Good MornING Asia - 6 July 2018

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No turning back

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By Robert Carnell

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Trade war starts this lunchtime - early lunch anyone?

I have to confess that now the canoe is very clearly headed over the edge of the waterfall, I am not sure why US equities staged a small rally yesterday. Were they taking some cold comfort from Fed minutes that noted that the trade war increased global risks? If so, it is a bit like the rallies that preceded the global financial crisis as the Fed cut rates at the back end of 2007. Short-sighted? Well yes, really. By 12:00 today, Singapore time (and thereby Beijing time and most of the rest of Asia) tariffs on $34bn of Chinese goods will be implemented, and at about 12:00:01, Chinese tariffs on a like amount of US goods will follow. We may look back on this period as one of the greatest acts of economic folly in our lifetime, though send me an email if you can think of worse. That will make interesting (though probably quite brief) weekend reading.

Sure, we will all wake up on Monday and the sun will still rise. Most of us will still have jobs to go to. And our incomes will still likely be enough to provide basic food and shelter for ourselves and our families. This is not economic armageddon. We will not have to hunt our food with pointy sticks. But it is applying the brakes to a global economy that has less durable momentum than appears to be the case. And which is still saddled with heaps of debt, and which has few policy tools left in the box to answer a slowdown of this sort, save to undo the damaging policies that could lead to a recession. It's too late to hope that reason will prevail, but hopefully, this period of economic nihilism will be short-lived. I wouldn't bet on that though. There is every chance that it gets worse before it gets better.

On a separate note, if you have access to Bloomberg, please read an excellent piece by Cameron Crise on 'Daybreak' (<DAYB> Go). writing about forward-guidance. It isn't related to my rant above, but it needs spelling out, and he does it brilliantly.

2.8% YoY

Expected US June hourly wages growth

Up from 2.7% in May

US jobs report

Yesterday's ADP survey, still the best of a very bad bunch of month on month forecasting tools for figuring our US non-farm payrolls (jobs to the rest of us), came in at 177,000. This is a little lower than the 189,000 recorded for the previous month, and a little lower than the 190,000 consensus payrolls forecast for June. But here's the point, NOT MUCH. And without doing the statistical tests to prove it, pretty obviously not statistically significant from the consensus view, even if indeed it proves to be an accurate forecast this month. Nor is it worth getting too excited over wages growth. As we wrote yesterday, even if we do see wages growth picking up to 2.8% as expected, and to 3.0% by August's release (seems highly likely) wages growth will still be historically very low, and very low adjusted for the rate of unemployment, and require no change in Fed policy other than to keep cautiously hiking. And that adjective, 'cautiously', encompasses everything from only one more hike this year to two, and everything from two to four hikes next year. The data will tell us how much. Not the Fed (there, I did manage to get in a reference to forward guidance after all).

May - make or break, though probably break

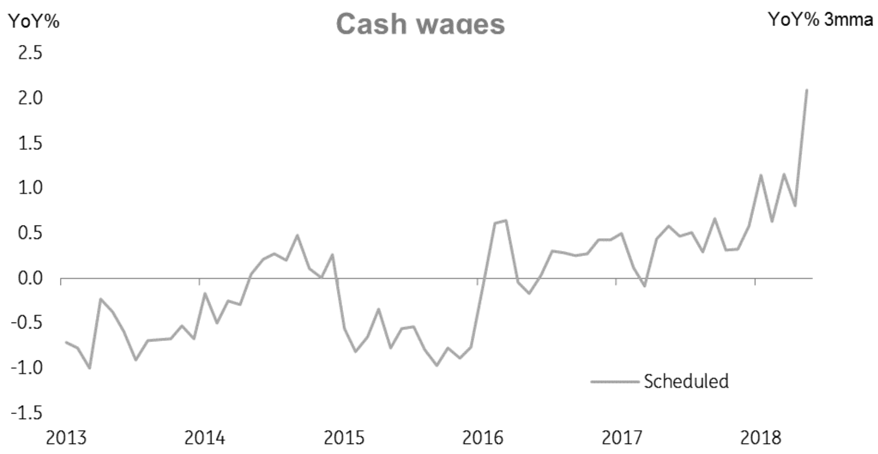
UK PM, Theresa May, meets her cabinet colleagues at the official retreat, Chequers this weekend, to try to thrash out a deal on Brexit. Having failed to satisfy everyone, my guess is that she will present version of Brexit that looks much like the 'Norway' option, in other words, membership of the single market for goods, but opt-outs and cherry picking on everything else. My guess is also that in trying to appease everyone, she will anger everyone. The EC will hate this, and so will her cabinet, though not for the same reasons. The EU is stepping up preparations for 'no-deal'. I think they are very wise to do so.

Asia today

Japan's labour cash earnings are a good measure to watch, and they have picked up recently. They are one of the reasons we are clinging on to a moderate growth forecast for Japan this year (1.0%), despite the loss of momentum shown by indicators like this week's Tankan survey. But notwithstanding a decent 2.1% YoY increase, they don't seem to be providing much of a boost to household spending, which fell a very nasty 3.9%YoY in May. We need a bounce in these figures, and soon, or we will be taking the axe to the Japan GDP forecasts, and looking hard too at the consumption tax hike scheduled for October 2019.

Elsewhere in the region, the day offers little more than some foreign exchange reserve data - not too interesting except for the current account economies, Philippines and Indonesia.

Japan: Labour cash earnings



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Downside risk to consensus on China reserve data

It's no longer a question if the US will go ahead with tariffs on Chinese imports tomorrow (6 July) - instead, it's now more a question about the aftermath – the impact on the world's second-biggest economy and then on the rest of the world. As a result, China's economic data for June will be under close scrutiny.

The data dump starts with foreign exchange reserves data this weekend (7 July), followed by inflation, bank lending, and trade over the course of the coming week, and then culminates into second quarter GDP release the following week.

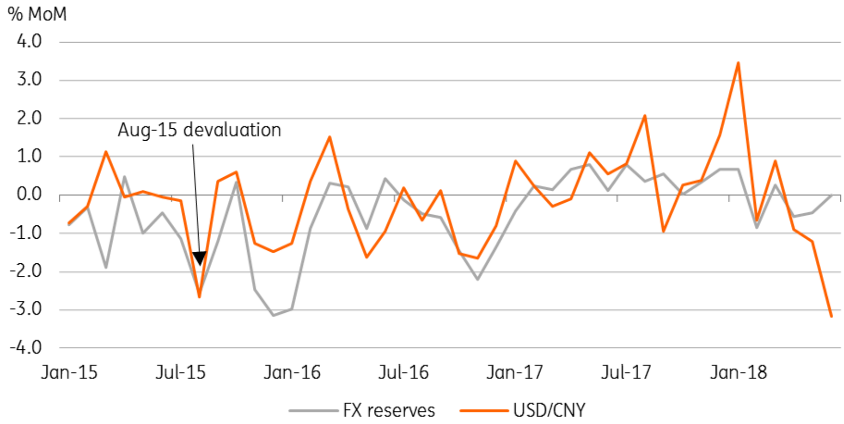
Of all, the foreign exchange reserves will be key given what's been happening to the Chinese yuan (CNY) following the US tariff announcement in mid-June – a shift from being Asia's outperformer until the announcement to underperformer with over 3% depreciation since. The latest depreciation reminds us of the 2.7% devaluation in August 2015 and judging from a $93bn fall in reserves in August 2015, the consensus of only $8bn reserves fall may appear to be understating the capital flight from China.

$3.103tr

Consensus on China fx reserves in end-June

Down by $7.6bn from end-May

China: Foreign reserves and USD/CNY



Source: Bloomberg, ING

Other data releases include exports, which are expected to have held up well in June ahead of the tariff kick-off, possibly led by front-loading of shipments before the tariffs take effect. The consensus on exports is 10.6% year on year growth in comparison to 12.6% in May, and for new yuan lending, it is CNY 1.535tr (CNY 1.150tr in May).

A surprise easing from the People's Bank of China with a cut in banks' reserve requirement should have supported the bank lending, while inflation continues to grind higher.

Korea and Malaysia central bank to stay on hold

Elsewhere in Asia, central banks in Korea and Malaysia will hold their monetary policy meetings, and the consensus is looking for no change in the rate policy by either. Hence all the attention will be on their policy statements, which, in all likelihood, will express caution on growth as the trade heat rises.

We're constantly watching our growth forecasts for regional economies for a downgrade and apart from a few Asian central banks, especially in countries where wide trade and current account deficits have battered currencies in the sell-off this year including India, Indonesia, and the Philippines, we expect monetary policy to remain on hold in the region.

India inflation data to lead RBI for next hike in August

India's consumer price inflation for June will condition expectations of the next Reserve Bank policy meeting in early August. On our forecast, inflation accelerated to 5.4% YoY in June from 4.9% in May on higher food and transport components.

The RBI forecasts inflation in a 4.8-4.9% range in the first half of FY19 (Apr-Sep 2018). Latest hike in the minimum support prices for agriculture produce and rising oil prices will sustain high inflation in the period ahead. We have been forecasting a 25bp RBI policy rate hike in August, and have now added one more 25bp rate hike at the October meeting.

Asia Economic Calendar

Country	Time	Data/event	ING	Survey	Prev.
		Friday 6 July			
Hong Kong	-	Jun Forex Reserves (US$bn)	430	-	432.1
Malaysia	0800	Jun 29 Forex reserves- Month end (US$bn)	-	-	107.9
Philippines	-	Jun Forex reserves (US$bn)	-	-	79202.4
		Monday 9 July			
China	-	Jun Forex Reserves (US$bn)	3101	3105	3110.62
Singapore	-	2Q A GDP (QoQ /YoY%)	-/-	-/-	1.7/4.4
Taiwan	0900	Jun Exports (YoY%)	13.9	8.1	14.2
	0900	Jun Imports (YoY%)	13.6	-	12
Taiwan	900	Jun Trade balance (US$bn)	13.9	8.1	14.2
		Tuesday 10 July			
China	0230	Jun PPI (YoY%)	4	4.6	4.1
	0230	Jun CPI (YoY%)	1.8	2.2	1.8
	-	Jun Money supply (M2) (YoY%)	8.3	8.4	8.3
Philippines	0200	May Exports (YoY%)	-4	-	-8.5
	0200	May Imports (YoY%)	11	-	22.2
	0200	May Trade balance (US$mn)	-3684	-	-3615
		Wednesday 11 July			
Malaysia	0800	Overnight Policy Rate	3.25	-	3.25
South Korea	0000	Jun Unemployment rate (% SA)	4	-	4
		Thursday 12 July			
India	1300	Jun CPI (YoY%)	5.4	-	4.87
	1300	May Industrial production (YoY%)	5.8	-	4.9
	-	Jun Trade deficit (US$bn)	-15.9	-	-14618
	-	Jun Exports (YoY%)	11	-	20.18
	-	Jun Imports (YoY%)	15	-	14.85
Malaysia	0500	May Industrial production (YoY%)	3.4	-	4.6
Singapore	0600	May Retail sales value (MoM/YoY%)	2.9/2.7	-/-	-0.2/0.4
South Korea	-	7-Day Repo Rate	1.5	-	1.5
China	-	Jun Financial institution loans (Yuan bn)	1617	1535	1150
		Friday 13 July			
China	-	Jun Trade Balance (US$bn)	23	-	24.922
	-	Jun Exports (YoY%)	14.4	-	12.6
	-	Jun Imports (YoY%)	22.4	-	26
Singapore	-	2Q GDP - advance (QoQ/YoY% saar)	2.0/3.8	-/-	1.7/4.4

Source: ING, Bloomberg

Malaysia: Downside trade surprise

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Source: shutterstock

3.4% Export growth in May

year-on-year

Worse than expected

A downside export surprise

Malaysia's exports in May grew by 3.4% year-on-year, slower than the consensus forecast of 6.4%, while import growth of 0.1% was in line with expectations. These growth rates are down from 14% and 9% respectively in April. The high base effect explains some of the slowdown: both export and import growth peaked above 30% in May 2017. Commodities and electronics continue to dominate the overall trade picture, both posting a sharp growth slowdown in May.

The year-to-date export growth of 6.9% YoY and import growth of 1.3% have both slowed sharply from 23% and 28% respectively a year ago. But the trade surplus of MYR 54.5bn in the first five months was still wider than MYR 33bn surplus in the same period of 2017.

The trade war clouds outlook

The trade war clouds the outlook for Malaysia's trade and GDP growth for the rest of the year. We expect the pass-through of weakening global trade to commodity prices, and then to Malaysia's export weakness, to shift the MYR from being Asia's outperformer to being one of its underperformers in the rest of the year (see Asian foreign exchange in tariff tantrum). We have revised our USD/MYR forecast for end-2018 for further weakness to 4.35 from 4.05 (spot 4.05).

Snap | 5 July 2018 Philippines

Philippines: Inflation soars in June

Further monetary policy tightening is likelier at the next meeting, after inflation soared to 5.2% in June

Source: Shutterstock

5.2%

Inflation rate in June

Exceeds central bank forecast of 4.3- 5.1%

Higher than expected

Inflation surprising on the upside could require a more aggressive monetary tightening.

Inflation soared to a 5.5-year high of 5.2% in June from May's 4.6% and beat the upper end of BSP's forecast range of 4.3-5.1%. Consensus was at a more moderate 4.8%. Core inflation also jumped to 4.3% in June, from May's 3.6%. Higher inflation for food and non-alcoholic beverages, utilities, transportation and education combined to bring the upside inflation surprise. The cost of education plays a significant role every June as school tuition and fees are paid just before the start of the school year. Excluding the impact of education, headline inflation would still be high and would be at the upper end of BSP's forecast range. Full implementation of the government's supply augmenting measures would moderate inflation. However, additional cost-push pressures are emerging. Three regional wage boards approved 4-5% increases in minimum wages. Another regional wage board might approve a 6% increase. In addition, the government has allowed a 12% increase in minimum transport fares for the country's capital and two adjoining regions. Expanding the increase to other regions could follow. Another price pressure is through the recovering oil price. PHP weakness is another price pressure and it depreciated by c.7% YoY in June. Demand pull price pressures from strong economic activity and income tax reform are likely to exacerbate the tught price environment. These price pressures, together with the upside June inflation surprise, fuel expectations of high inflation. Reining in inflation expectations, aside from stabilizing PHP, may require a more aggressive central bank response. We now expect BSP to raise policy rates at the next policy rate meeting (in August) by at least 25bp. A higher policy rate increase is possible.