

## Good Morning Asia - 25 October 2018

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By Robert Carnell



#### ASEAN Morning Bytes

General market tone: Risk-off. Markets pulled back in the United States as poor housing data and uninspiring earnings hit risk sentiment

# Signs of weakness emerging in Asia

Weak Korean GDP in 3Q18 could be a barometer for the outlook elsewhere in Asia



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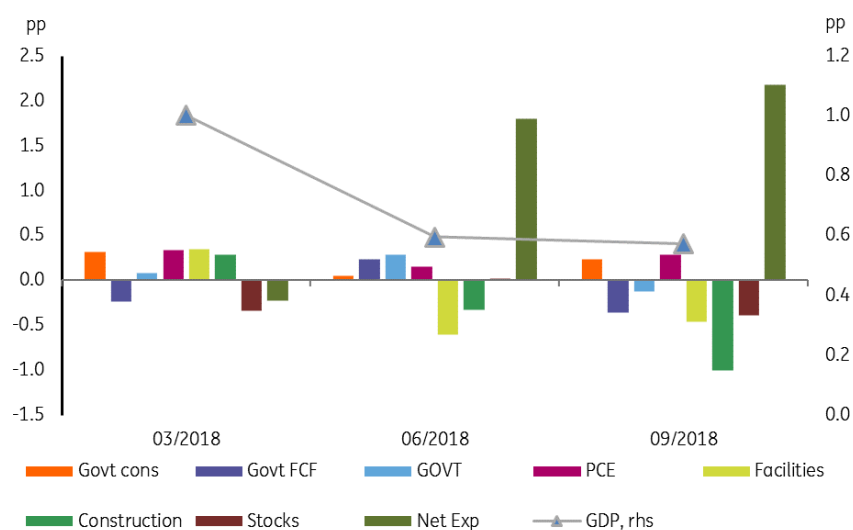
## Korean GDP expands at only a 2.0% YoY rate in 3Q18

Korea has felt a bit like a 2% economy for a while, along with some others in the region. And while the 2.0% YoY 3Q18 GDP growth out-turn was on the lower side of expectations (consensus was 2.3%, ING f = 2.1%) it was not wholly surprising.

Indicators of capacity have been indicating an excess for some time, and a further negative gross fixed capital formation (investment) result had been on the cards. The scale of it, at -4.5%QoQ was, however, unexpectedly large, and alone stripped 0.4pp from the 0.6% QoQ growth total. Within that gross fixed capital total, construction spending was also extremely weak, falling 6.4%QoQ, and the only positives in this segment of GDP were intellectual property (IP) products. Some years ago, research and development and other components of IP were not even part of GDP. If we had been compiling the figures on the old basis, the year on year growth rate would have been below 2.0%.

As usual, personal consumer spending was one of the stronger elements of the release, providing 0.3%pp to the total QoQ growth. And net exports provided their usual safety net, offsetting the falls in fixed capital. Without the net export boost, GDP growth would have been closer to 1.0%.

## Contribution to QoQ GDP growth - Korea (pp)



## Downward revision to GDP - implications for BoK

We are revising down our 2018 GDP forecast for Korea to 2.5% from 2.6%. The Bank Of Korea (BoK's) recent Economic Outlook revised the 2018 forecast to 2.7% from 2.8%. This would now need 0.8%QoQ in 4Q18, which we don't see happening. We are also revising down our 2019 forecast to 2.0%.

In the light of this weakness, the recent excitement over a possible November rate hike seems entirely misplaced. Absent an upside shock to the October CPI figures released on 1 November, we will stick with our "no change" call for the November meeting.

We ought to keep an eye out across the region given this weakness. Taiwan and Singapore share some, though not all, of Korea's economic characteristics. The only bright spot in this outlook is net trade. Given the current circumstances, feels rather worrying.

## Global stocks and FX

While Asian stocks managed a mixed performance yesterday, with the Shanghai Composite even managing to end the day in the green, the rout in US stocks overnight suggests that today will be somewhat different. In currency space, the CNY still seems to be creeping higher and the 7.0 USDCNY level is still our target for the year-end, though we now see this being breached in 1Q19 and reaching 7.30% by the middle of the year.

Elsewhere, Asian FX seems to be holding up reasonably well, especially the high yielders. Falling oil prices could be providing them with some fundamental support. This is more than can be said for the EUR, which now has a 1.13 handle. The market may be selling US stocks, but it is still buying US treasuries, and that is keeping the USD supported, relative to the Euro.

At today's ECB meeting, ECB President Draghi will probably try to put a brave face on the outlook and suggest no re-think on the ECB's normalization schedule. Italy is likely to be centre-stage of the Q&A session, and it is hard to see how Draghi can say anything helpful here. If Italy begins to accede to the stability and growth pact rules, then the ECB can lend assistance, if not, it can't. As

for Italian Banks, and using Italian Treasury bonds as collateral for liquidity, this could be an issue of Italian sovereign debt gets downrated to junk, but under such extreme circumstances, we imagine the ECB would be imaginative with its rules on eligibility. It has been before. But it won't indicate this today.

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### International theme: Investors wait on ECB and US GDP print for direction

Disappointing new home sales data out from the US coupled with slowing PMI numbers out from the Eurozone sapped risk sentiment from the market. Investors now look to the ECB meeting and 3Q GDP print from the US for direction.

### EM Space: Asian markets likely to move sideways with downward bias

- **General Asia:** Asian markets are likely to move sideways with a downward bias after the poor showing on Wall Street while poor Korean 3Q GDP is likely also seen to drag on risk appetite.
- **ASEAN:** Strengthening bi-lateral economic ties towards an “enhanced strategic economic partnership” status, Malaysia and Thailand have agreed to open up their borders for 24-hour cross-border trading. Malaysia’s Prime Minister Mahathir is on a two-day visit to Thailand.
- **Philippines:** Negotiations for wage petitions are on-going with employers offering a Php20 pay hike, much lower than the request for a Php344 increase in minimum wage. The Php20 increase in wages will be in-line with BSP’s recent assumption wage adjustments, which is

currently factored into their forecast for 2018 and 2019 inflation.

- **Philippines:** The government is looking to import 203,000 MT of rice via government-to-government deals after its recent auction only attracted private companies to supply 43,000 MT of the allocation of 250,000 MT. If done quickly, this will help augment supply in the coming months going into December with the recent data showing rice prices have continued to trend lower, down 0.5% week-on-week for regular-milled rice.

## What to look out for: 3Q US GDP and ECB meeting

- ECB meeting (25 October)
- Fed Bostic and Fed Mester (25 October)
- US durable goods orders (25 October)
- US 3Q GDP and core PCE (26 October)
- Fed Clardia (26 October)

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