

Good MornING Asia - 31 January 2019

Thanks to a helping hand from Fed Chair Powell, Asian currencies are looking stronger across the board today. Risk assets in the region will take heart from the Fed's capitulation to markets. But don't write off hikes too soon

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Source: shutterstock

Another great piece by London's James Knightley on [the FOMC decision overnight](#) - he's not paying me to write this either (though James, you know where to send the cheque if you insist). I particularly liked it as it entirely coincides with my own unofficial view of the Fed, that June still looks a good call for another rate hike, with both wages, and inflation likely to be sending a strong message for a further (and possibly final...) hike then.

And this is where I take issue with the current message from the FOMC. Because if the data says, "hike" and both James and I seem to agree that before too much longer it will, then the market currently isn't poised for this and is being steered by the Fed to an entirely different conclusion. We can all enjoy the risk-on sentiment while it lasts. But such inconsistent guidance sets us all up for an awkward correction later on. This could be particularly nasty as the higher inflation and wages backdrop might coincide with a weaker projection for future growth, and that is a tough one for risk assets, especially equities to digest. Summertime blues then?

Time for some regional rate cuts

In the last 5 days, most Asian FX strength has come from the CNY, but also the perennial outperformer, the THB, and SGD. PHP hasn't been too far behind. The near term might provide

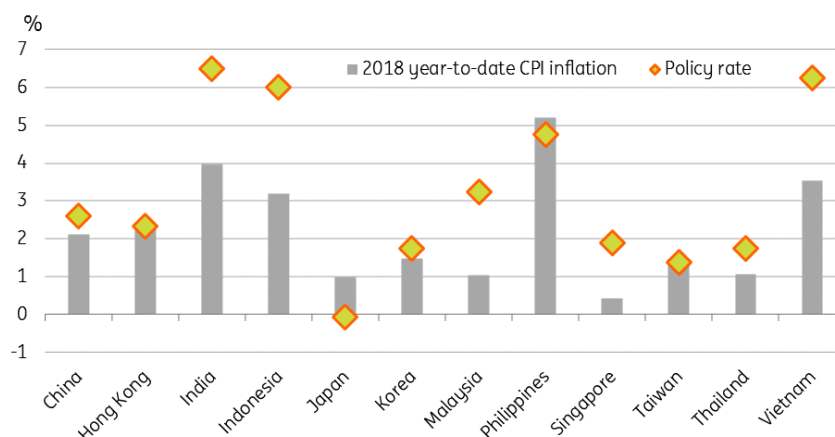
some further boost to external balance offenders, IDR and INR, which stand to benefit most along with the PHP from generalized USD weakness. The Asia Dollar index is pushing higher above its 200-day average and most likely will widen the gap now.

Which makes us think, with Asian FX pushing higher against the USD, inflation largely under control and likely to remain that way, and global headwinds to growth growing, isn't there a case for some regional rate cuts this year, against expectations for no change for most central banks?

Both the Reserve Bank of India (RBI) and Bank Indonesia (BI) have the greatest room to cut in our opinion, with high real interest rates giving them room to ease back. RBI meets next week, and though we aren't forecasting a cut from them, we would certainly put this in the category of "don't rule it out". The main argument against cuts for both the RBI and BI is that stronger oil offsets the weaker USD. but not entirely.

Another two Asian central banks spring to mind, both of which hiked last year for reasons we struggle to fathom. Bank of Thailand (BoT) and Bank of Korea (BoK) could both reverse last year's hikes. With the THB one of the regions strongest currencies, there is certainly no need to protect the currency with unnecessarily high rates. indeed, the domestic economy could do with a boost to get their massive current account surplus closer to balance.

Asia Real rates



Today's movers and shakers

There's a fair bit on the calendar to digest today. Korean industrial production for December was down 1.4%MoM. I don't care than the year on year rate exceeded the consensus 1.5%YoY forecast by 0.1pp - that only tells me that the near term history has been revised to look a little less bad. but today's December month on month number suggests that the downturn in production is accelerating. That is cause for concern. Japan's production figures aren't much better, falling 0.1%MoM, and -1.9%YoY. We will almost certainly be revising our 2018 full year forecasts for Japanese GDP downwards, and that probably implies a downward nudge to the 2019 forecasts too.

PMI data out of the region is likely to make for difficult reading. China's manufacturing PMI index is likely to fall a further 0.1pp or more today. 4Q18 GDP data from Taiwan are not likely to impress either, with a 1.6% print expected by our Greater China Economist, Iris Pang (consensus 2.0%YoY).

Don't all rush

And finally, I learned from Singapore's own Money FM radio channel on a call with them today that it is "Hug an Economist" day today. See [here](#) for more details. Please form an orderly queue.

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ASEAN morning bytes

General market tone: Risk-on. A dovish Fed will likely push risk-taking behavior on Thursday with the US and China now in fresh trade talks.



EM Space: A “patient” Fed sparks risk-on tone

- **General Asia:** Powell stuck to script and then some as he also made changes to his balance sheet reduction strategy, all in all pointing to a more dovish Fed in the coming months as data will either be delayed or tainted by the government shutdown. Meanwhile, the high-level US-China trade talks enter into the second day on Thursday with investors also keen on PMI data out from China in the morning session.
- **Malaysia:** Exports surprised on the upside in December with 4.8% YoY growth, which with a slowdown in imports boosted the monthly trade surplus to over MYR10bn. Wider surplus means improved net trade contribution to GDP in the 4Q18, supporting our view of a pick-up in GDP growth to 4.6% from 4.4% in the previous quarter. If sustained, the renewed uptrend in global oil prices will be positive for the Malaysian economy and the currency this year.
- **Singapore:** 4Q18 labor report is due. The weaker activity subjects the consensus of the unchanged unemployment rate at 3Q's 2.1% to upside risk. We expect 2.2%.
- **Thailand:** December balance of payments data due today is expected to show a rebound in the current account surplus, as what happened to the customs-based trade surplus in the last month. We estimate a current surplus of \$3.9bn, larger than \$3.5bn consensus and up from \$1.6bn in November. But the annual current surplus narrowed in 2018 to about 7% of GDP from 11% in the previous two years. This is still large enough to support the THB's outperformance, though the appreciation is likely to be capped by rising political risk in the

run-up to general elections in March.

- **Indonesia:** Bank Indonesia Governor Warjiyo expects that the nation's 4Q current account deficit remained substantial at \$8bn or roughly 3% of GDP as import growth outstripped exports for the year. Warjiyo also expressed government's desire to curb import the growth further to reign in the current account deficit and that the central bank remained cautious and looked to maintain stability. Meanwhile, the national government expects growth to hit 5.3% in 2019 driven by both consumption, investment and a narrowing of the trade gap.
- **Philippines:** Philippine budget secretary Diokno indicated that 2018's deficit to GDP ratio may have exceeded the target of 3% with government spending heavily in the 4th quarter to buttress growth momentum. The secretary allayed concerns about the breach, pointing to investments in infrastructure as the main reason for moving past target.

What to look out for: US-China trade talks and China PMI data

- China PMI manufacturing and non-manufacturing (31 January)
- Thailand trade (31 January)
- India 2018 GDP (31 January)
- India FY2020 budget (1 February)
- South Korea inflation (1 February)
- Thailand inflation (1 February)
- China Caixin PMI manufacturing (1 February)
- US NFP (1 February)

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Malaysia: Exports end 2018 on a firmer note

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Source: shutterstock

4.8%

December export growth

Year-on-year

Higher than expected

Firmer exports, weaker imports in December

Malaysia's export growth accelerated to 4.8% year-on-year in December from 1.6% in the previous month. The outcome was better than the consensus of 1.3% export growth but short of our 5.8% forecast. Import growth slowed in line with the consensus to 1.0% YoY from 4.7% in the previous month.

Strong growth in electrical and electronics exports (+14% vs. -1.7% in November) and chemicals (37% vs. 15%) stood out. Meanwhile, a crash in global oil prices in the last quarter is reflected by

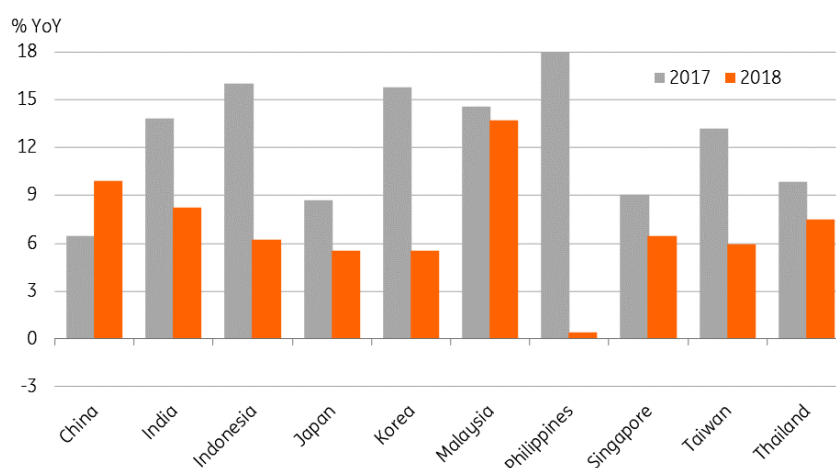
weak petroleum product and natural gas exports, though crude petroleum export growth remained steady. By destination, weak demand from China continued to weigh on Malaysia's exports. Weak transport equipment imports pulled total import growth lower.

2018 was best year for exports in Asia

Annual export growth of 6.7% in 2018 was down from 18% in 2017. The corresponding figures for imports are 5.0% and 20%.

The authorities report trade data in local currency (Malaysian ringgit or MYR). After converting to US dollars, the 14% export growth in 2018 is, in fact, the best performance among Asian countries, for which we credit improved terms of trade from higher commodity prices. Stripping out the price and exchange rate effect, growth in the volume of exports more than halved to 5% in 2018 from 11% in the previous year.

Asian export performance



Source: Bloomberg, ING

Positive net trade contribution to GDP growth

The trade surplus jumped to MYR 10.4 billion in December from MYR 7.6 billion in November. The annual surplus of MYR 120 billion in 2018 was MYR 21 billion higher than 2017, the second consecutive year with a widening trade surplus.

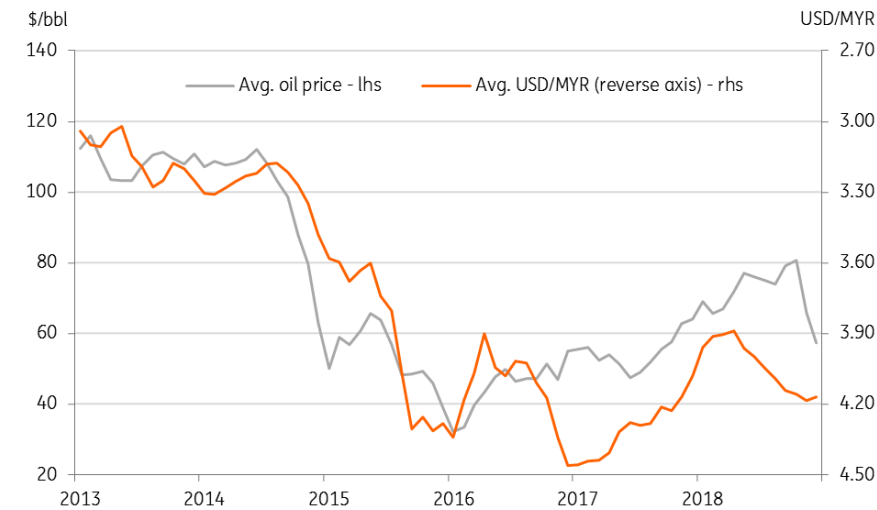
A wider trade surplus means positive net trade contribution to GDP growth. Indeed, that was the case in the first two quarters of last year, although net trade turned out to be a drag in the third quarter. We think it turned positive again in the final quarter; MYR 7.3 billion widening of the 4Q18 surplus from a year ago followed MYR 1.1 billion narrowing in 3Q18. This supports our view of a pick-up in 4Q GDP growth to 4.6% from 4.4% in the previous quarter, leading to full-year average growth of 4.7% (4Q18 GDP data is due on 14 February).

Firmer oil price, firmer currency

If sustained, the renewed uptrend in global oil prices will be positive for Malaysia's economy and the currency coming into 2019. This, together with a softer dollar, drove the USD/MYR below 4.10 this month, a level not seen since August last year. However, underlying our view of the pair

weakening to 4.20 by mid-2019 are expectations of an intensified US-China trade war and strong US dollar. We are reviewing our forecast.

Oil prices driver MYR exchange rate



Source: Bloomberg, ING

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