

# Asia Morning Bites

Recession fears dominate markets as yield curve inverts



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### Macro outlook

- **Global:** Despite, or maybe because of the inversion of the 2s10s yield curve yesterday – historically a reliable predictor of recessions two years hence – US equities ignored the sea of red in European bourses and made modest gains. These were mostly concentrated in the tech sphere – the NASDAQ rising 1.75% on the day, whilst the S&P500 barely broke even. Both indices are giving little away in terms of futures today, though this feels like an unconvincing rally, based on low volumes, in markets that technically don't look oversold. The rest of the week will be interesting. 2-year US Treasury yields continued to fall, but only just, while the yield on 10Y bonds fell 7.5bp. 10Y yields are now 2.805%. 2Y yields are 2.818%. Some people are downplaying the 2s10s curve inversion, saying that it's the 3m10Y slope that matters. I'd have to say that this not a particularly bright approach, and with the 3m T-bill currently yielding 1.826%, and a 75bp hike due next month, followed by 50bp the month after, you don't have to be a particularly astute forecaster to realize that it is only a matter of months before this becomes a mathematical certainty, unless the 10Y massively sells off between now and then.

What the bond yield moves have also done is drive a surge for the USD. EURUSD is now 1.0263, and there will certainly be talk of parity imminently. The AUD has fallen back to 0.6781, and Cable is now below 1.20, not helped by PM Johnson's woes as top cabinet

members quit. The JPY is faring slightly better. It might not be the safe-haven currency it once was, but the yield disparity argument that has been battering it recently is looking a bit less forceful today after US yield declines. Yesterday's Asian FX moves showed broad-spread, but modest weakness apart from the AUD which fell sharply. Today likely beckons more of the same. One ray of light on all of this may be energy prices. Front-month Brent crude oil dropped sharply yesterday, falling to \$102.77/bbl. We haven't seen a sub\$100 Brent since end-April, but maybe that too is on the horizon ([see also Commodity Feeds this morning](#))

- **G-7 Macro.** German factory orders for May will probably make for grim reading later today. The consensus expects year-on-year orders to decline by 5%. Eurozone May retail sales may not send a much more upbeat message. Energy shortages and price rises seem to be pointing towards some form of recession in Europe. The only real question now seems to be what sort. In the US, the service sector ISM index could shed light on Friday's payrolls. A strong payrolls figure may temper recession fears briefly, though it will also likely drive up 2Y yields and probably won't be regarded as unambiguously positive by the equity investment community.
- **Taiwan:** CPI and WPI for June will be announced today. We expect CPI inflation will edge up in June. But this higher inflation should be short-lived as food prices are coming down. The central bank still has time to observe how food price changes in the coming months are affecting inflation before its meeting in September.
- **China:** As we have repeatedly said, tighter Covid measures could return to China. And there are more positive Covid tests once more in Shanghai. But even if there are more lockdowns, we expect these to be a lot more localised than the ones in March to May, as the government is trying to balance controlling Covid and growing the economy.

Even if the tech war doesn't make headlines these days, it actually never stops. Even old semiconductor machines may be banned from being exported to China. This would push China to accelerate the manufacture of its own semiconductor equipment. While this would be a challenge, the threat forces the need for China to do so.

## What to look out for: FOMC minutes

- Malaysia BNM policy rate (6 July)
- Taiwan CPI inflation (6 July)
- US ISM services (6 July)
- FOMC minutes (7 July)
- South Korea BoP (7 July)
- Australia trade balance (7 July)
- US trade balance and initial jobless claims (7 July)
- Japan BoP (8 July)
- Taiwan trade balance (8 July)
- US non-farm payrolls (8 July)

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