Key Developments[1] & Chart of the week

29 Oct 2021

US headline inflation holds steady, but Europe's rises. US trade deficit makes a new record.

	Outcome	Previous	Comment
US GDP (Q3, q-o-q annualised)	+2.0%	+6.7%	Slowest since Q2 last year
US goods trade deficit (Sep)	-\$96.3bn	-\$88.2bn	Another new monthly record
US PCE deflator (Sep, m-o-m)	0.3%	0.3%	Flat: and 'core' eased by 0.1ppt
Euro-area CPI (Oct, m-o-m)	0.8%	0.5%	Up: but 'core' eased by 0.1 ppt
UK budget	Expenditure up £150 bn over three years, plus tax hikes		
Australia CPI (Q3, q-o-q)	+0.8%	+0.8%	'Underlying' inflation surprised
Central banks	ECB, BoJ, and Bank of Canada on hold; but Brazil tightens		

US GDP growth. Slugged by delta and supply chains

- The US economy grew at a 2.0% annual rate in Q3, its slowest pace since the pandemic-induced contraction in Q2 last year. Personal consumption spending grew only 1.6% annualised.[2]

US merchandise trade. Another record monthly deficit

- The US September merchandise trade deficit widened by \$8.1bn to \$96.3bn – a new monthly record, with exports falling 4.7% while imports rose by 0.5%.[3]

US PCE deflator. Slight evidence in favour of 'transitory'

- The October headline figure was unchanged, at 0.3% m-o-m, while 'core' was down 0.1 ppt.[4]

Euro-area CPI. Not looking quite so transitory

- Headline CPI rose 0.3 ppt m-o-m, driven by energy prices.[5] The 'core' eased by 0.1 pp to 0.3% m-o-m, with bottlenecks important, particularly for cars. Q3 GDP growth was steady at 2.2%.

UK Budget. A response to demographic and regional imperatives

- The budget reflects pressures to meet social needs: but the associated tax hikes may be risky.[6]

Australia inflation. 'Underlying' rate a challenge to the RBA's stance.

- The CPI rose 0.8% in Q3. Importantly, the annual 'underlying' rate rose to 2.1%: the RBA may have difficulty maintaining that it will keep its cash rate at its current record low until 2024.[7]

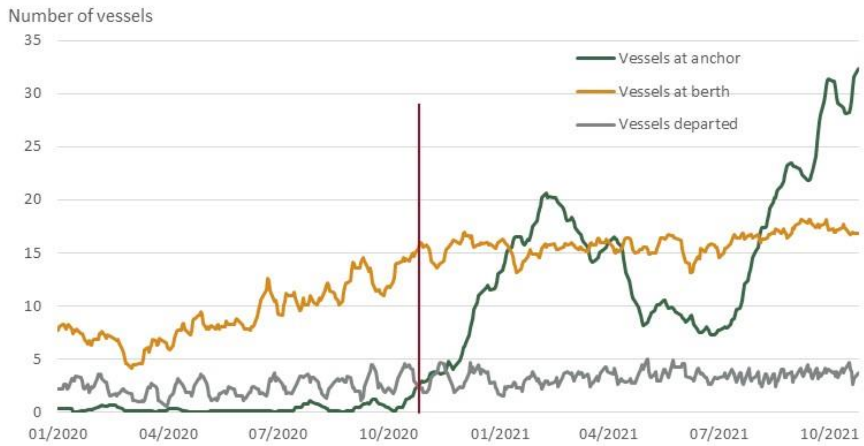
Central banks. Rates on hold, but ECB and BoC taper

- The ECB, the BoJ, and the Bank of Canada all left rates on hold, as expected. But the Bank of Canada and the ECB foreshadowed gentle policy tightening.[8]
- Brazil's central bank raised its SELIC rate another 150 bp (50 more than expected) to 7.75%.[9]

***Bottom line**: provided that inflation moderates, our World View will remain intact*

Chart of the week. The queue for berths at the Port of Los Angeles reaches a new high

- Full capacity was reached a year ago. Excess demand rose until February, fell till July: but then surged anew.



Source: Macrobond and Llewellyn Consulting Note: 1-week moving average

[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] **US** spending on durable goods fell at a 3.4% rate, due to supply shortages, while 'delta' outbreaks damped other categories of personal spending. Supply-chain disruptions also caused a contraction in housing and the non-IP components of business investment. Net exports also detracted from growth, for the fifth quarter in a row.

[3] The **US deficit** for the first nine months of this year topped US$1 tr – this compares with $803 bn for the first nine months of 2020.

[4] **US 'core' PCE deflator** fell slight m-o-m, from 0.3% in September to 0.2% in October. Year-on year figures were 4.4% for the headline, 3.6% for the 'core'.

[5] **Euro-area energy prices** were up 23.5% on a year earlier, compared with 17.6% in September.

[6] In a break with earlier **UK** Conservative government philosophy, this budget responds to strong demographic and social pressures for more and better social services. But there were tax hikes too, and the National Institute for Economic and Social Research judges these as risky for the recovery:

> *"The Chancellor is moving too quickly to consolidate government finances when risks to the economy are far from behind us. A slower pace of consolidation would provide a more solid base for the recovery, would be fiscally responsible, and would allow the Bank of England to raise interest rates further away from the zero lower bound. The policy mix resulting from the Budget is too tight fiscal policy and too slack monetary policy, thus simultaneously increasing risks to both growth and inflation*."
>
> Paul Mortimer-Lee, Deputy Director (Macro-economic Modelling and Forecasting) See: NIESR's Response to the Autumn Budget and Spending Review 2021 | National Institute of Economic and Social Research

[7] **The Reserve Bank of Australia's** preferred measures of 'underlying' inflation rose 0.7% on the month − the largest increase in nine years – pushing the annual 'underlying' inflation rate up to 2.1%, the first time in almost six years that it has been inside the RBA's 2-3% target range – something that the RBA had not expected to occur until Q4 2023. The RBA may thus have difficulty maintaining its long-held position that it will keep its cash rate at its current record low until 2024.

[8] **The Bank of Canada** brought forward its forecast of when the 'output gap' would close (and hence when it would start raising rates) to *"some time in the middle quarters of 2022*". **The ECB**, by contrast, "*after a lot of soul-searching to test our analysis*" (as Mme. Lagarde put it) firmly re-asserted its view that the "*current phase of higher inflation*", though now likely to "*last longer than originally expected*" would nonetheless "*ease in the course of 2022*".

The Bank of Canada said that it would cease purchasing government bonds (other than to replace maturities), while the ECB said it would purchase bonds at a 'moderately lower pace' than in the past two quarters.

[9] This was **Brazil's** sixth hike so far this year, and foreshadowed another 175bp move before year-end. In addition to higher-than-expected inflation, Brazil's Central Bank pointed to the risks posed by fiscal policy settings to 'de-anchoring inflation expectations'.