

Good MornING Asia - 13 April 2020

With much of the world still on holiday, this will be a quiet start to the week, though an OPEC deal and some stabilisation in Covid-19 cases provide a steady start. Increasingly, thoughts will turn to the process of deconfinement, something that we expect will be very slow and phased

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China's GDP report for the first quarter will provide some sense of the damage the pandemic has inflicted on economies in that part of the world



OPEC+ deal: Not so fast

The OPEC+ alliance has agreed to cut oil output by 10MMbbls/d starting in May, however, this is conditional on Mexico accepting its allocated cut. So far,...

By Warren Patterson



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Australian QE: A premature tapering?

After hinting at tapering if conditions improve, Australia's central bank actually trimmed its daily bond-buying today. However, an excessive...

By Francesco Pesole

Opinion | 13 April 2020

Deal for OPEC+

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Source: Shutterstock

OPEC+ deal

Since Warren Patterson put his [preliminary note out last night](#), OPEC+ does seem to have dragged Mexico on board for a deal. But the 10MMbbls/d decline isn't quite what it seems, once baseline conditions are taken into account, and it is also not enough to bring the market into balance this quarter, given the amount of demand destruction there has been. For more, watch out for our Commodity guys' note later this morning, which will do a better job of spelling out what this all means. But I suppose you could say, while it might not be enough to push oil prices decisively higher, it is definitely better than no deal.

Covid-19 - also steady

The news over the extended weekend on Covid-19 has also been a bit less grim. Yes, the death toll is still alarmingly high, but new cases seem to be levelling off in the low 30,000s for the US, and on a state-wide basis (which is how you have to look at these figures to really be able to say anything sensible about the national numbers), few states look particularly alarming. Texas and Georgia are

both still worth watching. Their numbers are erratic and a clear trend is hard to observe - made more tricky by what we have observed to be a "weekend" effect, where new cases can dip at, or shortly after weekends. The extended Easter break may be playing a role here. Florida, Virginia and Maryland still appear to be on an upward trend, but the other states with rising new case numbers either have a small number of total cases, or are unlikely to offer a high peak due to low populations (North Carolina, Rhode Island). Elsewhere, case numbers seem to be steady or in decline. The death toll will follow with a lag.

The news from Europe also continues to improve, though the UK is more in the "steady" camp of the US, rather than showing any outright decline. Talk is beginning to grow about easing movement restrictions. Italy and Spain may be in a position to do this within the next two weeks or so if their improvements continue. The degree of their success will shine a light for other countries to follow.

Globally, there are still areas where this virus is still in the ascendancy. Russia is one of the notable hotspots, having kept its numbers low for a long time. Japan is also seeing its new case numbers rise after weak restrictions on movement were imposed last week. It is our belief that these measures will be further tightened in the days ahead.

Data - China GDP the week's highlight

With Easter foreshortening the week, there won't be too much on the economic calendar globally this week.

But we do get the 1Q20 China GDP figures on Friday. Given the depth of unease generally over the accuracy of China's GDP figures, it will be hard to extract the signal from any noise these numbers deliver. Already, the market consensus is splattered across a range from -20%QoQ to -5%QoQ. That tells us that the consensus really has no idea at all what to expect - or how much "fudging" of the underlying data to allow for in the final figure. Certainly, the amount of stimulus has been substantial. But can anyone seriously be expected to believe anything other than a sharp decline in 1Q20 output? We don't think so. But let's wait and see what the data brings.

y has no clue, and

India - lockdown to be extended

Prakash Sakpal writes this on the Indian lockdown today, "The central government is considering an extension of the nation-wide lockdown, which is due to end on Tuesday (14 April), while some state governments have decided to continue with the current restrictions until the end of this month. This imparts further downside risk to our forecast of a 5% GDP fall in the current quarter from a year ago. The market is waiting for the second stimulus package this week with targeted support for small businesses. And, today's consumer price data for March may be assessed for the easing options the Reserve Bank of India is left with after the 75 basis point emergency rate cut last month. We expect high food prices, amid a surge in demand, possible hoarding, and supply bottlenecks during the lockdown to sustain inflation above the RBI's 6% policy limit. Even so, we anticipate an additional 25-50bp rate cut in this quarter".

Author

Amrita Naik Nimbalkar

Junior Economist, Global Macro
amrita.naik.nimbalkar@ing.com

Alissa Lefebvre

Economist
alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific
Deepali.Bhargava@ing.com

Ruben Dewitte

Economist
+32495364780
ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee
kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands
marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic
420 770 321 486
david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing
sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China
lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist
michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland
michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Sector Economist, TMT & Healthcare

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist

samuel.abettan@ing.com

Franziska Biehl

Senior Economist, Germany

Franziska.Marie.Biehl@ing.de

Rebecca Byrne

Senior Editor and Supervisory Analyst

rebecca.byrne@ing.com

Mirjam Bani

Sector Economist, Commercial Real Estate & Public Sector (Netherlands)

mirjam.bani@ing.com

Timothy Rahill

Credit Strategist

timothy.rahill@ing.com

Leszek Kasek

Senior Economist, Poland

leszek.kasek@ing.pl

Oleksiy Soroka, CFA

Senior High Yield Credit Strategist

oleksiy.soroka@ing.com

Antoine Bouvet

Head of European Rates Strategy

antoine.bouvet@ing.com

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Edse Dantuma

Senior Sector Economist, Industry and Healthcare

edse.dantuma@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Rico Luman

Senior Sector Economist, Transport and Logistics

Rico.Luman@ing.com

Jurjen Witteveen

Sector Economist

jurjen.witteveen@ing.com

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Nicholas Mapa

Senior Economist, Philippines

nicholas.antonio.mapa@asia.ing.com

Egor Fedorov

Senior Credit Analyst

egor.fedorov@ing.com

Sebastian Franke

Consumer Economist

sebastian.franke@ing.de

Gerben Hieminga

Senior Sector Economist, Energy

gerben.hieminga@ing.com

Nadège Tillier

Head of Corporates Sector Strategy

nadege.tillier@ing.com

Charlotte de Montpellier

Senior Economist, France and Switzerland

charlotte.de.montpellier@ing.com

Laura Straeter

Behavioural Scientist

+31(0)611172684

laura.Straeter@ing.com

Valentin Tataru

Chief Economist, Romania

valentin.tataru@ing.com

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials

suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios

maarten.leen@ing.com

Maureen Schuller

Head of Financials Sector Strategy

Maureen.Schuller@ing.com

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Philippe Ledent

Senior Economist, Belgium, Luxembourg

philippe.ledent@ing.com

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

Inga Fechner

Senior Economist, Germany, Global Trade

inga.fechner@ing.de

Dimitry Fleming

Senior Data Analyst, Netherlands

Dimitry.Fleming@ing.com

Ciprian Dascalu

Chief Economist, Romania

+40 31 406 8990

ciprian.dascalu@ing.com

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content

+44 (0) 207 767 5331

owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM

+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com

ASEAN Morning Bytes

Market sentiment to remain jittery on virus concerns although Monday's focus maybe the oil deal



EM Space: Monday's focus may be on oil but Covid-19 will continue to dominate

- **General Asia:** The deal between major oil players will likely be the focus for Monday but investors will likely take their cue from developments related to the virus. Despite early and hopeful signs on the number of cases, infections and fatalities continue to mount across the globe and sentiment will continue to be affected by Covid-19 until we gain more clarity on the matter. In terms of data, market will likely be focused on reports out from China later in the week with GDP, retail sales and industrial production on deck.
- **Philippines:** Bangko Sentral ng Pilipinas (BSP) Governor Diokno indicated he would likely be lowering policy rates below 3% in the near term as the country continues to battle the virus. Previously, Diokno had pointed to 3% as a de facto floor or "normal rate" but he has since shown willingness to cut further to keep the economy afloat. Diokno will also cut reserve requirements by another 200 bps, possibly as early as this week to shore up liquidity in the financial market.
- **Indonesia:** After Indonesia implemented stricter social distancing guidelines in the country's capital last Friday, neighbouring towns of Bekasi, Depok and Bogor announced they are set to implement similar measures this Wednesday. Despite these measures, Indonesia's Jokowi remains defiant on implementing a full lockdown of the economy with the central

bank now forecasting GDP to dip to 2.4% with IDR gradually returning to the 15,000 level.

What to look out for: China data and Covid-19 developments

- Philippines money supply (13 April)
- Malaysia industrial production (13 April)
- Bank Indonesia policy meeting (14 April)
- China trade (14 April)
- Indonesia trade (15 April)
- Philippines remittances (15 April)
- US retail sales and industrial production (15 April)
- China home prices (16 April)
- US housing starts (16 April)
- Singapore non-oil exports (17 April)
- China GDP, industrial production and retail sales (17 April)

Author

Nicholas Mapa

Senior Economist, Philippines

nicholas.antonio.mapa@asia.ing.com

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Asia week ahead: How bad was 1Q20 for China's economy?

China's GDP report for the first quarter will provide some sense of the damage the pandemic has inflicted on economies in that part of the world



Source: Shutterstock

➔ China – 1Q20 report card arrives

While the economic data for March substantiates this view of the Chinese economy getting somewhat back on its feet, China's GDP report for the first quarter of the year due next week on 17 April will come as a testimony of the real dent to the economy due to the pandemic.

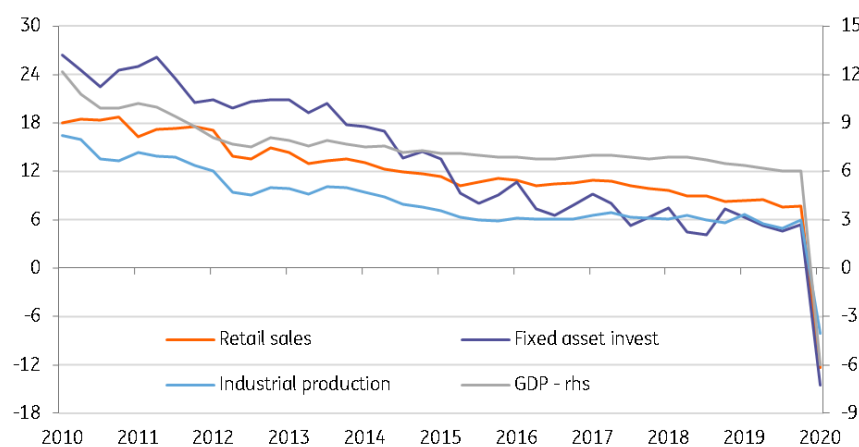
The consensus at the time of writing this is 6% year-on-year GDP fall, the country's worst performance in six decades. This is drawn out from expectations of continued contraction in key indicators – industrial production, retail sales and fixed asset investment, for which March data also

is due alongside the GDP release. In contrast, our Greater China Economist, Iris Pang, sees GDP growth staying in the positive territory, albeit a sharp slowdown to 3.6% YoY from 6% in 4Q19. This is based on her view that fiscal stimulus prevented a pronounced recession.

However, the key unknown here is a drop in overseas demand for Chinese goods, which with the ongoing global spread of the disease will remain a key drag on GDP growth for the remainder of the year. [Read here](#) what Iris thinks about China's recovery roadmap.

China draws a recovery roadmap

China: GDP and other key indicators (% year-on-year, quarterly data)



Source: Bloomberg, ING

Bloomberg consensus estimates for 1Q20.

➔ Rest of Asia – Trade figures, policy dominate

Trade figures from India, Indonesia and Singapore will be assessed for the Covid-19 impact. A sharp decline in exports is our base case, at least for India and Singapore with close to 20% YoY plunge, as movement restrictions depressed activity. Singapore's non-oil domestic exports will be a test of the resilient manufacturing in the first quarter with only 0.5% YoY fall in the advance GDP data for the quarter.

In India, the government is expected to announce additional stimulus for small businesses severely affected by the ongoing lockdown. The market talk is about \$13 billion (0.5% of GDP), taking the total stimulus to about 3.2% of GDP which is no comparison to the 10-20% figure, we've seen in some other Asian countries. We don't think it will make much of a difference to the economy. We expect GDP growth to fall by as much as 5% YoY in the current quarter, but we won't rule out more too.

Meanwhile, India's consumer price data for March may be scrutinised for the easing options the Reserve Bank of India is left with after the 75 basis point emergency rate cut last month, which was despite high inflation above the RBI's 6% policy limit. We expect high food prices, amid a surge in demand, possible hoarding, and supply bottlenecks during the lockdown to continue to exert upward pressure. This counter disinflationary effect of falling global oil price on utility and transport

components. That said, we don't see inflation stopping the RBI from cutting rates again. We anticipate an additional 25-50bp rate cut in this quarter.

Will Indonesia's central bank cut rates at the next policy meeting? We're not forecasting one, but won't be surprised if we get another 25bp cut from the current 4.5%. Weak currency with over 13% year-to-date depreciation, the most in Asia, complicates BI policymaking when the economy is demanding greater policy accommodation.

Country	Time Data/event	ING	Survey	Prev.
Monday 13 April				
India	1300 Mar CPI (YoY%)	6.3	5.92	6.58
Malaysia	0500 Feb Industrial production (YoY%)	-	1.2	0.6
Tuesday 14 April				
China	- Mar Exports (YoY%)	-4.15	-14	7.9
	- Mar Imports (YoY%)	-4.0	-9.8	16.5
	- Mar Trade Balance (US\$bn)	30	19.44	47.294
India	0730 Mar WPI (YoY%)	2.3	1.33	2.26
Indonesia	0820 Apr 14 BI policy decision (7-day reverse repo, %)	4.5	4.25	4.5
Wednesday 15 April				
India	- Mar Trade deficit (US\$bn)	-7.2	-7000	-9850
	- Mar Exports (YoY%)	-18	-	2.91
	- Mar Imports (YoY%)	-22	-	2.48
Indonesia	0500 Mar Trade balance (US\$mn)	718	900	2335.9
	0500 Mar Exports (YoY%)	-1.6	-6	11
	0500 Mar Imports (YoY%)	-2	-4.8	-5.11
Philippines	- Feb OCW remittances (YoY%)	3.1	3.1	6.6
Thursday 16 April				
China	0230 Mar New home prices (YoY%)	5.5	-	0.02
Friday 17 April				
China	0300 1Q GDP (YoY%)	3.6	-6	6
	0300 1Q GDP (Q) (QoQ% SA)	-17	-9.75	1.5
	0300 Mar Industrial Production (YoY%)	-5	-5.4	6.9
	0300 Mar Retail Sales (YoY%)	3	-10	8
	0300 Mar Fixed asset investment (YTD, YoY%)	5	-15	-24.5
Singapore	0130 Mar Non-oil domestic exports (MoM%/YoY%)	-26/-21	-3.7/-1.7	-4.8/3
S Korea	0000 Mar Unemployment rate (% SA)	-	-	3.3

Author

Amrita Naik Nimbalkar

Junior Economist, Global Macro

amrita.naik.nimbalkar@ing.com

Alissa Lefebvre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Sector Economist, TMT & Healthcare

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist

samuel.abettan@ing.com

Franziska Biehl

Senior Economist, Germany

Franziska.Marie.Biehl@ing.de

Rebecca Byrne

Senior Editor and Supervisory Analyst

rebecca.byrne@ing.com

Mirjam Bani

Sector Economist, Commercial Real Estate & Public Sector (Netherlands)

mirjam.bani@ing.com

Timothy Rahill

Credit Strategist

timothy.rahill@ing.com

Leszek Kasek

Senior Economist, Poland

leszek.kasek@ing.pl

Oleksiy Soroka, CFA

Senior High Yield Credit Strategist

oleksiy.soroka@ing.com

Antoine Bouvet

Head of European Rates Strategy

antoine.bouvet@ing.com

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Edse Dantuma

Senior Sector Economist, Industry and Healthcare

edse.dantuma@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Rico Luman

Senior Sector Economist, Transport and Logistics

Rico.Luman@ing.com

Jurjen Witteveen

Sector Economist

jurjen.witteveen@ing.com

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Nicholas Mapa

Senior Economist, Philippines

nicholas.antonio.mapa@asia.ing.com

Egor Fedorov

Senior Credit Analyst

egor.fedorov@ing.com

Sebastian Franke

Consumer Economist

sebastian.franke@ing.de

Gerben Hieminga

Senior Sector Economist, Energy

gerben.hieminga@ing.com

Nadège Tillier

Head of Corporates Sector Strategy

nadege.tillier@ing.com

Charlotte de Montpellier

Senior Economist, France and Switzerland

charlotte.de.montpellier@ing.com

Laura Straeter

Behavioural Scientist

+31(0)611172684

laura.Straeter@ing.com

Valentin Tataru

Chief Economist, Romania

valentin.tataru@ing.com

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials

suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios

maarten.leen@ing.com

Maureen Schuller

Head of Financials Sector Strategy

Maureen.Schuller@ing.com

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Philippe Ledent

Senior Economist, Belgium, Luxembourg

philippe.ledent@ing.com

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

Inga Fechner

Senior Economist, Germany, Global Trade

inga.fechner@ing.de

Dimitry Fleming

Senior Data Analyst, Netherlands

Dimitry.Fleming@ing.com

Ciprian Dascalu

Chief Economist, Romania

+40 31 406 8990

ciprian.dascalu@ing.com

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content

+44 (0) 207 767 5331

owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM

+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com

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OPEC+ deal: Not so fast

The OPEC+ alliance has agreed to cut oil output by 10MMbbls/d starting in May, however, this is conditional on Mexico accepting its allocated cut. So far, they don't appear willing, and until there is a concrete deal our price forecasts remain unchanged



Source: Shutterstock

President of Mexico Andres Manuel Lopez Obrador, Mexico City

Big cuts are coming... but how big?

Surprisingly OPEC+ managed to agree on sizeable production cuts, with the plan to cut oil output by 10MMbbl/s for two months starting in May. These cuts will then be reduced to 8MMbbls/d from July through until the end of this year, and then finally from January 2021 through until the end of April 2022 the group will cut by 6MMbbls/d. The group will next meet on 10 June to decide if any further action needs to be taken.

The reference for cuts would be October 2018 production, whilst for Saudi Arabia and Russia, their baseline for cuts will be 11MMbbls/d. Iran, Libya and Venezuela once again will be exempt from the deal.

The key issue holding up the deal at the moment seems to be the fact that the Saudis are keen on Mexico cutting their share

This deal is conditional on Mexico agreeing on its allocated cut. Under the deal they would need to cut by 400Mbbls/d, however, they are only willing to cut by 100Mbbls/d. While the US has said it would make up for the shortfall from Mexico through organic declines, it does seem as though the Saudis are keen on Mexico cutting by their share. This seems to be the key issue at the moment holding up the deal.

Assuming that Mexico finally agrees, or others agree to the US making up for Mexico, it is important to point out that this is not a 10MMbbls/d cut from 1Q20 levels. Given that output was higher during the reference month for this deal, the effective cut from 1Q20 levels is more in the region of 7MMbbls/d over May and June, and then around 5MMbbls/d for the remainder of the year. So while the cuts are significant, they are not as big as the headline numbers suggest, and therefore not as bullish as one would imagine.

What are the issues with deal?

The biggest issue is that this deal is still conditional on Mexico joining, something that OPEC+ is still working on. If Mexico refuses to cut its share by 400Mbbls/d, it does look as though the US is willing to make up for the Mexican shortfall with their organic declines. Meanwhile, if Mexico was to pull out of the deal, it shouldn't be too difficult to allocate their cut among the remaining members, given it is just 400Mbbls/d of cuts initially.

The next issue comes down to compliance. The bigger the cuts, the larger the risk we see some producers falling short of their quota such as Iraq

The other problem is that OPEC+ have taken too long to get to this point. Cuts are set to only start in May. The issue is that we are seeing significant levels of demand destruction right now - and these cuts are still falling short of bringing the market to balance over 2Q20. So we are still set to see a sizeable inventory build over the quarter, which should keep the market at depressed levels.

The next issue comes down to compliance. The bigger the cuts, the larger the risk we see some producers falling short of their quota. Iraq failed to comply with its quota under the previous deal altogether, and under this new deal, they have agreed to cut by around 1MMbbls/d over May and June. Clearly, given Iraq's performance with the previous deal, the market cannot have much confidence that they will comply with these cuts.

What about other oil producers?

After the OPEC+ meeting, G20 energy ministers also met, and expectations were that we would see an additional 5MMbbls/d of cuts from other producers to help bring the market to balance. However, the communique from the G20 meeting fails to mention any cuts from other producers. Instead, there were promises "to take all the necessary and immediate measures to ensure energy market stability."

While we may see some mandated cuts from other producers, it appears that the bulk of the decline in output will be market-driven rather than mandated.

The US energy secretary believes that US output could fall by 2MMbbls/d by the end of 2020, while the US Energy Information Administration's latest short-term energy outlook forecasts that US oil output in December will be around 1.6MMbbls/d lower than March estimates. Output declines from the US will be gradual rather than immediate, and so not offering as much relief in the very near term.

Author

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Australian QE: A premature tapering?

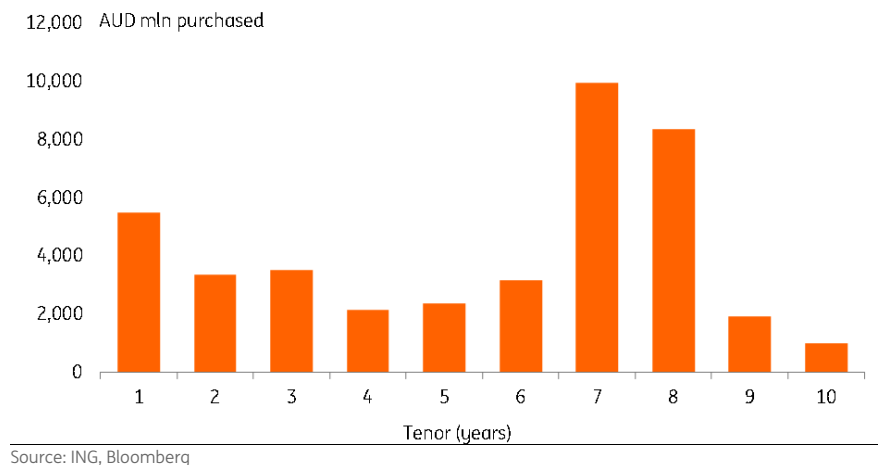
After hinting at tapering if conditions improve, Australia's central bank actually trimmed its daily bond-buying today. However, an excessive steepening of the yield curve may act as a deterrent to unwinding QE. Looking at AUD, we're not convinced the recent rally is an initiation of a sustained recovery just yet



Impact on the yield curve so far

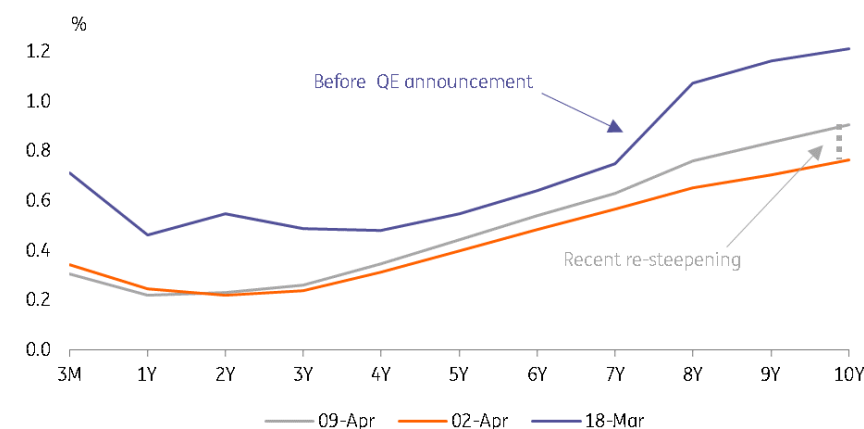
Since announcing a yield-curve-control scheme (keeping the 3-year yield at 0.25%) on 19 March, the Reserve Bank of Australia has purchased AUD 41.5 bn of government bonds on the secondary market. The breakdown of the bond purchases in terms of maturities (Figure 1) shows the Bank has intervened in various segments of the curve, especially in the 7- 8-year tenors.

Fig. 1 - Breakdown of RBA bond purchase by tenor



Whilst largely succeeding in keeping the 3-year yield at the 0.25% target, the whole AU yield curve has understandably shifted lower since the start of the bond purchase scheme (Figure 2). Looking at the slope of the yield curve, an initial fierce steepening around the QE announcement was followed by some stabilisation in the 10Y-2Y differential.

Fig. 2 - Australian sovereign yield curve (before and after QE)



However, the curve has started to steepen again in the past few days. This has largely been the result of the more upbeat global risk sentiment and consequent UST 10-year underperformance. However, the RBA policy statement on 7 March has likely come into play too lifting Australian 10-year yields as the central bank surprisingly hinted at some tapering “if conditions continue to improve”.

RBA trimming bond purchases

With only three weeks into the QE programme and – above all – with still little material evidence of the actual economic impact of Covid-19 on the global (and Australian) economy, the prospect of

tapering may look a bit premature.

It must be noted that tapering likely poses a risk of an extreme steepening of the yield curve

However, the RBA seemed to put words into action today and made the smallest daily purchase of securities so far: AUD 1.5 bn. Surely, we would need to see a trend in lower purchases to conclude the Bank is actually starting to unwind its QE scheme. Next week is likely to be crucial in this sense.

It must be noted that tapering likely poses a risk of an extreme steepening of the yield curve, especially if global risk sentiment keeps improving and US 10-year yields rise. The central bank may stick to its stated objective to control the short-end of the curve (also given the limited ability to control the UST-driven back-end), but recent buying of longer-dated bonds suggest that the Bank may not be entirely at ease with surging back-end yield.

This is understandable considering that supply is set to pick up soon as the government builds debt to finance its anti-pandemic fiscal stimulus plan.

AUD: Don't get too excited

The recovery in risk sentiment, accompanied by the hawkish wording in the RBA statement set the AUD for a substantial rebound this week. If indeed the RBA is determined to scale back its bond purchase, this would inevitably provide additional steam to the AUD.

However, we are still not convinced that the recent rally is an initiation of a more sustained recovery just yet. And this is largely because, despite the encouraging signals in terms of slowing contagion in Europe, lingering uncertainty around the depth of the upcoming global recession suggests a big deal of caution when betting on procyclical currencies.

Looking more specifically into AUD, a plunge in trade flows and a slowdown in Chinese demand doesn't bode too well for the export-dependent Australian economy, which may see the impact of the Covid-19 extending well beyond the lockdown-related disruptions. Commodity prices may also remain quite depressed, in particular iron ore (Australia's main export), whose price prospects were already gloomy on the back of an increase in supply from Brazil.

Finally, it is important to remember how the AUD has historically been the key shock absorber in turbulent times for the Australian economy, which suggests the RBA (and, even more, the government) may not be content with a large recovery in AUD as the country deals with the big hit. While direct FX interventions don't seem to be on the cards just yet, an appreciating AUD may be another disincentive to scale back QE.

As the USD appears to be bearing most of the brunt for the fall in risk aversion, we still expect defensive currencies JPY and EUR to be a safer bet than the procyclical currencies such as AUD in the near future.

Author

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

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