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USD weakness can be helpful for Asian economies, but there is a limit

In this bundle

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End of an era

US Treasury Secretary Mnuchin discards strong dollar policy

ripped dollar

The genie is now out of the bottle

US Treasury Secretaries have had a difficult time convincing markets that they were real advocates of the strong dollar policy. Hank Paulson had his work cut out to persuade markets, and even then many interpreted his remarks as being more in keeping with an "appropriately priced market-determined " dollar policy. Tim Geithner, early on in his Treasury career also had a few stumbles, and had to do a fair bit of back-pedalling to get markets back onside.

The problem is, of course, that once you tell markets that you are not really bothered about the value of your currency because it is expedient at the time to take that attitude, the cost of persuading them otherwise, should this be what you need in the future, is magnified many times.

The current US Treasury Secretary, Steven Mnuchin, let the Genie out of the bottle at Davos yesterday when he suggested that a weak dollar is actually good news, as it supports US trade. The USD decline was already well established, so Mnuchin's comments were pushing on an open door.

We have said before that a weak USD is helpful for Asian economies as it enables local central banks to go easy on monetary normalisation, and support domestic economies. But this view does not extend to rapid, and potentially disorderly USD declines, which could spur the Fed into more aggressive tightening, and raising bond yields worldwide. That is certainly not an environment that benefits Asia.

How will Draghi counter Mnuchin?

We had been holding open the possibility that European Central Bank President, Mario Draghi, might offer up some tantalizing taper hints at the press conference today - in line with the comments expressed in the ECB's last minutes. Now, Draghi is likely to adopt a damage limitation mode. We don't believe the EUR has exceeded the ECB's pain threshold line, which is probably somewhere around the 1.25 level. But rate of change can be as important as level for central banks, and so throwing more fuel on the fire with a hawkish testimony today would be counter-productive.

The problem is, would anyone believe Draghi if he offered a view in stark contrast to the minutes? This is reminiscent of the Emperor's New Clothes tale. And in true pantomime style, if Draghi tells the assembled press at today's conference that the Eurozone economy still needs emergency stimulus in the form of QE and negative rates, it would not be wholly inappropriate if they all shouted out "Oh no it doesn't". All that would be missing from the picture would be someone dressed as Widow Twankee.

Asia today - Malaysia should still hike.

Despite the USD weakness, and the MYR breaching 3.90, we still look for Bank Negara Malaysia to hike rates by 25bp today to 3.25%. Please follow the link to see further discussion of our thoughts on this central bank decision.

https://think.ing.com/articles/malaysian-central-bank-to-join-tightening-binge/

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Korean 4Q17 GDP dips

A surprisingly soft 4Q17 GDP figure for Korea should be viewed as a dip, little more. But it will help keep the Bank of Korea (BoK) on the sidelines for...

Korean won

A dip was expected - this is not all bad, on the plus side...

The first thing to note about the 0.2%QoQ contraction of 4Q17 Korean GDP is that is was not that far from expectations. The consensus view was a 0.1%QoQ rise, but then forecasters are bound by psychological resistance to making shocking pronouncements, so a few of them probably thought a negative figure likely. In fact, of the 13 Bloomberg economists forecast, 4 actually did have negative forecasts.

Moreover, within the total, there were a few glimmers of good news.

1. Firstly, private household consumer spending rose 1.1% on the quarter, that is the fastest quarter of growth since 4Q2015, and suggests that policy measures to support wages growth and boost benefits are having some positive effect at this level of the economy.
2. Government spending was also supportive, with a 0.5%QoQ rise.

After that, the news is less good...

...on the negative side

On the downside:

1. Gross fixed capital formation was down 2.0% on the previous quarter with construction and facilities investment both sliding sharply.
2. But it is the 5.5% decline in exports of goods and 4.6% decline in exports of services that did the most damage. Some of this blow was lessened by a 4.1% decline in imports.

Against this background, the recent tariffs imposed by the US government are particularly poorly timed, with the production measures of GDP showing that it was manufacturing declines that did most of the damage to the figures when GDP is viewed from a production, not the usual expenditure perspective.

Fiscal stimulus to remain expansionary, BoK to return to inactivity

We don't expect this export collapse to be anything more than a transitory blip. And in the light of this data, some of the criticism that has been leveled at the Moon administration's tax and spend type approach to economic management seems less robust. Such data weakness certainly supports maintaining, if not extending economic support through benefits, minimum wages increases and the like if there is no rapid improvement.

It also puts the Bank of Korea (BoK) back in their box for at least the rest of this quarter, and possibly longer. Their November 2017 rate hike might now be looking a little rash in hindsight. And the ensuing and unwanted Korean Won (KRW) strength rather predictable. With the USD slumping, BoK rhetoric is likely to be very dovish to stem the likelihood of KRW strength by default.

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