

## Asia markets wait for the Fed

Asian markets are quiet ahead of the Fed...China's data dump may stir things up a bit today, but the main focus will be on the Fed's message and any hints they may give about taper timing



Federal Reserve

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### Stuff you should read

Ahead of tonight's FOMC meeting, [here is the combined wisdom of our US economics, rates and FX colleagues](#). And there is also some commentary from James Knightley on the US [retail sales and producer price releases](#), which were respectively, weak, but from a very high base, and stronger than expected. And also on the [industrial output figures](#), which were more or less in line with expectations, rising 0.8% in May from April.

How much, if any of this recent data will impact the Fed's decision is hard to say, I suspect very little of it. And though it would be surprising if the Fed were to provide any indications that it is more seriously considering a taper, there are growing reasons for them to do something as money market funds battle with rates that are verging on negative. Suggestions that this could be solved by tweaking the zero rate on reverse repos seem to be ignoring the ultimate cause of these low rates - Fed asset purchasing. This is a bit like the rhyme of the old woman who swallowed a fly, then swallowed a spider to catch the fly and so on until she ends up swallowing a horse. You know

how this one ends.

A further caveat to the gentle decline for the USD suggested by our FX colleagues comes from the US TIC data for April released overnight. This helps explain two conundrums in markets currently, the rally in US Treasury bonds, and the stability of the USD. With TICs showing European flows into US government bonds the main driver for a net \$49bn of foreign inflow in April, this supports the recent remarks by our rates strategists that FX hedged returns on US Treasuries are looking extremely good right now ([this by Padhraic Garvey is worth another read even if you've already read it](#)), especially as the glut of dollars the Fed has created has dampened the cross-currency basis.

Moreover, with the "transitory inflation" story fully bedded into market pricing right now, there is little further movement the Fed could generate in that direction. Whereas acknowledging that although not yet necessary, the time is nearing when some consideration of the timing of the taper is warranted, might just be enough to provide a pop the other way. We will have to wait and see. Most likely, this will be a non-event.

The other potentially interesting event to watch today will be the Biden-Putin meeting. I don't think anyone has any high expectations for positive developments from this, though we hope it will be less acrimonious than the Alaska US-China meeting earlier this year. That could provide another reason for Treasury markets to rally.

## Asia today - it's all about China

Although the Fed meeting is dominating thinking here in Asia today, there is a lot of activity data released by China later on. Iris Pang in Hong Kong writes "We expect slower growth in retail sales and fixed asset investments in May due to the high base from last year. But industrial production growth is affected by a very mixed bag of factors, including a high base but chip factories already operating at full capacity as well as stronger construction activity.

We will also have a closer look into construction investment within the fixed asset investment release, and home prices too as there were more tightening measures on home buying activity in the month, which could continue for quite a while".

Japan has already released May trade data, which showed a much smaller surplus than had been expected, despite only a marginal under and overshoot of exports and imports respectively. The adjusted trade balance for May was JPY43.1bn, though still comfortably above zero. This shouldn't have much bearing on the JPY

Japan machine orders for May were also a bit soft on the month, rising only 0.6%MoM. Though this offsets last months surprising strength and year on year growth is still a reasonable 6.5%, though greatly flattered by base effects. As one of the main domestic-demand inputs into the 2Q 21 GDP estimate, this doesn't help thoughts that investment might offset consumption weakened by various prefectures' states of emergency (though these anecdotally are not having much of a binding impact).

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