

Searching for a theme

Several weeks of absence has not led to a build-up of exciting themes - persistently low inflation is the stand out



arrows

Distance brings perspective - usually

A couple of weeks away usually helps put the global macro and market story into a better perspective. Getting away from the thick of the woods does really seem to make the trees stand out better. Not so much this time, though things have definitely changed. Some of the big worries seem to have been replaced by smaller but persistent irritants. A few weeks ago, we spent time mulling the prospects of a global recession. We didn't buy into that story then and it seems to have largely gone away. Little time is also spent worrying about a Chinese hard landing - that too has been written off, as too are concerns about an escalating trade war.

Some central banks are returning to action

The persistent irritant comes from the observation that central banks no longer seem to have any of the answers to a persistent undershoot of inflation or of tepid growth. Those central banks that might have spent some of this year starting or extending policy normalization seem on hold, as inflation stays low, whilst others now look likely to move the cycle back towards easing. Illustrating the former group, Bank Indonesia will likely fall into this camp today, and in all likelihood, so too will the Bank of Japan. Yesterday's inflation driven hit on the AUD, as Reserve Bank of Australia rate cut expectations mount is a good example of the latter case. The RBNZ may be close behind in

cutting.

A new approach may be needed to deal with "lowflation"

So if there is one thing that stands out amidst a sea of "meh!", it is the slow chipping away at the growth/inflation framework that central banks have relied on as the yardstick for how to set policy. For all of the aggressive easing of past years to spur recovery, today's economies simply don't seem to respond to lower rates with much stronger activity or with higher prices or wages. The question is, should central banks respond with even more aggressive easing. We are beginning to suspect not, though that doesn't mean we don't think Central Banks like the RBA will hold back. They just won't achieve much by sliding back in the direction of zero rates.

Outlook for the BoK changes after terrible GDP

Another central bank that may well be reflecting over recent decisions to leave rates on hold is the Bank of Korea. They left rates at 1.75% at their meeting whilst I was on holiday earlier this month. I had thought that there was a chance they would cut. Their October 2018 25bp rate hike was hard to reconcile with the data back then, and it now looks clear that it was premature as the economy contracted -0.3%QoQ in 1Q19 to take year on year growth down to only 1.8%. 4Q18 GDP growth was 3.1% in comparison.

The KRW has already hit our 2Q19 target of 1150, and we may have to extend that forecast higher as expectations will surely mount that the BoK will reverse last year's decision, or even exceed it in reverse. Korean Treasury bonds also look set to see yields approach or push through the March lows, perhaps breaching the 1.8% level.

But until the global technology slump passes, this probably won't do all that much good. Government concern about the build-up of South Korean household debt may have some justification. And sometimes, a slowdown like this is inevitable. But finding the right balance between fighting the business cycle only to drive through undesirable unintended consequences is hard to do. Inaction will be criticized as weakness, and central bank independence will be threatened. There are no easy answers to this.

Author

Robert Carnell

Regional Head of Research, Asia-Pacific

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>.