

## Euro problems

Euro takes a beating as coalition talks suggest an anti-European government could emerge in Italy



Source: istock

### Never a dull moment in the Eurozone!

After suggesting yesterday that Italy's prospective government might not be much less market-friendly than previous ones, we feel we owe our readers a swift retraction. It is hard to say exactly what the latest state of play is, there have been so many allegations and denials. This is a fast-moving event. Full details of the Northern League / Five Star (North-Star?) coalition manifesto should be out within a few days, But despite suggestions to the contrary, it will apparently **not** contain a demand for Italy's debt held by the ECB to be cancelled, or a mechanism for countries to leave the Eurozone. It may, however, ask for some treaty changes. Whatever it contains, it is hardly going to support the Macron-Merkel (Mackerel?) plans for reform of the Eurozone, and the Euro (EUR) is caught in the cross-fire. EURUSD was down below 1.18 last night, before staging a modest recovery this morning. Asian FX might stage a modest rally as the EUR momentum shifts back in the EUR's favour in the short-term.

This story will doubtless deliver more entertainment over the coming days. But it is hard to see how it will be particularly Euro supportive. That said, there are plenty of factors on the other side of FX crosses to please all sides of the market, not least, what is happening in terms of the US-China trade talks.

Sterling has been a surprise gainer against the EUR (not the USD though). Our feeling is that trouble with Italy will make the Europeans even less likely to throw a lifeline to the UK in Brexit negotiations. It will be all hands to the pump to secure and save the single currency project. So there may be some room for a reversal here, with the USD probably the most likely way to play this if it begins to turn ugly.

## Not too boring in the US and UK either

Whilst the allegations over who paid whom for what in the US continue to provide news channels a steady stream of pap to dull the senses of their viewers, the fallout from the US-Korea air-drills this week has still not fully settled. N Korea is allegedly announcing it is not going to trade in its nukes for an economic boost. As that's all that Trump wants, the June 12 talks in Singapore may be a little less constructive than was initially hoped for.

We haven't talked about Brexit here for some weeks - deliberately, as we assume that tolerance for this is limited. But according to stories running in the British Press, PM Theresa May will set out to the EU her clarification on Brexit this week before they meet in June to discuss how to proceed. The latest reports suggest a combination of sliding extensions to the Customs Union post-2019 to enable the UK to come up with effective border controls and a feasible solution to the Irish border. Sounds a bit feeble to me. But anything that postpones the plunge into the abyss of life outside the EU seems welcome right now - that is if the EU decides to accept this proposal, which they may not.

## Run of G-7 economic data supports the geopolitical bias

Yesterday's data flow confirmed that core inflation in the Eurozone remains way off target and heading in the wrong direction. Oil price rises will in due course feed into core figures through second round channels like airfares. And with summer approaching in Europe, that probably won't take too many more months to become apparent. The US dataflow held few surprises yesterday. With April 2018 one of the coldest April's on record since 1895, it wasn't too surprising to see the housing starts and permits figures undershooting expectations - but not by much, so all in all, not a bad result. April industrial production was also pretty good - probably also helped by low temperatures.

Today's data flow from the G-7 can probably be mainly ignored. Japan's Machine orders data is mainly noise (-3.9%MoM), though the US Philly Fed survey may be worth half a glance when it is out later.

## Asia today - the fallout from EM concerns should see BI hiking

Today, another Asian central bank will likely have to respond to international capital outflows by hiking rates. First it was the Philippine Central bank, now it is Bank Indonesia. We expect a 25bp hike from them today, taking the policy 7-Day Repo rate to 4.50%. The real question is, will this be enough? For either them or the Philippines? The only sensible answer is that it will be sufficient once current account deficits generated by overstimulated economies start to respond. This may require further hikes, a slowdown in growth, and perhaps some winding back of fiscal stimulus. None of this will be easy, or popular. A stronger USD makes it harder still. Governments have fallen over less. The political calendar hots up from this August before national elections next year.

Malaysian GDP for 1Q18 should come in in-line with consensus at 5.6%, a little slower than the 5.9%. A little slowdown here won't hurt from these rates, and in any case, Malaysia does not have the current account issues of the other two SE Asian economies mentioned.

Singapore's April NODX was stronger than expected, rising 6.5%MoM, which was a good bounce back from March weakness, even when you take downward revisions for March into account. There was, however, another negative electronics element to these numbers, with electronics falling 6.9%YoY, so we will be poring through the data when more detail is released to get to the bottom of this.

Finally, Australian labour market data. Yesterday, wage cost indices were no better and perhaps even a little bit softer than the consensus view. I wouldn't be surprised to see whatever the headline employment figure is, to be dominated by part-time jobs. That could mean a decent headline, but a poor Full-time equivalence.

## Author

### Robert Carnell

Regional Head of Research, Asia-Pacific

[robert.carnell@asia.ing.com](mailto:robert.carnell@asia.ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.