

Markets respond to patient Fed

"No strong arguments for a move either way" clips the US rate-doves' wings, pushing USD higher.



Source: Federal Reserve

2.35%

Interest rate on US Excess Reserves

down 5bp

Lower than expected

Technical changes show how little real liquidity there is

James Knightley has done [his usual thorough job summing up last night's FOMC decision](#). Which can be characterized as highlighting the ongoing (though transitory) lack of inflation, whilst also flagging the better outlook for activity and the balance of risks.

2-Year Treasury notes responded to the cold water poured on rate-cut ideas by falling, with yields rising around 4bp, though it was a hairy ride, and they were at one point down 6bp.

The 10Y yield is almost unchanged at about 2.50%, resulting in a slightly flatter yield curve.

The technical adjustment to the interest rate on excess reserves (IOER) is interesting. With the Fed funds rate trading through the IOER recently, the Fed has acted to push the effective Fed funds

rate back towards the centre of the 2.25-2.5% target range. The IOER was lowered to 2.35% from 2.4% following recent sessions in which the effective Fed funds rate has traded above it. The IOER was designed to act as a type of ceiling to the Fed's target range, but recent price action shows that by paying the banks a decent rate for doing absolutely nothing, the real liquidity in the overnight dollar market is set outside the banking system, by the much smaller liquidity source of the Federal Home Loan Banks, which don't get IOER and so are free to lend.

There is a good piece on Bloomberg today, their Bloomberg Reaction, "Fed tweaks IOER but no Repo Facility Innovation", which discusses the next moves. A Repo tool would make sense. When the Fed first normalized policy, it used a reverse-repo facility to ensure the effective rate would hold the floor of the target-range. Now a repo facility to ensure the ceiling is not breached seems a sensible addition.

USD stronger on Fed decision

The dollar index is stronger following the FOMC decision and testimony, no doubt bolstered by the damage caused to the rate-cut thesis. Two currencies in the Asia-Pacific region to watch are the AUD and NZD. Both have upcoming rate meetings. Both have growing reasons to cut, with poor NZ employment data most recently, and soft Australian inflation.

The AUD is trading just above the 0.70 level. And although I would say that this might be a bit weaker than fundamentals would suggest, in the short term, we still like a foray into the AUDUSD 0.69-something area. The NZD should follow it lower, though which currency weakens most, will probably reflect a horse race between the two central banks to see which can out-do the other with dovishness.

Elsewhere in Asia, the story on FX is a mixed one, some up, some down, some unchanged. This micro-shift in the Fed may take a little thinking about when there are other factors at work, both domestic (rate cut thoughts in some economies) and international (the impact of oil prices weakening - good for INR, not so good for MYR, for example).

Korean inflation - not as bad as feared

After a string of weak reports, Korean inflation for April was not as bad as expected, with the core rate remaining unchanged at 0.9%YoY and headline inflation nosing up to 0.6% from 0.4%. Ignoring historical base effects and focussing only on price levels of subcomponents, the better outcome seems to have been heavily food driven, though there was a small increase in furnishings too as well as transport, which, bolstered by small monthly increases in other components, has helped keep the April figure from sliding further.

That said, the rate of inflation is substantially below the Bank of Korea's (BoK's) target rate of 2.0%. with weak exports and domestic activity. The BoK is resisting calls for a cut, but we suspect it is only a matter of time before they reverse last November's hike with a 25bp cut later this quarter.

Thailand provides stimulus measures

(From Prakash Sakpal): The Thai government announced a THB 13.2bn economic stimulus directed at farmers and low-income people. This follows the downgrade earlier this week of the government's GDP growth forecast for 2019 to 3.8% from 4.0%. At less than 0.1% of GDP, we doubt the package will be enough to shore up growth. The hawkish central bank and persistently

large current account surplus sustain the potential for THB outperformance, though we maintain our view of the USD/THB rate hovering around 32 through 3Q19.

Asia Day ahead - more PMIs, HK GDP, Indon inflation

The rest of the day is a mopping up exercise for those countries in the region that have not yet released manufacturing PMI data, Most of the ASEAN plus Korea. We aren't expecting any surprises or much to celebrate in these figures.

Indonesian inflation could nose slightly higher but remains moderate. And with BI more fixated on the external balance, we don't expect this to change policy settings meaningfully.

And with China on vacation today, HK GDP figures may be our closest thing to a proxy release on the strength of the Chinese economy.

Author

Olivia Grace

Editor

olivia.grace@ing.com

Julian Geib

Junior Economist, Global Trade

julian.geib@ing.de

Zoltán Homolya

Economic research trainee

zoltan.homolya@ing.com

Amrita Naik Nimbalkar

Junior Economist, Global Macro

amrita.naik.nimbalkar@ing.com

Mateusz Sutowicz

Senior Economist, Poland

mateusz.sutowicz@ing.pl

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@ing.com

Michiel Tukker

Senior UK & Eurozone 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

Senior Economist, Healthcare & Technology

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@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
Deputy Global Head of Editorial 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

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 Corporate 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 Kloek

Senior Economist, Netherlands

marcel.kloek@ing.com

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@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, 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