 0.7% 'delta'-driven increase in overall August retail and food services sales.[4] US industrial production rose a modest 0.4%.[5]

Chinese monthly partials. Unambiguously weak; and not attributable wholly to the virus

- Real retail sales in August were only 2.5% above a year earlier, the smallest increase in 29 years.[6] Industrial production rose just 6.7% over the year, also slow by historical standards.[7]
- Recent softness in a broad range of indicators[8] can be attributed only in part to virus outbreaks or natural disasters. China's economy is clearly slowing – and the authorities are not resisting.

Euro-area CPI and labour costs. Consistent with the 'transitory' story

- Headline CPI grew by 3.0% in the year to August, and 0.4% on the month, above the ECB target rate. But the annual core figure was an untroubling 1.6%.
- Importantly, these prices are not (at least yet) getting into wage costs, which fell 0.1% m-o-m.

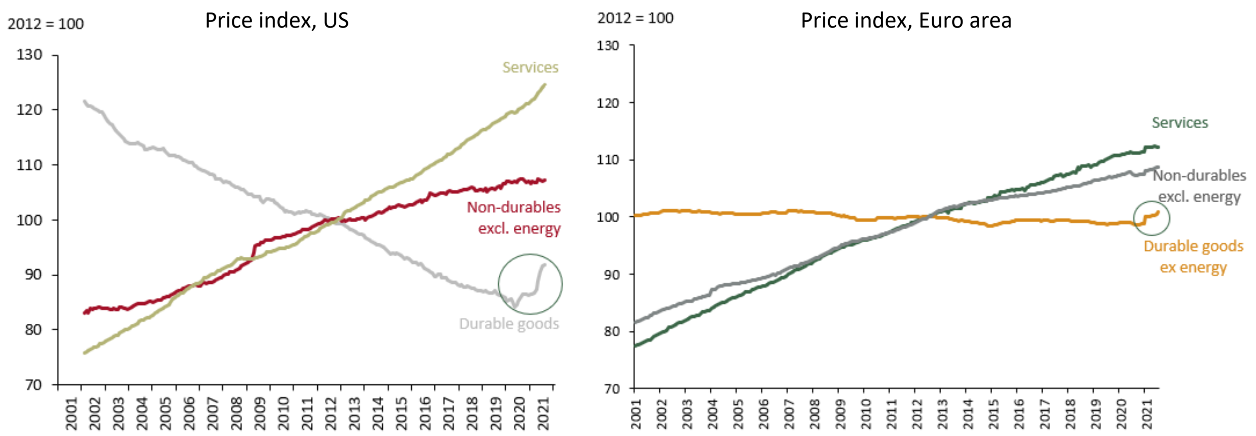
UK CPI and retail sales. Not a happy combination

- The UK CPI (both headline and core) were up 0.7% in August, 3.2% and 3.1% respectively y-o-y.
- Retail sales, however, were down 0.9% on the month, and flat on the year.

***Bottom line**: Inflation seems to be moderating gently. If so, our World View remains intact*

Chart of the week. Prices of durables pull inflation down: non-durables and services push it up

- But possibly, just possibly, that long-run trend behaviour could be coming to an end. This is one to watch.



Source: Macrobond, Saul Eslake, and Llewellyn Consulting. Notes: US price indexes are IPD's of Personal Consumption Expenditures; Euro area price indexes are Harmonised Index of Consumer Prices (HICP). Euro area non-durable goods and durable goods are non-energy industrial goods.

[1] ***Key Developments*** presents what in our judgement represent the past week's most important individual data, policy announcements, and any other developments that may support, or challenge, our understanding of the way in which key economies and financial markets are evolving.

These weekly judgements are cumulated and assessed in our quarterly ***World View & Risks***. When an issue warrants particular consideration, we examine it in detail in our ***Analysis*** pieces. And when in our judgement the accumulated evidence warrants it, we modify our quarterly ***World View & Risks.***

[2] Each of these measures increased by an average of 0.8% per month between April and June.

[3] The exception is the prices of new motor vehicles, which accounted for half the increase in the 'core' CPI in August. 'Statistical' measures of 'underlying' inflation (such as the Cleveland Fed's median and trimmed mean) also support the Fed's judgement that the earlier 'spike' would prove transitory.

Meanwhile, the September 'Philly Fed' manufacturing survey showed small declines in the prices paid and received by manufacturing businesses, which may indicate a lessening of at least some of the intense pressure on 'upstream' prices that has been evident this year.

And the September Michigan 5-year inflation expectations survey showed no change at 2.90%. The 1-year figure rose 0.1 ppt to 4.7%.

[4] The spread of 'delta' cases kept shoppers at home, and away from food services outlets (whose sales were flat). Meanwhile, supply-constrained motor vehicles and parts dealers' sales fell for the fourth successive month, to be down 14.1% since peaking in April.

[5] The 0.4% rise in US industrial production in August, the sixth consecutive monthly gain, nevertheless left the level 2.5% below its pre-recession peak, which was back in August 2018. Motor vehicle production is still 8.6% below its pre-recession peak (in June 2019) and capacity utilization in this sector is still only 70.5% (cf. 76.4% for manufacturing as a whole).

The not widely known Quarterly Survey of Plant Capacity Utilization shows 41% of manufacturers citing labour shortages, and 33% citing shortages of materials, as reasons for operating at less than full capacity in Q2 (compared with averages for the seven years prior to the onset of Covid-19 of 13% and 6% respectively).

[6] Apart from the first eight months of last year.

[7] Meanwhile fixed asset investment in the eight months ended August was 8.4% lower than in the corresponding period of last year (which was in turn 5.3% lower than in the corresponding period of 2019).

[8] Other than exports.