30 July 2020

ECONOMIC REVIEW | July 2020 US FOMC Meeting

Interest Rate Likely to Stay Low Longer as Covid-19 Cases Surge

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- *Multiple headwinds. The US economy is largely anticipated to fall into a recession this year mainly due to Covid-19. Fed projected the economy to contract by -6.5% in 2020. The trough is expected to occur in 2Q20 as several states were under mandatory lockdown orders during this period which stalled economic activities. While the outlook for 3Q20 onwards look slightly brighter due to reopening of economy in stages both domestically and globally, there are still multiple headwinds.*
- *We expect Fed to maintain rate at current level. Both domestic and external front are predicted to perform better in 2H20 however a full recovery seem to be a long way. The current 0-0.25% level on top of huge stimulus packages are anticipated to boost the domestic demand as cost of credit for consumers and businesses are very low. Such policy supports will be more effective when the economy begins to recover. As challenges remain at large, we foresee the Fed to maintain at current low levels at least for the remaining of the year.*

Interest rate left unchanged. The Fed kept its policy rate at 0-0.25% in its July's FOMC meeting, a widely expected decision as the Covid-19 outbreak still present a considerable risk to the macro outlook. Besides that, the Fed will also continue its quantitative easing program which include the bond purchases and the array of lending and liquidity programs to stimulate the economy that has been badly hit by the pandemic. The Fed announced an extension of its dollar liquidity swap lines and the temporary repurchase agreement facility for foreign and international monetary authorities through March 31, 2021. A firmly dovish stance is maintained despite some tentative signs of recovery. These measures will continue pumping cash into financial system and encourage bank loans to businesses and consumers.

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Signs of recovery. The US industrial production continued contracting for the tenth sequential months however at a softer pace of -10.8%yoy in June-20 (May-20: -15.4%yoy) as businesses resumed operations after being closed temporarily due to Covid-19 pandemic. On a monthly basis, IPI continued to be on a higher positive note of 5.4%mom and it was the largest growth since Dec-59. Manufacturing output in particular soared 7.2%mom, in line with the manufacturing PMI of the month which improved to 49.8 from 39.8 in the preceding month. The performance is expected to continue in upcoming month as reflected in the July's manufacturing PMI which returned to expansionary mode of 51.3 after four months of contraction. Meanwhile, the US retail sales growth rebounded to 1.1%yoy in June-20 from -5.6%yoy in May-20, the first growth since the pandemic started in Mar-20.

Fragile labour market but low inflationary pressure. The US NFP for June-20 escalated to 4.8 million, the most on record as economic activities resumed gradually. In a similar note, unemployment rate inched down further to 11.1% in the same month from 13.3% in May-20. Despite the improvement, unemployment rate remain high and the sustainability of NFP performance is uncertain especially with surging number of Covid-19 cases and US-China trade feud which could further deteriorate business sentiment. As for inflation, headline figure rose to a 3-month high of 0.6%yoy in June-20. Meanwhile, core CPI and the Fed's preferred core PCE remain unchanged at around 1%yoy. With continuous easing policies, inflation is expected to edge up moving forward. However, demand situation on the ground which are currently fragile would slow the process.

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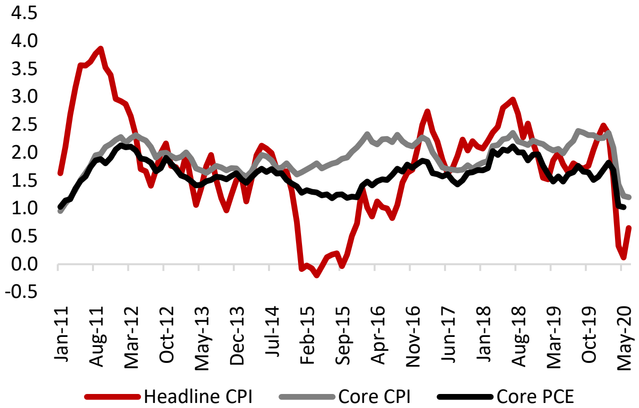
Table 1: Central Bank Policy Rate by Selected Economies (%)

	Nov-19	Dec-19	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Jul-20
Malaysia	3.00	3.00	2.75	2.75	2.50	2.50	2.00	2.00	1.75
Indonesia	5.00	5.00	5.00	4.75	4.50	4.50	4.50	4.25	4.00
Philippines	4.00	4.00	4.00	3.75	3.25	2.75	2.75	2.25	2.25
Thailand	1.25	1.25	1.25	1.00	0.75	0.75	0.50	0.50	0.50
Vietnam	6.00	6.00	6.00	6.00	5.00	5.00	4.50	4.50	4.50
Korea	1.25	1.25	1.25	1.25	0.75	0.75	0.50	0.50	0.50
India	5.15	5.15	5.15	5.15	4.40	4.40	4.00	4.00	4.00
Japan	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)	(0.10)
United Kingdom	0.75	0.75	0.75	0.75	0.10	0.10	0.10	0.10	0.10
EU	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
United States	1.50-1.75	1.50-1.75	1.50-1.75	1.50-1.75	0.00-0.25	0.00-0.25	0.00-0.25	0.00-0.25	0.00-0.25

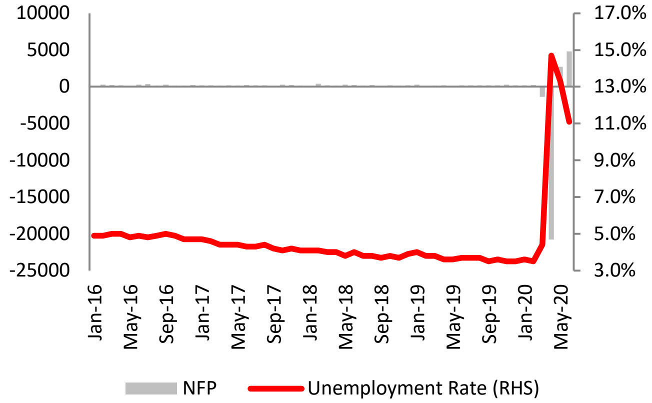
Source: CEIC; MIDFR

Chart 1: Headline vs Core PCE Inflation (%)



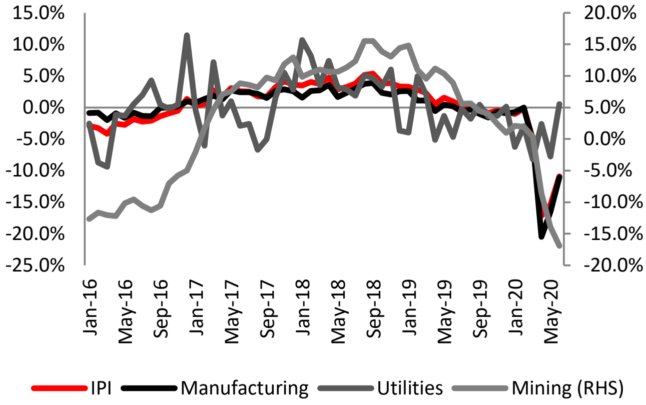
Source: CEIC; MIDFR

Chart 2: Unemployment Rate vs Non-Farm Payroll



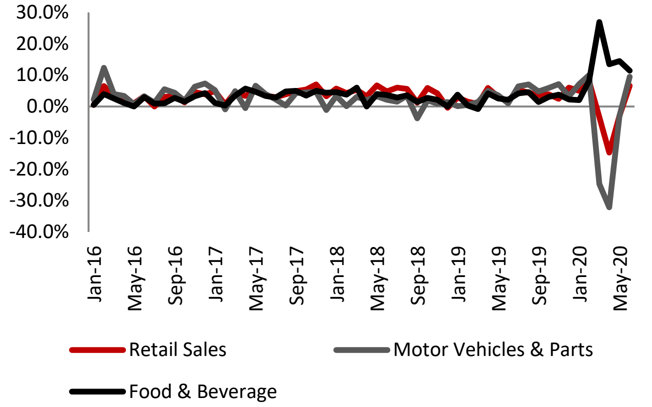
Source: CEIC; MIDFR

Chart 3: IPI Performances (YoY%)



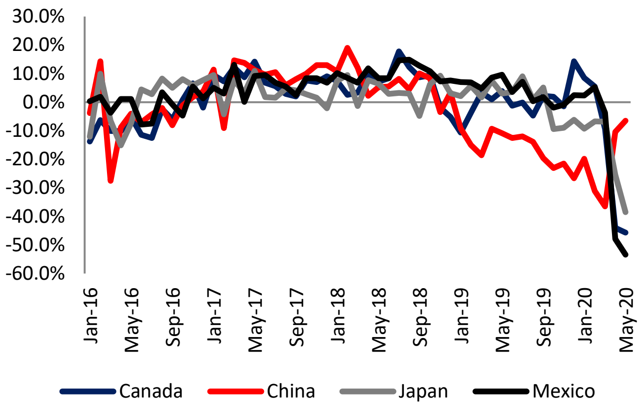
Source: CEIC; MIDFR

Chart 4: Retail Sales (YoY%)



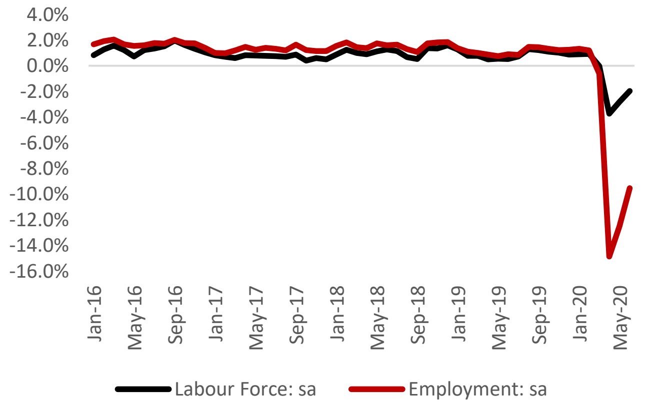
Source: CEIC; MIDFR

Chart 5: Imports from Major Destinations (YoY%)



Source: CEIC; MIDFR

Chart 6: Labour Market (YoY%)



Source: CEIC; MIDFR

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