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INSIGHT

October 2018

Economic News

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The U.S. Economy Added 134,000 Jobs in September—Extending a record run of hiring to eight full years. September was a milestone in the remarkable rebound that followed the fall of Lehman Brothers 10 years ago: eight straight years of monthly job growth. The unemployment rate fell to 3.7%, the lowest since 1969. Average earnings rose by 8 cents an hour and are up 2.8% over the past year.

Wall Street economists had expected an increase of about 168,000, according to MarketWatch. Full Story
Source: NYTimes, 10.05.18

Fed Raises Rates and Says More Coming, Brushing Off Trump Jabs—Federal Reserve officials raised interest rates and cemented expectations for another hike this year as they reaffirmed that a strong U.S. economy will probably warrant further gradual increases well into 2019. The quarter-point hike boosted the benchmark federal funds rate to a target range of 2% to 2.25%. The move reflected an upbeat assessment of the economy that was identical to the central bank's last policy statement eight weeks ago, despite concerns over President Donald Trump's escalating trade war.

"This gradual return to normal is helping to sustain this strong economy," Chairman Jerome Powell told reporters September 24 following a two-day meeting of the Federal Open market Committee in Washington. After a decade-long expansion that's been marked by mostly modest growth, Powell said "this is a pretty good moment for the U.S. economy." Growth and job gains have been "strong" and inflation remains near the central bank's 2% target, the FOMC said in its statement. Barring a negative surprise, updated "dot plot" forecasts made a December rate hike almost certain, with 12 of 16 officials now expecting another increase by year-end. That grew from eight in their June projections.
Full Story *Source: Bloomberg, 09.26.18*

Consumer Confidence Surges in September to 18-Year High, Near All-Time Peak—Americans are the most confident in the U.S. economy in 18 years and the level of optimism is not far from an all-time high, a closely followed survey shows. The consumer confidence index climbed to 138.4 in September from a revised 134.7 in August, the Conference Board said on September 25. That's the highest level since September 2000 — near the end of the Internet boom — and close to the record peak of 144.7 set in May of the same year.

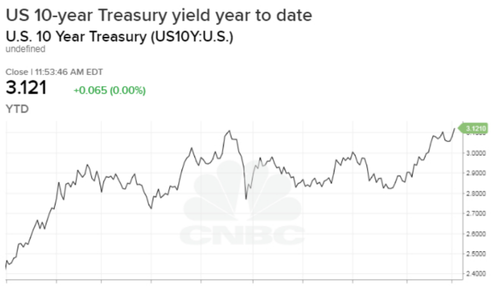
What happened: The present situation index, a measure of current conditions, edged up to 173.1 from 172.8. The future expectations index jumped to 115.3 from 109.3. Americans expect business conditions to improve and they say plenty of jobs are available. They also think their own finances will get better with incomes rising. Full Story
Source: MarketWatch, 09.25.18

Rates Are Surging With 10-Year, 30-Year Treasury Yields Touching Multiyear Highs

The yield on the 10-year Treasury note hit its highest level since July 2011 and the yield on the 30-year Treasury bond hit its highest level since October 2014 on October 3 after new data fostered views of a booming economy. Private companies added 230,000 more positions in September, according to ADP and Moody's Analytics, the best gain since February and well ahead of the 168,000 jobs added in August. The U.S. services sector, meanwhile, expanded in September at its fastest pace on record, according to the Institute for Supply Management.

The ISM non-manufacturing index rose to 61.6 last month, its highest level since the index was created in 2008. Economists polled by Refinitiv projected the index to hit 58 last month. The healthy economic reports preceding the sustained uptick in yields, with benchmark rates hitting multiyear highs. The yield on the 30-year Treasury bond hit its highest level since October 3, 2014, and was last seen at 3.309%. The yield on the benchmark 10-year Treasury note also jumped and was at 3.157% at 3:59 p.m. ET, down from 2011 highs hit earlier in the session.

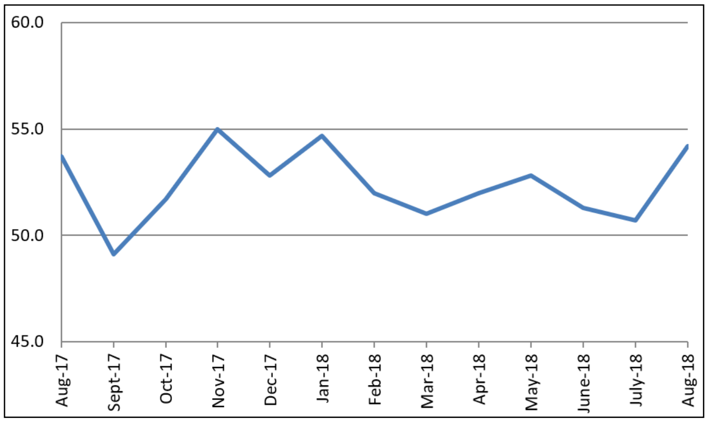
"The U.S. economy is strong; there's just no other way to frame it," said Nathan Sheets, chief economist at PGIM Fixed Income. "The economy is strong, growth is strong, inflation is gradually moving up as the Fed projects. And the reality is the U.S. Treasury will be doing a lot of issuing over the next few years, which all put upward pressure on rates in the near term," he said. The 10-year rate is especially important given its role in helping set rates for a whole range of business and consumer loans, including home mortgages. The rate on the two-year note hit 2.864%, its highest point since June 25, 2008. Bond yields move inversely to prices.



"ISM Manufacturing this morning showed a record for the series in the employment category, pushing out expectations for economic growth," he added. Hill said, however, that the current economic optimism may be only transient and tied to one-time stimuli like President Donald Trump's tax cuts. *Source: CNBC, 10.03.18*

KEY ECONOMIC INDICATORS

Architecture Billings Index (ABI)

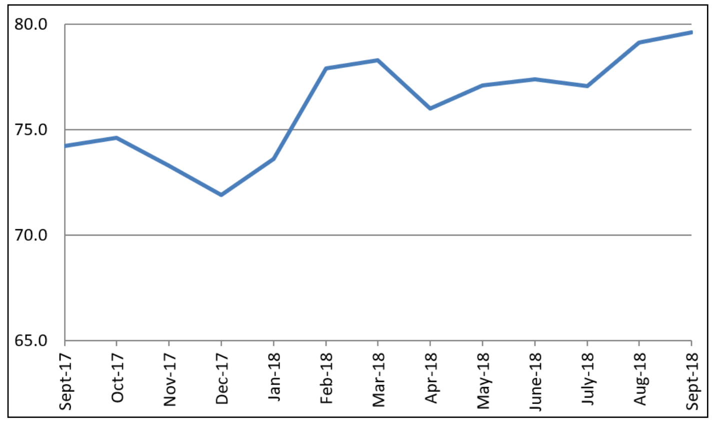


Architecture firm billings rebounded solidly in August, posting their eleventh consecutive month of growth, according to a report released September 19 from The American Institute of Architects (AIA).

AIA's Architecture Billings Index (ABI) score for August was 54.2 compared to 50.7 in July (any score over 50 represents billings growth). Most of the growth continues to come from the South and the multi-family residential sector.

The **Architecture Billings Index (ABI)** is a diffusion index derived from the monthly Work-on-the-Boards survey, conducted by the AIA Economics & Market Research Group. The ABI serves as a leading economic indicator that leads nonresidential construction activity by approximately 9-12 months. An index score of 50 represents no change in firm billings from the previous month, a score above 50 indicates an increase in firm billings from the previous month, and a score below 50 indicates a decline in firm billings from the previous month.
Source: American Institute for Architects, 09.19.18

Steel Capability Utilization

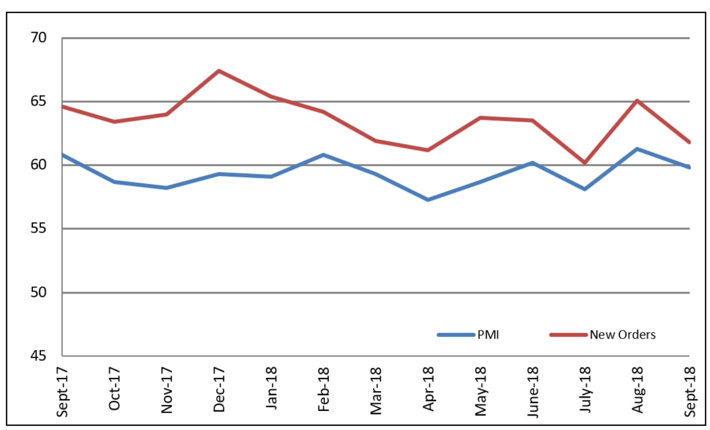


In the week ending on September 29, 2018, domestic raw steel production was 1,856,000 net tons while the capability utilization rate was 79.2%. Production was 1,711,000 net tons in the week ending September 29, 2017 while the capability utilization then was 73.4%. The current week production represents a 8.5% increase from the same period in the previous year. Production for the week ending September 29, 2018 is down 0.4% from the previous week ending September 22, 2018 when production was 1,863,000 net tons and the rate of capability utilization was 79.5%.

Adjusted year-to-date production through September 29, 2018 was 70,469,000 net tons, at a capability utilization rate of 77.5%. That is up 4.5% from the 67,425,000 net tons during the same period last year, when the capability utilization rate was 74.4%.

Steel Capability Utilization is a domestic report based on estimates from companies representing approximately 90% of the Industry's Raw Steel Capability as compiled by the American Iron and Steel Institute. *Source: AISI, 09.29.18*

Purchasing Managers Index®



The September PMI® registered 59.8%, a decrease of 1.5 percentage points from the August reading of 61.3%. The New Orders Index registered 61.8%, a decrease of 3.3 percentage points from the August reading of 65.1%. The Production Index registered 63.9%, a 0.6 percentage point increase compared to the August reading of 63.3%. The Employment Index registered 58.8%, an increase of 0.3 percentage point from the August reading of 58.5%. The Supplier Deliveries Index registered 61.1%, a 3.4-percentage point decrease from the August reading of 64.5%. The Inventories Index registered 53.3%, a decrease of 2.1 percentage points from the August reading of 55.4%. The Prices Index registered 66.9% in September, a 5.2-percentage point decrease from the August reading of 72.1%, indicating higher raw materials prices for the 31st consecutive month.

Of the 18 manufacturing industries, 15 reported growth in September, in the following order: Textile Mills; Miscellaneous Manufacturing; Plastics & Rubber Products; Computer & Electronic Products; Food, Beverage & Tobacco Products; Machinery; Apparel, Leather & Allied Products; Paper Products; Electrical Equipment, Appliances & Components; Chemical Products; Petroleum & Coal Products; Transportation Equipment; Furniture & Related Products; Fabricated Metal Products; and Nonmetallic Mineral Products. The only industry reporting contraction in September is Primary Metals. *Source: Institute for Supply Management, 10.01.18*

Industry News

Service Center Shipments of Steel, Aluminum Grow in August

U.S. service center steel shipments increased 6.7% year over year, reports the Metals Service Center Institute, Rolling Meadows, IL. Aluminum shipments increased 4.1% during the month, compared with August 2017. In Canada, service center shipments of steel decreased 6% in August, while shipments of aluminum product increased 3%.

U.S. and Canadian producers shipped an estimated 772.3 million pounds of aluminum sheet and plate in August, reports the Aluminum Association, Washington. Total shipments of sheet and plate products were up 4% year over year and 4.9% over July. Year-to-date shipments through August totaled 5.9 billion pounds, up 2.6% over the first eight months of 2017.

Shipments of can stock totaled 338.5 million pounds in August, down 5% from the year-ago month. Shipments of non-heat treatable sheet increased 6.6% for the month to 256.4 million pounds. Shipments of all other sheet and plate increased 21.5% in August to 177.3 million pounds.
Source: Metal Center News, 09.25.18

U.S. Factory Gains Cool to Still-Solid Pace as Bottlenecks Ease

"Despite the decline, the reported growth in 15 out of 18 manufacturing industries is a testament to the expanded economic activity in the manufacturing sector," said Anthony Sasso of TD Bank. A measure of U.S. manufacturing cooled in September from a 14-year high as supply bottlenecks and price pressures eased, Institute for Supply Management data showed on October 1.

The factory index dropped to 59.8 from 61.3 in the prior month.

The measure of new orders fell to 61.8 from 65.1 while the production index advanced to 63.9, the highest since January. And the gauge of prices paid slipped to a 10-month low of 66.9 from 72.1; biggest one-month decline since June 2017.

The ISM report indicates manufacturing is coming off the boil while still expanding at a solid pace amid steady demand and lower taxes. The industry is poised to contribute to economic growth this quarter even as trade tensions with China escalate.

Declines in gauges of backlogs and supplier-delivery times signal factories are catching up with demand, helping to dissipate price pressures. In prior months, producers' rush to buy materials ahead of U.S. tariffs and counter-levies by China triggered supply-chain disruptions and a surge in costs.

The employment index rose to 58.8, the highest since February, from 58.5. This bodes well for manufacturing payrolls, which are projected to rebound in September after a small drop in August.

"Albeit a slight decline, the economy's strength is holding, as we continue to see an increase in production, employment, new export orders and imports," states Anthony Sasso, head of equipment finance, TD Bank. "The reported growth in 15 out of 18 manufacturing industries is a testament to the expanded economic activity in the manufacturing sector. As we look ahead into 2019, we remain cautiously optimistic about continued economic growth while assessing the impact potential tariffs may have."

Other Highlights

- The gauge of supplier deliveries fell to a five-month low of 61.1 from a 64.5 reading that was near a 14-year high; shows lead times growing at slower pace as producers find it easier to meet demand
- The index of backlogs fell to 55.7 from 57.5.
- Inventories slid to 53.3 from 55.4.
- Export orders measure rebounded to 56, the first pickup in three months, from 55.2.

Source: Bloomberg, 10.01.18

Capacity Utilization Rate Hits 79.2%

The U.S. steel capacity utilization rate hit 79.2% for the week ending Sept. 29, according to an American Iron and Steel Institute (AISI) report. Year-to-date production is up 4.5% compared with the same time frame in 2017.

U.S. steel capacity utilization rate seems to be increasing, reaching 79.2% at the end of September. In 2017, capacity utilization rate for the same week was 73.4%. An increasing capacity utilization rate is driving lower steel imports in the U.S., which fell 1% from July to August.

Higher domestic production may move domestic steel prices lower. Supply concerns are easing; however, the potential ArcelorMittal disruption could create uncertainty again and move domestic steel prices higher.
Source: MetalMiner, 10.02.18

Industry News

Aluminum Hits 3 1/2 Month Peak on Supply Fears

Aluminum touched its highest price in more than three months on Thursday, October 4 supported by worries over potential shortages after the world's biggest producer of alumina announced a shutdown. The gains, however, could be overdone because Norsk Hydro's closure of the Alunorte alumina refinery in Brazil may only be temporary, said Capital Economics analyst Ross Strachan.

"I'm wary of reading too much into the prospects on the aluminum side," he said. Hydro said on October 3 that it would halt production indefinitely and lay off 4,700 people at Alunorte, which has been operating at half of its capacity since March because of an environmental dispute. "It almost makes you wonder if this is an attempt by the company to alleviate the situation by putting pressure on the government," Strachan said. "You would think that there will be a resolution to facilitate at least a significant restart, even if it's not able to go back to full capacity."

Three-month aluminum on the London Metal Exchange was up 2.6% at $2,264 a ton by 1020 GMT, having touched its highest since June 14 at $2,265.50. Gains were stretching into a fifth session after a 4.2% jump on October for its largest one-day gain since April.
Source: Reuters, 10.04.18

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Gas Prices Nearing Highest Levels in Four Years, Adding to Calls to Repeal Gas Taxes

Gas prices are creeping up nationally, now pennies a gallon away from their highest level since 2014, just in time for the November midterm elections when California will vote on rolling back its gas tax. Average prices topped $2.90 a gallon for unleaded October 3 for the first time since June, having risen about 6 cents a gallon in the past month, the Oil Price Information Service reports. If they rise by about another eight cents, they will be the highest in four years. That could spell trouble at the polls November 6 since voters often have gas prices in mind when they cast ballots. In California, which is second only to Hawaii as the state with the highest fuel prices, voters will decide whether to repeal a tax that raises $5.1 billion a year for road and bridge repair and public transit.

Gas prices are rising nationally because strengthening global economies and international politics have boosted oil prices. "It's been about demand growth worldwide," said Tom Kloza, global head of energy analysis for OPIS. And when it comes to sanctions on Iran, a major oil producer, "there's no shortage of scary comments" that inject fear into the market and drive up prices further.

The Trump administration is in the process of re-instituting sanctions on Iran after pulling out of an agreement negotiated under President Barack Obama that would limit that nation's nuclear development. On October 3, benchmark U.S. crude rose 1.6% to $76.41 a barrel in trading in New York in a week in which it hit a four-year high. In addition, the Organization of Petroleum Exporting Countries, OPEC, is hoping for rising prices as it heads toward a Dec. 6 meeting, said Patrick DeHaan, senior petroleum analyst for GasBuddy.com. He noted, however, that gas prices usually fall after the peak summer driving season, not rise. "I think we have a pretty good shot at seeing $3 a gallon if the OPEC or Iran (situations) continue to fan the flames," DeHaan said.

In California, perennially the top state for gasoline consumption prices will only have to rise another penny or two a gallon to hit their highest level since July, 2015, he said. On October 3, self-serve unleaded averaged $3.77. If prices hold or rise further through election day, that might help proponents of repealing an excise tax that went into effect last year that added 12 cents to every gallon in the Golden State. A repeal could ricochet into similar movements around the country: "At least 10 states in the last few years have increased their gas taxes," DeHaan said. ***Source***: ***CNBC, 10.04.18***

Special Section: Trade News

U.S., Canada and Mexico Just Reached a Sweeping New NAFTA Deal

Here's what is in it—September 30, President Trump got his wish for a significantly revised North American trade deal. After more than a year of intense negotiations, the United States, Canada and Mexico reached an agreement to update the North American Free Trade Agreement, the 1994 pact that governs more than $1.2 trillion worth of trade among the three nations.

New name. Goodbye NAFTA. The new deal will be known as the United States-Mexico-Canada Agreement, or USMCA.

Big changes for cars. The goal of the new deal is to have more cars and truck parts made in North America. Starting in 2020, to qualify for zero tariffs, a car or truck must have 75% of its components manufactured in Canada, Mexico or the United States, a substantial boost from the current 62.5% requirement. There's also a new rule that a significant percentage of the work done on the car must be completed by workers earning at least $16 an hour, or about three times what the typical Mexican autoworker makes. Starting in 2020, cars and trucks should have at least 30% of the work on the vehicle done by workers earning $16 an hour. That gradually moves up to 40% for cars by 2023. While many economists think these new rules will help some North American workers, they also warn that some small cars may no longer be made in North America because they would be too expensive under the new requirements.

Trump's victory: Canada opens up its milk market to U.S. farmers. Canada has a complex milk and dairy system. To ensure Canadian dairy farmers don't go bankrupt, the Canadian government restricts how much dairy can be produced in the country and how much foreign dairy can enter to keep milk prices high. Trump didn't like that, and dairy was a major sticking point in the negotiations. In the end, Canada is keeping most of its complex system in place, but it is giving greater market share to U.S. dairy farmers. U.S. negotiators say they got a major victory by forcing Canada to eliminate the pricing scheme for what are known as Class 7 dairy products. That means U.S. dairy farmers can probably send a lot more milk protein concentrate, skim milk powder and infant formula to Canada (and those products are relatively easy to transport and store).

Canada's victory: Chapter 19, allowing for a special dispute process, stays intact. Canadian Prime Minister Justin Trudeau said repeatedly that he wanted to keep Chapter 19 in place, and that's exactly what happened. The U.S. side pushed hard to eliminate this chapter, but in the end, it stayed. Chapter 19 allows Canada, Mexico and the United States to challenge one another's anti-dumping and countervailing duties in front of a panel of representatives from each country. This is generally a much easier process than trying to challenge a trade practice in a U.S. court. Over the years, Canada has successfully used Chapter 19 to challenge the United States on its softwood lumber restrictions.

Mexico and Canada get assurance Trump won't pound them with auto tariffs. Trump has repeatedly threatened to slap hefty tariffs on car and vehicle parts coming from overseas into the United States. Along with the new trade deal, his administration signed "side letters" allowing the two nations to mostly dodge Trump's auto tariffs. The side letters say Canada and Mexico can continue sending about the same number of vehicles and parts across the border free of charge, regardless of whether auto tariffs go into effect down the road. Only parts above that quota could face tariffs.

Trump's steel tariffs stay in place (for now). Canada wanted Trump to stop his 25% tariffs on Canadian steel. That didn't happen — yet. The two countries are still discussing lifting those tariffs, but a senior White House official said Sunday that process is on a "completely separate track." Trudeau has called the steel tariffs "insulting and unacceptable" because the two nations are such close allies.

Improved labor and environmental rights. The USMCA makes a number of significant upgrades to environmental and labor regulations, especially regarding Mexico. For example, the USMCA stipulates that Mexican trucks that cross the border into the United States must meet higher safety regulations and that Mexican workers must have more ability to organize and form unions. Some of these provisions might be difficult to enforce, but the Trump administration says it is committed to ensuring these happen.

Increased intellectual property protections. The new IP chapter is 63 pages and contains more-stringent protections for patents and trademarks, including for biotech, financial services and even domain names. Many business leaders and legal experts believed these updates were necessary given that the original agreement was negotiated 25 years ago.

Chapter 11, giving investors a special way to fight government decisions, is (mostly) gone. Chapter 11 is eliminated entirely for Canada and mostly for Mexico, except for some key industries such as energy and telecommunications. Chapter 11 gave companies and investors a special process to resolve disputes with one of the governments in NAFTA. The idea was that if investors put a lot of money into a project and then the government changed the rules, there was a clear dispute process — outside the court system — where investors could get their problem resolved. Critics argue that Chapter 11 was mainly used as a way for big corporations to get taxpayer money, but businesses say it was necessary to ensure they weren't harmed by sudden changes when new governments came into power in Mexico, Canada or the United States. In the end, Chapter 11 is mostly gone, except for a few key industries, such as oil, that lobbied hard to be able to challenge the Mexican government if it changes the rules and tries to nationalize its energy sector again. ***Source: Washington Post, 10.01.18***

Special Section: Trade News

Trade Pact Clause Seen Deterring China Trade Deal with Canada, Mexico

China's hopes of negotiating a free trade pact with Canada or Mexico were dealt a sharp setback by a provision deep in the new U.S.-Mexico-Canada trade agreement that aims to forbid such deals with "non-market" countries, trade experts said on October 2. The provision specifies that if one of the current North American Free Trade Agreement partners enters a free trade deal with a "non-market" country such as China, the others can quit in six months and form their own bilateral trade pact.

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The clause, which has stirred controversy in Canada, fits in with U.S. President Donald Trump's efforts to isolate China economically and prevent Chinese companies from using Canada or Mexico as a "back door" to ship products tariff-free to the United States. The United States and China are locked in a spiraling trade war that has seen them level increasingly severe rounds of tariffs on each other's imports. Under the clause, the countries in the updated NAFTA, renamed the U.S.-Mexico-Canada Agreement (USMCA), must notify the others three months before entering into such negotiations.

Derek Scissors, a China scholar at the American Enterprise Institute in Washington, said the provision gave the Trump administration an effective veto over any China trade deal by Canada or Mexico. If repeated in other U.S. negotiations with the European Union and Japan, it could help isolate Beijing in the global trading system. "For both Canada and Mexico, we have a reason to think an FTA with China is a possibility. It's not imminent, but this is a very elegant way of dealing with that," Scissors said. "There's no China deal that's worth losing a ratified USMCA," Scissors added. Full Story ***Source: Reuters, 10.03.18***

U.S. Advances Trade Policy with EU, Japan, South Korea

On the sidelines of the United Nations General Assembly in New York last week, U.S. Trade Representative Robert Lighthizer, European Union Commissioner for Trade Cecilia Malmström, and Japanese Minister of Economy, Trade, and Industry Hiroshige Seko met to discuss trade policy. After the meeting, the three leaders released a joint statement that outlined efforts to address non-market oriented policies in third countries, subsidies and state-owned entities, technology transfer, digital trade, and World Trade Organization (WTO) reform.

Lighthizer, Malmström, and Seko agreed to:

- Continue discussions to identify and share information on potential non-market oriented policies and practices, as well as to "deepen discussions" on enforcement and rule-making to address these issues.
- Devise concrete plans to co-sponsor a proposal on transparency and notification aimed at combating domestic industrial subsidies at the next meeting of the WTO Council on Trade in Goods, which is set for November 2018.
- Reaffirm joint work to "maintain the effectiveness of existing WTO disciplines," with each side working internally through the end of 2018 with a goal of launching negotiations on more effective subsidy rules.
- Conduct deeper discussions on ways to strengthen rules on industrial subsidies and state-owned enterprises (SOEs), with specific discussion on ways to address behaviors such as state-owned bank lending, preferential input pricing, and subsidies that boost industrial overcapacity.
- Work to advance the timely launch of negotiations of a new agreement on several issues, including the Global Forum on Steel Excess Capacity.

Later in the week, President Donald Trump and Japanese Prime Minister Shinzo Abe announced that they will start talks on a bilateral trade agreement. A joint statement said the United States wants more access to the Japanese auto market. In exchange, President Trump agreed to hold off placing tariffs on Japanese autos.

Also last week: President Trump signed a revised free trade agreement with South Korea that eased limits on U.S. auto sales in the country. The majority of the original trade pact remains intact, but in addition to guaranteeing the United States more access to South Korean auto market, the revised agreement:

- Requires South Korea to address issues with onerous and costly customs procedures that have hindered United States exports.
- Ends steel tariffs on South Korean imports, but limits steel imports from South Korea into the United States to a product-specific quota equal to 70% of that country's average annual import volume from 2015 through 2017.

Source: MSCI, 10.02.18