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Good MornING Asia - 17 March 2020

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EM Space: Governments close borders in an attempt to slow Covid-19

- **General Asia:** The panic selling in global markets persists as coordinated central bank action failed to calm investors worried about a deeper economic slump due to Covid-19. The Fed's second round of emergency easing over the weekend sent a worrying message for the markets. It also sent its global peers into a fire-fighting mode. However, the main worry seems to be the central banks running out of policy space needed to combat the impact of the virus. And this now calls for a coordinated fiscal response by the governments.
- **Singapore:** The economic data is yet to reveal the Covid-19 impact. Released this morning, non-oil domestic exports surprised with a 3% YoY growth in February, beating the consensus of about 7% fall in the month. Electronics was a source of upside miss in the headline; a 2.5% growth was the first positive in over a year and in stark contrast to the consensus of 17% YoY fall. Pharmaceuticals also helped with strong gains. This leaves NODX in the first two months almost flat at the level a year ago. We believe the Monetary Authority of Singapore will see through the positive data and join the global central bank easing bandwagon.
- **Malaysia:** The government announced a two-week lockdown to contain the spread of Covid-19 as new infection almost doubled to 566 in the last two days. Prime Minister

Muhyiddin also announced additional financial support for people to cope with the situation, including cash handout for low-income households and workers on unpaid leave, discounts on utility bills, etc. This is on top of a 20 billion ringgit (1.3% of GDP) stimulus program announced earlier to bolster the economy. We believe a 50bp Bank Negara policy rate cut is imminent and expect it to be way ahead of the next meeting on 4-5 May.

- **Indonesia:** Bank Indonesia (BI) indicated that it was not inclined to conduct an emergency meeting ahead of its scheduled 19 March decision although given the moves of central banks we now expect BI to be open to cut policy rates by at least 25bp. The previously reluctant central bank may opt to bolster the economy as the number of cases in Indonesia continues to rise rapidly. If the IDR remains severely pressured, BI may opt instead to reduce the reserve requirements while looking to the two fiscal packages unveiled by Minister Indrawati to support the economy.
- **Philippines:** Bangko Sentral ng Pilipinas (BSP) Governor Diokno ruled out resorting to emergency action with the BSP set to decide on monetary policy on 19 March. Diokno did, however, telegraph a possible 50bp rate cut, upsizing his previous hint for only a 25bp. Meanwhile, the national government announced a lockdown of the northern island of Luzon, including the capital Manila, which taken together accounts for 74% of economic output. The 30-day enhanced quarantine with businesses shuttered and economic activity halted will likely force GDP growth in the first half of the year to slide below 5%.

What to look out for: Covid-19 developments and central bank action

- RBA policy minutes (17 March)
- US retail sales and industrial production (17 March)
- US housing starts (18 March)
- Australia jobs report (19 March)
- New Zealand 4Q19 GDP (19 March)
- Philippines BSP policy meeting (19 March)
- Indonesia BI policy meeting (19 March)
- Taiwan policy meeting (19 March)
- US initial jobless claims (19 March)
- US existing home sales (20 March)

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An appalling set of activity data

The impact of Covid-19 on the Chinese economy has been extremely damaging, effectively bringing the country to a standstill. Almost all the available resources have been pulled in to save lives and contain the spread of the virus.

Industrial production fell 13.5% year-on-year year-to-date, fixed asset investments fell 24.5% YoY YTD and retail sales fell 20.5% YoY YTD. Industrial output was not as bad as fixed-asset investment and retail sales because there was still iron, steel, and copper production in February, otherwise, it would have been a lot worse than reported.

There is nothing in the history of this data to compare to this set of abysmal figures.

Recovery depends on the global spread of Covid-19

China is now at the recovery stage from the coronavirus but the global spread means that the economy is not going to recover fully anytime soon.

Investment might recover faster than retail sales and industrial production because the government has promoted "new infrastructure" investment to boost economic growth to support the recovery. So fixed asset investment in the coming months should rise from negative growth.

Retail sales have recovered only very slowly as consumers are still wary about going into shopping malls and restaurants. This could continue as there are some imported Covid-19 cases in major cities.

Industrial production will continue to be hit in March and April as the spread of Covid-19 in almost all countries means global demand will stop abruptly, and global supply chains will still be broken as factories around the world suspend operations. We are not optimistic about China's manufacturing and exports.

Downgrade GDP and yuan forecast

We have downgraded China's GDP and yuan forecasts just now. You can read about that here.

Forecasts on GDP and USD/CNY for 1Q20 are 3.6%YoY and 7.20, respectively.

Philippines’ central bank may double down on rate cuts, and soon

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The Diokno double down

BSP Governor Benjamin Diokno had previously signalled his intention to cut policy rates by 50 basis points in 2020 to gradually bring lending rates to more “normal levels”. The market had previously priced in a 25bp rate cut at the 19 March meeting but events have quickly overtaken this forecast with the national government imposing a “community quarantine” in the capital Manila, and the Federal Reserve dropping the Fed funds target range by 100bp over the weekend. With several Asian central banks holding meetings this week, will the BSP follow suit with aggressive policy action?

In an interview on Monday morning, Diokno signalled that a 25bp cut was all but a done deal while hinting at potentially more aggressive action. In light of this, we now expect the BSP to slash the policy rate by at least 50bp to help cushion the economy from the adverse impact of the virus, while the inflation outlook is softening further amid a plunge in global crude prices.

Bring out the heavy artillery

Diokno did share previously that targeted fiscal stimulus would be more effective to counter the slowdown in economic activity, however pending legislation for the supplemental budget for medical supplies (HB 6177 worth $30 million) and a Covid-economic rescue package (HB 6606 worth $2.1 billion) we believe BSP will act to deliver its own monetary stimulus by accelerating its rate cut plans. BSP will likely slash borrowing costs by 50bp to help stimulate growth while also making liquidity available via possible reductions to the reserve requirement (RR) or reductions to the volume of its term deposit facility. Such moves will complement existing facilities such as the peso rediscounting and dollar rediscounting windows to help banks manage their cash flows.

Given the size and scope of the impending economic slowdown and financial market stress from the Covid-19 outbreak, we cannot rule out a possible "all-in" scenario where Diokno slashes policy rates by 75bp and or advances the policy decision even before the scheduled 19 March meeting.

Despite the potential aggressive easing from the BSP, the local bond market may react more to global developments while the peso will face only mild depreciation pressure with the Philippines still viewed by investors as the economy to be least affected by Covid-19 relative to peers in the region.

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