

Good MornING Asia - 4 August 2021

Rising Delta variant Covid-19 cases are not yet dampening market expectations. But they easily could. The return of Covid to China is our biggest concern. Aggressive measures should bring it under control - the question is, how fast, and at what economic cost

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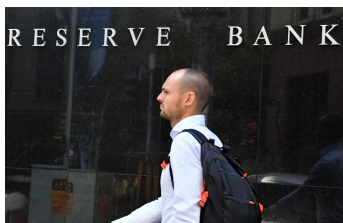


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Covid up, again

The Worldometer index we use for our global Covid cases shows a rise in the number of cases in a growing number of important countries as the cumulative global total ticks over 200 million. About a month ago, US daily cases were down at about 5,000. They are back at 96,000 now and rising. And the death tally has also picked up, showing 480 as of writing. The US is not alone. European countries are also showing further signs of Covid increase, while in Asia, while the latest wave is hardly news following the recent waves in SE Asia, the small but significant rise in cases in China is grabbing attention.

China has shown before that it is willing to take tough action to control Covid, and we don't doubt that it will do so again this time. Tough restrictions on movement and travel already in place will likely bring the desired results. But the delta variant is a particularly slippery little critter, and the concern for us, and we imagine, many others, is how quickly this will occur, and at what economic cost in the meantime. There are plenty of stories on newswires talking about weakening pressure on the CNY. And on top of Covid concerns, new talk of curbs on online gaming following a news agency report of games as "spiritual opium" is spooking investors, who may be wondering, what next, following the regulatory tightening up across a number of industries in recent weeks.

One this is for sure, and that is that talk of a synchronous global recovery is garbage. 2021 is still hurting due to Covid, and it may take some extra effort in terms of possibly a new targeted vaccine against the delta variant, boosters or some other remedial measures to ensure that 2022 lives up to what may now be looking like unrealistic expectations. People "in the know" are suggesting that for Delta, herd immunity may require 90% to have been vaccinated or have existing immunity after infection. That is still a reach for even the best-vaccinated countries.

Yet with all this Covid doom and gloom floating around, the equity markets seem, as ever, to be happy, making all-time highs in the US on the back of some stronger earnings numbers. It doesn't take a lot for US Treasury yields to decline, and they have done so again despite the equity move, though only by 0.5%. the 10Y UST now yielding 1.172%.

A decline in market sentiment, if it comes, will likely support the USD, though this will probably be tempered by thoughts that the Fed will be even more reluctant to do anything to policy in this environment, so that may help keep the currency anchored roughly in place. Recent history supports this view. In the last 24 hours, EURUSD tried to go higher and then lower, but returned to almost exactly where we were this time yesterday.

What to watch for today

There was little of interest in the economic calendar yesterday, with an unremarkable durable goods orders print from the US about all there was on offer from the G-7. Today, we get ADP and the service sector ISM ahead of Friday's payrolls, and we also get ISM services PMI's elsewhere, including in China, where the Caixin survey will provide one of the local highlights.

The Bank of Thailand also meets. Prakash Sakpal writes "Bank of Thailand meetings have been the least exciting central bank policy events in the region lately. Today's meeting will not alter this trend with the policy rate widely expected to remain at 0.50%, the lowest it has ever been since May 2020. Our only interest in today's meeting is whether the central bank cuts its 2021 growth forecast, currently 1.8%, as the Covid-19 spread further delays economic recovery. A senior BoT official recently warned about the current Covid-19 wave trimming 0.8 to 2.0 percentage points from GDP growth this year. We have revised our 2021 growth view from 2.1% to 1.4%. Inflation is back near the low end of the BoT's 1% to 3% policy target after a brief spike in April. Such an economic state warrants more policy support, but probably not from the BoT. We expect an on-hold BoT policy throughout 2022, which means the Thai baht depreciation trend has a long way to run. Our end-2021 USD/THB forecast is now 35.00 (spot 33.03)".

Author

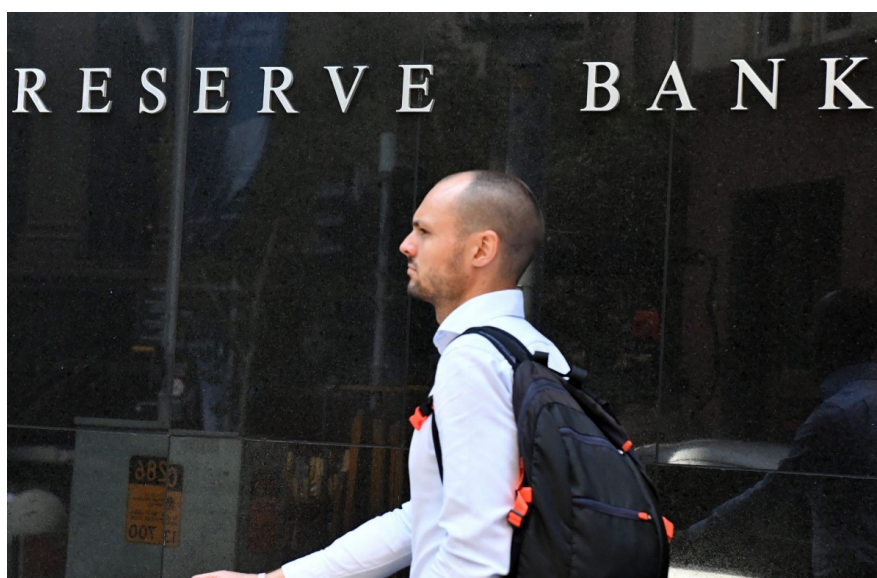
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AUD4bn

Lower than expected

Asset purchases per week

Next phase of the programme

No U-turn

[At its July meeting](#), the Reserve Bank of Australia (RBA) announced that after the current program expired in early September, it would conduct its asset purchase programme at a rate of AUD4bn per week. This was a "change" from the AUD100bn over the previous period from the second week in April until early September.

While the maths of this is a bit fuzzy - it seems the RBA agree that this is a slight reduction in pace, [and in the latest statement](#), they refer to the previous pace as AUD5bn per week. It seems a stretch to us to describe this reduction as a "taper". But many market participants regarded it as a

significant move at the time.

Moreover, a number of market participants have been suggesting that following the latest bout of lockdowns caused by a resurgence in Covid-19 cases, a "U-turn" by the RBA was warranted at this meeting. In contrast, we felt that as the change in policy noted in July was already so marginal, at most, only a token adjustment would be required.

In the end, the RBA has decided that even a token gesture was unnecessary. The asset purchase policy remains set to proceed at a pace of AUD4bn until mid-November after the current programme ends in September.

With little else to tweak at this meeting, we have scoured the text for any other hints and tweaks.

At the July meeting, the RBA made some room for future changes in its assertion that cash rates would not be raised until 2024, by suggesting that this was in line with its "central scenario" - implying that under a more robust outcome (an upside scenario), an earlier response was possible and the reverse was possible for a weaker scenario.

There is no change to this central scenario view and 2024 remains the main guidance. But the write up of the economy, while acknowledging the impact of the Covid lockdowns, remains relatively upbeat. The text suggests that it is pushing at the upper half of the central scenario. It also takes a relatively upbeat view on the speed of rebound of the economy once lockdowns are ended. *"The experience to date has been that once virus outbreaks are contained, the economy bounces back quickly. Prior to the current virus outbreaks, the Australian economy had considerable momentum and it is still expected to grow strongly again next year"*.

The statement also notes the strength of the housing market, the faster than expected recovery in the labour market, and higher than anticipated inflation. A further degree of flexibility is introduced due to the uncertainty of the wage response to unemployment at the low levels forecast. This again, in our view, provides a further caveat to the 2024 pledge and any hardening in the policy outlook in the quarters ahead.

So in short, nothing much here for markets to get too excited about. Though to the extent that they might have priced in a scaled-back taper, that has helped the AUD to find some strength today. 10Y Australian government bonds have reacted to the absence of any reduction of the taper with a small increase in bond yields of about 2-3bp at the time of writing, compared to first thing this morning.

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