

Good MornING Asia - 3 July 2018

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Still no inflation in Asia

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By Robert Carnell



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June inflation of 3.12% was the slowest since March 2017. As a result, we've now cut our inflation forecast for this year



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Still no inflation in Asia

South Korea's June inflation print is low, but this is actually a regional issue



Source: Shutterstock

Despite higher oil prices, Korean inflation remains subdued.

Korean consumer price inflation (CPI) for June rose 1.5%, unchanged from May, though the core rate of inflation slowed to 1.2% from 1.3%. The price level actually declined by 0.2%MoM, and looking at the underlying contributors would almost certainly have delivered an even lower inflation figure had it not been for the effect of rising crude oil prices pushing up vehicle fuel costs.

Perhaps this is just as well because over the coming months, the Korean won's weakness could suck in a little more inflation, as could other Asian currencies, all of which have been weak in recent months.

Ordinarily, this might have us responding by forecasting more rate increases from the regional central banks, and adding in some weaker domestic demand as these rates bit down on spending. In some economies, notably the balance of payment deficit economies of Indonesia, Philippines and India, rates have indeed been rising. Indeed, the Indonesian Finance Minister recently remarked that this would weigh on growth and that this would be tolerated. To do otherwise would simply suck in more imports and worsen the external balance...which is the original reason for the currency weakness. These three economies also have higher prevailing inflation rates than their Asian neighbours. Though none of them, in my view, have a particularly severe inflation issue currently.

Elsewhere, Asia is lucky that inflation really is really not a problem at all for policy setters. On the contrary, before this recent episode of currency weakness, the lack of inflation was one of the most obvious features of Asian economies, despite reasonable growth.

In other words, there is a buffer here. Currencies can weaken further if the trade war intensifies, as I believe it will, and for most of the regional economies. And inflation may tick up a little. But this need not result in any offsetting action. Korea, for example, does not look like it will need to trouble its central bank for any tighter policy until next year. For now, that view remains fairly safe.

1.5%

Korea June Headline inflation rate (YoY%)

Core inflation declined to 1.2%

Lower than expected

RBA - no hike today, tomorrow, and maybe next year

The RBA meets today, in what many will imagine will be a really uneventful meeting. No change in policy, no hints about a probable future move in policy and little new to say on the economy, will likely sum up this meeting. But there is an outside chance (a very, very small one) that RBA Governor Lowe will take a leaf out of the RBNZ's book, and add in two-way risk to the rate outlook.

I think this would be more likely to occur if the AUD were stronger now than 0.733 rate and weakening. It would also be more likely if the economy were notably weaker - recent data have been mixed, but by no means bad. So I would say it is very unlikely that Lowe will follow Orr's example. But for an otherwise hugely uneventful meeting, this is perhaps the only likely avenue for a market surprise.

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3.12%

June inflation rate

Slowest since 3.61% reported in March 2017

Higher than expected

Inflation slowdown partly due to base effects

June inflation slowed to 3.12% from May's 3.23% and June 2017's 4.37%. The slower June inflation is partly due to base effects and slower inflation for most major commodity groups of the consumer price index except for food and transport rates. Food inflation accelerated in June to 4.7% from May's 4.5% and 2.4% in June 2017. Transport inflation also accelerated to 1.9% in June from May's 1.7%.

Inflation forecast cut

We expect the positive base effects in the coming months to recede and bring about a reversal of the recent downtrend of inflation. The upward path of inflation in the second half would also be

gradual and could likely be a mirror image of the inflation path in the first half. Tighter monetary policy in the past two months which saw policy rates rise by 100 basis points would moderate demand pull inflation and assist in moderating the price impact of a weak Indonesian rupiah (IDR). Monetary policy will continue to pursue a stabilisation of the IDR, not only to help protect the financial system but also to keep inflation within target rate. We expect full-year 2018 inflation to average at 3.3%, slower than our previous 3.5% inflation forecast and close to the central bank's point inflation target of 3.5%.

Thailand: A downside inflation miss

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Source: Shutterstock

1.38% CPI inflation in June
Year-on-year

Lower than expected

Below-consensus June inflation

Thailand's consumer price inflation surprisingly slowed to 1.4% year-on-year in June from 1.5% in May. The consensus expectation was for inflation to remain unchanged at 1.5%. The Bloomberg headlines point to energy prices as a source of inflation – a result of rising global oil prices. But lower food-price inflation more than offset the energy increase to push the headline rate lower. Core inflation, which strips out food and energy prices, was steady at 0.8%.

Steady, low inflation ahead

We believe inflation is close to its peak in the current cycle. Absent significant supply shocks from

food or oil prices, we expect inflation to remain close to the low end of the central bank's (BoT) medium-term policy target of 1-4%. The commerce ministry has just announced a mild adjustment to its full-year 2018 average inflation forecast to 0.8-1.6% from 0.7-1.7%. The BoT's forecast is 1.1%. We forecast 0.9%.

Stable central bank policy

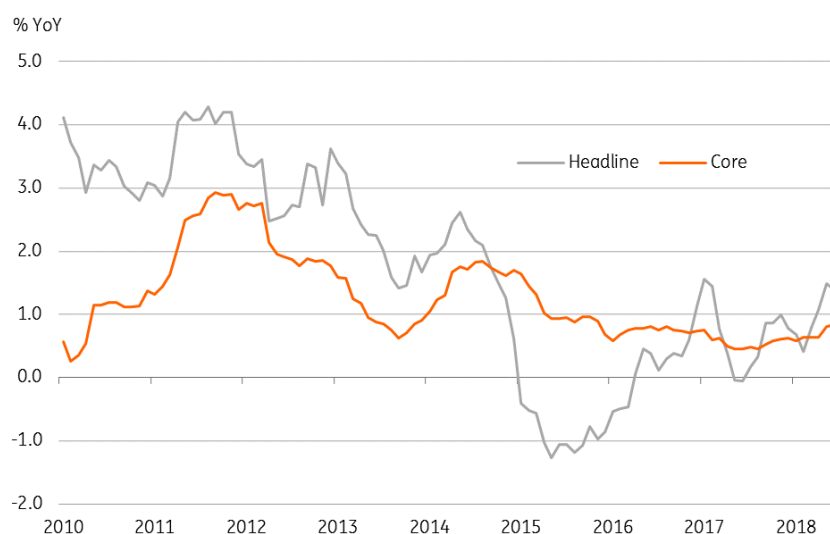
The BoT easing cycle started in early 2012 is finally beginning to see some light at the end of the growth tunnel, though this hasn't lifted inflation. With the lingering global trade risk to growth and persistently low inflation, we don't think the BoT will be in a position to unwind policy accommodation anytime soon. Nor do BoT policy-makers appear in any rush to do so, given their recent dovish rhetoric.



Chance of BoT policy move in 2018

"... private consumption continued to expand, although elevated household debt and the economic expansion had yet to benefit household income and employment in a broad-based manner, resulting in a gradual improvement in purchasing power". - the latest BoT policy statement

Consumer price inflation



Source: Bloomberg, ING

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