

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).

Author

Alissa Lefebre
Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials
marine.leleux2@ing.com

Jesse Norcross
Senior Sector Strategist, Real Estate
jesse.norcross@ing.com

Teise Stellema
Research Assistant, Energy Transition
teise.stellema@ing.com

Diederik Stadig
Sector Economist, TMT & Healthcare
diederik.stadig@ing.com

Diogo Gouveia
Sector Economist
diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux
Sector Strategist, Financials
marine.leleux2@ing.com

Ewa Manthey
Commodities Strategist
ewa.manthey@ing.com

ING Analysts

James Wilson
EM Sovereign Strategist
James.wilson@ing.com

Sophie Smith
Digital Editor
sophie.smith@ing.com

Frantisek Taborsky
EMEA FX & FI Strategist
frantisek.taborsky@ing.com

Adam Antoniak
Senior Economist, Poland
adam.antoniak@ing.pl

Min Joo Kang
Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist

samuel.abettan@ing.com

Franziska Biehl

Senior Economist, Germany

Franziska.Marie.Biehl@ing.de

Rebecca Byrne

Senior Editor and Supervisory Analyst

rebecca.byrne@ing.com

Mirjam Bani

Sector Economist, Commercial Real Estate & Public Sector (Netherlands)

mirjam.bani@ing.com

Timothy Rahill

Credit Strategist

timothy.rahill@ing.com

Leszek Kasek

Senior Economist, Poland

leszek.kasek@ing.pl

Oleksiy Soroka, CFA

Senior High Yield Credit Strategist

oleksiy.soroka@ing.com

Antoine Bouvet

Head of European Rates Strategy

antoine.bouvet@ing.com

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Edse Dantuma

Senior Sector Economist, Industry and Healthcare

edse.dantuma@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Rico Luman

Senior Sector Economist, Transport and Logistics

Rico.Luman@ing.com

Jurjen Witteveen

Sector Economist

jurjen.witteveen@ing.com

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Nicholas Mapa

Senior Economist, Philippines

nicholas.antonio.mapa@asia.ing.com

Egor Fedorov

Senior Credit Analyst

egor.fedorov@ing.com

Sebastian Franke

Consumer Economist

sebastian.franke@ing.de

Gerben Hieminga

Senior Sector Economist, Energy

gerben.hieminga@ing.com

Nadège Tillier

Head of Corporates Sector Strategy

nadege.tillier@ing.com

Charlotte de Montpellier

Senior Economist, France and Switzerland

charlotte.de.montpellier@ing.com

Laura Straeter

Behavioural Scientist

+31(0)611172684

laura.Straeter@ing.com

Valentin Tataru

Chief Economist, Romania

valentin.tataru@ing.com

James Smith

Developed Markets Economist, UK

james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials

suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios
maarten.leen@ing.com

Maureen Schuller
Head of Financials Sector Strategy
Maureen.Schuller@ing.com

Warren Patterson
Head of Commodities Strategy
Warren.Patterson@asia.ing.com

Rafal Benecki
Chief Economist, Poland
rafal.benecki@ing.pl

Philippe Ledent
Senior Economist, Belgium, Luxembourg
philippe.ledent@ing.com

Peter Virovacz
Senior Economist, Hungary
peter.virovacz@ing.com

Inga Fechner
Senior Economist, Germany, Global Trade
inga.fechner@ing.de

Dimitry Fleming
Senior Data Analyst, Netherlands
Dimitry.Fleming@ing.com

Ciprian Dascalu
Chief Economist, Romania
+40 31 406 8990
ciprian.dascalu@ing.com

Muhammet Mercan
Chief Economist, Turkey
muhammet.mercan@ingbank.com.tr

Iris Pang
Chief Economist, Greater China
iris.pang@asia.ing.com

Sophie Freeman
Writer, Group Research
+44 20 7767 6209
Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content

+44 (0) 207 767 5331

owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM

+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com