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GLOBAL ECONOMIC HIGHLIGHTS

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Fed to Wind Down Some Emergency Lending Programs; EU Politics Delaying Ratification of Recovery Plan

UNITED STATES: The Treasury Department on November 19 ordered the Federal Reserve to stop making new loans through its liquidity facilities funded by the CARES Act by year-end; several lending facilities which do not depend on CARES Act funding can continue. The Fed established these lending facilities in the spring as the pandemic reached the United States and financial markets melted down; the facilities allow the Fed to make loans available to American businesses, households, and local governments, either directly by buying bonds, or indirectly by channeling money through financial institutions. The programs helped restore confidence in the financial system in the spring, preventing financial turmoil from worsening the damage to the economy that the pandemic caused, which could have made the downturn much worse. Since then, financial market conditions have improved and most of the borrowers eligible for the Fed's facilities can get credit from private sources; as a result, the facilities made very few loans. Even so, the Fed publicly disagreed with the Treasury's decision, arguing that the credit facilities should stay around in case the financial system needs more support before the pandemic ends.

Housing continues to lead the recovery. Housing starts rose 4.9 percent in October to the 4th highest since the housing boom went bust in 2007; building permits were flat on the month, also at the highest since 2007. Existing home sales rose 4.3 percent from September to the highest since 2005, the year in which the last housing boom peaked.

Retail sales rose 0.3 percent in October, according to the Census Bureau; this was slightly below the consensus expectation for a gain of 0.4 percent. Sales growth in September was revised down to a 1.6 percent increase, from the initially reported 1.9 percent increase. This was the smallest increase in retail sales since they plunged during the early stages of the pandemic as businesses shut down. October retail sales were almost 5 percent above their February, pre-pandemic level. Sales excluding autos were up 0.2 percent over the month, as were sales excluding autos and gasoline. Control retail sales—sales excluding autos, gasoline, food service, and building supplies, and which go into consumer spending in GDP—were also up 0.2 percent in October. On a year-ago basis total retail sales were up almost 6 percent, including increases of 4.4 percent excluding autos and 6.5 percent excluding autos and gasoline. Control sales were up almost 10 percent year-over-year in October.

Industrial production rose 1.1 percent in October, close to the consensus expectation for an increase of 1.0 percent. Manufacturing output rose 1.0 percent, while mining output fell 0.6 percent and utilities output rose 3.9 percent. On a year-ago basis industrial production was down 5.3 percent, including declines of 3.9 percent in manufacturing and 3.0 percent for utilities. Mining output was down a huge 14.4 percent year-over-year, as low energy prices have led to big production cuts. Industrial production remains almost 6 percent below its pre-pandemic level, and its pace of improvement has slowed after very large gains in June and July. Mining in particular remains very weak. The capacity utilization rate rose to 72.8 percent in October from 72.0 percent in September but was well below the 76.9 percent rate in February. Wide swathes of excess capacity throughout the economy will make it difficult for businesses to raise prices, keeping inflation low throughout 2021.

Weekly economic data could be softening as the pandemic weakens the service sector; data also become more volatile and harder to interpret ahead of Thanksgiving. The Federal Reserve Bank of New York's Weekly Economic Index fell 2.8 percent from a year earlier in the first revision for the week of November 14, a touch worse than the 2.7 percent decline in the comparable release for the prior week. Initial claims for unemployment insurance rose 2.5 percent in the same week, to 746,000, reported as a 4.4 percent increase to 742,000 after seasonal adjustment; initial claims for Pandemic Unemployment Assistance rose to 320,000 from 296,000. There are still more than a million Americans filing new claims for unemployment insurance each week, a sign that job losses remain a huge problem for the economy even as the unemployment rate returns to single digits.

EUROZONE: The European Union has hit a predictable bump in the road on the way to implementing the €750 billion euro recovery and resilience plan agreed earlier this year by heads of states. Members of the EU parliament from Poland and Hungary vetoed the plan in parliament on November 16 to protest its provisions that pressure the Polish and Hungarian governments to restore independence to their judiciaries and make other democratic reforms. Financial markets are largely ignoring the standoff, which has minimal economic implications outside Poland and Hungary; if a compromise cannot be reached, the remaining 25 EU members will modify the fun to make it only for themselves. Similarly, the economic impact on Poland and Hungary is unlikely to affect the United States. As long as other EU members participate, divergences in yields across member states will stay small, allowing the ECB's monetary stimulus to flow through to the real economy; and financial conditions in the euro area will stay accommodative.

The EU economy is likely to contract again in the fourth quarter as lockdowns force service-sector businesses to curtail operations. In reaction, the ECB will probably add €250-€500 billion euros to its Pandemic Emergency Purchase Program at the December 10 Governing Council decision, and extend the operation of the PEPP to September or December 2021 (the current commitment is to keep the program active till June). The ECB will likely announce a schedule for additional rounds of longer-term refinancing operations (the PELTROs and TLTROs) to be conducted in 2021, too.

CANADA: CPI inflation picked up to 0.7 percent in year-over-year terms in October, beating consensus, after a 0.5 percent increase in September; the Bank of Canada's three measures of core inflation, CPI-common, CPI-median, and CPI-trim were 1.6 percent, 1.9 percent and 1.8 percent, respectively, in October, all below the Bank's 2.0 percent inflation target. The Teranet-National Bank House Price Index™ rose 8.1 percent in October from a year earlier, the biggest jump in over two years, following a 6.7 percent increase in September. Retail sales rose 1.1 percent in September from August after an upwardly revised 0.5 percent increase in August; from a year earlier, retail sales grew 4.6 percent in September. Housing starts rose 3.0 percent in October to 214,900 units at a seasonally-adjusted annualized rate, a healthy level; housing starts in the three months through September were the strongest since 2007.

JAPAN: Real GDP rose 21.4 percent annualized in the preliminary estimate for the third quarter of 2020 after a 28.8 percent annualized decline in the second; Japan's economy also contracted in the first quarter of 2020 and fourth quarter of 2019 following a hike in the value added tax (a kind of sales tax) in October 2019. Real GDP was 5.8 percent lower than a year earlier in the third quarter, a somewhat smaller contraction than the 10.2 percent plunge in the second quarter. Growth looks sluggish in the fourth quarter of 2020: The Jibun bank manufacturing PMI for Japan dipped to 48.3 in the November flash estimate from 48.7 in October, while the services PMI fell to 46.7 from 47.7.

BRAZIL: Fitch affirmed Brazil's sovereign credit rating at BB- with a negative outlook on November 18 citing the country's high and rising government indebtedness, rigid fiscal structure and weak economic growth potential. Brazil's Economic Ministry slightly upgraded its 2020 growth forecast to -4.5 percent from -4.7 percent citing upward revisions to third quarter economic activity.

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