Ulster Bank Weekly Economic Commentary

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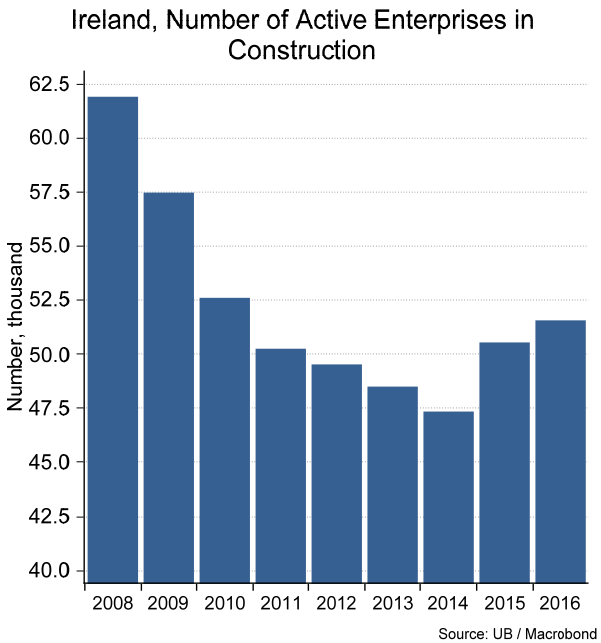
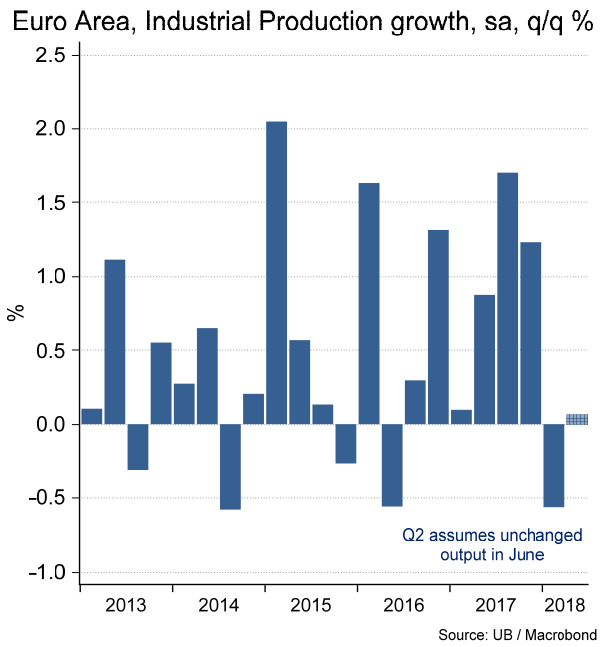
Ireland: Number of construction firms on the rise as the start-up rate doubles from the crisis low



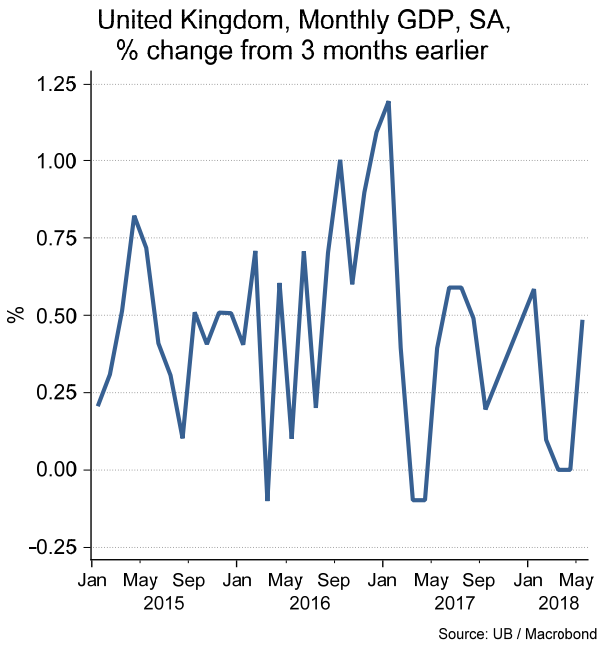
The latest results of the Ulster Bank Construction PMI survey showed some easing in activity growth in June. However, at 58.4, the headline PMI remains very much at levels which signal ongoing rapid activity gains, with particular strength again evident in the Housing and Commercial areas. Furthermore, confidence about future prospects remains very elevated, with 56% of respondents expecting activity to rise in the coming year. Indeed, the sector's favourable outlook is also a prominent theme in separately-released figures from the CSO. These showed that the rate of new business formation in construction more than doubled over the period 2010 to 2016, with over 4,600 construction start-ups accounting for almost a quarter of all start-ups across the Irish business sector in 2016 (the latest year available). Moreover, the start-up rate in construction is now the highest of the business economy's three main sectors, having – unsurprisingly - been the lowest during the crisis. We estimate a 9.1% start-up rate in construction in 2016, significantly ahead of the equivalent rates in industry (7.7%) and in the broad services sector (7.3%). The pickup in the start-up rate is resulting in a notable increase in the number of active construction businesses. There were over 51,500 active firms in 2016 - an increase of over 4,200, or 8.9%, on the crisis low point of 47,349 reached in 2014. While that is still some 10,000 fewer firms than were operating in 2008, it is the highest since 2010, with the ongoing increase in the number of active construction firms representing further evidence of the sector's turnaround.

Eurozone: Minutes confirm deliberate ambiguity of interest rate guidance



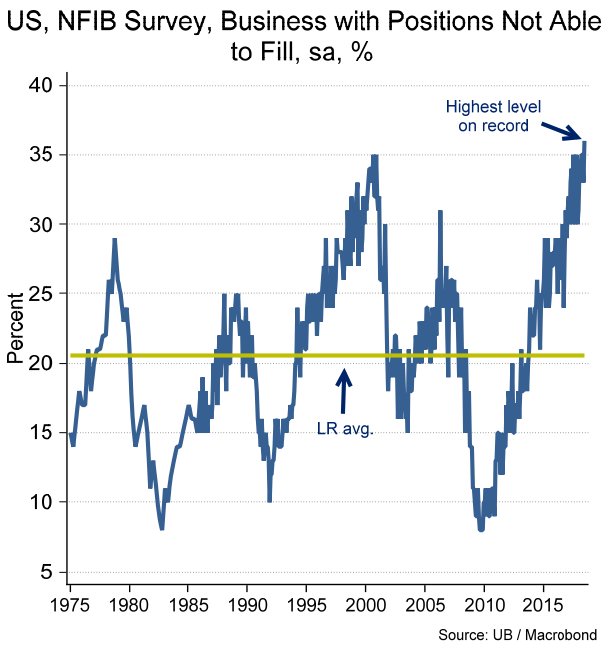
This week's account of the June ECB policy meeting reiterated some key messages from Draghi's post-meeting press conference. The decision to cease net purchases under ECB's quantitative easing programme at the end of 2018 following monthly purchases of €15bn over Q4 (from €30bn until Sep.) was rooted in the so far substantial progress towards a sustained adjustment in inflation, which is expected to continue over the period ahead. The minutes also confirmed that the new forward guidance on interest rates was left ambiguous intentionally (i.e. the ECB's commitment to keep rates unchanged through the summer of 2019 is open to interpretation), with members judging that the new formulation strikes a good balance between being sufficiently precise to anchor policy rate expectations and maintaining adequate flexibility. The latter underlines that despite ECB's choice to provide its interest rate guidance in calendar terms, the gradual normalisation of interest rate settings will remain subject to review and assessment as new information regarding the economy's performance and prospects becomes available. Meanwhile, this week's industrial production figures for May confirmed the rebound expected by the consensus, with output expanding by 1.3% m/m in May following a decline of 0.8% in April. Encouragingly, this suggests that industrial production is likely to be broadly neutral for q/q GDP growth in Q2 following a negative contribution of around 0.1 percentage points in Q1, providing some support for the view that growth may pick-up slightly in Q2 (from 0.4% q/q in Q1).

UK: Improved GDP performance leaves BoE on track to hike, though elevated political risk is a key source of uncertainty



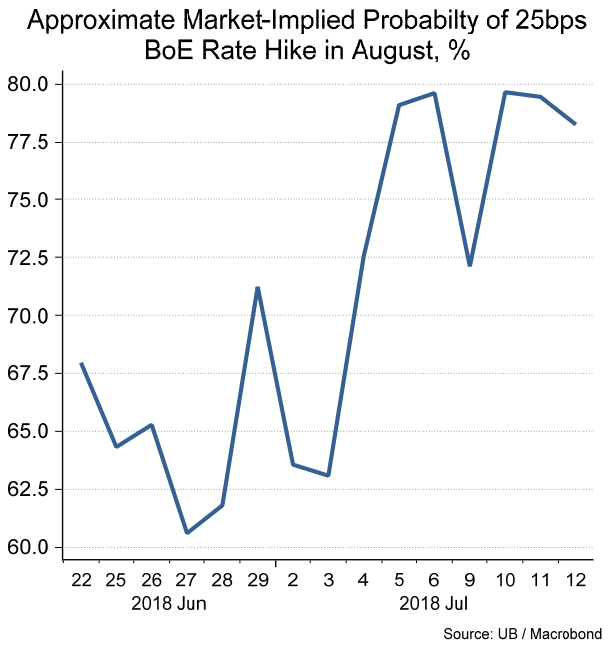
Reinforcing the signal from the recent PMI surveys we noted last week, this week's new monthly official GDP estimate confirmed that the UK has experienced a notable improvement in growth momentum following an early-year soft patch. Monthly growth in real GDP was 0.3% in May, following on from 0.2% in April, no growth in March and a 0.1% monthly decline in February. This improvement has largely reflected a strengthening in output growth in the dominant services sector (helped in part by firmer consumer spending), though there was also better news of a return to positive growth in both the manufacturing and construction sectors in May. While the May outturn for overall GDP wasn't any stronger than had been anticipated, the confirmation of the pattern of sequential improvement in growth performance is still a key takeaway in our view. For instance, the level of GDP in May is now 0.5% higher than it was 3 months earlier – a notable pickup from the 0.0% growth as registered on the same basis in March. Indeed, we note that it would now take a monthly figure of just 0.1% in June in order for the BoE's growth forecast of 0.4% q/q in Q2 to be realised. In other words, the 'hard' output data are providing important validation of the BoE's May Inflation Report view that the economy would quickly regain momentum after a disappointingly sluggish Q1. All else equal, that would leave the BoE on track to follow through on its guidance and raise rates at its August meeting, though the intensity of Brexit-related political uncertainty means a rate hike is not quite as assured as the economics would imply.

US: Hiring difficulties at record high as jobs market continues to tighten



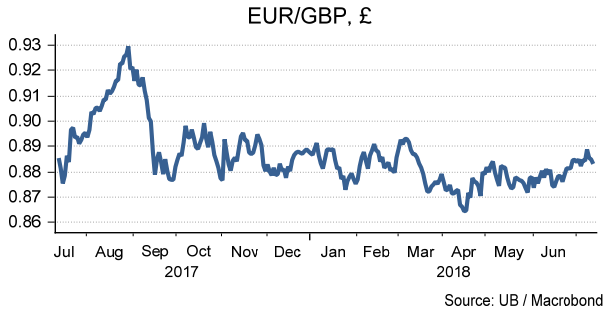
Incoming news continues to point to robust underlying trends in the labour market which reflect the strength of growth in the US economy more generally. The number of voluntary quits in the jobs market rose to 3.56 million in May, the highest on record since figures commenced in 2000. As a result, the quits rate (i.e. quitters as a share of employed people) ticked up to a 17-year high of 2.4%, highlighting ongoing confidence in US employment prospects. This confidence is being underpinned by tight labour market conditions, with job openings remaining above the number of unemployed workers in May, while this week's NFIB survey also showed that the shortage of qualified workers remains the main concern for business owners as the share of small business with positions not able to fill rose to a four-decade high of 36% in June. This offers some support for the view that pay growth will continue its gradual upward move over the period ahead, and indeed, small business plans to increase compensation remained very elevated, though at the margin eased slightly from May's record high. Measures of consumer price inflation also continue to edge higher, with the latest CPI inflation figures for June showing both headline and core inflation at multi-year highs of 2.9% and 2.3%, respectively. So overall, we think that this week's data provide further reasons to expect that the Fed will continue to gradually normalise US interest rates. However, risks associated with US trade policy continue to intensify following news that the Trump administration may impose tariffs on another $200 bn imports from China.

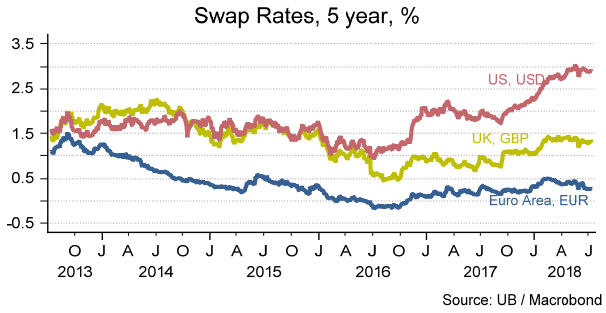
Financial Markets: Eur/GBP holds steady as growth data help offset political uncertainty, for now



It is a bit surprising that, despite all of the political upheaval in the UK over the past week, sterling is very little changed vs. the euro since last Friday, trading at 88.3p. While there was a spike to 89p on Monday as news of Boris Johnson's resignation broke, the downward pressure on sterling proved temporary, with Eur/GBP subsequently drifting back to sub 88.5p territory from mid-week. The encouraging signals from the UK growth data have no doubt offered some support, as they suggest the economy's trajectory is consistent with the need for a further modest tightening of BoE interest rate policy. Johnson's departure initially prompted a modest scaling back of the market-implied probability of an August hike from 80% to 72%, but, helped by the improving GDP data, the probability has since drifted back up to around 78%, in the process providing a modest lift to the pound. More broadly, we are reluctant to take much comfort from what might appear like a very resilient performance by the pound in the face of intense political uncertainty. While it is encouraging to see an emerging preference in Downing Street for softer forms of Brexit, there remains considerable uncertainty around the ability of the PM to push through such a strategy, and indeed around the willingness of the EU to agree terms acceptable to even the less extreme elements of the Tory party. This means that concerns about the risks of harder (including crash / no deal) forms of Brexit remain very valid in our view, so we should not be surprised to see higher volatility in sterling's price action in the weeks and months ahead.

Currency and interest rate market trends





Market Monitor

Foreign Exchange Markets

	Latest	weekly Δ, %
EUR/GBP, £	0.883	-0.1
GBP/EUR, €	1.132	0.1
EUR/USD, $	1.170	-0.4
GBP/USD, $	1.324	-0.3
EUR/JPY, JP¥	131.5	1.3
GBP/JPY, JP¥	148.8	1.4
USD/JPY, JP¥	112.4	1.7
EUR/CHF, CHF	1.171	0.7

Stocks & Commodities

	Latest	weekly Δ, %
ISEQ	7,024	0.3
STOXX Europe 600	384	0.5
FTSE 100	7,651	0.4
S&P 500	2,789	1.1
Dow Jones	24,899	1.8
Nasdaq	7,794	1.4
NIKKEI	22,188	1.8
OIL (London Brent)	73.5	-4.7
Gold	1,248	-0.6

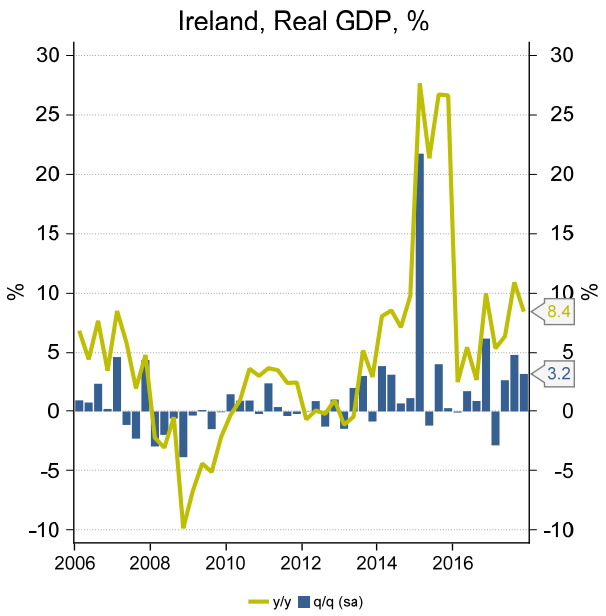
Interest Rate Markets

		Latest (%)	weekly Δ, bps
EUR	3 Month Euribor	-0.321	0.0
	2 Year Swaps	-0.17	1
	5 Year Swaps	0.27	1
	10 Year Swaps	0.87	1
GBP	3 Month Libor	0.731	1.8
	2 Year Swaps	1.05	-1
	5 Year Swaps	1.31	0
	10 Year Swaps	1.52	-1
USD	3 Month Libor	2.339	0.8
	2 Year Swaps	2.82	3
	5 Year Swaps	2.90	2
	10 Year Swaps	2.93	2

Note: the data in the tables are indicative only and are sourced from Bloomberg. Latest data are updated as at the time of publication. "weekly Δ" refers to the change from the previous week's closing levels.

Ulster Bank Cost of Funds Rate (365 day count) = 0.45%
Euro rates are quoted in 360-day convention.
To convert to 365 day count, divide by 360, & multiply by 365

Highlights for the week ahead: Irish national accounts, Powell testimony and UK data in focus



Source: UB / Macrobond

In a key week on the Irish economic calendar, the Q1 National Accounts (on Thursday) will provide a delayed update on GDP growth at the start of 2018. As usual, we will pay particular attention to those measures less subject to MNE-distortion such as household consumption and core domestic investment. The detailed annual national accounts may also include revisions to GDP growth in 2017 as a whole following an initial estimate of 7.8%. But with GDP growth likely to continue exaggerating the strength of the economy's underlying performance in 2017, the annual GNI* figures are also sure to receive attention, though the lack of a volume terms measure limits its use. Meanwhile, annual house price growth (on Friday) is expected to have remained elevated in May following a near three-year high of 13% in April.

Away from home, Fed Chair Powell is expected to use his semi-annual testimony to Congress (on Tuesday following tomorrow's Monetary Policy report) to reiterate the Fed's current core message that given current US economic conditions, the case for continued gradual policy tightening is strong. US trade policy is also expected to feature prominently in the discussion with lawmakers. We think that Powell will show some concern but highlight that key data does not yet suggest a meaningful impact. Meanwhile in the UK, next week's labour market, consumer price inflation and retail figures are the last key data points ahead of the August BoE policy meeting. Finally in the Eurozone, final figures for June are expected to leave headline and core inflation unrevised at 1.9% and 1%, respectively.

Economic calendar for the week commencing July 16th

Ireland / Eurozone	UK	US
Monday		
10.00 – EZ Trade Balance (May) 11.00 – Goods Exports and Imports (May)	00.01 – Rightmove House Prices (Jul)	13.30 – Retail Sales (Jun); Empire State Manufacturing (Jul); 15.00 – Business Inventories (May)
Tuesday		
07.00 – EZ New Car Registrations (Jun)	09.30 – Employment Change (May); Unemployment Rate (May); Av. Weekly Earnings (May)	14.15 – Industrial / Manufacturing Production (Jun); Capacity Utilisation (Jun) 15.00 – Fed's Powell testifies before Senate; NAHB Housing Market Index (Jul)
Wednesday		
10.00 – CPI – Final (Jun); Construction Output (May)	16.35 – CPI (Jun); RPI (Jun); HPI (Jun)	13.30 – Housing Starts (Jun); Build. Permits (Jun) 15.00 – Fed's Powell testifies before House 19.00 – Fed publishes Beige Book
Thursday		
11.00 – Quarterly National Accounts (Q1); National Income and Spending Annual Results (2017); Balance of Payments (Q1)	09.30 – Retail Sales (Jun)	13.30 – Initial Jobless Claims; Philly Fed Business Outlook (Jul)
Friday		
09.00 – EZ Current Account (May) 11.00 – Residential Property Price Index (May); Wholesale Price Index (Jun)	09.30 – Public Sector Net Borrowing (Jun)	13.00 – Fed's speech on Economy (Bullard – non-voter) 15.00 – Chicago Fed National Activity Index (Jun) 15.00 – Existing Home Sales (Jun)

The Calendar uses Irish local time

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