Asia Morning Bites

Markets embrace the recession narrative

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Macro outlook

- **Global**: Another day to digest the recent US inflation data, and another day closer to the June FOMC meeting, and global markets, we well as those here in Asia have been demonstrating that they don't like where the global economy sits right now. The asset class in the driving seat is most likely US Treasuries. After their 25bp rise in yield on Friday, 2Y UST yields rose another 29bp yesterday. US 10Y yields rose a further 20.4bp, taking them to their highest level this year at 3.36%. Though with the 2Y yield now at 3.35%, this is as close to inversion as is needed to get the signal that markets now expect recession. It was only a matter of time. It's also increasingly hard to see how the Fed will be able to avoid hiking at least 75bp at this week's meeting (which markets are almost fully pricing in now), without causing another sell-off. And it makes the forthcoming dot plot and forecast projections even more of a minefield than usual. Not surprisingly, stocks are taking a battering as optimistic forward earnings estimates get re-worked against a recession background, and the risk-free discount rate gets ramped up. A 3.88% fall in the S&P500 takes it into a bear market for the first time this year (-21.33% ytd) after a couple of close runs. The NASDAQ fell even harder, dropping 4.68% on the day. If you want a crumb of comfort, it is that the drops have come on increased volumes, though we have yet to have the sort of capitulation trade that would help signal we have touched bottom. Currencies behaved predictably.

Within the G-10 bloc, the EURUSD is now down to 1.0458, from just under 1.05 this time yesterday. Cable is at its weakest since June 2020 at 1.2187, and the AUD is weaker again at 0.6936. The JPY has been a touch steadier again, remaining around 134. But the BoJ is fighting a losing battle trying to keep the 10Y JGB within its target range, The current yield is 0.257%. The end-of-week BoJ meeting could see the JPY back under selling pressure if there is no hint of any policy change, and we don't think we will get one. Asian FX was again weaker, and once again, the sell-off was led by the KRW, which is now 1284 against the USD. The CNY also lost ground to the USD yesterday, rising to 6.7546 as of writing. The IDR also seems to have lost its stability from earlier this year, and surged to 14681 yesterday, within sight of its 14,738 intraday May high.

It's another relatively quiet day on the G-7 macro calendar, with Germany's ZEW forecast to show a very slight improvement from very low levels, the US NFIB Survey to cast light on corporate pricing intentions and labour market tightness, and the forecast of a slight decline in May US PPI inflation looking rather optimistic after the recent CPI release.

- **India**: Indian CPI inflation for May came in at 7.04%YoY (INGf 7.0%, Consensus 7.1%). This is down from the 7.8% April figure but is due almost entirely to administered excise duty cuts in May weighing on transport inflation and utilities. The overall CPI index rose 0.9% from the previous month. There was not much sign of moderating price pressures across other groups in the price index such as services, food and clothing. Such cuts in excise duty have a direct bearing on India's fiscal position. And with the projected deficit reduction this year starting from an unambitious starting point, credit rating agencies will be watching the impacts carefully.

- **China**: A bipartisan proposal in the US to limit US firms' investment in China is gaining ground. The proposal is part of a $52bn bill to boost US competitiveness with China and to expand chipmakers' US-based production. The limit on investment is likely to include Chinese semiconductor and advanced machinery manufacturers. China has purchased more semiconductor machinery since last year. But in the future, it is likely to face steeper hurdles to buying machines needed for semiconductor production. This will push China to strive for even more self-dependence in this sector. However, without advanced machinery, it will be even more difficult to achieve this goal. This sector is likely to come under selling pressure today.

- **South Korea**: The South Korean truckers strike is entering its 8th day today. Truckers have been protesting against a sharp rise in fuel costs and the sunsetting of the government safe fare program. As these lockdowns have been going on for more than a week, we are starting to see that these strikes are disrupting production and affecting port activity as well. We believe that if both parties reach an agreement within a few days, then production and shipments can still catch up with the losses already sustained. Even so, logistics costs are expected to increase, which will eventually be passed on to consumer prices with a lag. Also, if the strike continues for more than a week, then it will hurt production activity, including construction, and we will then have to revise down our 2QGDP forecasts.

  In terms of inflation, we expect June CPI to show growth of 6%YoY, as gasoline prices reached a historical high last week and preliminary fresh food prices are also on the rise due to severe drought during the early summer harvesting season. Also, utility prices are scheduled to rise in the coming months. We expect CPI inflation to stay above 6% in 3Q22.

- Japan industrial production (14 June)
- India trade balance (14 June)
- US PPI inflation (14 June)
- South Korea unemployment (15 June)
- Philippines remittances (15 June)
- Japan core machine orders (15 June)
- Australia consumer confidence (15 June)
- China 1-year medium term lending (15 June)
- US retail sales (15 June)
- FOMC meeting (16 June)
- Taiwan CBC meeting (16 June)
- New Zealand GDP (16 June)
- Japan trade balance (16 June)
- Australia employment change (16 June)
- BoE meeting (16 June)
- US initial jobless claims, building permits and housing starts (16 June)
- Singapore NODX (17 June)

- Malaysia trade (17 June)
- BoJ meeting (17 June)
- US industrial production (17 June)

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