Economic Preview: Week of 27 July 2020

Publication date: 24 July 2020

Week Ahead Economic Preview

Global overview

- **Second quarter GDP releases include updates for the US and Eurozone**
- **US policy in spotlight as FOMC meets**
- **Key Asia trade and output releases accompanied by GDP for Hong Kong, Taiwan and Japan, plus China PMI**

Insights into the depth of COVID-19 related economic downturns will be provided by second quarter GDP estimates for the US, Eurozone, Hong Kong and Taiwan, while the impact on companies will be revealed via earnings updates from no fewer than 833 firms. Policy action comes from the FOMC.

GDP data revealing economic recessions on scales not seen in post-war years are set to dominate the headlines. In the US, we are expecting an annualised GDP decline of around 35% for the second quarter (near double-digits in quarterly terms). While this should be followed by a rate of expansion of approximately 18% in the third quarter, renewed lockdowns pose a downside risk. Gauging the shape of the recovery will therefore dominate the FOMC meeting, from which markets will meanwhile be looking for more forward guidance about what it would take to keep the interest rates close to zero for an extended period (expected to be several years), and the extent to which inflation may be allowed to overshoot its target, or even whether yields on government securities might be targeted (page 3).

In Europe, second quarter GDP releases for the Eurozone will include national updates for Germany, France, Italy and Spain, all of which are also set to show eye-watering quarterly declines of roughly double-digit magnitude as COVID-19 lockdowns hit economic activity. Eurozone inflation numbers are also released while in the UK the main updates are for mortgage lending and consumer credit (page 4).

In Asia Pacific, Hong Kong SAR and Taiwan GDP for the second quarter are issued alongside a new estimate of first quarter growth in Japan. More timely monthly data for industrial production and trade are also updated for nations including South Korea, Thailand, Vietnam as well as Japan, which will help gauge recovery momentum as we head into the third quarter. The government-sponsored China PMI is also released and will give important clues as to the recovery path at the start of the third quarter (page 5).

Special reports

Asia Pacific: A look at how the Indian Economy looks set for a post-COVID rebound, especially as Foreign Direct Investment remains buoyant (page 6).

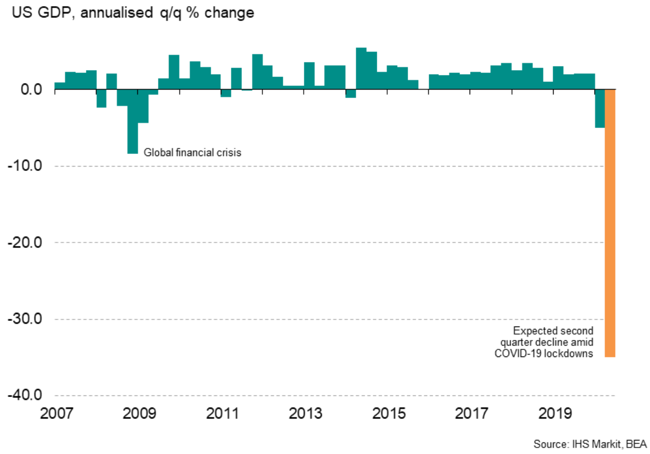
Upcoming PMI releases

3rd August: Final Global Manufacturing PMIs

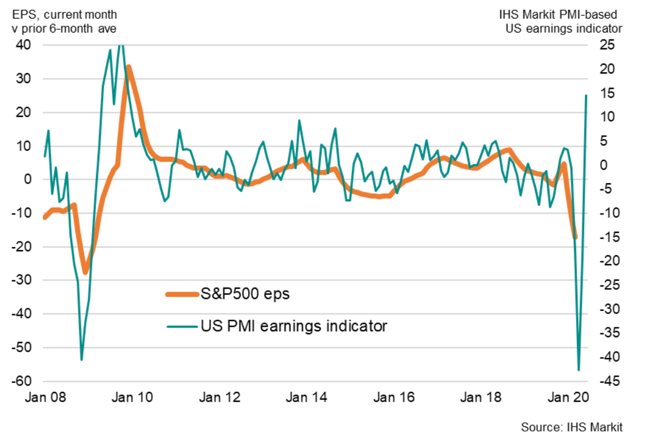
5th August: Final Global Services PMIs

6th August: Detailed global sector PMIs

IHS Markit expects the US economy to have contracted at an annualised rate of around 35% in the second quarter. Actual GDP data are updated on Thursday



The US earnings season is in full flow with COVID-19 lockdowns expected to have played havoc with second quarter performances according to survey data



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IHS Markit®

Key diary events (UTC)

Monday 27 July

China industrial profits (Jun)
Germany Ifo surveys (Jul)
Hong Kong SAR trade (Jun)
US durable goods orders (Jun)
US Dallas Fed manufacturing index (Jul)

Tuesday 28 July

Malaysia trade (Jun)
Spain unemployment rate (Q2)
US Case-Shiller home price (May)
US consumer confidence (Jul)
US Richmond Fed manufacturing index (Jul)
South Korea consumer confidence (Jul)

Wednesday 29 July

Australia inflation (Q2)
Taiwan consumer confidence (Jul)
Vietnam trade balance, industrial output, inflation (Jul)
Singapore jobless rate (Prelim, Q2)
Thailand industrial output (Jun)
France consumer confidence (Jul)
Hong Kong SAR GDP (Adv, Q2)
UK mortgage lending and approvals, consumer credit (Jun)
Brazil unemployment rate (Jun)
US goods trade balance, wholesale inventories, pending home sales (Jun)
FOMC meeting
South Korea business confidence (Jul)
Japan retail sales (Jun) 23:50 UTC
ECB non-monetary policy meeting

Thursday 30 July

Australia building permits (Jun)
Germany GDP (Flash, Q2), jobless rate (Jul)
UK nationwide housing prices (Jul)
Germany and Spain inflation (Prelim, Jul)
Euro area and Italy jobless rate (Jun)
Euro area economic sentiment, consumer confidence (Jul)
US GDP (Adv, Q2), jobless claims (25-Jul)
South Korea industrial output (Jun) 23:00 UTC
Japan jobless rate, industrial output (Jun) 23:50 UTC

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Friday 31 July

China NBS PMI (Jul)
Japan consumer confidence (Jul), housing starts (Jun)
Euro area, France, Italy and Spain GDP (Prelim, Q2)
Germany and Italy retail sales (Jun)
Euro area, France and Italy inflation (Prelim, Jul)
Taiwan GDP (Adv, Q2)
US personal income and spending, PCE price index (Jun)
US Chicago PMI (Jul), Michigan surveys (Final, Jul)

Saturday-Sunday 1-2 August

1/8: South Korea trade (Jul)
2/8: CBA Australia manufacturing PMI (Final, Jul)
2/8: Japan GDP (Final, Q1) 23:50 UTC

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United States Week Ahead

Second quarter GDP estimate, PCE prices data and FOMC meeting

By Siân Jones

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The advanced estimate of GDP for the second quarter leads the key upcoming data releases for the US, while the FOMC meets once again to decide on the current policy support offered during the COVID-19 crisis. An update to PCE and prices is also expected, as well as data on durable goods orders, home prices, consumer confidence, regional manufacturing surveys, home sales and international trade.

Advanced Q2 GDP estimate

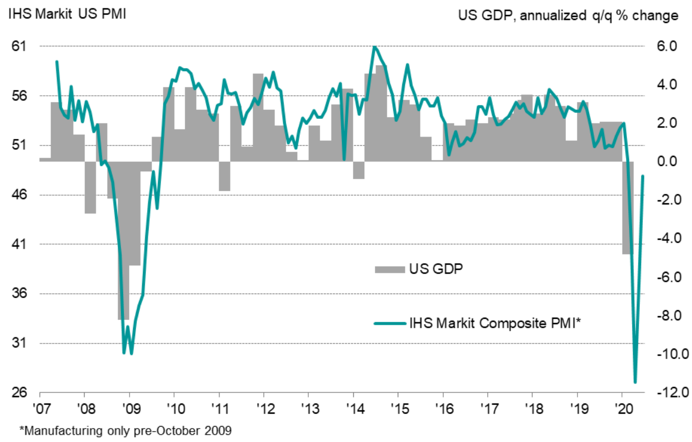
Although the outbreak of COVID-19 had already dented the performance of the US economy in the first quarter, the severity of lockdowns in April and May are expected to have dragged far more substantially on the economy in the second quarter, with our latest forecast pointing to an annualised fall of 35.5% in GDP. That said, moves towards a recovery have appeared sooner than many predicted, with retail sales and industrial production bouncing as lockdowns were lifted. The beginning of the third quarter is looking less upbeat, however, with the lockdown easing also delivering an unwelcome daily rise in new virus cases, surpassing previous records, and consumer sentiment wavering amid the return of lockdown measures.

FOMC meeting and PCE Prices

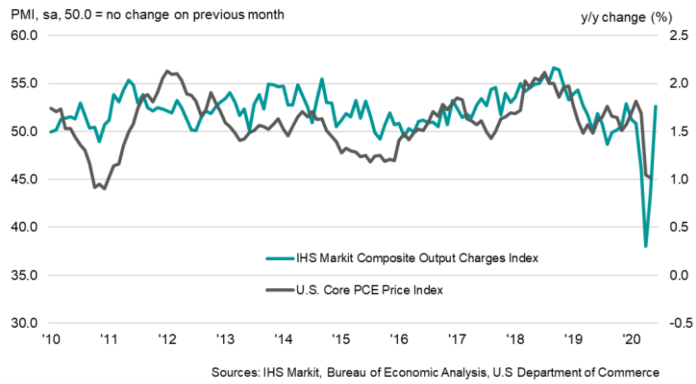
Amid ongoing economic uncertainty stemming from the virus outbreak, and a lack of job security, policymakers in the FOMC are expected to keep the federal funds rate at between 0-0.25% in their announcement on Wednesday. With a greater consensus on the need for forward guidance, it is unlikely there will be any shock movements or announcements, policymakers will be eager to assess the economic impact of rising COVID-19 case numbers. Markets will therefore be looking for more detail on forward guidance, and what new targets the FOMC might be assessing to help guide stimulus needs, such as government bond yields, amid times of volatile labour markets.

Meanwhile, core inflation rates have remained relatively subdued and well below the target rate in June. A pick up in retail sales volumes during June may have added some upward pressure to prices, but the rate of inflation is expected to remain below the Fed's target of 2% for some time.

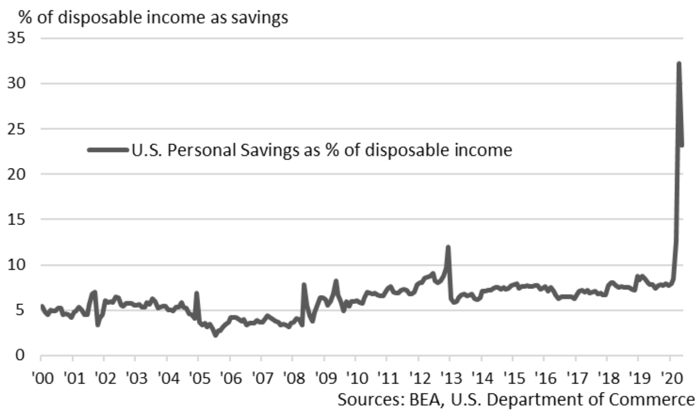
June data signalled a move towards recovery in the US private sector



Selling prices begin to pick up in June as demand improves, according to latest PMI data



Personal savings jump in April amid COVID-19 crisis and lockdown measures



Europe Week Ahead

Eurozone GDP, unemployment and inflation figures

By Paul Smith

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A big week ahead for the eurozone, with data for a hattrick of key macroeconomic health barometers – economic growth, unemployment and inflation – all slated for release. Consumer confidence and retail sales figures for Germany and Italy will add additional colour to the state of the recovery, whilst in the UK there are several releases to gauge the state of the nation's closely watched housing market.

Eurozone GDP to fall sharply…

Next Friday should see the confirmation of the largest ever quarterly decline in euro area gross domestic product (GDP). Whilst a simple nowcasting model using a logarithm of the PMI and industrial production points to a decline of around -8% over the second quarter – and meaning a drop in economic output of nearly -12% in the first half of 2020 – considerable uncertainty abounds and double digit declines across the region for Q2 alone are more than possible.

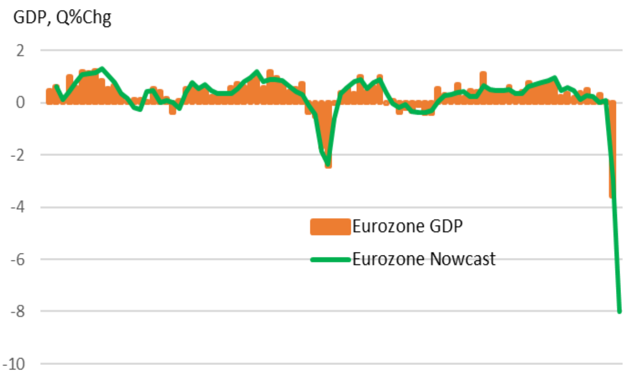
The GDP outcome for Q2 – and the recovery ahead – will be determined in part by a rebound in household consumption. In this regard, euro area retail sales have shown a positive trend, rising in May by 18% on the month and leaving volumes just 7% down on February's peak. Whilst full regional figures will be released later in August, June's figures for Germany and Italy will be keenly watched for further evidence of consumers getting back to previous activity levels.

…and joblessness set to rise

A major concern is that social distancing measures, subdued consumer sentiment and precautionary household savings are likely to weigh on the recovery, especially for non-essential services. Additionally, the spectre of mass redundancies in those sectors leading to a sharp rise in overall unemployment continues to dominate the outlook. Whilst furlough schemes have limited the jobs damage so far, a further increase in the region's unemployment rate seems inevitable.

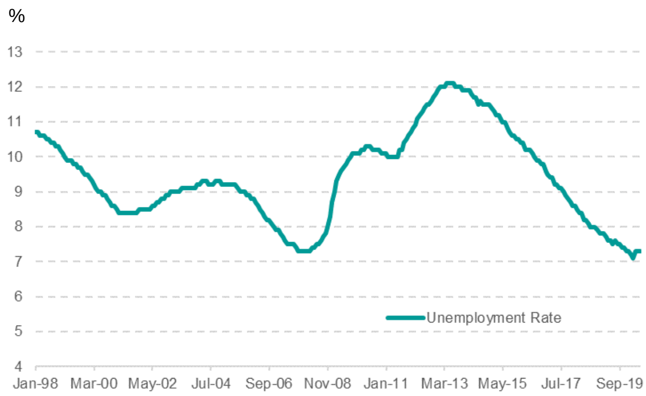
Finally, with weak demand and ongoing economic slack apparent, consumer price inflation – both at the headline and core levels – remains subdued. Expect to see more of the same with July's preliminary figures.

Eurozone GDP to show largest ever single quarterly drop of economic output in second quarter of 2020



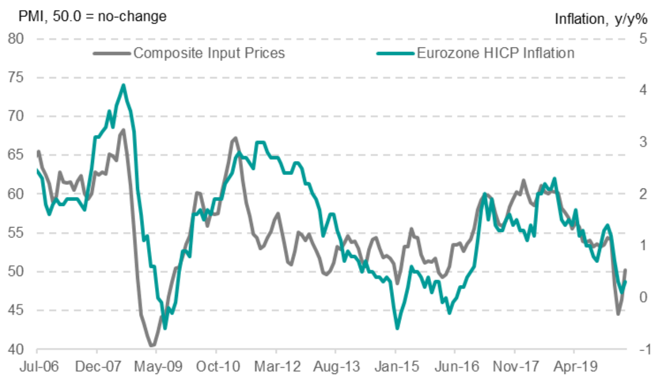
Sources: IHS Markit, Datastream

Reduced working hours and the extensive use of furlough schemes have so far limited the rise in the eurozone's unemployment rate



Source: Eurostat

Inflation in the eurozone remains subdued and well below the European Central Bank's target of "below but close to 2%"



Source: IHS Markit, Eurostat

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Asia Pacific Week Ahead

China PMI, Hong Kong and Taiwan GDP, Asia trade updates

By Bernard Aw
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With the GDP reporting season underway, next week will see Taiwan and Hong Kong SAR releasing second quarter GDP, but the government-sponsored China PMI will also be eagerly awaited for further signs of recovery. Trade and industrial production data in a number of Asian economies will also draw scrutiny, in particular South Korea and Vietnam, for which the trade updates are for July. Sentiment surveys in South Korea, Japan and Taiwan, coming on the heels of IHS Markit Business Outlook Survey, will provide further clues as to the potential recovery paths ahead.

Other key Asian data highlights are Japan's update on first quarter GDP, jobs, industrial output, retail sales and housing, Australia's building permits and inflation figures, as well as the final update for the July Australia PMI.

China PMI

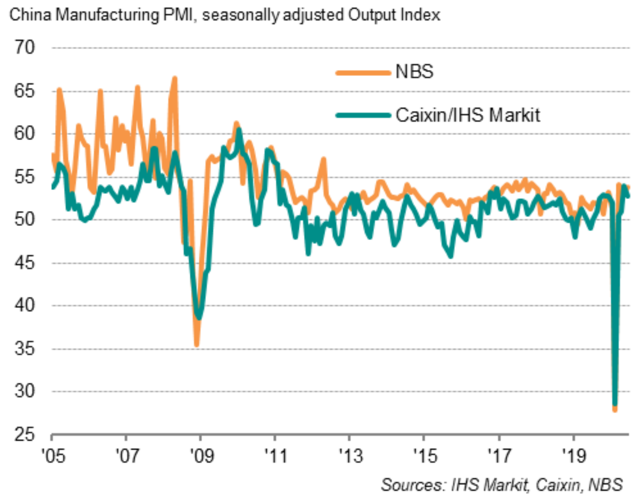
With China's economy returning to growth in the second quarter, adding to expectations that the recession may have been shockingly deep but also welcomingly brief, analysts will be keen to assess the July update to NBS China PMI data for signs that the recovery has extended into the third quarter. While business sentiment and order book growth have improved in recent months, the June survey also brought signs of a challenging recovery, including an ongoing decline in employment and indications that capacity pressure has remained subdued.

Hong Kong and Taiwan GDP

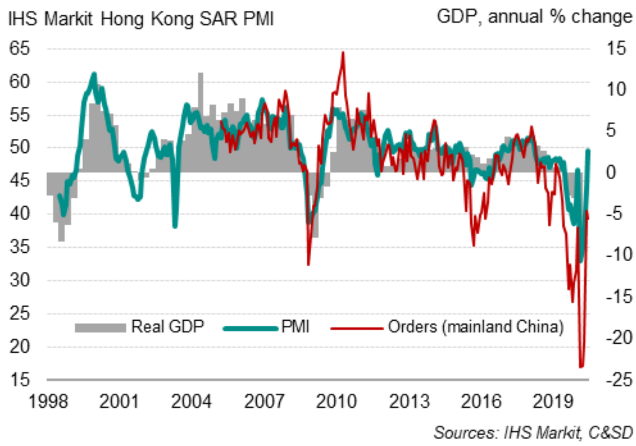
The second quarter GDP update for Hong Kong SAR is expected to show a rapidly deepening recession, with the economy likely shrinking by 11.5% year-on-year amid the full impact of global city lockdowns and travel restrictions.

The Taiwanese economy is meanwhile projected to have contracted at an annual rate of 3% during the second quarter, according to IHS Markit's estimate. The average manufacturing PMI reading for the three months ending June was the lowest since the height of the global financial crisis in fourth quarter of 2008, with Taiwan's factory sector remained severely affected by a global trade downturn.

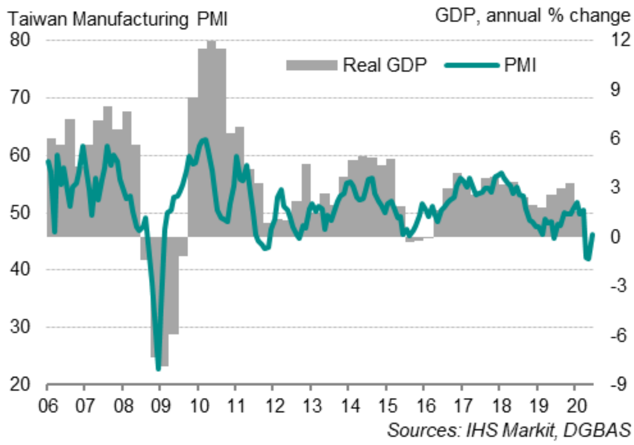
July updates to China PMI surveys will provide first insights into economic trends at the start of the third quarter



Hong Kong SAR PMI and economic growth



Taiwan PMI signals falling economic activity



APAC
Special Focus

Indian Economy set for post-COVID rebound as Foreign Direct Investment remains buoyant

By Rajiv Biswas
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The impact of the COVID-19 pandemic has plunged the Indian economy into its first recession since 1979, as the lockdown measures to contain the pandemic resulted in the collapse of industrial production and consumer expenditure in the second quarter of 2020.

However, as lockdown measures have been eased, the Indian economy has started to show signs of an economic rebound, as reflected in the latest IHS Markit Purchasing Managers' Index (PMI) surveys for Indian manufacturing and services in June. The decision by Google in mid-July to invest USD 10 billion in digital transformation projects in India has also been an important boost to investor confidence in India's medium-term economic outlook. However near-term challenges remain, including the continuing escalation in new COVID-19 cases in India and concerns about the impact of rising non-performing loans in the Indian banking sector.

Lockdown measures trigger economic slump

In India, a national lockdown began on 25th March and has continued in various phases, albeit with progressive easing of restrictions since late April. Despite the continued escalation in the total number of daily new COVID-19 cases, further gradual easing of restrictions has continued during the "Unlock 1.0" phase that started in June and transitioned into "Unlock 2.0" in July. This protracted lockdown has resulted in the severe disruption of industrial production and consumer spending, with GDP growth forecast to contract sharply during the second quarter 2020, pushing Indian GDP growth for the 2020-21 financial year into a deep recession, with GDP contracting by 6.3% in 2020-21, albeit rebounding to strong positive growth of 6.7% in 2021-22.

As a result of the lockdown measures, Indian industrial production was heavily disrupted during late March and during April. As lockdown restrictions on industrial production were eased on 22nd April and again in early May, the pace of contraction in industrial production moderated to 34.7% year on year (y/y) in May compared with a 57.6% y/y decline in April. Manufacturing output, which accounts for 77.6% of the total industrial production index, declined by 39.3% y/y in May, compared with a contraction of 67.1% in April.

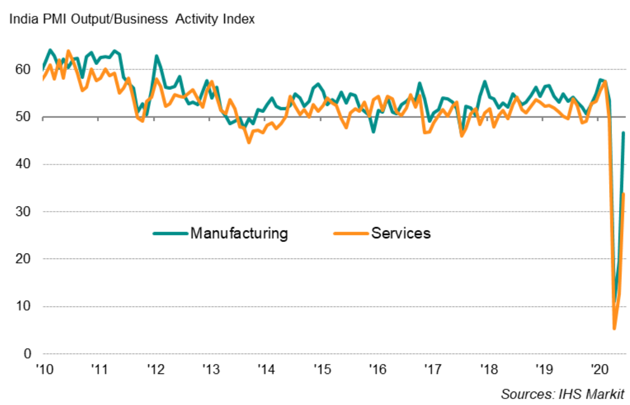
The services sector has also been badly hit by the impact of lockdown measures on retail trade and the collapse of domestic travel and tourism.

IHS Markit PMI surveys signal economic rebound

IHS Markit Purchasing Managers' Index (PMI) surveys for India showed that economic momentum improved in June, reflecting the easing of COVID-19 related restrictions during May and June. The Composite PMI Output Index, covering both the manufacturing and services sectors, rose from 14.8 in May to 37.8 in June. While the latest figure remained well below the neutral level of 50, still signalling a substantial decline in output, it showed a significant improvement compared with the extremely weak readings recorded in April and May. Nevertheless, overall demand conditions remained contractionary in June, accompanied by a broad-based decline in employment.

The IHS Markit India Manufacturing PMI data rebounded to 47.2 in June from 30.8 in May, indicating that the sector neared stabilisation in June. The contraction in output and new orders both moderated in June. However, the continued escalation in new coronavirus cases and the continuing lockdown extensions have continued to constrain the recovery.

IHS Markit India Manufacturing and Services PMI



In contrast to the manufacturing sector, services activity still contracted at a substantial pace in June, albeit not as severely as in April and May. The IHS

Markit India PMI Services Business Activity Index recorded 33.7 in June. This was up sharply from 12.6 in May but remained below the neutral 50.0 mark for a fourth successive month, signalling another decline in service sector output.

Fiscal and monetary policy response measures

The Reserve Bank of India (RBI) has taken significant action to mitigate the impact of the pandemic on the Indian economy. The RBI cut its policy repo rate by 40 basis points from 4.4% to 4.0% on 22nd May, owing to the severe macroeconomic impact of the pandemic. This followed a previous repo rate cut of 75bps in March 2020, proving a cumulative total easing of 115bps in the policy repo rate so far in 2020. The latest rate cut decision was made at an off-cycle meeting of the Monetary Policy Committee (MPC), which was held as a result of recent macroeconomic data showing the extend of economic damage that has been caused by the pandemic and protracted period of lockdown.

The RBI also announced that it would extend previously announced measures to ease financial stress by another three months from 1st June 2020 till 31st August 2020 taking the total period of applicability of the measures to six months starting from 1st March 2020. The measures taken to ease financial stress include:

(a) the granting of a three months moratorium on term loan instalments,

(b) deferment of interest for three months on working capital facilities;

(c) easing of working capital financing requirements by reducing margins or reassessment of working capital cycle;

(d) exemption from being classified as 'defaulter' in supervisory reporting and reporting to credit information companies;

(e) extension of resolution timelines for stressed assets; and

(f) asset classification standstill by excluding the moratorium period of three months, etc. by lending institutions.

On the fiscal policy front, the Indian government has announced large-scale stimulus measures to mitigate the impact of the pandemic on low-income households as well as measures to assist the corporate sector through the severe economic stress during the pandemic. Overall, announced measures amount to around 10% of total GDP, although actual additional fiscal spending measures amount to a relatively smaller share of the total announced measures. direct spending and foregone or deferred revenue is estimated at around 2% of GDP. Other measures such as credit provision for various sectors such as small-to-medium enterprises and other corporates, as well as to the farm sector amount to a further 5% of GDP.

Foreign Direct Investment surge signals investor confidence in India

Over the past five years, total foreign direct investment (FDI) inflows into India have doubled, rising from USD 24 billion in 2013-14 financial year to USD 50 billion in the 2019-20 financial year. Although the moderating pace of economic growth during 2019-20 and the economic slump in the first half of 2020 due to the COVID-19 pandemic triggered concerns about a downturn in FDI, there has been a strong surge of new foreign investment inflows announced during 2020 year-to-date.

A major boost to investor confidence in the Indian medium-term economic outlook has come from new foreign direct investment into India by US technology companies. In mid-July, Google announced a USD 10 billion investment into Google India's Digitization Fund, to fund a wide range of investments in projects related to India's digitization. Out of that total, Google announced that USD 4.5 billion will be invested in Reliance Jio Platforms, to develop digitization infrastructure and new mobile phones for the Indian consumer market. Facebook has also committed to invest USD 5.7 billion in Reliance Jio Platforms in April 2020. Amazon has also announced a USD 1 billion investment into India in early 2020. Consequently, total FDI into India by US technology firms in the first seven months of 2020 has already reached around USD 17 billion.

In mid-July, Walmart also announced that it is leading a USD 1.2 billion fresh capital injection by a group of investors into Flipkart, an Indian ecommerce company in which Walmart had previously acquired a majority stake. Taiwan's Foxconn has also announced plans for an additional USD 1 billion investment in India to expand its factory facilities to increase production of mobile phones.

India has also attracted large FDI inflows from multinationals for establishing and expanding R&D centres of excellence. Due to its large pool of highly skilled graduates in information technology, engineering and science, India has become a leading global R&D hub for multinationals, with around 150 large multinationals having already established significant R&D hubs in India. Technology firms are among the most important investors in India for R&D, with global tech giants such as Google, Microsoft, Apple, IBM, Cisco and SAP having large R&D centres in India. Samsung R&D Institute India in Bangalore is the largest R&D centre for the Samsung Group outside of South Korea. In the auto sector, Hyundai Motors has two R&D centres in India, while Mercedes Benz also has a major R&D hub in India. In the aerospace sector, Boeing, Airbus and General Electric also have significant R&D and IT hubs located in India.

Supply chain diversification

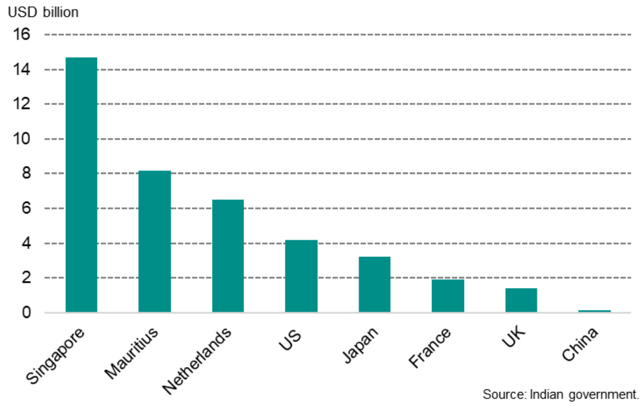
An extended process of supply chain diversification has been underway in the Asia-Pacific region since 2011, driven by a series of political and economic factors as well as natural disasters that have forced firms to reshape their supply chains. Japan's great Tohoku earthquake in 2011 followed by the extensive Thai floods the same year caused severe supply chain disruptions for many manufacturing firms. The political tensions between China and Japan over disputed territorial claims also created a wave of economic disruption to Japanese business activity in China during 2012. These supply chain disruptions had already triggered a process of reshaping of supply chains, with Southeast Asia and South Asian countries having benefited from some shift in new FDI flows. India has been an important beneficiary of new FDI inflows over the past decade, into a wide range of industries, including manufacturing, services, infrastructure and logistics.

The massive disruptions to industrial production worldwide caused by the COVID-19 pandemic have triggered another new wave of reconfiguration of global supply chains to reduce vulnerabilities. In April 2020, the Japanese government announced a USD 2.3 billion subsidy program to assist Japanese companies to diversify their supply chains away from China following the COVID-19 supply chain disruptions.

In the first round of Japan's project subsidy announcements made in July, the 87 Japanese projects moving out of China were all either reshoring to Japan or relocating to Southeast Asia. However, this trend of Japanese firms diversifying their supply chains away from China will also eventually support increased Japanese foreign direct investment into India. Japanese firms have already been steadily investing in new manufacturing facilities as well as other investments such as infrastructure projects in India. This reflects the large size of India's domestic consumer market and long-term revenue growth opportunities.

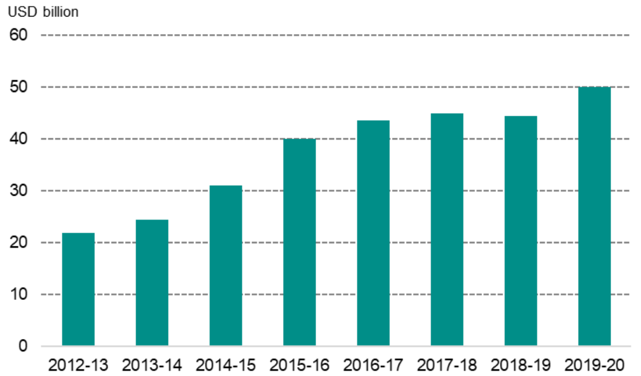
In the auto sector, Japanese OEMs including Toyota, Honda, Suzuki and Nissan have plants in India, with various Japanese components manufacturers having established production in India to provide parts to the Japanese automakers.

India: FDI inflows by country (FY2019-20)



Source: Indian government.

India: Total FDI inflows



Source: Indian government.

Medium term economic outlook

As a result of the severe economic shocks to industrial output, consumption spending and investment, the Indian economy is forecast to be in recession during the 2020-21 financial year.

Despite the severe recession that has engulfed the Indian economy due to the global pandemic, early signs of an economic rebound are already becoming evident as lockdowns are gradually being rolled back. Consequently, economic growth momentum is expected to gradually improve during the second half of 2020, with export orders boosted by the improvement in economic growth momentum in the EU and US as their lockdowns have been gradually eased.

Although economic recovery is expected during 2021, with relatively rapid economic growth of 6.7% y/y forecast, a key risk to the path of economic recovery over the medium term will be the impact of the lockdown on banking sector non-performing loans. The Indian banking system had faced significant problems in recent years with high non-performing loans, particularly in the public sector banks. A further surge in non-performing loans as a result of the latest economic shockwaves from the pandemic could further impair bank balance sheets, constraining the pace of credit expansion and post-pandemic economic recovery.

Despite these downside risks, the medium-term outlook for the Indian economy remains favourable, supported by a number of key growth drivers. An important positive factor for India is its large and fast-growing middle class, which is helping to drive consumer spending. IHS Markit forecasts that India's consumption expenditure will double from USD 1.6 trillion in 2020 to USD 3.2 trillion by 2030, measured in constant prices.

The digital transformation of India that is currently underway is expected to accelerate the growth of e-commerce, changing the retail consumer market landscape over the next decade. This is attracting leading global multinationals in technology and e-commerce to the Indian market.

By 2030, 1.1 billion Indians will have internet access, more than doubling from the estimated 500 million internet users in 2020. The rapid growth of e-commerce and the shift to 4G and 5G smartphone technology will boost home-grown unicorns like online e-commerce platform Snapdeal, logistics start-up Delhivery and the fast-growing online grocer BigBasket, whose e-sales have surged during the pandemic.

The large increase in FDI inflows to India that has been evident over the past five years is also continuing with strong momentum in 2020, driven by large inflows of investments by global technology MNCs that are attracted to India's large domestic consumer market.

Overall, despite a number of significant downside risks, India is expected to continue to be one of the world's fastest growing economies over the next decade. This will make India one of the most important long-term growth markets for multinationals in a wide range of industries, including manufacturing industries such as autos, electronics and chemicals to services industries such as banking, insurance, asset management, health care and information technology.