Good MornING Asia - 29 May 2019

There is a lot of doom and gloom, but how much of it is justified?

In this bundle

Reading the tea-leaves

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Asia Morning Bites

ASEAN Morning Bytes

General market tone: Risk-off. Trade concerns continue to fester and will likely weigh on sentiment on Wednesday.

Philippines

Philippines: Inflation could dip below 3% in May

Inflation in the Philippines, something of a scourge in 2018, looks set to decelerate further as rice prices continue to fall

Thailand

Thailand: Manufacturing surprisingly swings back to growth in April

We don't think the worst is over just yet and maintain our view of a central bank policy rate cut in June

Opinion | 29 May 2019

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Source: Shutterstock

Today's theme is...

My daily ritual of trying to make sense of all the various news headlines and opinion pieces starts on the way into work and usually concludes within about ten minutes of turning on my PC. It isn't a conscious process, but by then, I've usually arrived at what today's key theme will be all about, or discovered a "straw man", which I will attempt to cut down. Not always, it has to be said...

Today is a mixture of the two. Starting with extremely depressed longer-term bond yields, where yields on the ten-year US Treasury fell further overnight and now sit at 2.26%, quite a long way below 3M USD Libor (2.52%).

10Y yields this low only makes sense if you think the Fed is going to cut rates. Our house view is that they won't. So is my own personal view. Why? Well to envision rates actually being cut, and according to market pricing, quite soon, you have to really imagine the US economy to be in trouble.

That takes me to a headline about factory orders in the US being weak and that this is probably a sign of looming manufacturing weakness brought on by the trade war.

Except it probably isn't.

Yes, April durable goods orders fell (data released a few days ago, this isn't breaking news). I've been looking at this series for decades, and I can tell you that there is no, that is precisely **no** information in one month's numbers. This data swings all over the place. We would predict recessions 50% of the time if we focused on month-on-month swings in this. Which is why they very helpfully provide a three-month moving average of the core series (four-month would be better, but who's complaining...). Looking at this smoothed series, the numbers look fine, actually quite reassuring. April may be the start of a trend, and a further month of weakness would begin to sow doubts in my mind, but we haven't had that yet. Right now, this signals nothing.

Other areas of weakness include the US housing market. Here, the news continues to run luke-warm. House price growth has slowed right down. But compared to a year ago, the rate of increase is slowing at a slower pace. It looks to be moderating. This isn't alarming. It's actually a signal that there is no bubble bursting, but a market repricing.

Trade war the key

Now the additional tariffs on China may change all that, and the ping-pong of threats is beginning to look quite ugly. Proposed tit-for-tat bans of rare earth exports from China to the US and technology access to China from the US don't improve the picture. And it is possible to conjure up a very dismal outlook over a twelve-month timeframe. It would be very encouraging to hear the US President beginning to steer both sides towards some sort of deal that would also allow China to back away from its' retaliation measures. Other news stories point to further weakness in the Chinese data, though I'm less concerned about that, given China's fairly well-stocked policy arsenal, though this does take place against a steady rise in indebtedness. That is always faintly disturbing.

Harvard's Carmen Reinhart is also fretting openly about the global risk from a China recession - so this isn't all idle fancy by market participants with too much time on their hands. If it were to happen, it would be very bad.

Stocks to show the way?

But then I return to what may ultimately may matter more to policy-makers and the administration in the US, and that is the equity market. Right now, it's poised on support. If it drops, it could drop big. And that would take US Treasury yields closer to 2%.

But it is also what probably causes a rethink on the trade war. In my view, anyway.

Asia day ahead

It's quiet today - very quiet. We have had the RBNZ Financial Stability report and statements from Governor Orr - though nothing really to report here. The RBNZ still have some further easing to do in our view, though that wasn't really the subject matter fo this discussion today.

South Korea has released business survey data. Soft. This Backs up the arguments for a rate cut from the BoK. They probably won't, at this meeting anyway, though the arguments for them to do so are overwhelming, in my view.

And Prakash Sakpal writes on Thailand: Highlighting the lack of fiscal support for the economy, Thailand's finance ministry yesterday announced a delay in the budget for fiscal 2020 (Oct 2019-Sep 2020) by three months due to the transition to a new government. During the transition period, outlays would be capped at 50% of that budgeted for current fiscal 2019. Weak government spending boosts the case for a June rate cut in our view.

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ASEAN Morning Bytes

General market tone: Risk-off. Trade concerns continue to fester and will likely weigh on sentiment on Wednesday.

EM Space: No news means bad news for risk sentiment as dealers likely to pull back

- **General Asia:** With scant developments on the trade front, market players will likely focus on the sustained dip in US Treasuries yields. Fears of a full-blown trade war will likely grip markets again on Wednesday. Crude oil prices inched higher with supply disruptions feared in the US market.
- **Thailand:** A surprising rebound in manufacturing in April bodes well for GDP growth in the current quarter, though we don't think the worst is over just yet and maintain our call of a central bank policy rate cut in June. Highlighting the lack of fiscal support for the economy, finance ministry yesterday announced a delay in the budget for fiscal 2020 (Oct 2019-Sep 2020) by three months due to the transition to a new government. During the transition period, outlays would be capped at 50% of that budgeted for current fiscal 2019. Weak government spending boosts the case for a June rate cut in our view.
- **Philippines:** The Philippines improved in terms of global competitiveness, according to the Institute for Management Development (IMD), nudging higher to 46th out of 63 from the previous ranking of 50th as economic growth remained robust and labor market developments were positive. Despite the improved, the Philippines lagged the rest of the region, placing 13th among 14 Asia Pacific countries.

- **Singapore:** Singapore displaced the US as the world's most competitive economy, reclaiming the top spot it last had in 2010.

What to look out for: US and China data

- US GDP (30 May)
- Fed Potter (30 May)
- China PMI manufacturing and services (31 May)
- Thailand GIR and trade (31 May)
- Bank of Korea meeting (31 May)
- Indonesia money supply (31 May)
- Philippines money supply (31 May)
- Fed Clarida and Bostic (31 May)
- South Korea trade (1 June)

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Snap | 28 May 2019 Philippines

Philippines: Inflation could dip below 3% in May

Inflation in the Philippines, something of a scourge in 2018, looks set to decelerate further as rice prices continue to fall

Rice for sale at a market in the Philippines

9.8%

Weighting of rice in CPI basket

Philippines

Rice falls a 6th straight week

Rice is the basic staple in the Philippines and is often the main determinant in differentiating a full meal from a snack. As a commodity in the CPI basket, rice commands nearly ten percent of the total and was one of the main reasons for the 2018 inflation pop that saw price gains top 6.7%. Bad weather and delayed importation both contributed to the price spike which saw the central bank, BSP, rattle off a series of aggressive rate hikes that have since begun to sap the growth momentum of one of the region's fastest growing economies.

With rice supply chains normalising even ahead of the implementation of the Republic Act 11203 which lifted import restrictions, rice prices have fallen for 6 straight weeks according to latest data from the Philippine statistics authority. Meanwhile, the rest of the food basket, which corners 38% of the CPI basket, has seen disinflation for 7 straight months, helping headline inflation exhibit that humped-shape curve given the supply-side nature of the 2018 episode. With the government proactively importing foodstuffs (up 22.5% YTD) with the El Niño dry spell in effect, we can expect food prices to remain stable for the next few months.

Philippine inflation could slip below target

With food prices likely stable or decelerating, we can expect overall headline inflation to be tame for the rest of the year. The May figure could fall below the BSP's inflation target of 3% as fuel prices saw only marginal gains year-on-year, although utility costs are projected to be slightly higher for the said month. And although global crude oil prices remain elevated (up 29.5% YTD), we've seen only a marginal effect on headline inflation given transportation's 8.06% weight in the CPI basket. With supply conditions stable for now, we expect the BSP's forecast for 2.9% inflation in 2019 to hold with possible further easing given the BSP's dovish leaning.

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Article | 28 May 2019 Thailand

Thailand: Manufacturing surprisingly swings back to growth in April

We don't think the worst is over just yet and maintain our view of a central bank policy rate cut in June

Source: Shutterstock

2.0% April manufacturing growth

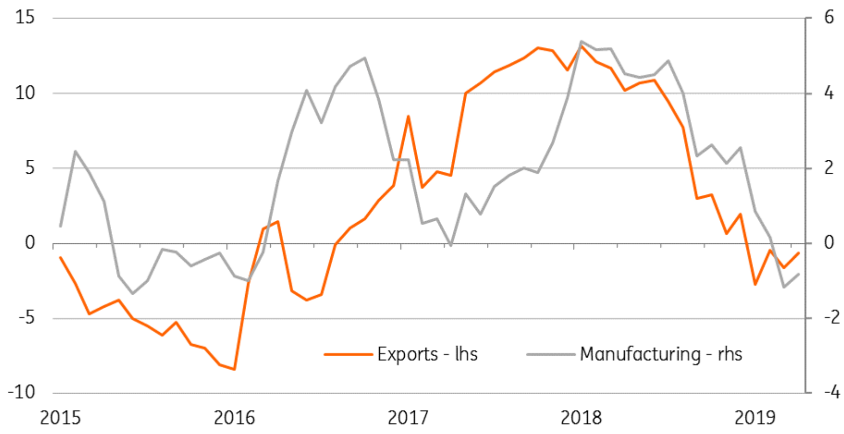
Better than expected

A pleasant manufacturing miss

Contrary to the expectation of continued decline, Thailand's manufacturing output rose by 2.0% year-on-year in April after two consecutive months of contraction. The consensus estimate was -0.9%, and we were more bearish at -1.5%. Meanwhile, March growth was revised lower to -2.7% from the -2.5% initial estimate.

The Songkran (Thai New Year) holiday typically dents economic activity in April. The added whammy this year was weak exports owing to all the trade noise globally, which earlier this month forced a downgrade of the official export growth forecast for this year to 2.2% from 4.1%. Despite this, the 17% month-on-month (unadjusted for seasonality) fall in the manufacturing index was the smallest fall for the month since 2010. Likewise for exports whose 13.5% fall in April was the smallest in the last three years.

Exports drive manufacturing (% YoY, 3-month moving average)



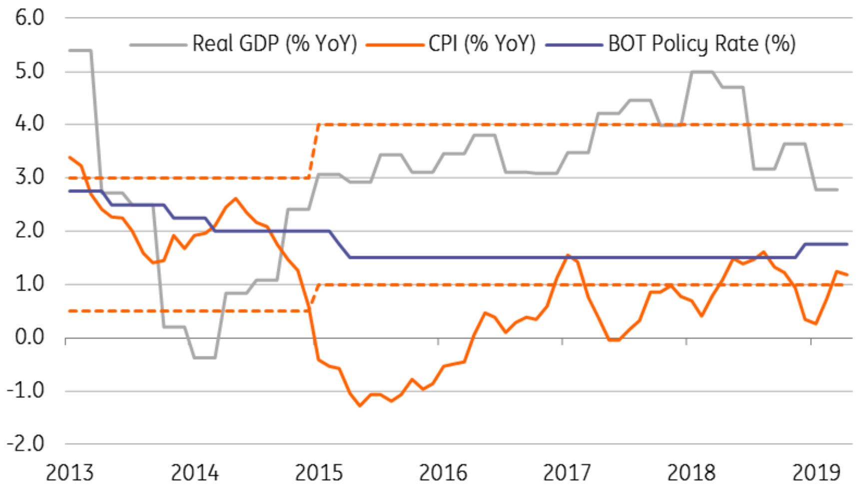
Source: CEIC, ING

Still, a strong case for central bank easing

However, this doesn't change the underlying story of weak exports and manufacturing continuing to depress GDP growth over the rest of the year. Moreover, inventory re-stocking had been a key driver of GDP growth in recent quarters and, absent any recovery in demand, it could turn out to be a potential drag on growth. That said our forecast of a slightly better, 3% YoY GDP growth in the current quarter than the 4-year low of 2.8% registered in the first quarter, benefits from the low base year effect rather than demonstrating any underlying improvement in the economy. We see growth remaining stuck below the government's 4% comfort level for the rest of the year.

Following the dismal first-quarter GDP report earlier this month we revised our 2019 growth forecast to 3.1% from 3.8%, and also our view on the Bank of Thailand's policy from stable policy interest rates, currently 1.75%, to a 25 basis point cut at the next meeting in June. While the policy forecast revision has put us outside the consensus, which is solidly behind no policy change this year, we believe the BoT will bite the bullet and at least reverse the December 2018 rate hike that wasn't required in the first place. And still, with persistently low inflation, it will be left with enough policy space for future easing.

The BoT has enough space for easing



Dotted lines are BoT's target for CPI inflation, currently 1-4%.

Source: Bloomberg, CEIC, ING

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