

Asia Morning Bites

Markets volatile amid Fed "re-pivot" and Pelosi's visit to Taiwan



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Macro outlook

- **Global markets:** Asian markets yesterday were roiled by the visit to Taiwan of Nancy Pelosi, which saw the island harried by Chinese military aircraft. Asian stocks and FX were both weaker, and we will probably face more of the same today and at least until Pelosi departs for the rest of her Asian tour as China conducts more military exercises. US stocks were lower yesterday, but this seems more the result of a slew of Fed speakers, Mary Daly, Loretta Mester and Charles Evans - variously noting that the Fed was not nearly done with tightening policy. Evans also remarked that a 75bp hike was not inconceivable in September, even if he favoured a 50bp move. The effect of this was to push short-dated Treasury yields much higher. The yield on the 2Y Treasury rose more than 18bp to 3.05%, the 10Y yield rose a little less (17.5bp) to 2.748%. This, rather than the furor in Taiwan over the Pelosi visit was the likely cause of the small sell-off in US stocks, which led to the S&P500 falling 0.67% and the NASDAQ falling 0.16%. US equity futures are today pointing to a small positive. The surge in US shorter-dated yields has provided a lift for the USD, even against currencies like the JPY, which ought to have been regarded as a safe-haven play during the Pelosi visit. The JPY instead was the most exposed to a resurgence in US rate hike expectations, rising from just below 131.0 to 133.46 now. The unwinding of the Fed rate hike pivot will probably dominate safe-haven concerns today. The resurgence in the USD has taken the AUD back below 70 cents, to around 0.6913. And Cable has dropped back to

1.2156 from about 1.2255. There were small losses in most of the Asian FX pairs against the USD led by the SE Asian currencies. The INR bucked the trend with a slight gain yesterday helped by lower oil prices. Front-month Brent crude futures are trading at about \$100.5/bbl.

- **G-7 Macro:** The service sector ISM survey today is another of the regular pre-payroll points of interest ahead of Friday's US labour report. As well as the employment sub-index, the overall state of the service sector index will be a useful gauge for how, if at all, the main sector of the US economy is slowing in response to the Fed's tightening. This could feed into the rate hike re-pivot story that is unfurling. Final factory orders/durable goods can probably be skipped, as too can final PMI indices from Europe.
- **China:** China will conduct missile tests and military drills around, and maybe even above Taiwan between 4 to 8 August. This is a demonstration of China's political stance toward the US and Taiwan. At the same time, a Chinese battery company has deferred a decision to build a factory in the US. It appears that Pelosi's visit to Taiwan has already triggered economic retaliation from China, and we expect the US to react to this. It now looks very unlikely that the US will withdraw any tariffs on Chinese goods. Deteriorating political and economic tensions between China and the US will further raise the costs of doing business, which will be negative to both economies' growth prospects.
- **Korea:** As of the end of July 2022, Korea's foreign exchange reserves stood at USD438.6bn, an increase of USD330m from June. This was mainly due to an increase in foreign currency asset management income and foreign currency deposits from financial institutions.
- **Australia:** The consensus forecast for 2Q22 retail sales ex inflation is for a 1.2%QoQ rise, the same as in 1Q22. If it happened, this would be a fairly sizeable increase and might cast some doubt on the more measured tightening pace markets [inferred from yesterday's RBA decision](#), where the Reserve Bank hiked rates by a further 50bp to 1.85%.

What to look out for:

- China Caixin services PMI (3 August)
- Japan Jibun PMI service (3 August)
- US ISM services, durable goods and factory orders (3 August)
- Australia trade balance (4 August)
- US initial jobless claims and trade balance (4 August)
- Philippines CPI inflation (5 August)

- Thailand CPI inflation (5 August)
- Indonesia GDP (5 August)
- RBI policy rate (5 August)
- Singapore retail sales (5 August)
- Taiwan CPI (5 August)
- US non-farm payrolls (5 August)

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