

## Good MornING Asia - 24 July 2018

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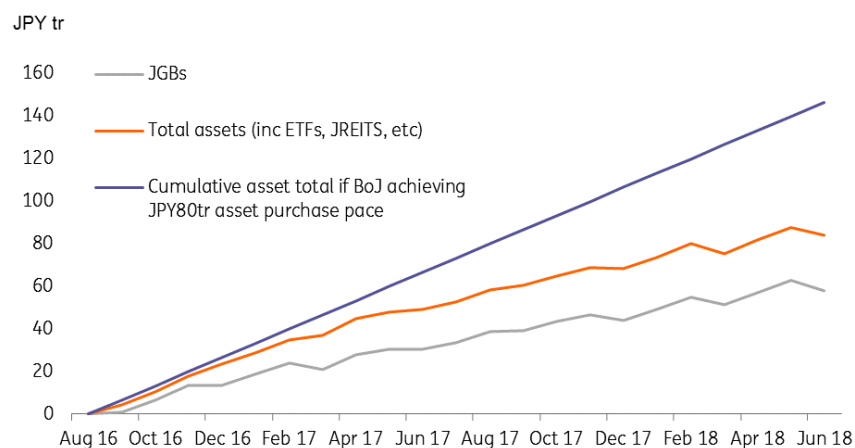
# Stealth normalization

Of all the market moves in the panoply of markets forecasts, I bet few had anticipated a global yield curve steepening, driven by a long-tenor JGB sell-off. This is unlikely to last. The next Bank of Japan rate meeting is on 31 July.



Source: istock

## BoJ Asset purchases - cumulative, compared to JPY80tr target pace



Source: CEIC, ING

## This is only a market squeeze, unless the BoJ delivers next week

Honestly, I didn't imagine I would be talking about the Bank of Japan (BoJ) as the lead story in one of my daily rambles when I pre-wrote my monthly Japan economic update at the end of last week (pre-wrote as am heading off on vacation for 2-weeks). There had been some chatter about a change in policy following the April meeting's omission of any reference to meeting the 2% inflation target by 2019. That should not have startled anyone. The lowest forms of animal life on the planet stopped believing the BoJ's inflation target some years ago.

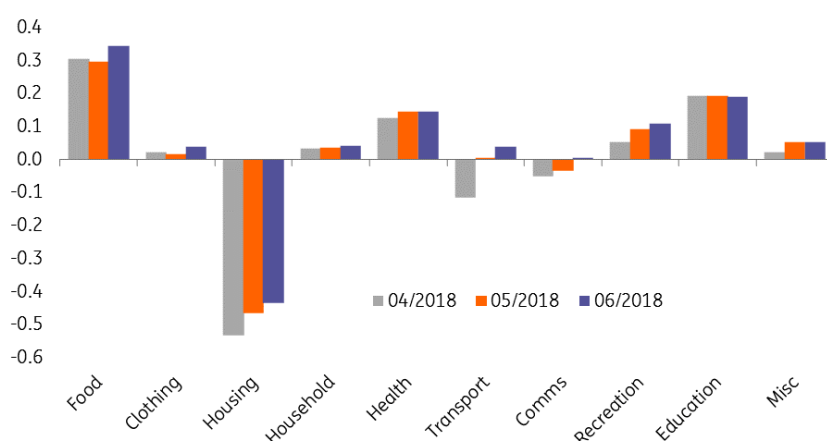
But somehow, the story seems to have lingered. Japanese newspapers have been carrying stories talking about the possibility of an (unspecified) change in the BoJ's policy stance on 31 July.

I don't see it myself. The BoJ is known for its so-called "kite-flying" exercises. As the mere rumour of a policy change has sent 10Y Japanese Government Bond (JGB) yields soaring above 0.1% (last seen early Feb this year - so not exactly an unprecedented level), the likelihood of them following through with any concrete change in policy is, in my opinion, extremely low.

I certainly don't think abandoning, or amending the BoJ policy targets, including inflation, are on the table. But the official pace of asset purchasing might be. As the BoJ is consistently under-buying assets compared to its stated pace of about JPY80tr per annum, a low-cost move might be to simply officialize this under-buying at its current rate, approximately JPY45tr p.a. Should the BoJ wish to moderate its stimulus still further, it can covertly lower its actual asset purchasing still further, say to JPY25tr, or some other rate consistent with maintaining JGB yields "close to" zero., Even this "close to" can get diluted over time. If markets get used to 0.1% as meaning "close to zero" then in time that will become the new zero, just as JPY45tr has become the new JPY80tr.

"Stealth normalization" - clever huh? The same notion as boiling a frog by slowly heating up the water, The frog doesn't notice. This apparently is untrue, however. Please don't boil frogs or any other amphibians.

## Contributions to YoY% Singapore CPI growth

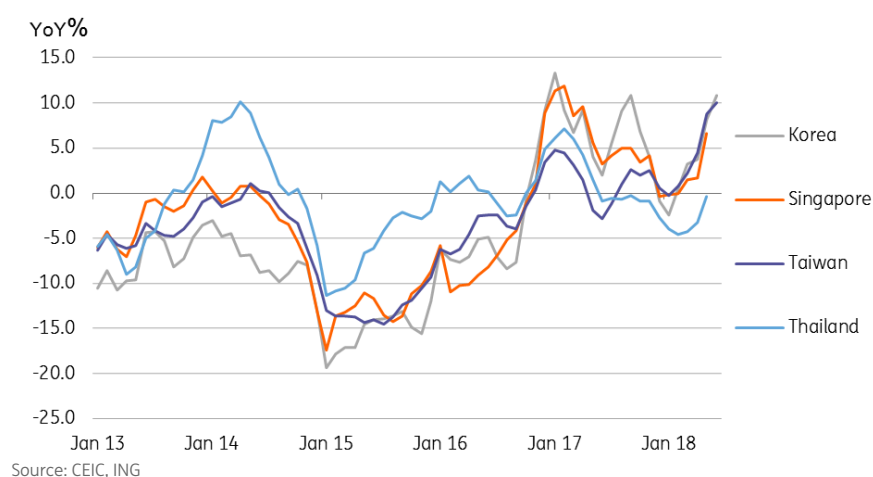


## The downside of a weaker currency - higher inflation, weaker domestic growth

Singapore's headline inflation nudged up to 0.6%YoY in June, but the core rate rose too, now

reaching 1.7%YoY, a considerably stronger result than had been expected, The cause? Well a breakdown of the components of Singapore's CPI shows that basically everything is either slightly more positive, or slightly less negative. It wouldn't surprise us to find that the SGD's recent USD weakness had led to some import of inflation. Singapore's import price inflation is now running a little over 6.5%YoY. 3 months ago, it was less than zero. It isn't just Singapore. This is an Asia-wide phenomenon. And it has implications. Central Banks may respond with tighter policy relative to the counterfactual of stable currencies. I don't anticipate the MAS tightening their nominal effective currency target path further in October as a result. But higher inflation might prevent them from reversing their April 2018 tightening decision.

## Asian Import Price inflation rising on weaker currencies



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Article | 23 July 2018

## Taiwan: Revising currency and GDP forecasts on trade war worries

Taiwan's industrial production surprised on the downside on both a monthly and yearly basis. This could suggest that manufacturers are cautious about maintaining inventory during a possible trade war. We are revising GDP down to 2.4% in 2018 from a previous forecast of 2.6% and expect USD/TWD to depreciate to 31.00 from a previous forecast of 30.6



Source: Shutterstock

### Manufacturing activity dims

Manufacturing activity slowed even before bilateral tariffs between Mainland China and the US were imposed on 6 July.

While Taiwan could win some orders from the substitution of Mainland products (for example, electrical machinery), manufacturers could be hit by a fall in global demand if the trade war intensifies.

We therefore revise our GDP growth forecast downward to 2.4% in 2018 from 2.6%, and USD/TWD to 31.00 from 30.6 (spot 30.64).

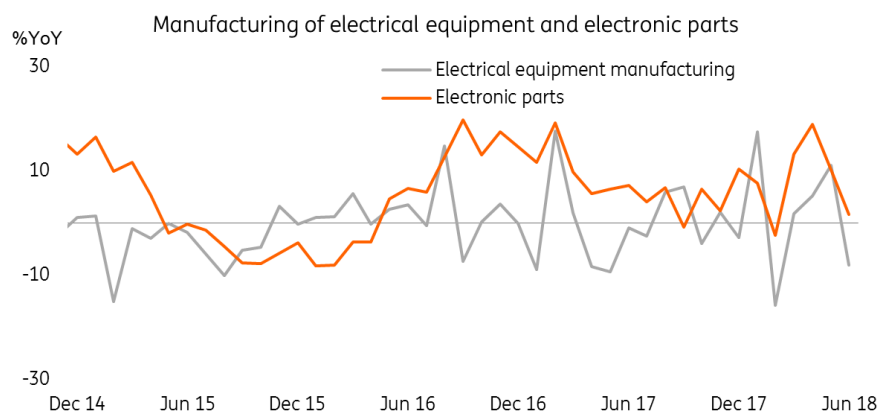
**-3.5%**

Taiwan industrial production MoM down from 8.2% MoM in May

0.36% YoY in June from 7.61% in May

Lower than expected

## Taiwan's electronic-related production growth dims



Source: ING, Bloomberg

## Manufacturers should be de-stocking

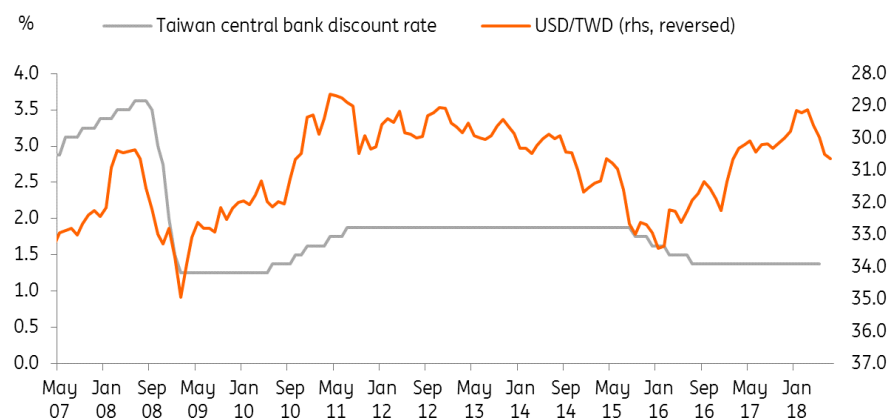
Manufacturing activity fell to 0.36% year-on-year from 7.61%, though the drop was partly a result of the high base effect last year. The monthly data also pointed to negative growth (-3.5% MoM) for all manufacturers except for tobacco, other transport equipment and those involved in the repair and installation of industrial machinery, who posted the strongest monthly growth. The data suggests that manufacturers have been cautious about building up inventories. They could be using inventories before increasing production.

## Taiwan's central bank can do little but TWD can weaken further

Taiwan's central bank is in a difficult position if it's considering an interest rate cut, as the level of its current policy rate is 1.375%. If the economy faces a further downturn, there's little room for additional cuts. We believe the central bank will likely save its bullets for a more severe economic environment, which is why we expect it to stay put.

Still, this doesn't mean the Taiwan dollar can't weaken against the US dollar. Unless the USD were to weaken amid a tit-for-tat trade war, the TWD together with other Asian currencies would likely weaken further. So we revise USD/TWD to 31.00 at end 2018 (spot 30.64).

## Taiwan central bank has little room to cut rate



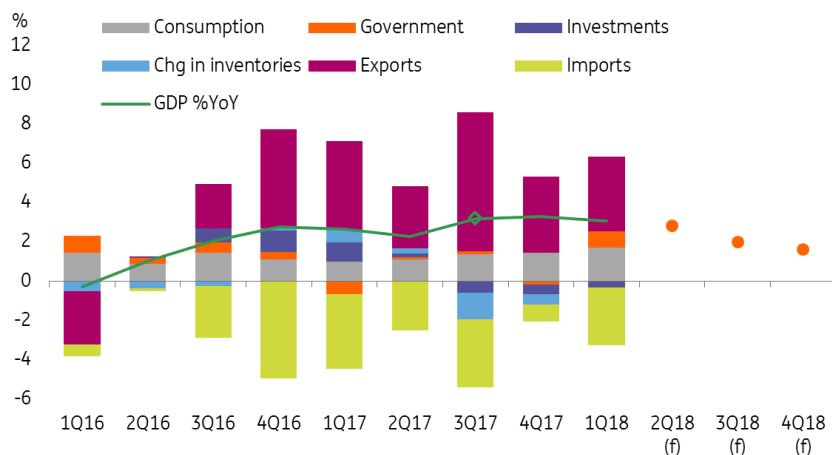
Source: ING, Bloomberg

## With little fiscal and monetary power, GDP growth will slow

As a small and open economy, Taiwan is subject to volatility in external demand. The bilateral trade war between Mainland China and the US is likely to lead to a fall in global demand. It is just a matter of time. And today's industrial production data sends a signal that the economy is fragile in the face of such a trade war.

We are therefore revising our GDP growth forecast for Taiwan to 2.4% in 2018 from our previous forecast of 2.6%.

## Taiwan relies on exports to grow



Source: ING, Bloomberg

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