Good MornING Asia - 23 July 2020

Market sentiment could sour as US-China tensions flare up overnight

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By Robert Carnell

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Source: Shutterstock

3.3% GDP decline

We were looking for a 2.5% fall in GDP in 2Q from Korea, only slightly more bearish than the -2.4% consensus view, so -3.3% looks bad. But to be honest, it isn't that big a surprise, and once you start registering quarter-on-quarter declines of more than a full percentage point, the difference between minus 2-something and minus three-something isn't really all that interesting. It's just bad.

But there is still scope for some improvement in 3Q, and taking this into account, we should now see Korean GDP for the full year come in at around -1.6% in 2020 (let's just say somewhere between -1 and -2% - decimals are no longer helpful).

The data breakdown for this initial GDP release is based on sectoral output, rather than expenditures. In terms of the weakest sectors, these include (in QoQ % terms):

1. Agriculture -9.7%
2. Manufacturing -9.0%
3. Transport / storage -8.6%
4. Cultural/ other -9.3%

And the few sectors registering some growth were

1. Utilities +2.8%
2. Finance / insurance +3.7%

This result has little bearing on policy. The Bank of Korea has highlighted fairly clearly that it is done with easing, amid rising concern once more over house prices. And the government has also put in place a lot of fiscal stimulus - 3 supplementary budgets so far this year, so there probably won't be any more from them for a while either.

US data today - focus on claims

My US-based colleague, James Knightley, has very helpfully sent me a preview of what he is looking for in terms of the initial claims data out today, so I'm just going to cut and paste it in below, amended only to account for the time difference from where he is writing (thanks JK!).

"Today's US initial jobless claims data are expected to show another 1.3mn people lodging a new unemployment benefits claim for the week of 17 July. However, we feel the risks are skewed to the upside given the reintroduction of Covid containment measures in a number of states following a spike in cases. This has led to renewed shuttering of businesses in the hospitality industry with high-frequency jobs data from Homebase (an employee scheduling software provider for small businesses) suggesting employment peaked in late June and has been drifting lower nationally ever since. This will be the 18th consecutive week with a reading at or above 1.3mn, underling the stressed situation in the labour market.

The key number to watch though is the number of people claiming benefits under ALL programs, which is currently up at 32mn. That is because an additional 14.3 mn people receive benefits under the Pandemic Unemployment Assistance program that don't qualify for state unemployment insurance benefits (only 17mn do) – people that left their last job voluntarily, students looking for a first job or people who didn't work enough time or earn the minimum earnings to be eligible.

The federal CARES Act has provided huge support to households impacted by joblessness, through extending unemployment insurance benefits by 13 weeks, but more substantially through the extra $600 per week it has been providing in benefits to all 32 million. This means, according to the University of Chicago's Becker Friedman Institute, that 68% of claimants are actually on higher incomes today than when they were working with the median uplift being about a third.

This has massively benefited the economy with low-income households driving the recovery in retail sales based on data from www.tracktherecovery.org. The challenge is that this expires on July 25th. Talks are ongoing about another round of stimulus and we could see a temporary bridge until the new package is agreed, but we are likely as a minimum see the $600/week tapered to something closer to $200-450 per week given Republican concerns about the cost and whether it is actually creating a disincentive to finding work. In an extreme case where the Republicans, the Democrats and the President (who is trying to force through another payroll tax cut) fail to reach an agreement before recess, this additional payment could disappear completely.

Either way, incomes will be falling significantly for those 32 million people at a time when job opportunities are increasingly scarce due to renewed Covid lockdowns – JOLTS data suggests there are four unemployed people for every job opening. We are already concerned that we could see both retail sales and employment post declines in July and if this $20bn per week in income support is cut significantly we will be threatened with the prospect of more bad economic news in 2H2020"

This won't help the USD, which continues to reel against Asian currencies, with the glaring exception of the CNY and CNH, which are softer today in response to the renewed tension flare-up between China and the US over the closure of the Chinese consulate in Houston. Given the way these things operate, we would be very surprised if we did not see tit-for-tat reprisals.

Inflation absent in Asia

In another spot of cut-and-pasting of my colleagues' work, Prakash Sakpal below highlights today's soft Singapore inflation outlook, and reviews yesterday's inflation data from Malaysia. In both cases, the simple message is, there is no inflation in these economies. That is a statement you could roll out across most of the region and is unlikely to change markedly over the rest of the year.

"**Singapore:** June CPI inflation data is due today. The consensus is looking for a less negative headline inflation rate of -0.5% YoY (vs. -0.8% in May). The improvement mainly results from base effects rather than any underlying demand recovery even if the phasing out of the Covid-19 circuit-breaker in June should have released some pent-up demand. The core inflation rate is likely to be unchanged at -0.2% YoY. As in most Asian economies with negative inflation, we see Singapore’s negative trend lasting through the end of the year, or maybe beyond.

Malaysia: Higher food, fuel and transport prices helped to deliver the full percentage point improvement in CPI inflation in June (-1.9% YoY vs -2.9% in May). This brings average inflation in 2Q20 to -2.6%, slightly weaker than our -2.5% forecast and a sharply negative turn from +0.9% in 1Q. Besides continued weak demand, base effects are at work to cause more negative inflation in 3Q. That said, we are revising our full-year forecast for 2020 to -1.8% from -2.5%. We are keeping our view of at least one more 25bp BNM policy rate cut in this cycle, at the September meeting".

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EM Space: US-China tensions rise after the US closed China's consulate in Texas

- **General Asia:** Investors may turn defensive on Thursday with market players awaiting possible retaliation from China after the US abruptly closed a Chinese consulate in Texas. Potential additional stimulus efforts from the US will also be in focus although sentiment will likely still be driven mainly by Covid-19 developments and rising US-China tension on Thursday.
- **Malaysia:** Higher food, fuel and transport prices helped to deliver the full percentage point improvement in CPI inflation in June (-1.9% YoY vs -2.9% in May). This brings average inflation in 2Q20 to -2.6%, slightly weaker than our -2.5% forecast and a sharply negative turn from +0.9% in 1Q. Besides continued weak demand, base effects are at work to cause more negative inflation in 3Q. That said, we are revising our full-year forecast for 2020 to -1.8% from -2.5%. We are keeping our view of at least one more 25bp BNM policy rate cut in this cycle, at the September meeting.
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maybe beyond.

- **Philippines:** The Philippines recorded a surprise budget surplus of Php1.8 bn in June, with revenue collections surging as the government relaxed some of its strict lockdown measures. Revenue collection expanded 117.1% as delayed income tax returns were recorded in June with the rise in collections outpacing government expenditures, which increased 26.7%. For the year, the budget deficit settled at Php560 bn or 2.7% of GDP and we can expect the deficit to widen in the second half of the year as government spending will likely accelerate to offset the slowing economy.

What to look out for: US-China tension and Covid-19 developments

- Singapore inflation (23 July)
- Taiwan industrial production (23 July)
- US initial jobless claims (23 July)
- Singapore industrial production (24 July)