Good MornING Asia - 17 June 2021

With the Fed putting the world on notice that it is not asleep at the wheel, expect markets to be a lot less range-bound than they have been

In this bundle

Asia's response to a more hawkish fed

With the Fed putting the world on notice that it is not asleep at the wheel, expect markets to be a lot less range-bound than they have been

Fed Chair, Jerome Powell

Wake up, smell the macro

Today's essential reading can be found on this link - covering the Fed decision, and market reaction. Do please take the time to read it. It will be more useful than my rant below.

The last few months have been extremely frustrating. The macro story in the US (and Europe) has unfolded even more strongly than forecast, with stronger growth and higher inflation, and yet financial markets have been content to have their direction dictated to them by the Fed's guidance, which now turns out to have been inaccurate and overly dovish.

Talk of transitory inflation has only ever looked like a partial explanation of what is going on in the US (and globally) and has raised questions like, "how long exactly is transitory?" This is not the first time we have seen markets behaving like this. But since the global financial crisis, I would say that markets have been far too willing to just wait and react to what they are told to believe by central banks, and have done far less thinking and forward-looking for themselves. Strong growth, bottlenecks in labour supply, high inflation - this stuff all screamed "higher rates and sooner". But it has taken the Fed to tell markets how to think for them to respond appropriately.

I guess this is the by-product of reliance on "forward guidance". But it is worth remembering that central banks do not have perfect foresight, and they have a vested interest in trying to massage markets in a favourable direction, which, when it proves wide of the mark, results in an inevitable spike in volatility as markets catch up with reality. We appear to be experiencing a small dose of that today. There could be more to come if markets pay a little more attention to macro than they have been doing. Bottom line, there is still a job for economists with a critical eye...!

It is also interesting and noteworthy to see markets break out of the ranges they have been stuck in for the last couple of months - the EURUSD break on the downside is perhaps most noteworthy, and has reflected in Asia space in a big weakening in the KRW - the region's proxy currency. So far, equity moves have been quite modest. But if we are to see a larger shift to a risk-off position, we can expect more of this, with the KRW likely joined by the IDR, though all but the JPY will likely be hit to some extent if this is the direction markets travel.

The AUD and NZD were also both hit hard overnight - though the NZD less so - helped this morning by a strong 1.6%QoQ 1Q21 GDP figure, which lends support for expectations for a more hawkish RBNZ. The RBA's Governor, Philip Lowe, is speaking as I write, ahead of the labour market data released at 09:30 SGT. We will write that up later if it is worth comment.

Asia today

In Asia today we have a reasonably busy calendar with some central bank (in)action. But before that, we already had Singapore's May non-Oil domestic exports, which delivered a disappointing 8.8%YoY increase off the back of a 0.1% MoM decline. Electronic exports did manage to maintain an 11%YoY pace of growth. But there is nothing in this release to threaten the Monetary Authority of Singapore's current stance (neutral path) on the nominal effective rate for the Singapore dollar when it formally considers this again in October.

Bank Indonesia meets today, and will not be changing their 7-day repo official policy rate, though we may need to consider nudging the timing for their first hike next year against this more hawkish Fed backdrop. sooner than we had thought is the likely forecast change.

And Taiwan's central bank will also not change its official policy rate today, though may set out what support measures it will undertake should the current Covid wave worsen.

Author

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

Alissa Lefebre
Economist
alissa.lefebre@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.schroder@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

Article | 17 June 2021

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ASEAN Morning Bytes

Asian markets likely to react to the adjustment to the Fed hike timeline

EM Space: EM markets likely to react to acceleration of Fed rate hike timeline

- **General Asia:** Asian markets will likely react to upgraded economic projections and the change in the Fed's rate hike timeline. With the Fed bringing forward rate hikes into 2023, bond yields in the EM space will likely track the move in US treasuries overnight with currencies also likely coming under pressure on Thursday. Several central banks are scheduled to meet in the coming days with monetary authorities in Indonesia, Taiwan and Japan to discuss policy.
- **Singapore:** Non-oil domestic export growth of +8.8% YoY (-0.1% MoM) was a disappointment for the markets looking for nearly double that pace (ING forecast 19.9%), though it was still a slight pick from 6% YoY rise in April. The low base effect held year-on-year growth in positive territory. But, the second consecutive month-on-month fall (following -8.8% MoM in April) reflects a possible pause in the export-led recovery as the Covid-19 second wave struck the economy via tighter restrictions on activity. On a more positive note, the key NODX driver of electronics held on to its strength (up 11% YoY and 6.4% MoM). Pharmaceuticals clawed back part of their 24% MoM April fall with a 15% MoM bounce in May, though that was still not enough to pull year-on-year growth into positive territory (-18% YoY). We remain hopeful that the post-pandemic recovery in global demand

will support Singapore's NODX recovery during the rest of this year. Nothing as yet warrants any change to the Monetary Authority of Singapore's zero S$-NEER appreciation policy in the next policy review in October 2021.

- **Indonesia:** Bank Indonesia will likely keep policy rates untouched at its policy meeting today as Governor Warjiyo continues to focus emphasis on currency stability even as inflation stays below the central bank's target range. The IDR has come under pressure over the past couple of trading sessions ahead of the Fed policy meeting and will undoubtedly come under pressure again after the Fed signalled an earlier than expected tightening cycle. Thus we expect BI to keep policy rates unchanged in the near term to balance out the need to support the currency and to provide monetary support for the economic recovery. Meanwhile, we do not rule out BI bringing forward its own tightening cycle should IDR come under extreme pressure in the coming months with Warjiyo intent on maintaining FX stability.

What to look out for: US initial jobless claims and Covid-19 developments

- Bank Indonesia policy meeting (17 June)
- Taiwan CBC policy meeting (17 June)
- US initial jobless claims (17 June)
- Bank of Japan policy meeting (18 June)

Author

Nicholas Mapa
Senior Economist, Philippines
nicholas.antonio.mapa@asia.ing.com

Snap | 16 June 2021 China

China: Covid, autos and chip shortages hit May activity data

The combined hit from Covid, chip shortages and weak auto sales hit investment, production and retail sales in May. This will continue into June

Source: Shutterstock

Visitors observe various kinds of chips are exhibited at different booths by semiconductor companies at the 18th China International Semiconductor Expo, Shanghai, China

Cars hit retail sales, not Covid

The timing of the Covid resurgence in China is important. Though retail sales slowed down to 12.4% year-on-year in May from 17.7% a month ago, this was mainly due to very slow growth in car sales of 6.3% YoY. Other sales items were largely unscathed by this new wave of the virus, which came after the Golden Week holiday in the first week of May. As such, jewellery sales grew 31.5% YoY.

Industrial production sees double whammy from Covid and automobiles

In Guangdong province, an area which specialises in electronic manufacturing, Covid cases peaked at around 20 cases per day, but this was enough to hit industrial production, which grew 8.8% YoY in May, down from 9.8% YoY in April. Workers lined up for testing and some local areas were locked down to stop the virus from spreading. Moreover, automobile production contracted by 4% YoY due to a lack of chips.

Later this month, we will also see the hit from Covid on China's exports and imports.

Cars, again, hit investment

From the detailed breakdown of the fixed asset investment data, it seems that Covid did not affect fixed asset investment too much, with growth of 15.4% YoY in May from 19.9% YoY a month ago. The slower growth of the headline number was mainly a result of a 3.7% YoY year-to-date contraction in automobiles. It is now clear just how much chip shortages have hit the automobile industry.

Other important areas of fixed asset investment, e.g. transportation equipment and computers, continued to grow at 34.2% YoY YTD and 27.6%YoY YTD, respectively.

In short, it seems that only automobiles have been affected by chip shortages so far.

What to expect from the June data and our GDP forecast

Covid affected two weeks of activity in June and while this has now subsided, restrictions on movement will continue to be tight for the whole of June and will be gradually relaxed from there. So Covid will impact June's activity data.

Chip shortages are now an obvious problem for the automobile industry. We will closely monitor the impact of this on other industries, such as the production of smartphones and other consumer devices because sales of these items should pick up as US and Europe starts to recover from Covid and the summer shopping spree is on the way.

We maintain our forecast for China GDP at 8.7% for 2021.

Author

Iris Pang
Chief Economist, Greater China
iris.pang@asia.ing.com

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