Week Ahead Economic Preview

Global overview

- **US-China trade war impact to be gleaned from industrial production and retail sales updates**
- **Global business outlook surveys**
- **US and China inflation**
- **UK GDP and labour market updates**
- **Special reports on Spain's growth slowdown and an overview of the new RCEP free trade agreement in Asia-Pacific**

US-China trade developments are dominating markets and the coming week will see the release of important indicators of how both economies have been faring. Industrial production updates will give insight into the impact on manufacturing while retail sales numbers will help assess the scale of any spill-over to consumers. IHS Markit's Global Outlook Survey also reveals business expectations for the year ahead from a panel of 12,000 companies and will give further clues as to trends in economic growth, which the monthly PMI showed to have slipped globally to its lowest since February 2016.

For the US, the PMI survey data hint at some steadying of manufacturing from the downturn seen earlier this year, but both inflation and retail sales could remain under pressure amid signs that weak demand is limiting pricing power. Service sector inflows of new business were the lowest since 2009 in October. Fresh inflation numbers will also be eagerly awaited (page 3).

For China, the overall picture from the PMI surveys remains one of an economy struggling as trade war tensions exacerbate the underlying trend of slower economic growth. Elsewhere in Asia, the week brings GDP updates from Japan, Malaysia and Hong Kong, while New Zealand and the Philippines will decide on monetary policy (page 5).

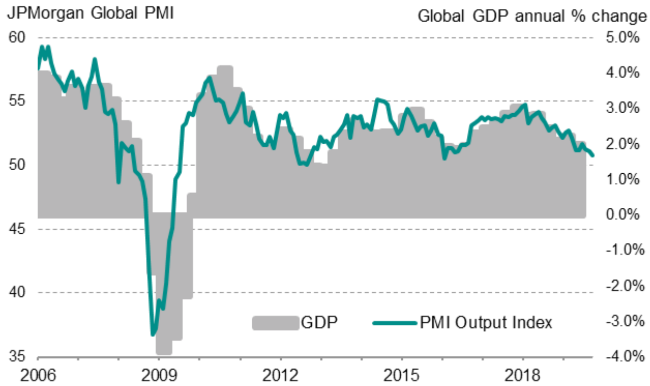
In Europe, third quarter GDP growth trends will be revealed for Germany and the UK, both of which are skirting with recession. The latter also sees key labour market updates, which will be eagerly assessed by a divided monetary policy committee at the Bank of England (page 4).

Our special reports this week look at why Spain is set for slower economic growth over the coming year (page 6) ahead of a general election widely expected to deliver more uncertainty, and we discuss the potential impact of the new RCEP free trade agreement in Asia-Pacific (page 9).

Contents

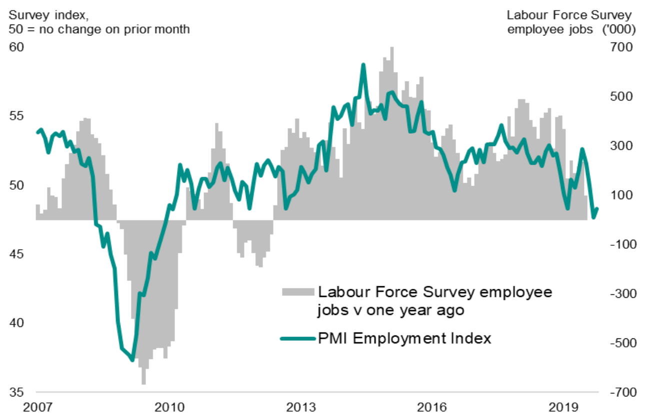
Special reports

Business outlook surveys will give insights into firms' expectations for the year ahead after PMI data showed global output growth slipping to the lowest since 2016



Source: IHS Markit.

The Bank of England has been late in signalling the potential need for stimulus among the world's largest central banks, but two policymakers voted for a rate cut in October. Updated UK GDP and labour market data could provide an important steer on the next policy move



Source~: IHS Markit, ONS.

Key diary events

Monday 11 November

IHS Markit Global Business Outlook surveys (Oct)
Japan Machinery orders (Sep), Eco Watchers (Oct)
BoJ Summary of Opinions (30-31 Oct)
Malaysia industrial output, jobless rate (Sep)
Italy industrial output (Sep)
UK GDP, business investment (Prelim, Q3)
UK industrial output, trade balance (Sep)
Russia GDP (Prelim, Q3), trade balance (Sep)

Tuesday 12 November

Australia business confidence (Oct)
UK jobless rate, average earnings (Sep), claimant count change (Oct)
Euro area and Germany ZEW economic sentiment index (Nov)
India inflation (Oct)

Wednesday 13 November

BRICs Summit in Brazil (13-14 Nov)
Deadline for US to decide auto tariffs
South Korea unemployment rate (Oct)
Australia consumer confidence (Nov), wage price index (Q3)
New Zealand monetary policy decision
Germany inflation (Final, Oct)
UK and US inflation (Oct)
Euro area industrial production (Sep)
Brazil retail sales (Sep)

Thursday 14 November

US monthly budget statement (Oct)
Japan GDP (Prelim, Q3)
Australia jobless rate, employment change (Oct)
China fixed asset investment, FDI, industrial output, retail sales (Oct)
India WPI (Oct)
Germany GDP (Flash, Q3)
France and Spain inflation (Final, Oct)
Philippines monetary policy decision
China new yuan loans, total social financing, M2 (Oct)
UK retail sales (Oct)
Euro area GDP (2nd Est, Q3), employment change (Prelim, Q3)

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Friday 15 November

China house price index (Oct)
Indonesia trade (Oct)
Malaysia GDP (Q3)
Japan industrial output (Final, Sep)
Hong Kong GDP (Final, Q3)
Euro area inflation (Final, Oct), trade balance (Sep)
US retail sales. Industrial output (Oct)

United States Week Ahead

Industrial production, inflation and retail sales

By Siân Jones
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Following divergent signals from manufacturing survey data in October, industrial production data will be keenly watched to see if the sector is starting to emerge from its recent slowdown. Also on the agenda is the latest set of inflation figures and an update on consumers through fresh retail sales data.

Industrial production

An important indication of the health of the goods producing sector will be gleaned from official industrial production data. The latest PMI numbers from IHS Markit signalled a slight recovery in the manufacturing sector, with output and client demand improving during October to hint at a pick up in the performance at the start of the fourth quarter, albeit with growth remaining very subdued. In contrast, however, the ISM survey pointed to an accelerating rate of decline of industrial production.

Inflation

Consumer price data will meanwhile be eyed for clues as to whether price pressures continue to ease. September's data showed CPI unchanged during the month, leaving the annual rate of inflation at 1.7%, down from 2.5% a year ago. According to the latest PMI data from IHS Markit, subdued inflationary pressures look set to have persisted, in line with previously published long-term inflation expectations.

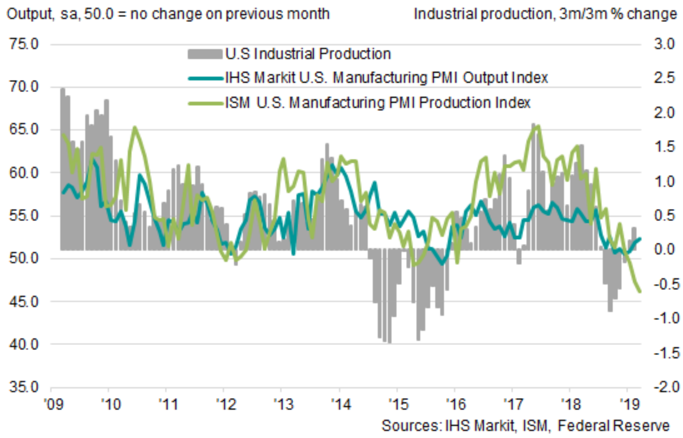
Retail sales

Annualised GDP growth of 1.9% in the third quarter was heavily attributed to strong consumer spending, buoyed in turn by a tight labour market. However, a shock monthly decrease in retail spending in September showed signs of more tentative consumption patterns which could spread into the first month of the final quarter of 2019. A recent drop in consumer confidence has added to concerns about the health of the consumer.

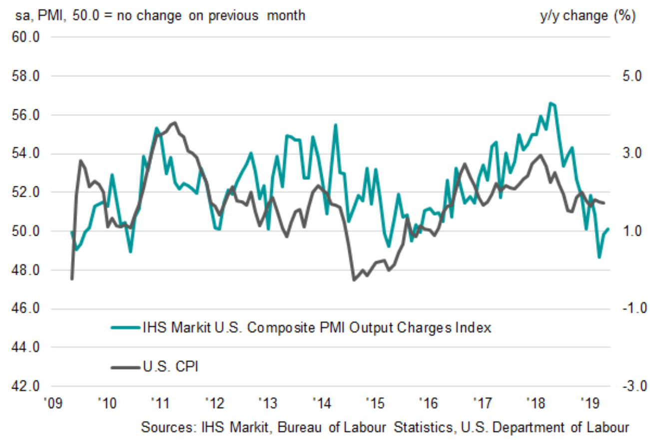
October's retail sales data, as well as the industrial production numbers, will therefore provide useful inputs into nowcast models for fourth quarter GDP.

Also featuring on the economic calendar are NFIB Business Optimism Index, PPI data and the New York Empire State Manufacturing Index.

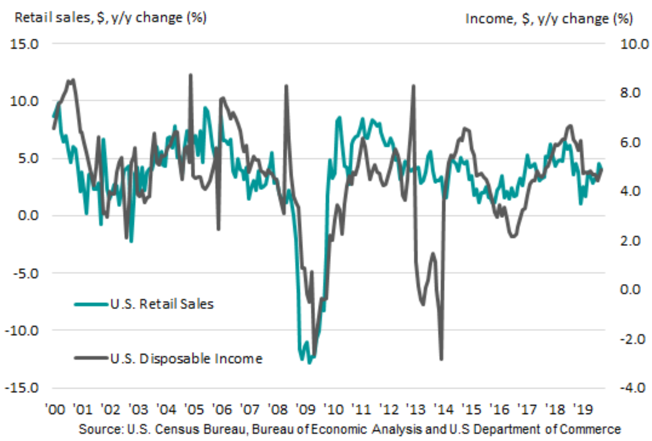
Divergence in survey trends for industrial production



Inflationary pressures remain muted but start to pick up



Slower retail sales growth expected amid more tentative consumer expectations



More insight into the US economic outlook is available from our award-winning team at Macroeconomic Advisers.

Europe Week Ahead

German and UK GDP, Eurozone industrial output

By Joe Hayes
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A slew of macroeconomic data across Europe comes with some crucial updates, most notably in Germany and the UK, where third quarter GDP estimates are published. The common ground here is that both economies contracted in the second quarter, but both countries appear to have taken different paths since.

The second estimate of Eurozone GDP is also due, as well as September industrial output data. UK retail sales and labour market statistics will meanwhile also be closely watched by a split Bank of England Monetary Policy Committee.

German GDP

GDP data for Germany will be a key release of the week amid the risk of the economy entering a technical recession. The PMI showed a protracted factory downturn and increasing signs of spill-over into the domestic economy in October, with September's official industrial output data having also disappointed. Our nowcast points to a 0.1% GDP decline.

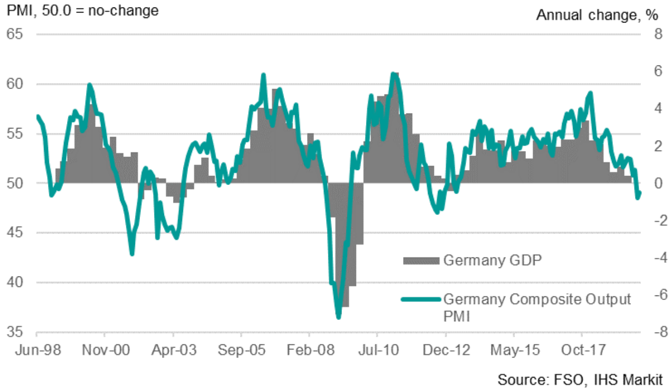
The second estimate of third quarter euro area GDP is due, as well as September industrial production data. October PMI data showed that the euro area economy was broadly flat at the start of the fourth quarter, dragged down by a steep industrial downturn, with output falling at a quarterly rate of approximately 1%.

UK economy update

A busy week of macroeconomic data comes for the UK, with third quarter GDP leading the bill. Growth has been volatile in the year-to-date amid Brexit stock-building. As such, it seems a GDP contraction in the second quarter will be unwound with an expansion of as much as 0.3% in the third quarter, but PMI data suggest the underlying trend is flat at best, with downside risks heading into year-end.

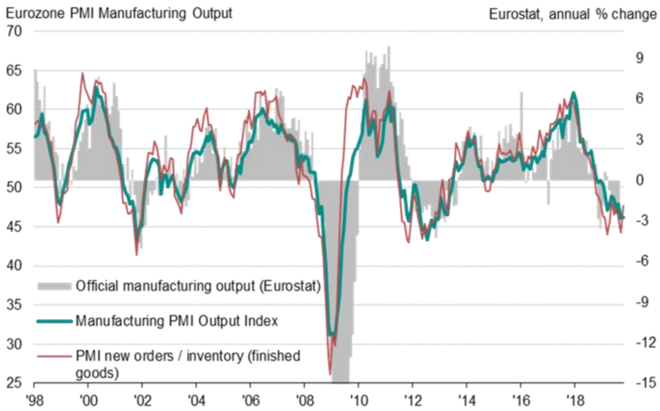
Retail sales and a comprehensive labour market update are also due. Both will carry more crucial weighting from a political perspective also as the December general election draws closer, but will also be eyed closely by a Bank of England whose policymakers showed signs of moving towards a rate cut at their November meeting. Recent survey data have hinted at a cooling labour market.

Technical recession risk for Germany

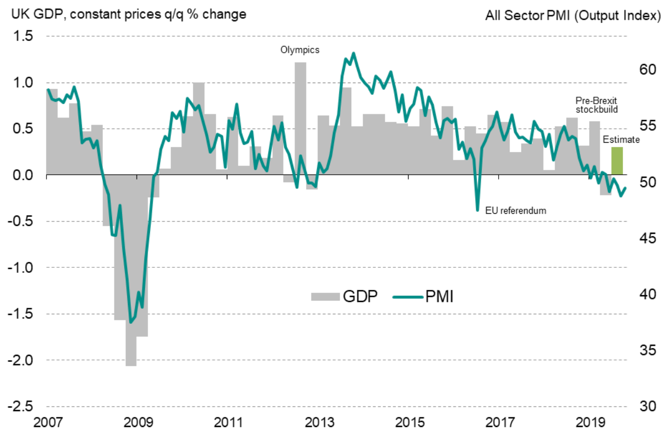


Source: FSO, IHS Markit

Eurozone manufacturing sector still flagging in October



Underlying GDP trend is flat in the UK, with second quarter contraction expected to be unwound in Q3



Asia Pacific Week Ahead

China data, Japan GDP, RBNZ and BSP, business outlook surveys

By Bernard Aw
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The release of official economic data in China will form the central highlight of the week ahead in Asia, providing further insights into Chinese economic performance amid mixed signals indicated by PMI surveys. The week will also bring GDP updates from Japan, Malaysia and Hong Kong, while New Zealand and the Philippines will decide on monetary policy. Eyes will also be on the BRICs summit for any fresh developments on US-China trade deal following the cancellation of the APEC summit. Finally, the release of IHS Markit tri-annual business outlook surveys will offer a glimpse into business expectations for the year ahead across 11 major economies, including China, Japan and India.

China data

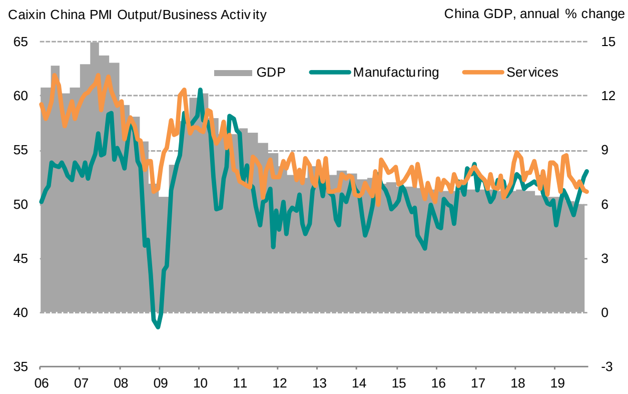
China watchers will eagerly anticipate the clutch of economic data released next week after the latest government-sponsored NBS manufacturing PMI survey and Caixin data (compiled by IHS Markit) indicated a divergence that confounded analysts. Updates to industrial production, fixed asset investment and credit growth for October will therefore provide additional insights into economic activity across China that also help to gauge the extent to which stimulus measures are successful in supporting growth.

Japan and Malaysia GDP

According to IHS Markit estimates, Japan's economic growth is expected to accelerate to an annual rate of 1.5% during the third quarter when GDP data are updated, up from 0.8% in the previous quarter, lifted by front-loaded demand ahead of the October's sales tax hike. As such, this boost to growth is expected to be temporary, and the latest PMI data are already showing the first decline in business activity in three years during October.

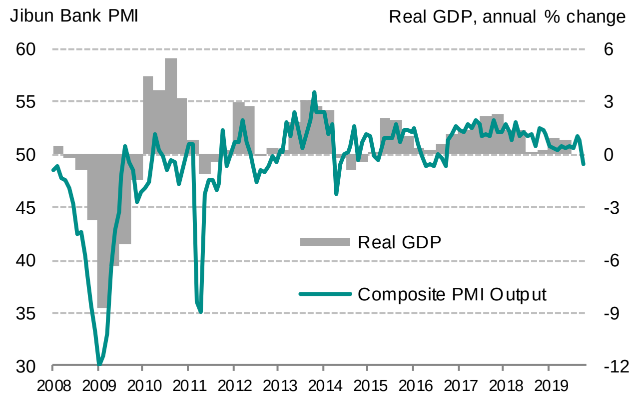
Malaysia's third quarter GDP is meanwhile forecast to have decelerated to 4.3%, down from 4.9% in the second quarter. However, welcome signs of Malaysian manufacturing turning a corner appeared in October with the latest PMI data showing production buoyed by improved domestic demand in particular, hinting that the pace of economic growth could accelerate in the fourth quarter.

Caixin China PMI: manufacturing and services



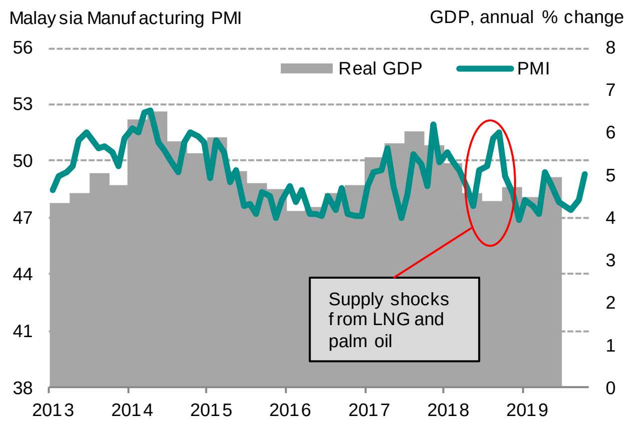
Sources: IHS Markit, Caixin, NBS

Japan PMI suggest payback at start of Q4 following front-loaded demand ahead of tax hike



Sources: IHS Markit, Jibun Bank, Cabinet Office

Malaysia PMI and economic growth



Sources: IHS Markit, DoS

Europe Special Focus

Gains in Spain clearly on the wane

By Ken Wattret
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Spain's economic renaissance has been one of the success stories of the post-crisis expansion in the eurozone, with improvements in competitiveness and domestic rebalancing contributing to sustained growth outperformance.

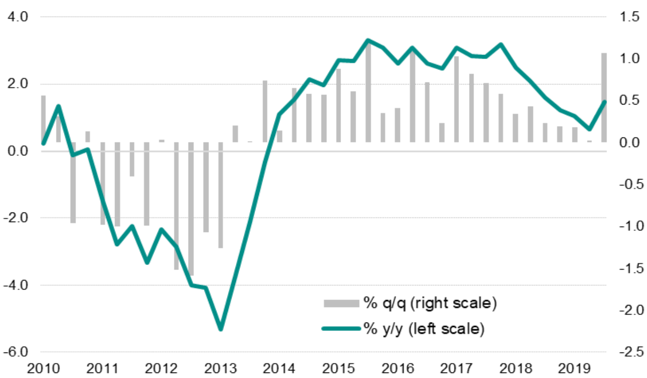
However, the GDP growth rate in Spain has decelerated markedly in recent quarters and we expect the slowdown to persist. Weakness in exports is a key drag but there are domestic demand headwinds too, including lower employment growth and a downturn in construction.

Spanish growth well down on cycle highs

Based on Q3's initial estimates, the y/y growth rate in Spanish GDP (2.0%) outpaced the growth rate for the eurozone as a whole (1.1%) for the 20th time in the past 21 quarters. However, the growth differential in Spain's favour has more than halved relative to its two percentage point peak back in the second half of 2015. Moreover, on a q/q basis, Spain's average growth rate of 0.4% in Q2 and Q3 was the weakest for over five years and roughly a third of its cycle highs in 2015.

Q3's growth rate would have been lower still were it not for an unsustainably strong 1.0% q/q surge in private consumption (Chart 1).

Chart 1: Unsustainable surge in Spanish private consumption in Q3



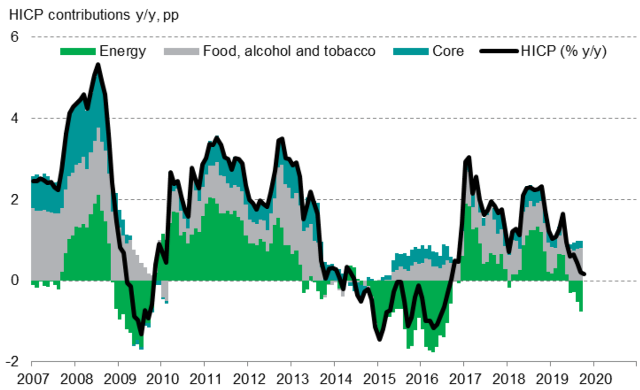
Source: IHS Markit, Eurostat

With private consumption accounting for almost 60% of Spanish GDP, this contributed 0.6 percentage points to the overall q/q GDP growth rate in Q3, the largest contribution for ten quarters.

Consumer boost from low inflation to fade

The surge in consumer spending growth dovetailed with a sharp rise in household real disposable income, driven in large part by a collapse in inflation which has been primarily driven by energy developments (Chart 2). The headline rate of harmonised consumer price inflation in Spain has plummeted over the past year, dropping to just 0.2% in October versus a cycle peak of 2.3% a year previously. While inflation will remain low in the coming months, the downward pressure from energy is pretty much played out already, while base effects will lean upwards later this year and early next.

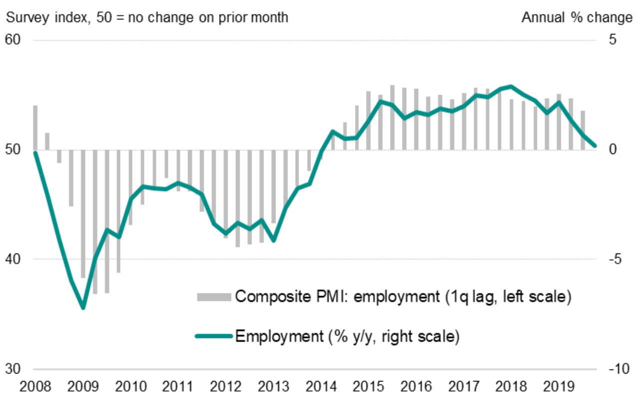
Chart 2: Slower Spanish inflation led by energy



Source: IHS Markit, Eurostat

While Spanish employment growth in Q3 was a still impressive 1.8% y/y, it too has lost significant momentum relative to its 3% peak in 2015. A range of leading indicators, including IHS Markit's PMI data, point to a further, potentially sharp, deceleration (see Chart 3).

Chart 3: PMI points to lower growth rates in Spanish employment



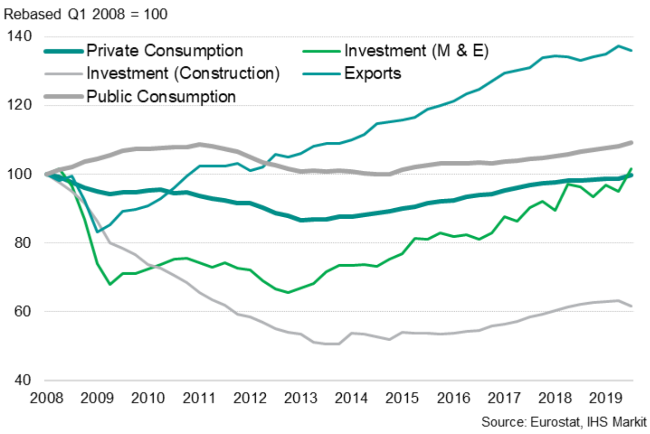
Source: IHS Markit, Eurostat

Public consumption has also been a key contributor to domestic demand growth in Spain and it remained robust in Q3, rising by 0.9% q/q and contributing 0.2 percentage points to the q/q GDP growth rate. Given the challenging political backdrop, public consumption is likely to continue to support growth, though other areas of expenditure will be much more influential (Chart 4).

Export outperformance post-crisis

The performance of exports has been the standout feature of the post-crisis period, as Chart 4 highlights. Spanish exports as of Q3 this year were 36% higher than their Q1 2008 level, prior to the two crises which engulfed the domestic economy. The cumulative rise in Spanish exports has comfortably outstripped those in France (27%) and Italy (14%) over the same period and has even surpassed the increase in Germany (33%, up to Q2 this year).

Chart 4: Spanish GDP expenditure components rebased

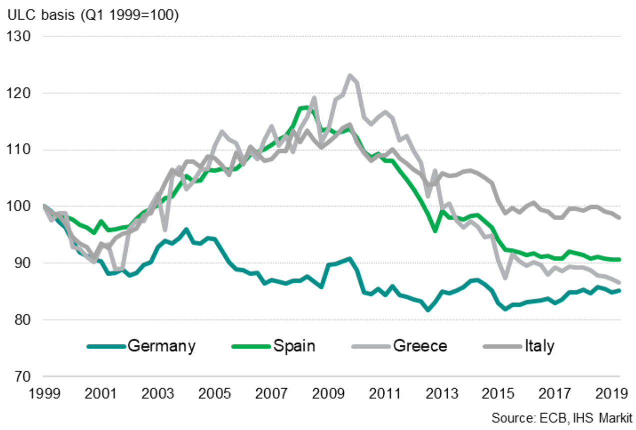


But export composition and competitiveness trends unhelpful

Momentum has fallen away in recent quarters, however. Q3 showed only the second q/q contraction in Spanish exports in more than six years, with the y/y growth rate of 2.3% roughly a third of its cycle high. The composition of Spain's exports by type is an important issue, as intermediate products dominate, accounting for around 56% of total exports. This is a concern in an environment of shrinking global trade.

Improved competitiveness was also a key driver of Spain's export outperformance. This is shown in the evolution of its harmonised competitiveness index (HCI) from 2008 onwards (Chart 5). The HCIs are calculated by the ECB and reflect movements in relative unit labour costs weighted across key trading partners. As with trade-weighted exchange rates, a decline indicates an improvement in competitiveness. Prior competitiveness losses in Spain from 2000 to 2007 were more than unwound from 2008 onwards during the severe post-crisis adjustment, with the HCI ending up around 10% below its 1999 level by 2016. In the period since then, however, Spain's HCI has pretty much flatlined, constraining its ability to continue to increase export market share.

Chart 5: Spain's harmonised competitiveness index has flatlined



Construction hits the wall

Another striking feature of Chart 4 above is the divergence between the two key investment sub-sectors: machinery and equipment, and construction. The former has been on a markedly improved trajectory since 2013 and recently surpassed its pre-crisis level. The latter, in contrast, is still around 40% below its pre-crisis level.

Investment overall rose by a decent 1.3% q/q in Q3, though again the y/y rate of increase, at 2.0%, was well down on its 8% cycle high. A surge in machinery and equipment investment drove the increase in Q3 and this strength is unlikely to be sustained given the backdrop of high uncertainty over demand prospects and continued weakness in the manufacturing sector. The manufacturing PMI in Spain has been below 50 in each of the five months to October and has fallen to its lowest level in over six years.

Construction, meanwhile, has been on a weakening trend recently and contracted in Q3 on a q/q and y/y basis, with residential and especially non-residential construction declining versus the prior quarter. As we have highlighted previously, the signs for the Spanish construction sector cross various indicators do not look positive. See Eurozone investment divergence ahead.

Growth rate heading sub-2%

Annual GDP growth in Spain averaged 3% between 2015 and 2018. 2019's growth rate is pretty much baked in the cake already with data to Q3 available and our forecast remains for a slowdown to 2.0%. With the factors leaning down on external and domestic demand set to persist, sub-2% growth rates are likely to follow in both 2020 and 2021.

Asia Pacific Special Focus

RCEP Deal Creates Giant New FTA in the Asia-Pacific

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A deal has been reached among 15 Asia-Pacific nations on 4th November 2019 to conclude the Regional Comprehensive Economic Partnership agreement after years of negotiations since the initiative was first launched in 2013. The RCEP deal, which is expected to be signed by the 15 member governments in February 2020, provides a further boost to trade liberalization in the Asia-Pacific region.

The RCEP deal is a further positive boost for regional trade liberalization at a time when the export sectors of many Asia-Pacific nations have been hit by trade disputes between some of the world's largest economies, notably the US-China trade war.

RCEP creates platform for further regional trade liberalization

The Regional Comprehensive Economic Partnership (RCEP) is a positive regional trade liberalization initiative that will help to boost trade and investment flows among the 15 nations that have agreed to the trade deal. The RCEP members comprise the 10 nations of ASEAN, plus China, Japan, South Korea, Australia and New Zealand. Asia-Pacific economies have suffered considerable negative contagion effects from the US-China trade war since 2018, as the wider Asian manufacturing supply chain has been hit by the impact of high tariff barriers on US-China trade flows. This has helped to galvanize political momentum for concluding RCEP, to help improve regional trade and investment flows.

Negotiations have been concluded among the 15 nations for all 20 chapters of the RCEP talks, with the text of the RCEP agreement now due to be subjected to detailed fine-tuning of the text.

When eventually ratified and implemented by the member nations, the RCEP agreement will create a new free trade area in the Asia-Pacific region that will provide a strong platform and building block for further regional trade liberalization initiatives. The scope of RCEP includes reducing tariffs on trade in goods, as well as creating higher-quality rules for trade in services and reducing non-tariff barriers to trade among member nations.

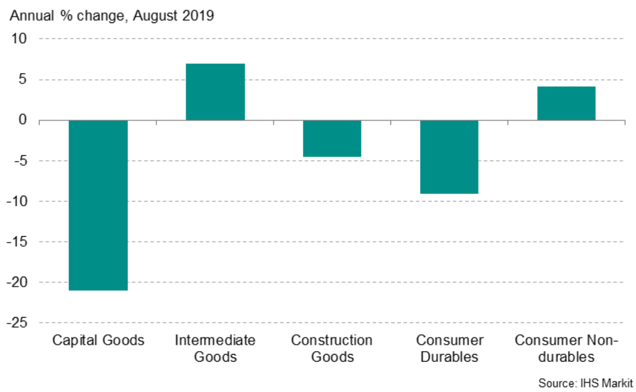
However, the decision by India, which was one of the 16 countries taking part in the RCEP negotiations, not to join the RCEP deal in the first wave will reduce the scale of the new free trade area significantly. India is already a USD 3 trillion economy that is equal in size to the 10 ASEAN member states combined.

India stands aside to allow RCEP to be implemented

India's decision not to join the RCEP deal reflects considerable domestic concerns amongst political parties, as well as industry groups in India, about the potential economic shock to Indian industries from dismantling tariff barriers for trade with the other RCEP member nations. In particular, India had been concerned about the potential impact of significantly reducing tariff barriers for trade with China, as India feared that many domestic industry sectors would not be able to compete effectively with Chinese manufactures in a wide range of industry sectors.

India's manufacturing sector has been facing considerable challenges in 2019, with the Indian auto industry facing a severe crisis due to slumping vehicle sales. Consequently, Indian industry has heightened concerns about the potential negative impact of an RCEP deal on their own domestic market shares.

India's industrial production

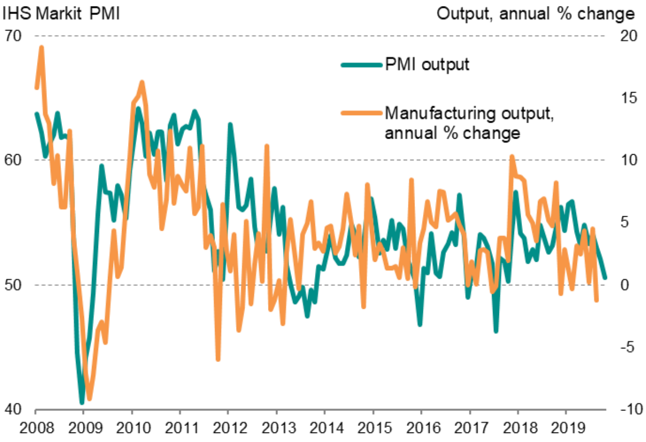


In the April to June 2019 quarter, Indian GDP growth slowed to 5.0% year-on-year, the weakest pace of growth since 2013. The pace of manufacturing output growth has also stalled. In August 2019, manufacturing production contracted by 1.2% year-on-year, with 15 out of 23 sectors of manufacturing showing a contraction in output compared to a year ago. A key concern is that output of capital goods declined by

21% year-on-year, signalling continuing weak capital expenditure.

For the April to August 2019 period, manufacturing output was up just 2.1% year-on-year, less than half the pace of expansion recorded in the same period of 2018, when manufacturing output rose by 5.5% year-on-year. This has created a very difficult political and economic backdrop for the Indian government to ratify the RCEP legislation through the Indian parliament. Risks had increased of a significant backlash within India against RCEP.

IHS Markit India Manufacturing PMI



Source: IHS Markit

Unlike ASEAN, India does not have a bilateral free trade agreement in place with China. The Indian government decided that the overall economic and political costs of dismantling bilateral trade barriers with China would far outweigh the economic benefits, which were assessed to be relatively modest in size relative to the economic costs

India has had a large and chronic trade deficit with China for many years. India's bilateral trade deficit with China was USD 58 billion in 2018, notably due to a large imbalance in trade in manufactures. Consequently, the Indian government feared that dismantling existing tariff barriers for Chinese imports would further erode India's domestic manufacturing market share at a time when the Indian government is trying to accelerate the development of India's manufacturing sector through the "Make in India 2025" policy, which is championed by Prime Minister Modi.

India also runs a trade deficit with Australia, but the size is relatively moderate compared with India's trade deficit with China. As Australia is a strategic source of supply for Indian imports of key commodities such as LNG and metallurgical coal, the trade relationship with Australia provides critical raw materials for Indian industry and does not compete significantly with India's manufacturing industry.

Although India decided that it is not able to join the RCEP agreement in the first wave, there may be the possibility for India to negotiate a later entry date into RCEP to allow a longer transition period for Indian industry to adapt to the new trade rules. Many other RCEP member nations are keen to have India as a member of RCEP, particularly since India, which is now the world's fifth largest economy, would substantially increase the long-term trade and investment benefits of the RCEP agreement.

Having stepped aside from RCEP, India is likely to refocus on concluding a bilateral trade deal with the US as a high priority. The US remains India’s most important export market. In the 2018 calendar year, the US accounted for around USD 83 billion of Indian exports of goods and services. A key concern for India has been the Trump Administration’s decision in March 2019 to end India’s status as a beneficiary of the US Generalised System of Preferences (GSP). The US decision was made based on its assessment that India had not provided equitable and reasonable access for US products into the Indian market. Efforts have been underway to find a compromise bilateral trade deal, although US-India trade negotiations have faced significant hurdles due to the complex range of outstanding issues to be resolved.

Outlook for RCEP

The RCEP deal is a further step by APAC governments to liberalize regional trade flows, following the implementation of both the Japan-EU Economic Partnership Agreement (EPA) and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) deals in quick succession earlier in 2019.

Once ratified and implemented by member nations, the RCEP free trade agreement will become a building block for further advancing trade liberalization in the Asia-Pacific, both through expanding the scope of the existing agreement and through the accession of other nations to the agreement.