



## Key Developments<sup>1</sup> & Chart of the week

27 Aug 2021

US core inflation slows slightly; Euro area and UK PMIs suggest recoveries slowing

	Outcome	Previous	Comment
US core PCE deflator (Jul, m-o-m)	0.3%	0.5%	Slight easing of price pressures
World trade (Jun, m-o-m)	+0.5%	-0.8%	Affected by port disruptions
US DG orders (Jul, m-o-m)	-0.1%	+0.8%	'Core' capital goods orders slowing
US new home sales (Jul, ar)	708K	701K	Down from 871K average Jan-Apr
EA composite PMI (Aug)	59.5	60.2	Still high; manufacturing slowing
UK composite PMI (Aug)	55.3	59.2	6-months low; services fall sharply
Bank of Korea (base rate)	0.75%	0.50%	First Asian central bank to raise rates

### US PCE deflator. No fireworks this month

- The core PCE deflator, the Fed's preferred measure of inflation, rose by a modest 0.3% on the month in July, after 0.5% in June, with the annual rate remaining steady at 3.6%.<sup>2</sup>

### World trade volume. Partial recovery in June from a fall in May

- The volume of world trade rose by 0.5% in June, partially reversing the 0.8% decline in May.
- China's imports fell by 5.2%, but Chinese and other Asian countries' exports more than offset.<sup>3</sup>

### Euro area and UK composite PMIs. Slowing recoveries

- Eurozone PMI remained close to a 15-year high, but slowed for a second month, driven by manufacturing, which hit a 6-month low due to supply chain disruptions.<sup>4</sup>
- Likewise, UK PMI data suggest that the recovery is losing momentum, driven by significant and widespread staff and materials shortages. Wage pressures are also increasingly reported.<sup>5</sup>

### US capital goods orders and new home sales. Both slowing

- **Orders** for non-defence capital goods excluding aircraft<sup>6</sup> rose by less than 0.1% in July, following a 1.0% gain in June.<sup>7</sup>
- **New home sales** rose 1.0% in July to a 708K annual rate, after falling 2.6% in June.<sup>8</sup>

### Central banks. Fed to stay the course

- Jay Powell reiterated that the Fed expects the inflation spike to be transitory; and considers the present policy stance "well positioned." Tapering seems likely towards year-end – but no hikes.
- The Bank of Korea became the first in Asia to raise interest rates since the onset of Covid-19.<sup>9</sup>

**Bottom line:** If inflation continues to moderate gently, our World View will remain intact

### Chart of the week. Taiwan export orders suggest a slowing in global trade.

- Taiwan, with its pivotal role in the global semi-conductor industry, is also a useful harbinger of world trade.



Source: Macrobond and Llewellyn Consulting.

<sup>1</sup> **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**.

<sup>2</sup> The annual rate of US inflation was revised upwards to 3.6% from the previously reported 3.5%. As regards the monthly breakdown, durable goods inflation eased, while that on non-durable goods and services remained unchanged.

<sup>3</sup> World trade (as measured by the Dutch Economic Planning Bureau, CPB) continues to be disrupted by port closures, most recently at Ningbo (China's third largest port) which have also contributed to the enormous increase in shipping container costs this year (a result of many containers being stranded in places other than where they are needed). Another drag on world trade has been the persistent shortage of semi-conductor chips, which are nowadays a crucial input into motor vehicle manufacturing. Given Taiwan's pivotal role in the global semi-conductor industry, the decline in its export orders since February is a harbinger of some further slowing in world trade growth (see Chart of the Week).

<sup>4</sup> Employment has stayed notably strong, growing at a rate matching July's 21-year high as firms expanded capacity in line with the recent order book growth and promising outlook. Meanwhile firms' costs and prices charged continued to grow at some of the fastest rates for two decades.

Separately, but consistent with the wider Eurozone data, German business sentiment deteriorated again in August amid supply chain issues. The IFO business climate index fell to 99.4 from 100.7 in July, and below expectations.

<sup>5</sup> Inflation pressures showed signs of easing in August, with input prices rising at the weakest pace for three months. However, many firms commented on higher wages due to tight labour market conditions. Similarly to the Euro area, the employment component was particularly strong: "Efforts to rebuild capacity and strong optimism towards the business outlook contributed to the fastest rise in employment numbers since the index began in January 1998. Nonetheless, backlogs of work increased for the sixth month in a row as businesses struggled to keep up with customer demand." <https://www.markiteconomics.com/Public/Home/PressRelease/4b9df9b7743e47fd8955068a75783205>

<sup>6</sup> This is the most important component of the wider durable goods orders series.

<sup>7</sup> This is an inherently volatile series month-to-month, but the underlying trend has slowed from 1-1.2% per month at the turn of the year to 0.9% in June and July, which suggests an easing in growth in business equipment investment.

<sup>8</sup> Over the past three months the pace of new home sales has slowed to an average annual rate of 710K, from 871K in the first four months of 2021, and 950K in the second half of last year. The pace is still well above the average 638K level of 2017-2019 though. Existing home sales have followed a similar pattern. However prices are continuing to rise rapidly – new home sale prices were 16.5% higher in July than a year earlier, while existing home sale prices were up 20.7% over the same period.

<sup>9</sup> 'Core' inflation in Korea was below 1% between August 2019 and February this year, but since then has climbed to 1.7%, the highest in four years, while headline inflation has been above the BoK's 2% target for four months in a row. However the BoK's statement appeared to place more emphasis on financial stability concerns (including rapidly rising house prices) than on inflation.

Elsewhere, Iceland's central bank raised its policy interest rate by 25 bp to 1.25%, the second such increase this year; Hungary's central bank raised its base rate by 30bp to 1.5%, the third increase in three months; and Paraguay's central bank became the sixth Latin American central bank to raise rates this year, lifting its base rate (for the first time in 5½ years) by 25 bp to 1%.

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