Economic Research

20 May 2019

Week Ahead Economic Preview

Global overview

- **Flash PMI surveys for the US, Eurozone, Japan and Australia**
- **US-China technology war impact in focus**
- **Japan first quarter GDP, FOMC minutes**

Economic data will take a back seat to escalating US-China trade tensions, the impact of which is the focus of our special report (page 6). Similarly, European parliamentary elections will be closely watched, especially in the UK where the leading parties look set for heavy defeats amid Brexit chaos. Analysts will also be watching for any changing balance between populist and centre-ground parties elsewhere in Europe, notably in Italy. In Asian, a key focus will also be on the outcome of the Indian and Australian elections and economic policy implications.

However, that's not to say the week doesn't see some major data releases. With the US Federal Reserve having changed tack from preparing the markets for a rate hike in 2019 to a more dovish stance, FOMC meeting minutes will be scoured for appetite for the next move to be a rate cut. Flash PMI data for May from IHS Markit will add to the picture for second quarter US GDP growth and inflation trends: the recent surveys showed a slowing in the pace of expansion in April alongside weaker price pressures (see page 3).

In the eurozone, flash PMI surveys will also help determine whether a rebound in GDP growth will fade again in the second quarter. Any strengthening could see bond markets think twice about further stimulus from the ECB (see page 4). UK inflation and retail sales numbers are also updated, though will do little to change the immediate policy picture for a central bank paralysed by Brexit uncertainty.

In Asia-Pacific, Japan's GDP data for the first quarter are eagerly awaited, with stagnation pencilled-in. A disappointing GDP number will add to concerns about the economy's ability to withstand a scheduled sales tax rise later this year (see page 5).

Flash PMI data are also updated for Japan and Australia which, together with the US and Eurozone numbers, will help provide a steer on global economic growth trends, especially for manufacturing, where growing trade tensions have now pushed worldwide exports lower for an eighth successive month.

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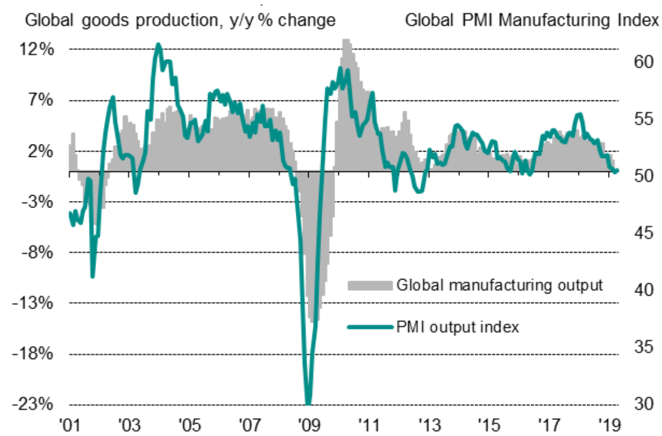
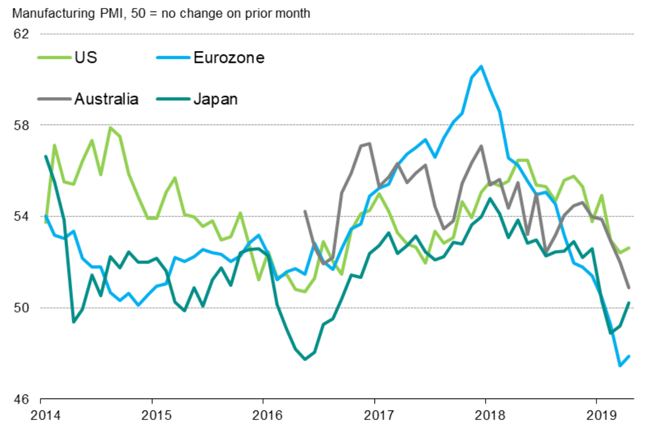
Special reports

Global manufacturing has stalled. Flash PMI data will give insights into momentum in May



Sources: IHS Markit, JP Morgan.

Flash PMI releases will include the US, Eurozone, Japan and Australia



Sources: IHS Markit, Nikkei, CBA.

Key diary events

Monday 20 May

Japan GDP (Prelim, Q1), Industrial production (Apr)
Eurozone current account (Mar)
Hong Kong unemployment rate (Apr)
Chicago Fed national activity index (Apr)
Bank of Israel monetary policy decision

Tuesday 21 May

Reserve Bank of Australia meeting minutes
Thailand GDP (Q1)
UK CBI survey industrial orders (May)
Eurozone consumer confidence (flash, May)
Greece, Spain current account (Mar)
US existing home sales (Apr)
New Zealand retail sales (Q1)

Wednesday 22 May

Japan machinery orders (Mar), exports, imports (Apr), tankan surveys (May)
Thailand exports, imports (Apr)
Spain industrial orders (Mar)
UK inflation, public sector net borrowing (Apr)
South Africa inflation (Apr)
US mortgage applications (May)
Canada, Mexico retail sales (Mar)
Russia, Poland industrial production (Apr)
FOMC minutes

Thursday 23 May

European parliament elections
Australia Commonwealth Bank flash PMI (May)
Japan flash Nikkei manufacturing PMI (May)
Singapore inflation (Apr)
Germany GDP (Q1, final est.)
Eurozone, Germany, France flash PMI (May)
France, Turkey business confidence (May)
Germany Ifo surveys (May)
IHS Markit flash PMI, initial jobless claims (May)
Kansas Fed manufacturing index, new home sales (Apr)
South Africa Reserve Bank interest rate decision
India general election results

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Friday 24 May

European parliament elections
Japan inflation (Apr)
Singapore GDP (Q1, final est.), industrial prod (Apr)
US durable goods orders (Apr)
Taiwan, Mexico GDP (Q1, final est.)
Malaysia inflation (Apr)
UK retail sales (Apr)

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20 May 2019

United States Week Ahead

FOMC minutes and flash PMI surveys

By Siân Jones

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The release of flash PMI data for May and April's durable goods orders figures lead the economic release calendar for the US. The April FOMC meeting minutes are also published.

Flash PMI data

April PMI data signalled a slowdown in the US service sector, with business activity rising at the softest pace since March 2017. Although manufacturers indicated a slight pick up in output growth, this was historically muted and translated to broadly unchanged levels of production.

The service sector expansion is expected to remain subdued, with forward-looking indicators such as the New Business Index signalling less robust client demand. Furthermore, hiring was reined in during April and business expectations slipped to the lowest since June 2016. Therefore, overall private sector growth is predicted to ease during the second quarter. IHS Markit currently forecast GDP to rise by 2.0% in Q2, with the PMI having indicated a 1.9% pace of expansion in April.

Durable Goods Orders

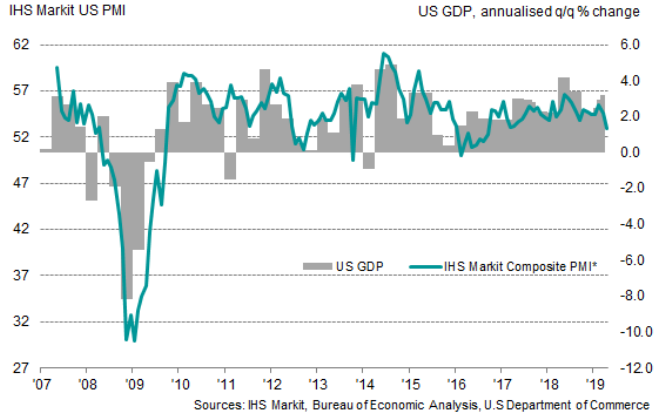
Following on from a slight contraction in industrial production in April, the trend in durable goods orders is expected to have broadly stagnated. Testing demand conditions and heightened global trade tensions are forecast to dampen order books.

FOMC meeting minutes

As was widely expected, the April FOMC meeting concluded with a unanimous hold in interest rates. Although GDP came in above consensus in the first quarter of the year, the Committee are concerned about below target inflation and a likely slowdown in the second quarter. The release of the minutes from the April meeting will give an indication of the possibility of any rate changes in 2019, and especially the appetite for a rate cut.

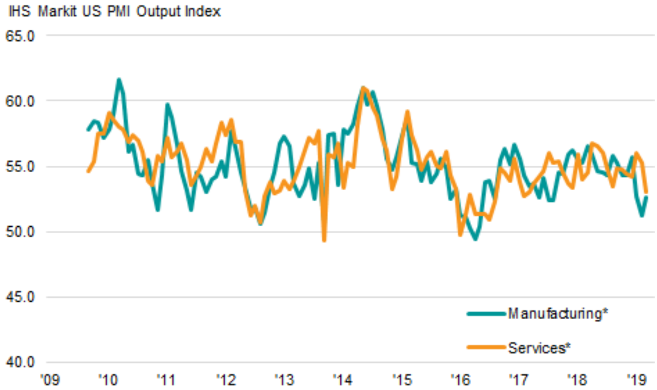
Other key data releases include existing and new home sales data, the Chicago Fed Activity Index and the Kansas Fed Manufacturing Index.

US GDP set to ease on back of slower service sector growth



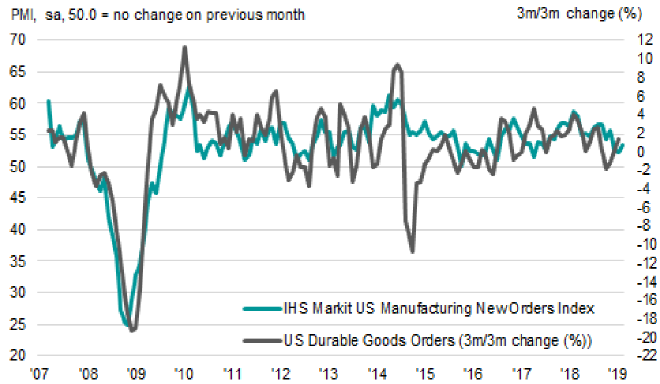
Sources: IHS Markit, Bureau of Economic Analysis, U.S Department of Commerce
*Manufacturing PMI only pre-October 2009

Gap between US manufacturing and service sector performances closes



Source: IHS Markit

Subdued increase in US goods orders



Sources: IHS Markit, US Census Bureau

Europe Week Ahead

Flash Eurozone PMI and European parliamentary elections

By Joe Hayes
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May's Flash PMIs for the eurozone will help distinguish whether the surprising strength of GDP in the first quarter can be sustained or if the expansion will prove all-too brief. Other economic data releases include eurozone consumer confidence, the final German GDP estimate and Ifo surveys, as well as UK inflation, public sector borrowing and retail sales data

European parliamentary elections meanwhile kick off on Thursday and carry across the weekend. The results for the UK will be particular interest for any potential Brexit implications. Gains by populist and far-right movements across Europe could also shift the existing political landscape, most notably in Italy where the balance of power in the coalition could change.

Flash PMI surveys for May

First quarter GDP estimates showed a better-than-expected improvement in the euro-area economy, but a big question remains as to whether this simply represented pay-back from unusual weakness late last year. The PMI surveys have pointed to only sluggish growth so far this year by comparison, hinting that second quarter GDP could disappoint. May's flash PMI data could therefore provide valuable insight into underlying growth trends. The April PMI data had shown a resilient eurozone service sector helped business activity in Germany expand at the fastest rate in seven months growth and return to growth in France. But the euro-area manufacturing PMI held close to March's six-year low.

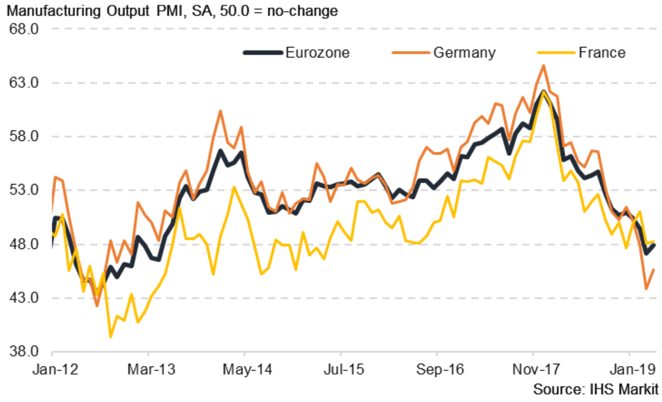
Eurozone consumer confidence, the final estimate of German GDP and the Ifo surveys are also due.

UK Inflation

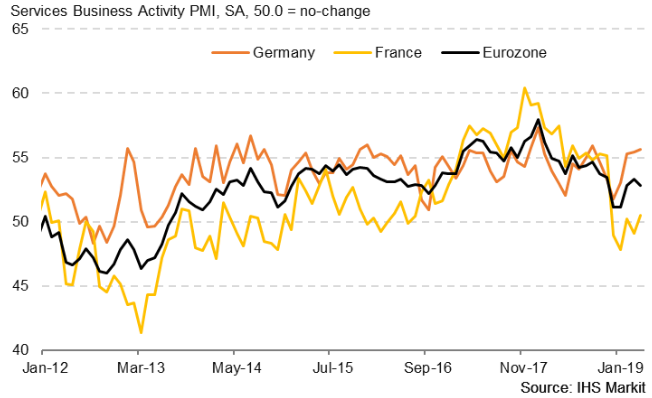
While most economists don't expect the Bank of England to risk a rate hike in 2019, UK inflation and retail sales data will be closely watched. At 1.9%, inflation remained below the 2% target in March, and the BoE expects it to remain close to the target in the near term as subdued economic conditions suggest that demand pressures are unlikely to drive the price level higher.

Retail sales data for the UK are also due, having risen in each of the first three months of the year.

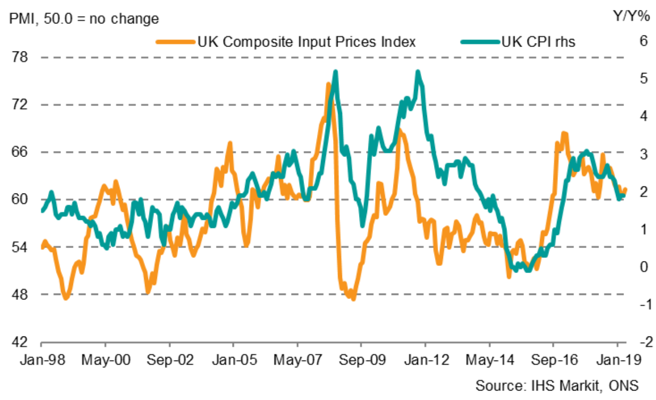
Manufacturing weakness has persisted into second quarter



Resilient domestic markets have supported the Eurozone service sector



PMI suggests UK inflationary pressures are no cause for concern for now



Asia Pacific Week Ahead

Japan GDP, Tankan and flash manufacturing PMI

By Chris Williamson
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Japan features heavily in the economic data calendar for Asia Pacific next week, though markets will inevitably be dominated by the US-China trade spat. General elections also take place in India and Australia

The escalating trade and technology wars between the US and China pose risks to growth in China, covered more fully in our special focus this week (see page 6), but trade tensions have also affected export growth across the region, hurting manufacturers. This has been especially apparent in Japan, where Nikkei PMI surveys have recorded marked falls in both goods exports and factory output in recent months, albeit with the rate of decline easing in April. Flash survey data for May will add further insight, and are accompanied by updated official industrial production data for April and the Bank of Japan's Tankan survey.

Japan also releases its first quarter GDP numbers, being one of the last of the major economies to publish growth statistics. The consensus is for GDP to have stagnated after a 0.5% gain in the closing quarter of last year, though we note that upside surprises have so far been recorded in China, the US, the euro area and the UK. While manufacturing is likely to have acted as a drag on GDP, services have remained more resilient so far this year, according to the PMI.

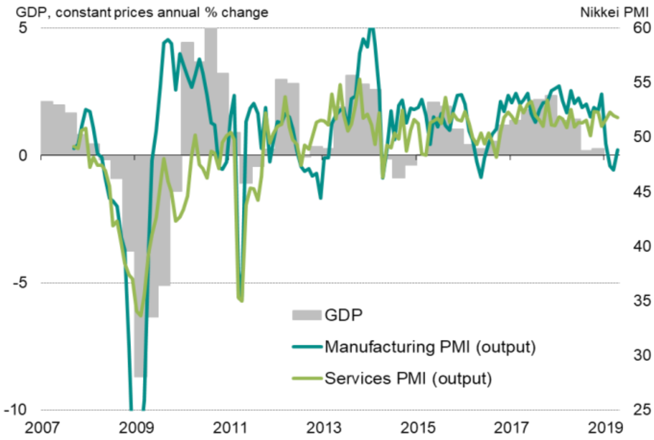
Australia PMI

Flash PMI data are also published for Australia, the previous flash CBA survey having indicated the first expansion for three months in April. The surveys nevertheless indicate that the soft-patch for the economy seen late last year, fueled by slower global trade and manufacturing growth, has carried over into 2019. A big question is whether fiscal policy changes will boost domestic consumer demand and help drive a further upturn in the PMI, feeding through to an improvement in GDP growth in the second quarter to welcome in the new government.

Thailand GDP

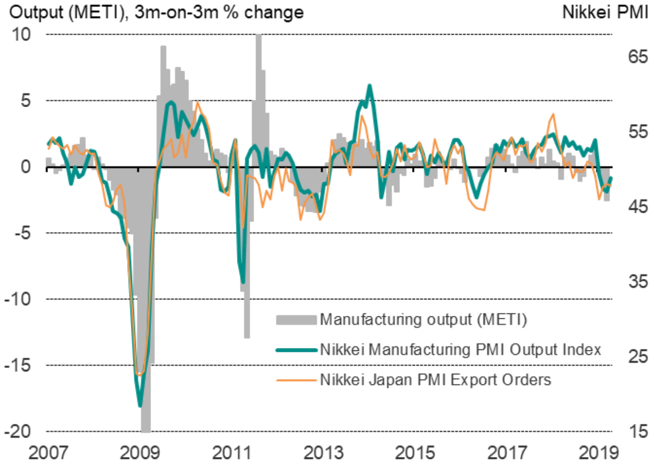
Thailand also releases first quarter GDP. Economic growth recovered moderately during the fourth quarter of 2018; with real GDP up 3.7% year on year. PMI data have also improved in recent months However, after picking up to 4.1% in 2018, IHS Markit expects Thai real GDP growth to moderate to 3. 7% in 2019.

Nikkei PMI and Japanese GDP



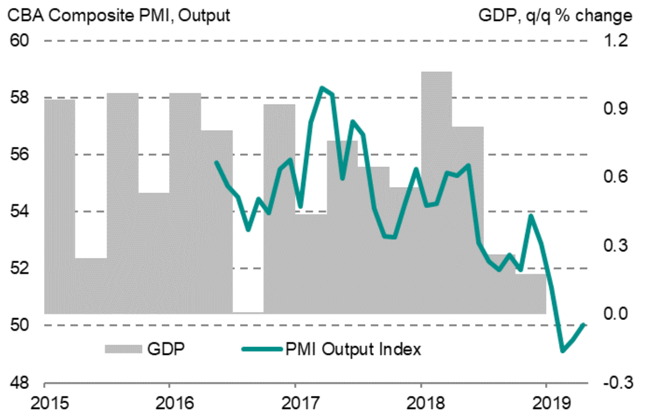
Sources: IHS Markit, Nikkei.

Japanese manufacturing



Sources: IHS Markit, Nikkei.

CBA PMI and Australian GDP



Sources: IHS Markit, CBA.

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Asia Pacific Special Focus

Escalating US-China technology war adds to storm clouds facing China

By Rajiv Biswas

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On 15th May 2019, President Trump signed an executive order that will ban US firms from using telecommunications equipment and services supplied by firms that are deemed to pose a national security risk. While no country or company was specifically named in the executive order, the US Department of Commerce's Bureau of Industry and Security immediately added Huawei Technologies Co Ltd and 70 of its affiliates to its Entity List. This immediately bans US firms from selling or transferring technology to Huawei without first obtaining a US government license.

The combined impact of the US-China technology war and the escalating US-China trade war is clouding the near-term outlook for the Chinese economy amidst signs that domestic economic growth momentum also softened in April.

The US-China technology war escalates

President Trump's executive order will intensify the US-China technology war, with the US Department of Commerce having been tasked with implementing the executive order. This could eventually result in a US ban on use of equipment and services provided by many telecommunications companies from mainland China.

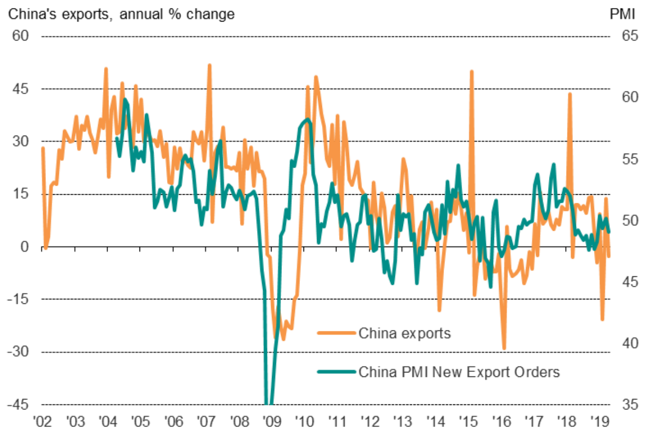
The US executive order follows just days after the US Federal Communications Commission rejected an application by China Mobile to provide communications services in the US. Many recent Chinese M&A proposals for the acquisition of US technology companies have also been rejected by the US Committee on Foreign Investment in the United States (CFIUS), a US government interagency committee that screens proposed M&A deals to assess the national security implications. The heightened US regulatory restrictions have resulted in a collapse of Chinese M&A acquisitions in the US during 2018 and early 2019 by deal value.

US-China Trade War Intensifies

As the US-China technology war has escalated, the bilateral trade war has also intensified. Following the US government's decision to hike tariffs on USD 200 billion of Chinese products from 10% to 25% on 10th May, China has retaliated with countermeasures on 13th May, increasing tariffs on around USD 60 billion of US products from 1st June.

Adding to the downside risks for China's export sector, the US government announced on 13th May that another tranche of US tariff measures against China are under preparation, with a 25% tariff planned to be imposed on a further USD 300 billion of Chinese products that are exported to the US. This next tranche of US tariffs would be another significant negative shock to China's export sector.

China's manufacturing exports



Sources: Caixin, IHS Markit.

It is not a realistic strategy for China to try to mitigate the impact of the 25% tariff by allowing further sharp declines in the yuan. A key priority for the Chinese government since 2015 has been to stabilize the exchange rate and prevent large capital outflows, in order to protect its foreign exchange reserves. Furthermore, if the US assesses that there has been significant currency manipulation, additional US countermeasures could be applied by ratcheting up the tariff rates on Chinese imports to even higher rates.

Impact on China's Economic Outlook

The combined impact of the US-China technology war and the escalating US-China trade war is clouding the near-term outlook for the Chinese economy amidst signs that domestic economic growth momentum also softened in April.

Weak Chinese industrial production and retail sales data for April highlight the downside economic risks to the Chinese economy in 2019 from moderating domestic demand combined with the impact of the escalating US-China trade war. China's retail sales in April moderated to a 7.2% year-on-year growth rate, compared with an 8.7% y/y pace in March. The April retail sales growth rate was the weakest since May 2003, some 16 years ago. New vehicle sales fell by 14.6% year-on-year in April, according to the China Association of Automobile Manufacturers, the tenth consecutive month of declining auto sales.

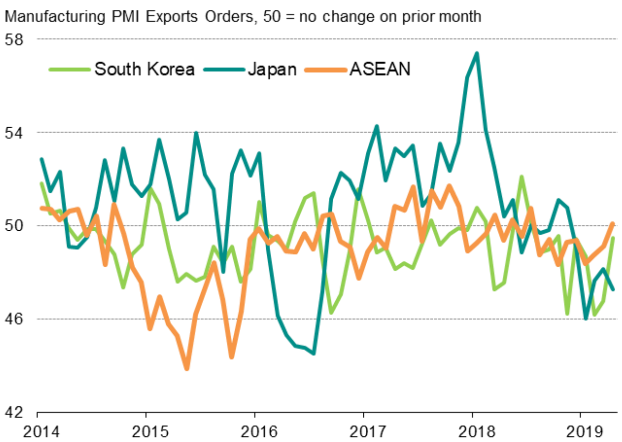
With private consumption having become an increasingly important growth engine for the Chinese economy in the past five years, the significant slowdown in the retail sales growth in April is a warning sign. If weakness in private consumption persists in coming months, this could become a key downside risk to the growth outlook for China in 2019-2020.

Confronted with increasing risks to the economic outlook, Chinese policymakers will therefore need to roll out further fiscal and monetary policy stimulus measures to ensure that GDP growth in 2019 reaches the target range of 6.0-6.5% that was set by the Chinese government in its annual Government Work Report, presented in March by Premier Li Keqiang.

Contagion Effects in APAC Region

China has been the largest growth engine for the APAC region over the last decade, with its rapidly growing economy having driven strong growth in bilateral trade with many Asia-Pacific economies. With Chinese economic growth expected to be dented by the impact of the intensifying US-China trade and technology wars, contagion effects will spill over into the Asia-Pacific manufacturing supply chain.

Manufacturing PMI survey export orders



Sources: IHS Markit, Nikkei.

Economies such as Japan and South Korea, which send a high share of their total exports to China, are particularly vulnerable to any further slowdown in China's export sector and signs of softer domestic demand in China.

Significant uncertainties and downside risks to the export outlook have contributed to the decisions by a number of APAC central banks to ease monetary policy settings so far this year. The People's Bank of China announced another cut in the reserve requirement ratio for small to medium-sized banks on May 6th, immediately after President Trump's announcement on May 5th that he would hike tariffs on Chinese imports. The Reserve Bank of New Zealand, Bank Negara Malaysia and the Philippines central bank, Bangko Sentral ng Pilipinas, also announced rate cuts in early May, with the weaker export outlook being among the factors cited in their rate cut decisions. The Reserve Bank of India has also eased policy rates twice already in February and April, albeit driven mainly by moderate domestic inflationary pressures and concerns about overall growth momentum in the domestic economy.

Many APAC economies also have scope to use supplementary fiscal measures to boost economic growth to mitigate the impact of weak export growth. For example, the South Korean government introduced a USD 5.9 billion supplementary budget on 23rd April, with a key focus of the fiscal measures being to boost the weak export sector through programs such as boosting export credit financing.

However, the escalating US-China trade and technology wars are likely to reinforce trade diversion effects, as US buyers shift their orders to other manufacturing hubs. Multinationals are also increasingly likely to restructure their manufacturing output across their global supply chains to reduce exposure to the US tariff measures. Some emerging APAC manufacturing hubs would therefore likely gain increased export orders from the US as a result. ASEAN manufacturing hubs such as Vietnam, Malaysia and Thailand are likely to benefit from some diversion of export orders as well as stronger foreign direct investment flows over the medium-term, as multinationals diversify their global supply chains away from China.

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