Good MornING Asia - 6 June 2019

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In this bundle

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Cut fever

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One snippet of weak data - several more strong

It's the big release of the month from the US tomorrow, the labour report, and that has markets fixated on all potential indicators for this market-moving data. Over many years, I have looked at this data closely. I have examined almost every available complimentary data source and examined them for their predictive power for the month-on-month non-farm payrolls series that forms the heart of the report.

What comes next may shock you.

1. The ADP is far and away the best predictor of non-farm payrolls, beating the employment indices of the ISM surveys (both strong incidentally), job vacancies, monster survey etc.
2. It is still rubbish

The labour report remains, despite the best efforts of economists, a virtually unpredictable survey, and until it comes out, the result will be in question, as will its implications for the Fed. Tomorrow will, therefore, be important. For more on this, please see the labour market preview by James Smith.

Beige Book improves - yeah, whatever

The US Fed's Beige book, its interview-based assessment of the state of the economy, in contrast to the doom-and-gloom being peddled by the rate-cut soothsayers, showed an improvement in the economy overall, with the economy growing at a "moderate pace" up from "slight-to-moderate" pace the previous month. The outlook for employment was also described as similar to the previous period. No slowdown is evident here...

Yet it seems even sensible FOMC members are being carried along on the wave of self-fulfilling pessimism that is dominating markets, well, the bond market in particular, though I note this morning that bond yields are actually up since I was last in the office on Tuesday.

- Robert Kaplan: Wants to see evidence of slowing economic growth before deciding if an interest rate cut is necessary in response to the escalating dispute between the US and trading partners.
- Charles Evans: It would be prudent to take a look at the monetary policy setting. Would be open to considering a rate cut. Nervous about low inflation.
- Brainard: Need to be prepared to adjust policy to sustain growth.
- Richard Clarida: The Fed will deploy policies to deliver on the dual mandate.

And of course, earlier in the week, James Bullard suggested a rate cut may be warranted.

The USD continues to look weak, as a result, and as a corollary, Asian FX, like the KRW and TWD for example, looks stronger (the AUD has been flirting with 0.70). Firmer (higher) Treasury bond yields are probably a response to the equity market, for whom bad news = rate cuts = lower discount rate = higher NPV of future earnings = higher price.

Or "bad = good" in its reduced form.

"Not nearly enough"

"Not nearly enough" was Donald Trump's response to Mexico's diplomatic initiative to stave off tariffs. In case we lose sight of where we are in the rapidly globalizing trade war, this comes as a useful reminder. India, take note. India has hinted that it will be able to talk its way out of the preferential treatment on goods duties that the US has said it is stripping away from it. Looking at the Mexico situation, the cost of the plane tickets from New Delhi to DC for the Indian delegation might be better employed elsewhere.

Market pressure spreads

There are signs that the "global recession" anxiety is spreading across a wide swathe of markets now. Gold prices (fear factor) are up. Oil prices (crude glut) are down. Copper prices (the so-called "smart metal" due to its alleged cycle-predicting properties) is down. Now, these commodity prices may still be influenced by global risk sentiment like pure financial asset prices, but they ought also to shine a spotlight more closely on the real world. Their decline is somewhat concerning. Although I am dismissive of the recession argument, it can become self-fulfiling, and this is perhaps some evidence that it is becoming so. We need to keep watching stuff like this, as well as the US macro figures and Fed speakers.

Focus on the RBI today

(From Prakash Sakpal) In India, it’s an RBI decision day. A dismal 4Q FY2018-19 GDP has swayed the consensus in favour of a 25bp rate cut. We are in the minority forecasting no policy change. This is partly a case of what we think the RBI should be doing, not what it necessarily will do. We believe two back-to-back-rate cuts in February and April combined with extremely loose fiscal policy is enough accommodation for an economy that still faces the danger of potential inflation spike from supply shocks to food and fuel prices. A cut today could take the INR past USDINR 70, and potentially lead to an awkward reversal later this year, earlier than the 2Q20 forecast we currently have penciled in.

Ending the long-standing political uncertainty, Thailand's new parliament has elected Prayuth Chan-Ocha as prime minister. Prayuth's Palang Pracharath party, which leads a 19-party coalition, still faces stiff opposition in the lower house. However, with a strong backing of the military-dominant Senate, Prayuth should be able to push ahead with his economic agenda of boosting infrastructure investment to revive the beleaguered economy. But this is something the economy would benefit from over a longer term. For now, the cyclical slowdown with intensified downside risks from the global trade war looks unavoidable. Besides a more accommodative fiscal policy, a reversal of a central bank's late-2018 policy rate hike should help to ease the short-term pain.

And in the G-7, the ECB meets today. Carsten Brzeski has previewed the meeting here. With no rate movement at all likely, the main focus of the meeting will be new macro projections, including a likely lower inflation outlook, some more details on the TLTRO's slated for introduction in September, and probably little if any further reference to tiering, which probably will only resurface if further easing looks imminent.

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ASEAN Morning Bytes

General market tone: Risk-on. Asian markets look to tiptoe higher with Fed rate cut hopes to bolster risk sentiment.

EM Space: Fed talks up rate cuts while ADP supports claim

- **General Asia:** Weak ADP jobs numbers coupled with the Fed's beige book and commentary from officials helped push the Fed rate cut story further. Offsetting the tone was data on the US services sector which bested market consensus to show that the economic growth momentum remained intact at least for now.
- **Thailand:** Ending the long-standing political uncertainty, new parliament elected Prayuth Chan-Ocha as prime minister. Prayuth's Palang Pracharath party, which leads a 19-party coalition, still faces stiff opposition in the lower house. However, with a strong backing of the military-dominant Senate Prayuth should be able to push ahead with his economic agenda of boosting infrastructure investment to revive the beleaguered economy.
- **Philippines:** Consumer price inflation for the month of May caught the market off guard, clocking in at 3.2% as food prices jumped higher by 3.4%. The index heavy food basket was the main driver for the upside surprise but the central bank appears unfazed by the latest print, suggesting that more rate cuts would be on the way. Bangko Sentral ng Pilipinas Governor Diokno pledged to cut rates in the coming months, indicating that the timing would remain dependent on incoming data.

What to look out for: Trade war developments, Fed speakers, US NFP

- Fed Kaplan (6 June)
- Euro zone GDP and ECB meeting (6 June)
- US initial jobless (6 June)
- US NFP (7 June)