Economic Preview: Week of 21 September 2020

Publication date: 18 September 2020

Week Ahead Economic Preview

Global overview

- **Flash PMI for the US, UK, Eurozone and Japan**
- **Policy decision in New Zealand and Thailand**
- **US durable goods orders**

The coming week sees flash PMI surveys released for the US, Eurozone, Japan, UK and Australia, which will provide the first insights into how these economies have ended the third quarter. The August PMI data indicated a further strengthening of the rebound of global business activity from the collapse seen in the second quarter, but many consumer-facing sectors remained in decline and worries over renewed lockdown measures amid fresh waves of infections have hit activity, notably in Europe.

While IHS Markit's PMI surveys have signalled a strong US economic rebound in the third quarter so far, the manufacturing expansion remained lacklustre and consumer services providers continued to report falling activity as virus worries persisted. The September manufacturing and services data will therefore provide a valuable guide to whether momentum is being sustained or lost as we head into the fourth quarter. Additional insight will come from Kansas and Richmond Fed manufacturing surveys. The US also publishes durable goods orders data for August, alongside key housing market metrics for new and existing homes sales, as well as home prices (page 3).

Flash PMI data for the eurozone and UK will be especially eagerly awaited, not least by policymakers seeking a grasp on recovery momentum. While the UK led the PMI growth rankings in August, sub-indices from the survey hinted that the upturn lacked legs, notably with a steepening loss of jobs being reported. Meanwhile, rising COVID infection rates caused renewed economic contractions in Italy and Spain during August, according to the PMIs, raising fears that the eurozone's recovery is fading. IFO and other national sentiment indices are also released (page 4).

Over in Asia Pacific, China's industrial profits are issued as well as industrial production data for Singapore and Taiwan, plus trade numbers for Taiwan, Hong Kong SAR and Thailand. As these data only show the situation to August, it's the timelier PMI numbers for Japan and Australia for September that will likely steer sentiment on recovery trajectories for the region. Policy meetings are meanwhile convened in New Zealand and Thailand (more on page 5).

Special reports

Asia Pacific electronics: The pandemic has created tremendous disruption to Asia's electronics manufacturing sectors, but a rebound is underway and the outlook is buoyed by rising demand for certain products (page 6).

Eurozone inflation: A look at the policy outlook as an appreciating euro causes alarm at the ECB, especially given already uncomfortably low inflation (page 9).

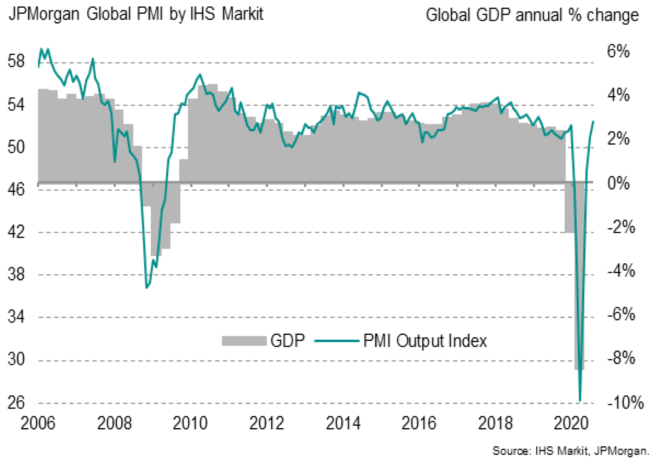
Upcoming PMI releases

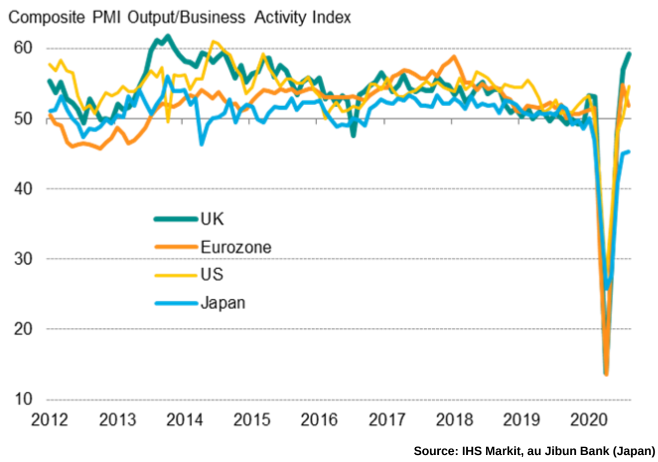
23rd September: Flash PMIs (US, UK, Eurozone, Japan & Australia)

1st October Final Global Manufacturing PMIs

5th October: Final Global Services PMIs

Flash PMI data will provide the first insight into global economic conditions in September





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Key diary events (UTC)

Monday 21 September

China loan prime rate (Sep)

Spain trade balance (Jul)

Taiwan export orders (Aug)

US Chicago Fed national activity index (Aug)

Brazil business confidence (Sep)

Tuesday 22 September

Thailand trade (Aug)

Taiwan jobless rate (Aug)

Hong Kong SAR current account (Q2)

Euro area consumer confidence (Flash, Sep)

US existing home sales (Aug), Richmond Fed manufacturing index (Sep)

IHS Markit Australia PMI (Flash, Sep) 23:00 UTC

Wednesday 23 September

IHS Markit flash PMI for US, Eurozone, UK, Germany and France (Sep)

au Jibun Bank/IHS Markit Japan PMI (Flash, Sep)

New Zealand and Thailand interest rate decision

Malaysia and Singapore inflation (Aug)

Germany consumer confidence (Oct)

Spain GDP (Final, Q2)

Taiwan industrial output and retail sales (Aug)

US house price index (Jul)

New Zealand trade (Aug)

BoJ meeting minutes (14-15 Jul) 23:50 UTC

ECB non-monetary policy meeting

Thursday 24 September

Singapore industrial output (Aug)

France business confidence (Sep)

Germany Ifo business climate (Sep)

Hong Kong SAR trade (Aug)

US initial jobless claims (19-Sep), new home sales (Aug), Kansas Fed manufacturing index (Sep)

South Korea and UK consumer confidence (Sep)

ECB general council meeting

Friday 25 September

France consumer confidence (Sep), jobless benefit claims (Aug)

Italy consumer and business confidence (Sep)

US durable goods orders (Aug)

Saturday-Sunday 26-27 September

26/9: Vietnam FDI (Sep)

27/9: China industrial profits (YTD, Aug)

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United States Week Ahead

Flash PMIs, durable goods and jobless claims

By Siân Jones

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With the Fed revising up its forecasts to indicate a less severe economic contraction than previously thought for 2021, citing stronger than expected growth in the past two months, eyes will turn to the development of any recovery over the coming months as the COVID-19 pandemic continues. In the coming week, the release of flash PMI and regional Fed surveys will give the first major clues as to the economy's recovery trajectory in September. Also released are updates to jobless claims and durable goods orders.

Flash PMIs

Flash PMI data for September will show an early signal as to the health of the US private sector at the end of the third quarter. The rebound signalled in July and August is expected to have aided the quarterly performance, improving upon the challenging conditions seen during the depths of the pandemic in the second quarter. That said, uncertainty surrounding the upcoming election weighed on business confidence in August, exacerbating COVID-19 related disruptions and the expiration of pandemic jobless benefits, especially among consumer service providers, which remained firmly in decline.

Durable goods

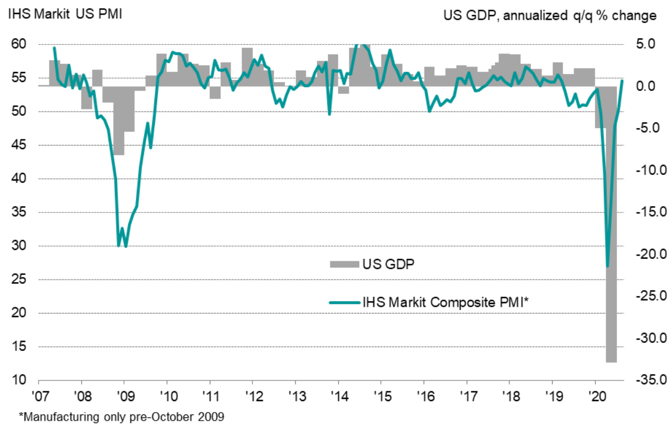
Alongside the flash PMI, the health of the manufacturing sector, and demand for business equipment in particular, will be eyed from the durable goods orders data. Stronger demand for manufactured goods in July, as signalled ahead by PMI data, was reflected in a move towards stabilisation in durable goods orders. With the survey gauge of new orders expanding at a faster pace in August, the updated durable goods orders numbers are expected to indicate growth midway through the third quarter.

Unemployment data

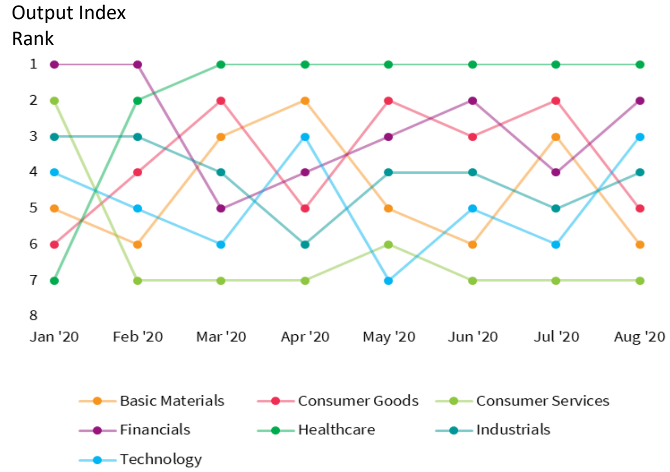
Jobless claims data will provide an update to the labour market, with concerns mounting that the job gains seen earlier in the recovery could be fading.

Meanwhile, updates to regional survey data, including the Richmond and Kansas Fed indexes, and housing market data will be released.

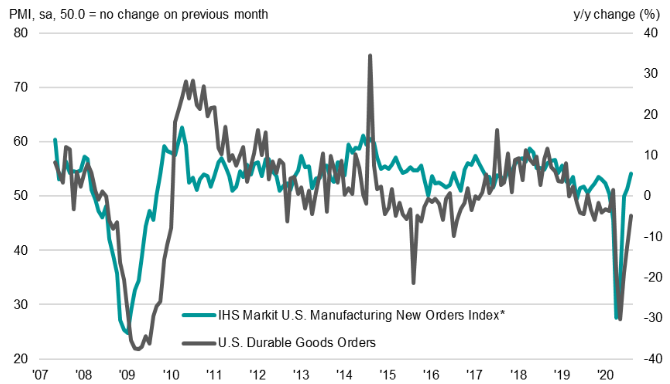
Flash PMI data for September to show whether recovery continued at the end of the third quarter



Consumer services continued to post lacklustre performance in August's IHS Markit US PMI surveys



Durable goods orders picked-up on rising demand in July, and should show further gains in August



Sources: IHS Markit, US Census Bureau

Europe Week Ahead

Flash PMIs under spotlight in week dominated by survey-based indicators

By Paul Smith

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The European economic data release cycle turns once again towards business and consumer surveys next week. Eurozone consumer sentiment data for September is provided Tuesday, with several member states also releasing their own updates later in the week. Business confidence figures from France and Germany will also be released, whilst our September flash PMIs for the euro area, France, Germany and the UK are published on Wednesday.

Eurozone Flash PMIs

August eurozone PMI data showed a divergence in performance between the manufacturing and service sectors, with goods producers recording an acceleration in growth compared to a near stalling in services. September's flash PMI figures for the eurozone will therefore be closely watched to see whether signs of recovery fatigue in services continues and spreads into manufacturing.

Key to determining the growth outcome, not just in September but clearly for the months ahead, will be demand-side developments. To date the recovery has been largely been driven by internal regional demand, with exports struggling to regain traction. With the recent appreciation of the euro an increasing worry for exporters (and for the ECB – see page 9), and with rising unemployment expected to undermine domestic demand later in the year, risks to the outlook for the region's recovery remain tilted to the downside.

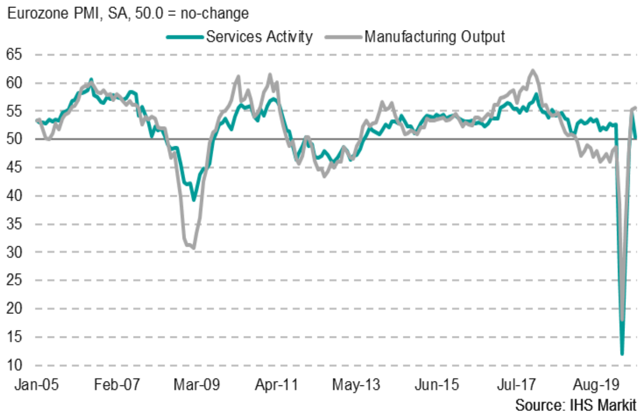
UK Flash PMIs

Over in the UK, growth across manufacturing and service economies expanded at the strongest rate since mid-2014 according to August PMI data whilst official GDP data for July showed the economy continuing to recovery strongly.

With the UK government's "eat out to help out" scheme having now ended, September's PMI data will be closely eyed for signs of any slowdown in the recovery.

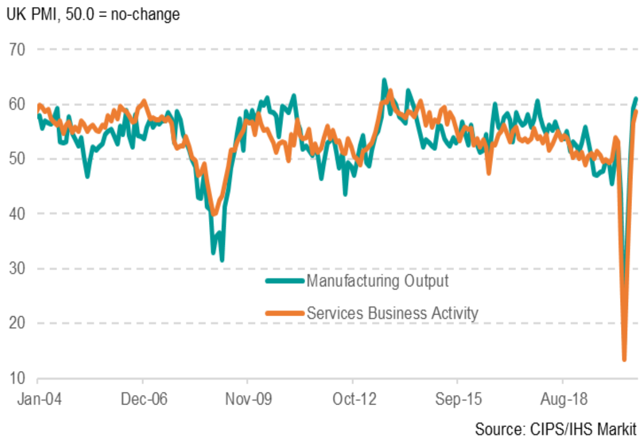
Developments on the employment front will also be of noticeable interest, especially as recent PMI figures have shown employment continuing to be cut at historically marked rates ahead of the scheduled end to the furlough scheme in late October.

Eurozone growth diverged by sector during August



Eurozone manufacturing exports have struggled to recover from the heights of the pandemic and regain meaningful growth traction

The UK recovery has been broad-based by sector so far but worries about the outlook persist given likely rises in unemployment as government schemes are withdrawn



Asia Pacific Week Ahead

Flash Japan and Australia PMI, monetary policy and trade updates

By Bernard Aw
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The coming week sees the release of September flash PMI surveys for major economies, including Japan and Australia, which will provide the latest insights into the shape of the economic recovery. Latest business surveys indicated a further strengthening of global economic growth in August, but countries showed varying degrees of resilience in terms of their economies rebounding. These worries are amplified by rising infection rates in parts of the world, leading to pandemic restrictions tightening. Monetary policy decisions will come from New Zealand and Thailand, while minutes of the July Bank of Japan policy meeting will be scrutinised for clues of future policy moves.

China will update the loan prime rates and industrial profit figures, while August trade and industrial output data for several Asian economies will be sought for signs of further recovery. Meanwhile, South Korea's consumer confidence will be keenly watched.

Third quarter GDP clues from flash PMI

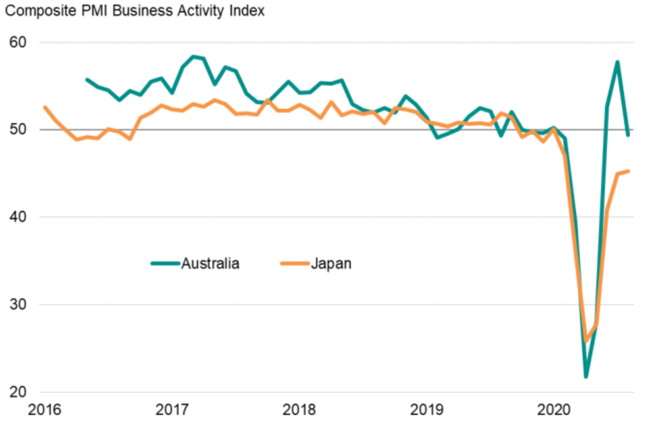
In Asia, focus will turn to the flash PMI survey data for Japan and Australia, with the latter drawing particular attention after an easing of restrictions in Victoria. In Japan, where the PMI has lagged other major developed economies, analysts will be eager to assess as to whether the economic recovery has gained momentum at the end of the third quarter, particularly in the manufacturing sector.

Monetary policy

The Bank of Thailand meets next week in what will be outgoing governor Veerathai's final policy meeting. Market expectations are therefore for monetary policy to remain unchanged. However, analysts will monitor for clues of future policy action at a time of increasing uncertainty over the fiscal policy. PMI survey data indicated the Thai manufacturing sector moved closer to stabilisation in August, supported by increased domestic orders, though export sales remained weak.

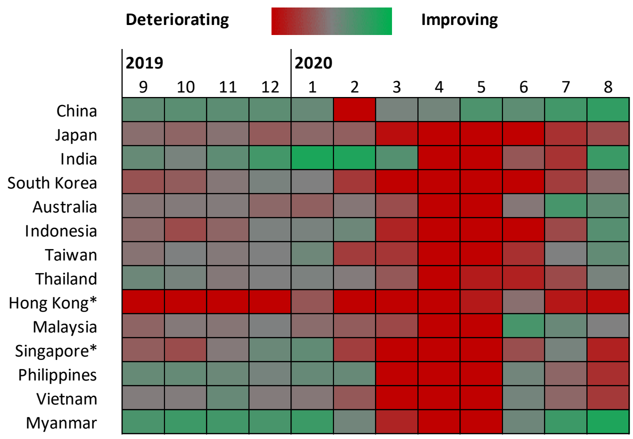
Meanwhile, analysts will monitor the Reserve Bank of New Zealand's monetary policy meeting next week for signs as to whether the central bank will lower interest rates into negative territory, following recent monetary measures that included an expansion of the asset purchase programme in size and time.

Flash PMIs will provide insights into third quarter GDP performance in Australia and Japan



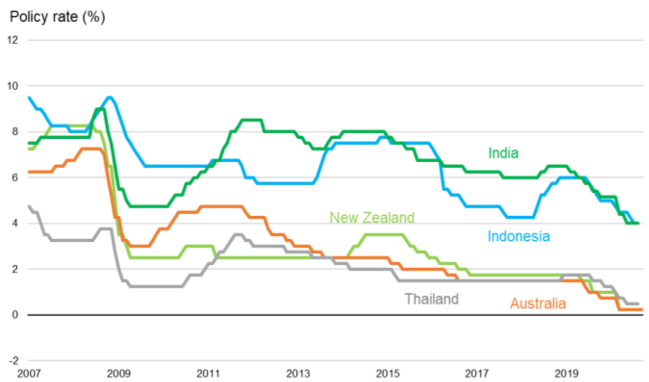
Sources: IHS Markit, au Jibun Bank, CBA

August PMI survey data indicate varying rates of recovery across Asia Pacific



*Represented by Whole Economy PMI. Non-asterisk are shown with manufacturing PMI
Sources: IHS Markit, Caixin, au Jibun Bank, Commonwealth Bank

Selected policy rates in Asia Pacific



Sources: Various central banks

APAC
Special Focus

Covid-19: APAC Electronics Sector Rebounds from Downturn

By Rajiv Biswas

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The Asia-Pacific electronics industry, which is a significant part of the manufacturing sector for many East Asian economies, has been significantly impacted by the COVID-19 pandemic. The pandemic has created tremendous disruption to industrial production, retail store operations as well as consumer spending in many of the world's largest economies, which has hit electronics output and new orders.

The IHS Markit Global Electronics Purchasing Managers' Index, which is based on surveys of manufacturing conducted in major industrial economies worldwide, shows that the electronics industry has been hit by the pandemic. The composite Global Electronics PMI index has been contracting for the past ten months. However recent survey data shows signs of a gradual recovery in global electronics output, as the world economy has slowly emerged from the severe economic impact of the pandemic and lockdowns in the first half of 2020.

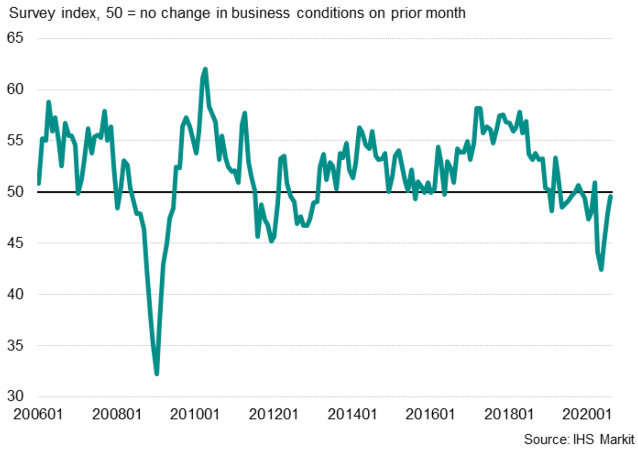
COVID-19 disruptions to APAC electronics sector output

The electronics manufacturing industry is an important part of the manufacturing export sector for many East Asian economies, including China, South Korea, Taiwan, Malaysia, Singapore, Philippines, Thailand and Vietnam. Furthermore, the electronics supply chain is highly integrated across different economies, with China being an important supplier of intermediate electronics parts for a number of Southeast Asian electronics sectors. The complete shutdown of Chinese industrial production for a protracted period consequently created significant supply chain disruptions to the electronics manufacturing sector in many Southeast Asian economies during February and March.

As the impact of the pandemic widened in the Asian region during April, the headline IHS Markit Global Electronics PMI fell to 43.3 in April, down from 48.6 in March, to signal a sharp deterioration in business conditions faced by electronics manufacturers. The April reading pointed to the fastest decline since April 2009, with many businesses temporarily closed amid the global COVID-19 outbreak.

In addition to supply side disruptions to electronics output, widespread lockdowns of retail businesses in many major markets worldwide also disrupted consumer demand for electronics goods as well as products that have significant electronics components, such as autos. Extended periods of lockdown in major electronics manufacturing hubs, including China and Malaysia, as authorities tried to control the spread of the pandemic, resulted in disruption of industrial production and consumption, impacting on global supply chains.

IHS Markit global electronics PMI



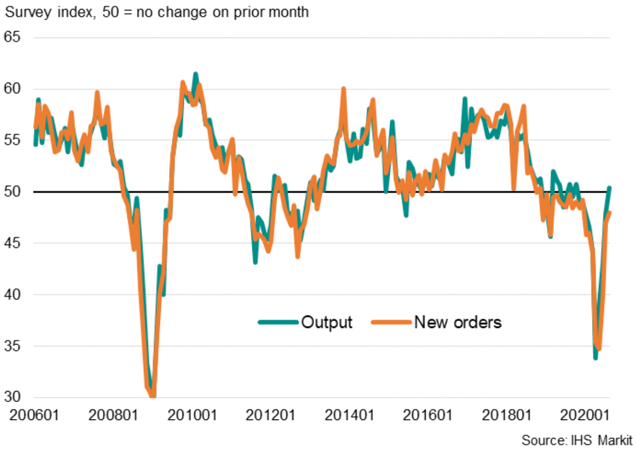
However, since April, the IHS Markit Global Electronics PMI has showed significant improvement, with the headline index rising to 49.7, almost back to neutral conditions after contracting during the previous nine months. The Global Electronics PMI's output index (which measures changes in production) returned to positive territory, reaching 50.4 in August, signalling slight expansion. This is in comparison with severe contraction in April, as reflected in the index reading of 33.9 for that month.

In Malaysia, production of electrical and electronic products fell by 34.2% year-on-year (y/y) in April, as the government's strict lockdown measures resulted in a sharp contraction in industrial production. However, as the lockdown restrictions were eased from May onwards, production rebounded. In June, production of electrical and electronic products rose by 13.2% y/y, continuing to rise by 9.6% y/y in July.

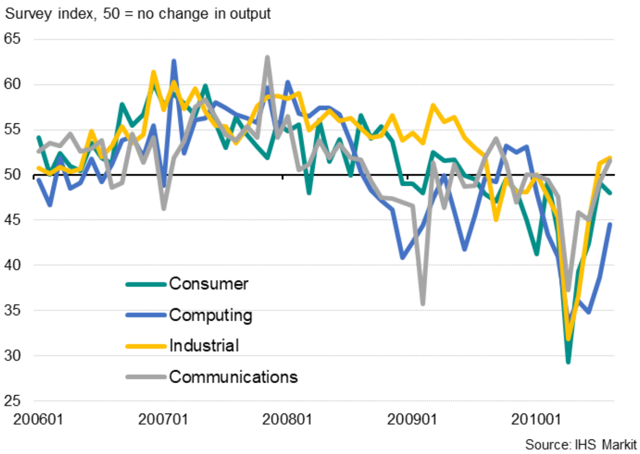
According to the PMI data, global electronics new orders rose from a calendar year-to-date low of 34.7 in

May to a level of 48.0 by August, reflecting a significant easing in the downturn in demand for electronics goods. The strongest recovery has been in new orders for communications electronics, which reached 50.9 in August, helped by improving demand for mobile phones. In South Korea, the shift to remote working globally has continued to boost export orders for some segments of electronics goods, with exports of computers and peripheral devices rising by 98% y/y in August.

IHS Markit Global Electronics PMI, output and new orders



IHS Markit Global Electronics PMI, output by product category

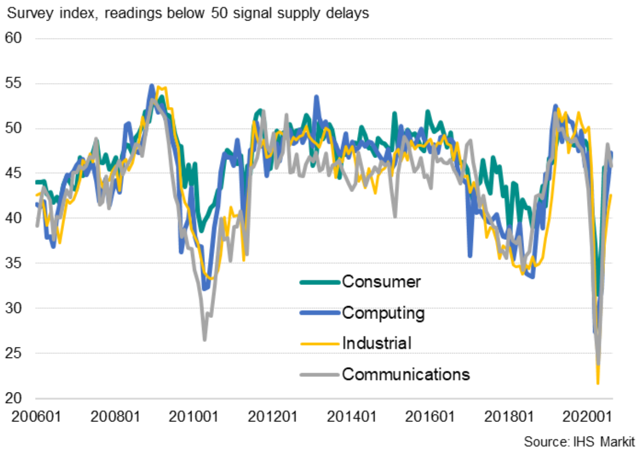


Electronics industry suppliers' delivery times hit by supply chain disruptions

Due to the extensive disruption of manufacturing output in many leading electronics manufacturing hubs due to the COVID-19 pandemic, the situation in April reflected severe supply-side problems in electronics supply chains. April PMI survey data pointed to input delivery times lengthening drastically. In fact, the rate at which vendor performance deteriorated in April to set a new survey record. During April, companies widely cited difficulties in obtaining inputs, particularly from the US, Europe and China.

Despite supply chain disruptions, there has been a considerable easing in the number of global electronics suppliers' delivery delays in recent months, with the PMI's index of delivery performance up from a low of 24.9 in April to 46.0 by August. A number of Asian economies have reported strong growth in electronics exports in the second and third quarters of 2020, as the global shift towards working from home and ecommerce retailing resulted in surging demand for laptops and smartphones from companies, governments, and households.

IHS Markit Global Electronics PMI, supply delays by product category



Reshaping of electronics supply chains in APAC

The process of diversification of manufacturing production and supply chains away from China has already been underway over the past decade, initially driven by rapidly rising manufacturing wage costs in coastal provinces of China. The escalating US-China trade war since 2018 has further intensified this process of supply chain diversification, as firms shifted some production of manufacturing exports for the US market away from mainland China in order to mitigate the impact of US tariff measures. The COVID-19 pandemic has become a further driver for this supply chain diversification process. All of these factors are continuing to reshape APAC supply chains for the electronics industry.

One of the biggest winners of the shift in electronics supply chains away from China over the past decade has been Vietnam. Vietnam has attracted large inflows of foreign direct investment into its electronics manufacturing sector, notably from South Korean electronics firms. The importance of Vietnam's electronics industry has risen dramatically, with the electronic industry's share of total GDP rising from around 5% in 2010 to around one-quarter of GDP by 2019, a key factor helping to drive rapid growth of both exports and GDP.

Total electronic and electrical manufacturing exports accounted for 33% of total Vietnamese merchandise exports in 2019. Vietnam has become the biggest foreign production hub for Samsung Electronics, which booked USD 66 billion of sales in 2018 out of its Vietnamese operations, which was equivalent to around 28% of Vietnam's GDP.

Vietnam's new EU-Vietnam Free Trade Agreement (EVFTA) which was implemented on 1st August 2020 will also help to boost Vietnam's electronics sector.

The Indian economy is also benefiting from new investment inflows into its electronics industry, linked to the rapid development of telecoms infrastructure. The rollout of 4G networks is helping to support the medium-term outlook for new smartphone sales and will be further boosted by the development of 5G networks. The strong growth of India's mobile phone market is attracting a large number of foreign electronics firms to increase their manufacturing capacity in India.

The decision by Apple to increase its manufacturing of iPhones in India has resulted in a significant number of its component manufacturers also shifting production and diversifying supply chains to India. Apple component maker Wistron is hiring an additional 10,000 staff in India as it increases its local manufacturing capacity. This reflects the strong growth potential of India's domestic market as well as supply chain diversification away from China as US-China technology tensions have escalated in recent months. Apple suppliers Foxconn and Pegatron has also planned to significantly increase production capacity in India.

The estimated value of domestic Indian manufacturing of mobile phones reached USD 24.3 billion in the 2018-19 financial year, compared with just USD 3.1 billion in 2014-15. The overall exports of mobile handsets from India were valued at USD 2.6 billion in the 2018-19 financial year, according to the Indian Department of Commerce.

APAC electronics sector outlook

The gradual easing of lockdown restrictions in many of the world's largest economies has resulted in a rebound of world consumer demand since June 2020. This is helping to boost demand for electronics products, as well as a wide range of other consumer goods and industrial goods that utilize electronics components. New orders from the US and Europe for the Christmas season will also help to support recovery in new orders for the electronics sector in coming months.

Over the medium-term outlook, a number of factors should continue to support further recovery in the global electronics cycle. Firstly, a return to positive economic growth in the world economy is forecast for 2021, which should help to boost consumer demand for electronics products. Secondly, the rollout of 5G networks will support increasing demand for new model 5G smartphones over the next three years, helping to boost demand for communications electronics. Thirdly, the continued development of industrial automation and increasing use of robotics and smart devices for industrial applications and new technologies such as autonomous vehicles will also help to boost demand for electronics components such as semiconductors. These trends will help to boost output and exports in the electronics sectors for many Asian economies.

Europe Focus

The Eurozone: Euro elevation puts the ECB in a stew

By Ken Wattret

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The ECB's recent communication signals a heightened alarm about the effects of currency strength, given already uncomfortably low inflation rates.

We continue to expect an additional expansion of the ECB's Pandemic Emergency Purchase Programme (PEPP) to be announced in December.

The chances of a further reduction in the Deposit Facility Rate have also increased but we see this as a risk rather than the most likely scenario assuming the euro's ascent stalls.

ECB highlights concern over euro appreciation

To nobody's great surprise, the European Central Bank's policy meeting on 10th September concluded with no change in the policy stance. The subsequent communications, however, have reinforced our expectation of additional easing in December.

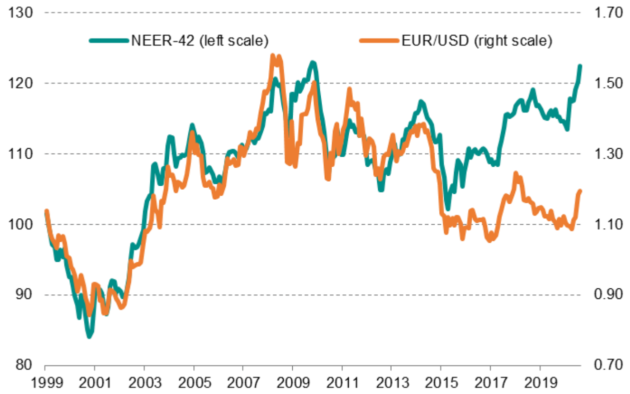
The post-policy meeting statement retained its explicit easing bias and contained various tweaks to the assessment of growth and inflation prospects. It also included one standout change: that is, the inclusion of two explicit references to the strength of the euro exchange rate.

First, in the current environment of elevated uncertainty, the Governing Council "will carefully assess incoming information, including developments in the exchange rate", with regard to its implications for the medium-term inflation outlook.

Second, in the near term, price pressures will remain subdued owing to weak demand, lower wage pressures and "the appreciation of the euro exchange rate".

Given the strength of the euro versus the US dollar since July, plus the rise in the ECB's own, broad nominal measure of the trade-weighted euro (NEER-42) to a record high (see Chart 1), the inclusion of references to the currency's strength were widely expected.

Chart 1: Trade-weighted euro hits a record high



Source: IHS Markit, ECB

That the references were included in the ECB's statement and not just the Q&A session is significant as this signals that the concern over euro strength is widespread across the members of the ECB's Governing Council. President Christine Lagarde also acknowledged in the Q&A that the euro was the subject of "extensive" discussion (accompanied by a reiteration that the ECB does not target a specific exchange rate level).

Despite this, the initial market reaction to the ECB's comments saw the euro rise sharply against the US dollar. This reflected a few factors, including a comment from President Lagarde that a further increase in the Pandemic Emergency Purchase Programme (PEPP) had not been discussed at September's policy meeting. The absence of explicit references to the possibility of Deposit Facility Rate (DFR) reductions and the unexpected upward revisions to the ECB's core inflation projections may also have contributed.

ECB communication reboot

The euro fell back subsequently, however, as a day after the press conference, ECB Chief Economist Philip Lane followed up with a relatively dovish update of his blog. This sounded notably less upbeat than President Lagarde's comments the day before, citing amongst other things the need to avoid complacency. Comments from other Council members since have had a similar tone.

This appears to be part of a new rhythm of ECB communication: that is, recalibrating the commentary from the regular press conference should the market reaction merit. This was initially evident back in mid-March when Mme Lagarde's comments about it not being the ECB's job to close yield spreads were followed by a pronounced sell-off in peripheral sovereign debt markets, then a rather different take on the issue from Mr Lane shortly after.

On track for PEPP expansion in December

All things considered, the bottom line is that the ECB retains a clear easing bias and we continue to expect additional stimulus to be agreed at December's policy meeting, in tandem with the next set of macroeconomic projections. These will be extended in December out to 2023 for the first time and we expect the ECB to forecast yet another year of well below-objective inflation, consistent with the need for additional policy accommodation.

Our view is still that the PEPP remains the ECB's favoured policy instrument. As such, our baseline forecast is for an additional EUR500bn of asset purchases under the PEPP to be announced on 10th December.

DFR cut possible, but not the baseline scenario

A key question, however, now the exchange rate is being explicitly flagged as a concern, is whether this could be accompanied by a reduction in the Deposit Facility Rate (DFR). September's policy statement merely reiterated that the ECB continues "to stand ready to adjust all of its instruments, as appropriate."

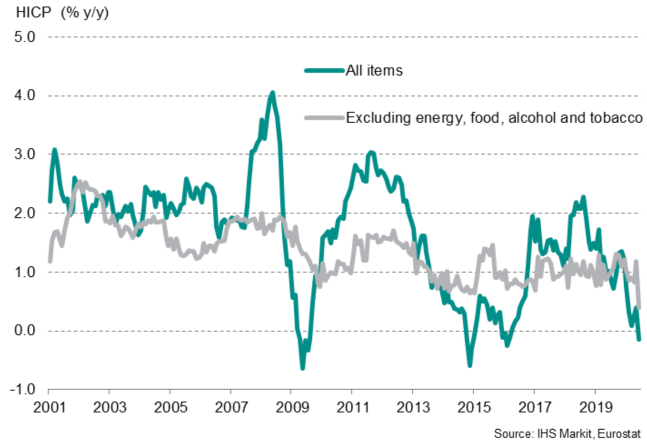
In our baseline scenario, we assume that the DFR will remain unchanged (at the current -0.50%). However, we do not rule out a further 10 basis point reduction, potentially even as soon as December should the euro surge between now and then.

Alternatively, if the ECB's verbal intervention succeeds in stalling the euro's appreciation, along with the recent rise in COVID-19 cases, then cuts in the DFR probably stay off the table given worries about the implications for the banking sector – the most probable scenario in our view.

Look beyond near-term inflation distortions

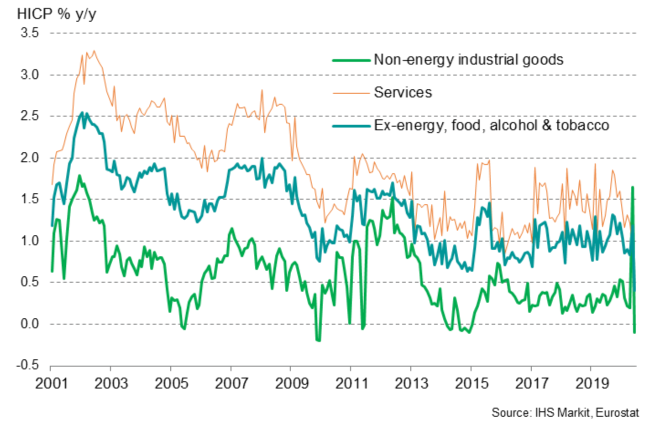
That said, further, pronounced euro gains would be difficult for the ECB to ignore, given the uncomfortably low levels of eurozone HICP inflation (Chart 2). As expected, September's press conference played down August's drop in headline and core rates, citing distortions from seasonal factors, particularly the timing of sales.

Chart 2: Sub-zero headline inflation in August, record low core



We had already flagged this as short-term noise, with the goods inflation rate excluding energy see-sawing in July and August (Chart 3). Looking beyond this distortion, however, the outlook remains one of persistent disinflationary forces in the eurozone, which the ECB is obliged to try to counter given its primary objective of price stability.

Chart 3: Core goods inflation volatility due to seasonal effects



Whatever the ECB opts for policy-wise in the coming months, the big picture for longer-term monetary policy prospects in the eurozone remains much the same. That is, a highly accommodative stance for the foreseeable future given the backdrop of considerable economic slack and persistent low inflation and inflation expectations.

ECB to follow Fed lead, but no time soon

Indeed, ECB president Lagarde acknowledge in the press conference Q&A that the Governing Council took note of the recent (dovish) changes to the US Federal Reserve's policy framework.

The ECB's own policy strategy review is under way and we see an increasing probability of the ECB following the Fed's lead in some key respects, including more flexibility in interpreting the price stability objective, potentially allowing inflation to overshoot after a prolonged undershoot. This will likely generate national tensions, however.

Moreover, as things stand, the ECB's strategy review is not expected to be concluded until mid-2021 at the earliest, so any announcements in this respect are a long way off. This suggests a tendency towards further euro appreciation against the US dollar, though we expect it to be more gradual than during the summer (we target 1.22 for year-end).

The account of September's monetary policy meeting will be published on 8th October and could shed some additional light on the various issues highlighted above.