There are signs of better times ahead for the economy

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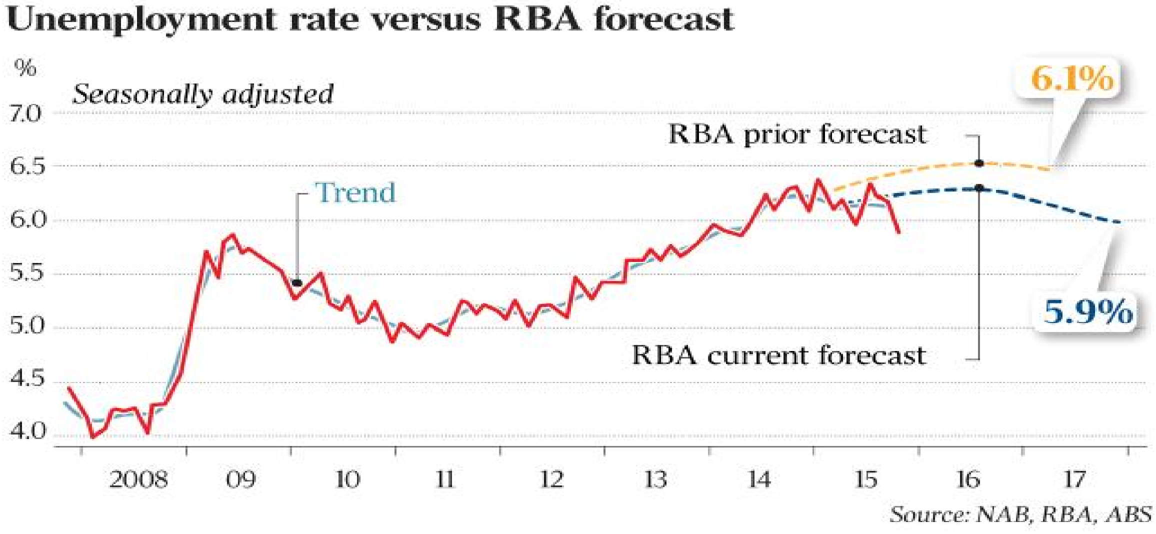

Unemployement rate and forecast.

Some economic data released in recent weeks suggest the US and Australian economies are on the mend and the Chinese economy is beginning to stabilise. Could we be close to turning points in business conditions? Which of the myriad of reports and statistics on the economy should investors be watching?

The US and Australia both recorded strong growth in jobs last month and measured unemployment rates fell (in the US from 5.1 to 5 per cent and in Australia from 6.2 to 5.9 per cent). In China, several forward-looking indicators levelled out in October, and consumption growth exceeded expectations.

The US jobs data led to a strengthening of views the Fed will raise its cash rate in mid-December from the near-zero level it's been at since late 2008. Investors shouldn't rush to the exit: even in 12 months' time, the US cash rate could still be 1.5 per cent or less. In Australia, the October report on labour market conditions caused a scaling back in market predictions for two further cuts in our cash rate in 2016. The US and Australian dollars moved a little higher.

However, the prevailing view in investment markets is for economic growth to remain modest in the US and lacklustre here, and for China's economy to slow a lot further.

Many investors and market commentators attribute the October reports of strong labour market gains in the US and Australia (and Canada, too) to wobbles in the monthly data. Here are two extracts from those reactions:

¬“Too good to be true: labour force figures can’t be believed.”

¬“The laughable outcome is that not only did the Treasurer leap upon the seemingly laughable data with glee … but that currency traders bounced the currency upward.”

Adam Boyton at Deutsche Bank puts the Australian numbers in a broader context: “did the (Australian) economy really create nearly 60,000 jobs last month? Probably not. But it also certainly didn’t lose 800 jobs the month before either. (As an aside, it’s interesting that when the data are on the soft side, the ‘media/analyst disbelief factor’ is often so much less). Hence the need to step back, look at the trend and cross check.”

Trend growth in employment has been moving up; and Deutsche Bank’s “employment tracker”, which comprises 10 series (none compiled by the Bureau of Statistics), has been on an upward course for about a year.

In a report on the October numbers headed “A cyclical turn in unemployment?” Ivan Colhoun of the National Australia Bank also makes a balanced assessment: “While we don’t believe the large moves in either the employment or unemployment rate, we believe the signals, i.e. that employment is strengthening (driven by NSW and, importantly, an improving trend for Queensland) and to an extent that is sufficient to see the unemployment rate continue to decline.”

I suggest investors allow that the rate of economic growth here is shifting up a gear — from lacklustre to moderate — and they keep particularly close watch on indicators of employment, unemployment, business confidence and business credit.

As a result, the Reserve Bank is more likely to leave the cash rate unchanged through 2016. And many companies will have somewhat better opportunity to grow their sales and earnings — though for resource companies, the serious cutbacks in global oversupplies necessary to boost their earnings could take much further time.

For the Chinese economy, the key series to watch include the purchasing managers’ indexes (the PMIs) — which, let me stress again, don’t tell us whether the economy is “contracting”, “expanding” or “flat” but illustrate what’s happening to the rate of growth — as well as statistics on industrial production, retail sales and fixed asset investment.

In October, Chinese PMIs were little changed. In the 12 months to October industrial production rose by 5.6 per cent, retail sales by 11 per cent, and fixed asset investment by 10.2 per cent. Hardly indicators of a hard landing.

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