

A question of confidence

Recent market moves are like a game of chicken between optimists - geared up by tax-cut fuelled economic growth, and pessimists weighed down by rising valuations and borrowing costs. What happens next in aggregate may be determined by the tiniest of changes in sentiment.



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The mood is black in Asia

In the US, strong growth data has pushed up sentiment, causing the stock market and other risk asset markets to rise, and bonds to sell off. That same bond market sell-off raises the risk-free rate, undermining stock valuations and causing some long-risk investors to trim positions, sending risk asset prices down again. Bond yields fall. Today we are roughly back where we started yesterday. The 10Y US Treasury yield is about 3.18, though got as high as 3.23% yesterday. Stocks, however, are lower. The USD stronger.

In Asia, it isn't even that good. The growth story is at best trundling along with no significant uptrend in sight. In some economies, even that so-so growth appears challenged. China is still achieving growth, but at what cost to deleveraging and overcapacity? The external deficit economies of India, Indonesia and the Philippines are having to squeeze growth with higher rates to prevent their currencies from dropping sharply. We will see just how successfully later today when the RBI decides how to address its problems. Near neighbour, Sri Lanka is also running into trouble. The lesson India should learn from them is, not hiking is a good way to see your currency plunge. Central bank rhetoric and import curbs aren't much use when confidence

evaporates. Even intervention is usually only a short-term stop-gap.

The same rise in global (US) yields is also opening up a gap with local Asian yields and weighing on Asian FX performance. Today, we will see inflation data from the Philippines for August, partly influenced by recent hurricane damage to food and therefore food prices, but also reflecting a weaker peso and higher import prices. Our economist in Manila, Nicky Mapa, sees a higher than consensus 6.9%YoY inflation print today - some further growth dampening tightening appears warranted here too. Even in Korea, where the growth data has been fairly disappointing, today's September inflation print came in noticeably higher than expected, with headline inflation now at 1.9% and core inflation back above unity at 1.2%YoY. Some of the blame must be due to a weaker KRW. Ever higher oil prices don't help.

Is good news bad news?

With the potentially market-moving jobs report from the US out later today, what's the best outcome for Asia. Well if it's anything like Wednesday's strong ADP report, Asia could do with a weak number. In particular, I think a softer wages figure could help trim optimism and put some downward pressure on shorter-term US yields and thereby the USD. And softer wages is looking likely. Our house view is for the wages growth to fall from 2.9% to 2.8%YoY. but even that will require a further 0.4%MoM increase, which would be a real step up in the monthly wages run rate. Last year, September wages grew an impressive 0.5%MoM (rounded), though dropped 0.2% the following month. Is there some crazy out of step seasonal at work here? We'll find out later today, but if there is, and we see either a revision down to last month's growth data (often happens) or an undershoot of the 2.8% consensus view, then such bad news might be regarded by Asian investors as rather good. Until then, however, Asia is likely to remain under pressure.

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