US ECONOMIC UPDATE NOVEMBER 2020

Q3 bounce; but COVID-19 risks remain

NAB Group Economics

As expected, there was a large bounce in GDP in Q3. However, even after this, GDP remained well below its pre-COVID-19 level. With fiscal support unwinding and COVID-19 surging, growth will come under pressure in coming quarters. The possibility that COVID-19 related restrictions get ramped up presents downside risk.

Q3 GDP Bounce

GDP rebounded in Q3 following the falls in H1 2020 – which were concentrated in Q2. Both the Q2 decline (-9.0% q/q), and the subsequent bounce back in Q3 (+7.4% q/q), are well outside any post WWII precedent. However, this left GDP 3.5% below its end 2019 (i.e. pre-COVID) level.

The recovery was broad based across the major private expenditure categories – consumption, business fixed investment, residential investment, exports and inventories all contributed to growth. In contrast, public demand declined.

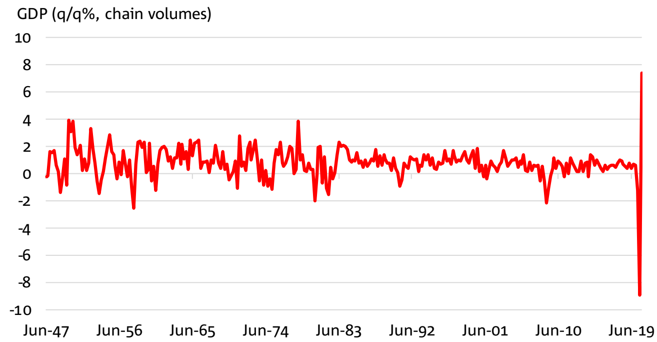
However, looking at a more detailed breakdown it is evident that the recovery to-date is very uneven and there have been major changes in spending patterns. Private goods consumption in Q3 was 6.7% above its pre-COVID level while services consumption was still 7.7% below (with transportation, recreation, food services and accommodation all between 19 to 32% below pre-COVID levels).

Similarly, within business investment, computing equipment and software outperformed other categories (in part due to increased work from home). Mining has been the worst impacted (structures investment down 50% since 2019 Q4).

After Q3 – slower recovery with downside risks growing

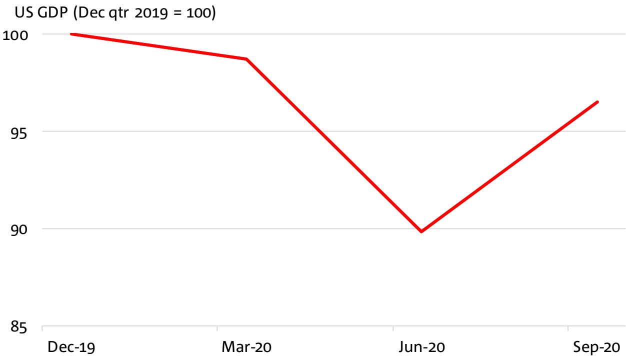
The latest readings for most of the monthly indicators of activity are above their Q3 level. For example, September consumption (the largest expenditure category in GDP) was 1.1% above its Q3 average. Initial October data are generally positive – employment increased again, as did the number of oil and gas rigs in operation, although there was a slight dip in motor vehicle sales. This points to growth in Q4 GDP unless there is significant weakness in the latter part of the quarter.

After the Q2 plunge, a large bounce back in Q3

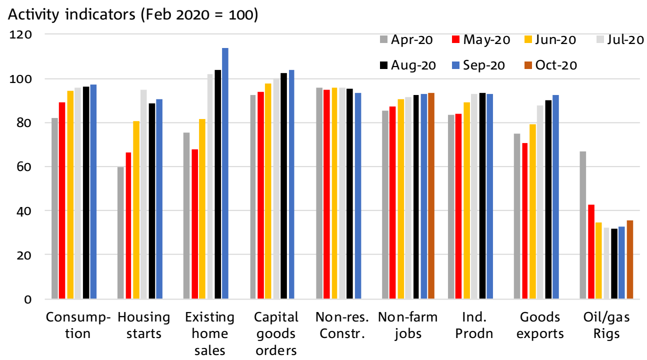


Source: BEA

But activity still well below its pre-COVID level



Most monthly activity data continuing to improve



Source: Refinitiv. Capital goods orders are ex transport & defence ('core')

The concern is that the current surge in the number of COVID-19 cases may lead to another dip in activity.

Date **November 2020** | Author Tony Kelly – Senior Economist

This could be either through more cautious behaviour by individuals (or business) or new restrictions imposed by authorities. So far additional restrictions have largely been localised and limited to reducing social interaction or aimed at hospitality. This could of course change; in the last few days a couple of states have put in place 'lockdowns' – New Mexico has put in a place a two week stay at home order and Oregon has a two week 'freeze'. The experience from earlier in the year, and recently in Europe, is that a shift to more widespread and much tougher restrictions can happen abruptly.

While an increasing number of localised restrictions can creep up to become substantial, there is no clear evidence of a major impact at this stage. OpenTable data on dining and TSA traveller numbers have come off somewhat, and credit card spending data may also have eased slightly.

In contrast, other high frequency indicators have held up. Similarly, business surveys for October remained well above their break even level (of 50 for PMIs/ISM). Both the ISM and Markit PMI manufacturing sector indexes improved in October. While there was a small decline in the ISM non-manufacturing it remained at a sold level, and the Markit services PMI increased.

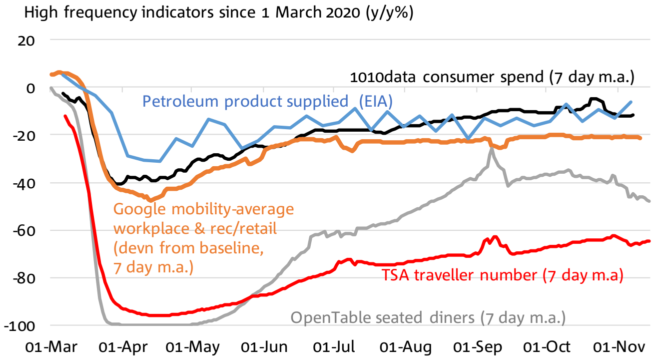
Two other factors are also potentially weighing on growth. Firstly, the re-introduction of nationwide restrictions (lockdowns) in Europe to curb COVID-19 and the unwinding of fiscal support in the US.

We expect Euro-zone and UK GDP to decline by 3% or more in Q4 2020. This will likely have some impact on US exports, but it is unlikely to be significant. US exports are around 12% of GDP, with around 25% of these going to the European Union and the UK. This suggests a headwind to US GDP of only -0.1%. Moreover, the European restrictions are mainly targeted at service sectors, many of which are not heavily traded outside of travel (which in Q3 was only 25% (to all countries) of their pre-COVID level so the scope for further major falls is limited).

Fiscal policy concerns have been around for a while given the failure to pass any further fiscal support since April. Concern really kicked in after July with the end of the Pandemic Unemployment Compensation Payments; a program that (temporarily) increased the level of unemployment benefits. As a result, household income declined in August, but it increased in September as the President's executive order extending PUC (in a pared back form) kicked in.

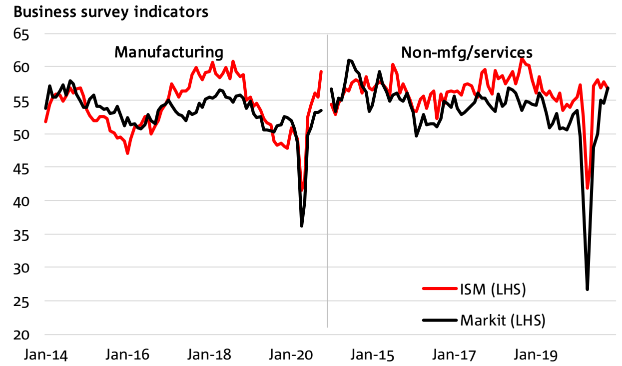
However, funding for the PUC extension is limited. Moreover, applications for the Paycheck Protection Program closed in early August; although income relating to this program was still being recognised by the statistician in September this will decline in time.

High frequency data–hospitality/travel weakening?

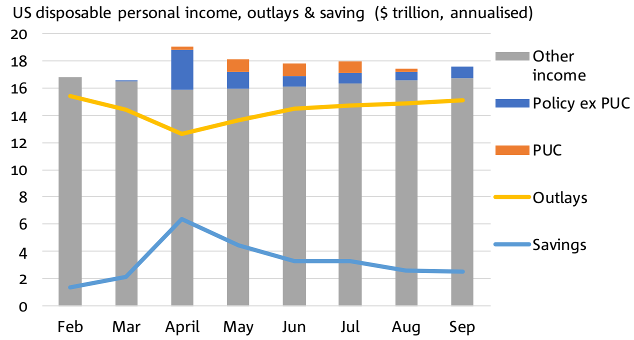


Sources: Google, US EIA, TSA, 1010data, OpenTable

October business surveys – recovery still underway



Despite fiscal policy unwind, h'hold income still higher than pre-COVID-19



Source: BEA; income from Policy is limited to COVID-19 response. PUC = Pandemic Unemployment Compensation program. Coumns are income components

That said, with the labour market continuing to recover, by September household disposable income excluding COVID-19 fiscal support payments were only 0.8% lower than its pre-COVID (February) level. Including government support it was 4.5% higher.

Further, since COVID-19 the level of household savings has been elevated. Taking the February level of savings as the baseline, by September households had accumulated savings above their baseline level by around 7.5% of annual income. In other words, even as government support has started to unwind households have built a buffer to draw on (in aggregate, circumstances for individuals will vary widely) which will help mitigate the impact of unwinding fiscal measures.

That is not to say that additional fiscal support wouldn't help speed the recovery. The need for further stimulus has wide support, including from the

US Federal Reserve. The combination of increasing COVID-19 cases and growing activity restrictions coupled with further unwinding of fiscal support as other elements of the earlier stimulus packages come to an end, represents a clear downside risk to the outlook.

Recent positive vaccine trial news raises the prospect that a vaccine will be available soon; if this were to occur and it was rapidly delivered in scale, then this would represent upside risk.

Bearing in mind these risks, we expect GDP to decline by 3.6% in 2020 and then grow by 3.3% in 2021. This forecast allows for growth to slow in coming quarters – due to the rising number of COVID-19 cases and unwinding fiscal support.

US Election - President Biden

The full results of the US election are still unclear. While Mr Biden will become the next President in January, and the Democrats have retained control of the House, which party will control the Senate is unclear. This will depend on run-off elections for two Senate seats. The Democrats would need to win both to effectively take control of the Senate. Based on election day voting patterns the Republicans are favoured to win both these races, but the margin was narrow and so a different result is quite possible.

If Republicans do retain control of the Senate, this will act as significant curb on the new President's agenda. The promised large spending and tax increases promised would be unlikely to get off the ground as would any controversial policies that require legislative approval.

There may some scope around issues where there is (at least some) bi-partisan support – such as the need for more investment infrastructure.

It is still also still possible that there will be a further COVID-19 stimulus package. Post-election the Republican Senate leader indicated that a new relief package was needed, raising hopes that something would be done even ahead of the President (and new Congress) taking office in January (or at least shortly thereafter). However, both Republican and Democrat leaders have been supportive for a while of the need for further stimulus – the thornier issue has been getting agreement on the specifics (size and composition), and this dynamic doesn't appear to have been changed by the election, at least so far.

The President can also act in areas where Congressional approval is not required. Most notably, the President has considerable leeway around foreign relations and trade (including tariffs). Mr Biden is likely to take a less aggressive tack on trade/foreign policy issues, and while pressure on China over trade & technology issues will remain, it will probably be less confrontational.

Mr Biden has also formed a task force to provide advice around the handling of COVID-19. Already one taskforce member has floated the idea of a 4 to 6-week national lockdown. However, it is unclear whether the new President will push for this and, even if he does, whether he has the legal authority to do so.

A fuller discussion of the issues, and the policy platform of the new President, was provided in our pre-election report.

CONTACT THE AUTHOR

Tony Kelly
Senior Economist
Antony.Kelly@nab.com.au

U.S. ECONOMIC & FINANCIAL FORECASTS

	Year Average Chng %					Quarterly Chng %											
						2020				2021				2022			
	2018	2019	2020	2021	2022	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
US GDP and Components																	
Household consumption	2.7	2.4	-3.8	3.9	2.3	-1.8	-9.6	8.9	1.0	0.5	0.7	0.6	0.6	0.6	0.6	0.6	0.5
Private fixed investment	5.2	1.9	-2.9	4.1	4.3	-0.3	-8.3	6.5	0.8	0.8	1.1	1.2	1.1	1.1	1.0	0.9	0.9
Government spending	1.8	2.3	1.1	-0.2	1.3	0.3	0.6	-1.1	-0.4	0.1	0.2	0.3	0.4	0.4	0.4	0.4	0.4
Inventories*	0.2	0.0	-0.7	0.7	0.0	-0.4	-1.1	1.7	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net exports*	-0.3	-0.2	0.1	-0.8	-0.1	0.4	0.1	-1.4	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Real GDP	3.0	2.2	-3.6	3.3	2.4	-1.3	-9.0	7.4	0.7	0.5	0.8	0.6	0.6	0.6	0.6	0.6	0.5
Note: GDP (annualised rate)						*-5.0*	*-31.4*	*33.1*	*3.0*	*2.0*	*3.0*	*2.5*	*2.4*	*2.4*	*2.3*	*2.3*	*2.2*
US Other Key Indicators (end of period)																	
PCE deflator-headline																	
Headline	2.0	1.5	1.2	1.9	1.8	0.3	-0.4	0.9	0.4	0.4	0.5	0.4	0.5	0.4	0.5	0.5	0.5
Core	2.0	1.6	1.4	1.7	1.8	0.4	-0.2	0.9	0.3	0.4	0.4	0.3	0.5	0.4	0.5	0.5	0.5
Unemployment rate - qtly average (%)	3.8	3.5	6.7	5.8	5.5	3.8	13.0	8.8	6.7	6.4	6.0	5.9	5.8	5.8	5.7	5.6	5.5
US Key Interest Rates (end of period)																	
Fed funds rate (top of target range)	2.50	1.75	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25

Source: NAB Group Economics

*Contribution to real GDP growth

Group Economics

Alan Oster
Group Chief Economist
+(61 0) 414 444 652

Dean Pearson
Head of Behavioural & Industry Economics
+(61 0) 457 517 342

Jacqui Brand
Personal Assistant
+(61 0) 477 716 540

Australian Economics and Commodities

Gareth Spence
Senior Economist
+(61 0)436 606 175

Phin Ziebell
Economist – Australia
+61 (0) 475 940 662

Kaixin Owyong
Senior Economist, Research
+(61 0) 436 679 908

Behavioural & Industry Economics

Robert De Iure
Senior Economist – Behavioural & Industry Economics
+(61 0) 477 723 769

Brien McDonald
Senior Economist – Behavioural & Industry Economics
+(61 0) 455 052 520

Steven Wu
Economist – Behavioural & Industry Economics
+(61 0) 472 808 952

International Economics

Tony Kelly
Senior Economist
+61 (0)477 746 237

Gerard Burg
Senior Economist – International
+(61 0) 477 723 768

Global Markets Research

Ivan Colhoun
Global Head of Research
+61 2 9293 7168